

# FOCUS

## ANTI-MONEY LAUNDERING



December 2006

## CIVIL PENALTY PROVISIONS IN *ANTI-MONEY LAUNDERING AND COUNTER-TERRORISM FINANCING ACT 2006*

Reporting entities could have to pay up to \$11 million if they contravene the civil penalty provisions in the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth). Partners Peter Jones and Anna Lenahan and Senior Associate Judy Maguire report.

The new *Anti-Money Laundering and Counter-Terrorism Financing Act* introduces harsh civil penalties for breaches

### HOW DOES IT AFFECT YOU?

- Breaches of the civil penalty provisions in the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) can attract a pecuniary penalty of up to \$11 million for a body corporate and \$2.2 million for individuals.
- There is no reason to suggest that the courts will hesitate to impose significant pecuniary penalties.

### BACKGROUND

The *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) (the **Act**), which came into force on 13 December 2006, will be implemented in stages over two years. Some substantive provisions already apply.

### THE CIVIL PENALTY REGIME

#### WHAT IS A CIVIL PENALTY?

Many of the obligations in the Act are described as 'civil penalty provisions', including the obligations to:

- not provide a designated service to a customer before carrying out an applicable customer identification procedure;
- carry out ongoing customer due diligence;
- report suspicious matters, threshold transactions or international fund transfer instructions;
- not provide a designated service without having adopted an anti-money laundering (**AML**) and counter-terrorism financing (**CTF**) program (and to maintain that program);



- not enter into a correspondent banking relationship with a shell bank or to carry out due diligence on correspondent banking relationships; and
- keep records.

Where breach of such an obligation occurs, the Australian Transaction Reports and Analysis Centre (**AUSTRAC**) can apply to the Federal Court for a 'civil penalty order' and, if the court is satisfied that a person<sup>1</sup> has contravened a civil penalty provision, it may order the person to pay a pecuniary penalty to the Federal Government.

Where the person is a body corporate, the penalty must not exceed \$11 million and in all other cases it must not exceed \$2.2 million. In considering the amount of any pecuniary penalty, a court must take into account certain criteria (described below under the heading **Deciding an appropriate penalty**).

In earlier versions of the Act breaches of these obligations attracted criminal penalties. In line with the Government's view that a civil penalty regime is more appropriate for a regulatory scheme that places obligations largely on financial institutions, many criminal penalties no longer apply.<sup>2</sup> Consequently, it will be much easier to establish a contravention of a civil penalty provision. This is because:

- the civil standard of proof will apply. It will only be necessary to establish on the balance of probabilities that a person contravened a civil penalty provision; and
- it will not be necessary to prove any fault element (eg knowledge or recklessness) on the part of the person (for example that a person intended to breach a civil penalty provision).

## WHO IS LIABLE

Unlike some overseas AML/CTF regimes, the civil penalty regime does not target individuals. AML/CTF obligations which give rise to civil penalties are imposed on 'reporting entities'. The reporting entity must comply with the obligation and it is the reporting entity which contravenes the civil penalty provision if it does not comply. Pecuniary penalties will be enforced as if they are judgment debts.

1. Defined as: an individual; a company; a trust; a partnership; a corporation sole; or a body politic.

2. Some breaches remain criminal offences such as tipping off and providing or receiving a designated service using a false customer name or customer anonymity.

## BODIES CORPORATES

Pecuniary penalty orders of up to \$11 million can be imposed on reporting entities that are body corporates.

Where the reporting entity is a body corporate the AML/CTF obligations are imposed on the body corporate. There is no provision in the Act that directly imposes any obligation on the directors of a body corporate.<sup>3</sup>

It follows that a civil penalty provision will be contravened by the body corporate (and not by the directors or senior management) and any pecuniary penalty order will be imposed on the body corporate (and not on the directors or senior management). The Act does not extend liability for a pecuniary penalty order to the directors of a body corporate as a class.

However, failure by directors of a reporting entity to ensure that it complies with its AML/CTF obligations under the Act could be a breach of other relevant legislation (for example, the directors duties under the *Corporations Act 2001* (Cth)). In addition, directors could be liable as ancillaries (see below).

Additionally, the imposition of a substantial pecuniary penalty order could have serious implications for an Australian Prudential Regulation Authority (**APRA**) regulated entity which is subject to APRA's capital and solvency requirements. Other consequences could include reputational risk, loss of market share and shareholder dissatisfaction.

## PARTNERSHIPS

Where a civil penalty provision is contravened by a reporting entity that is a partnership the provision is taken to have been contravened by each partner.

It follows that a pecuniary penalty order can be made against individual partners and enforced against their individual assets. However, a partner may avoid liability if they establish that they:

- did not know of the circumstances that caused the contravention; or
- did know but took all reasonable steps to correct it as soon as possible after learning of those circumstances.

3. Chapter 8 of the Draft AML/CTF Rules (released with the 2nd Draft Exposure Bill in July 2006) requires that boards and senior management must approve and have ongoing oversight of a reporting entity's AML/CTF program. However the requirement in the Bill to adopt and maintain an AML/CTF program is imposed on the reporting entity and can only be contravened by the reporting entity and not the individual directors.

## TRUSTS

Where the reporting entity is a trust with one trustee the obligation is imposed on that trustee and the trustee will be liable for any pecuniary penalty order. Where the trust has multiple trustees, the obligation is imposed on each trustee and any contravention will be taken to have been contravened by each trustee.

This has significant implications for directors of corporate trustees who must personally discharge a liability of the trustee if the trust itself cannot meet the liability (and is not entitled, in certain circumstances specified in the Corporations Act, to be indemnified against the liability out of trust assets).<sup>4</sup>

A trustee will not be taken to have contravened a civil penalty provision if it establishes that it:

- did not know of the circumstances that caused the contravention; or
- did know but took all reasonable steps to correct it as soon as possible after learning of those circumstances.

## UNINCORPORATED ASSOCIATIONS

Where a civil penalty provision is contravened by a reporting entity that is an unincorporated association the contravention is taken to have been committed by each member of the association's committee of management. However, this will not be the case if a member establishes that it:

- did not know of the circumstances that caused the contravention; or
- did know but took all reasonable steps to correct it as soon as possible after learning of those circumstances.

## INDIVIDUALS

Where a reporting entity which is an individual (eg a sole proprietor stockbroker or an Australian Financial Services Licence holder providing an item 54 designated service) breaches a civil penalty provision that individual will be responsible for the contravention and will be personally liable for any pecuniary penalty imposed.

An individual who is an employee of a reporting entity cannot contravene a civil penalty provision as the obligation is imposed on the reporting entity. There is no provision in the Act extending that obligation to individual employees of a reporting entity. This means that staff (eg front line staff who fail to make a suspicious

matter report) cannot contravene a civil penalty provision (except as an ancillary – see below) and cannot be subject to a pecuniary penalty order.

## THE MONEY LAUNDERING COMPLIANCE OFFICER

It is significant to note that although the Draft AML/CTF Rules<sup>5</sup> require a reporting entity to appoint a money laundering compliance officer (**MLRO**), the Act does not extend any specific obligations or liability to that officer. It follows therefore that an MLRO cannot (except as an ancillary) contravene a civil penalty provision or be subject to a pecuniary penalty order.

## ANCILLARY CONTRAVENTIONS

Section 174 of the Act extends liability for contraventions of civil penalty provisions to persons other than reporting entities. These ancillary contraventions (similar to those in the *Criminal Code Act 1995* (Cth)) mean that that any person (natural or legal) who:

- attempts to breach a civil penalty provision;
- aids, abets, counsels, procures such a breach;
- induces such a breach;
- is knowingly concerned in such a breach; or
- conspires to effect such a breach,

will itself be in breach of the Act and liable for a pecuniary penalty. This would catch individuals who are not themselves reporting entities but who have been instrumental in a contravention (eg a senior manager who decides, without justification, not to make a suspicious matter report, or a director of a responsible entity who instructs that designated services be provided knowing that the entity's AML/CTF program is inadequate).

## AUSTRAC'S ENFORCEMENT POLICY

Civil penalty regimes are not new to the financial services sector. Other regulators, including the Australian Securities and Investments Commission (**ASIC**) and the Australian Competition and Consumer Commission (**ACCC**), can institute proceedings for breach of civil penalty provisions and have been successful in obtaining court orders for substantial pecuniary penalties.

4. Section 197(1) of the Corporations Act.

5. Released with the 2nd Draft Exposure Bill in July 2006.

To date, AUSTRAC has favoured a cooperative approach to enforcement.<sup>6</sup> It will be interesting to see if it continues to apply this approach in the light of its expanded enforcement powers.

Other regulators tend to use the civil penalty provisions as a last resort. The ACCC approach has been described<sup>7</sup> as an 'enforcement pyramid' comprising:

- education advice and persuasion at the bottom of the pyramid;
- voluntary compliance initiatives at the next level;
- followed by a more interventionist approach using enforceable undertakings; and
- then civil penalties if an effective settlement cannot be negotiated.

A similar conciliatory approach is adopted in other jurisdictions. The UK Financial Services Authority (*FSA*), has said<sup>8</sup> that if a firm demonstrates that it has put in place an effective system of controls that identifies and mitigates its money laundering risks then enforcement action is unlikely. However, it is likely where a firm has not taken adequate steps to identify its money laundering risk, not put in appropriate controls to mitigate those risks and failed to take steps to ensure those controls are being effectively managed.

## DECIDING AN APPROPRIATE PENALTY

Section 175 (3) of the Act provides that, in deciding what will be an appropriate penalty, a court must take into account all relevant criteria, including:

- the nature and extent of the contravention;
- the nature and extent of any loss suffered as a result of the contravention;
- the circumstances in which the contravention took place; and

- whether the person has been found:
  - by a federal, state or foreign court to have engaged in similar conduct; or
  - by a court in proceedings under the *Financial Transaction Reports Act 1988* (Cth) to have engaged in similar conduct.

Similar criteria are found in other federal legislation<sup>9</sup> and have been applied in a number of cases.

In *Trade Practices Commission v CSR Limited* [1991] ATPR 41-076, the court set out a checklist of matters which it<sup>10</sup> regarded as appropriate to take into account in proceedings for pecuniary penalties. Apart from those listed above, these matters included:

- the size of the contravening company;
- the degree of power it has, evidenced by its market share and ease of entry into the market;
- the deliberateness of the contravention and the period over which it extended;
- whether the contravention arose out of the conduct of senior management or at a lower level;
- whether the company had a corporate culture conducive to compliance with the Trade Practices Act as evidenced by educational programs and disciplinary or other corrective measures in response to an acknowledged contravention; and
- whether the company in question had shown a disposition to cooperate with the regulatory authority.

Other criteria include the financial position of the contravening corporation and the deterrent effect of the proposed penalty, both specifically for the contravener and generally.

Not all of these principles can be transferred directly into the AML/CTF context. The degree of market share, for example, is not likely to be relevant to the imposition of a penalty under the AML/CTF regime, but the issue of corporate culture and management's role will be highly relevant.

---

6. In his foreword to the AUSTRAC *2005-2006 Annual Report*, the Director of AUSTRAC commented that 'AUSTRAC's principal regulatory philosophy of co-operation and facilitation will continue ... However, in cases where serious non-compliance is detected AUSTRAC will seek to take appropriate enforcement action.'

7. In a speech by Louise Sylvan of the ACCC to the Trade Practices and Competition Law Conference 16 February 2004.

8. In a letter from Philip Robinson of the FSA to the Joint Money Laundering Steering Group dated 25 October 2004.

---

9. Section 1317G of the Corporations Law, section 76(1) of the *Trade Practices Act 1974* (Cth) and section 481(2) of the *Environment Protection and Biodiversity Act 1999* (Cth) are examples.

10. The check list has been cited in subsequent decisions.

The Australian courts have not been adverse to imposing substantial penalties against businesses that breach civil penalty provisions. The ACCC has recently been successful in obtaining multi-million dollar penalties<sup>11</sup> and in October 2006 the Federal Court imposed penalties of \$5.5 million for contraventions of the *Spam Act 2003* (Cth).<sup>12</sup>

## ENFORCEMENT OVERSEAS

The high maximum penalty level introduced by the Act is intended to reflect penalties imposed under the US AML/CTF regime.<sup>13</sup> Substantial penalties are common in the US and other jurisdictions and relate often to AML/CTF compliance failures rather than instances of actual money laundering.

Recent overseas penalties for AML/CTF breaches have included:

- in the US:
  - in September 2006 a settlement agreement in the amount of US\$7.5 million between Bank of America Corporation (**BAC**) and the Manhattan District Attorney stemming

11. In January 2006 the Federal Court handed down penalties totalling \$8.9 million on Australian Safeway Stores Pty Ltd in proceedings relating to misuse of market power. In May 2002 penalties totalling approximately \$15 million were ordered against Schneider Electric and others (Schneider's penalty of \$7 million was reduced on appeal to \$5.5 million). In April 2004 penalties of \$14 million were ordered against APP Power Transmission Pty (in liquidation) and ABB Transmission and Distributions Ltd.

12. *Australian Communications and Media Authority v Clarity1 Pty Ltd* (2006) FCA 1399 (27 October 2006).

13. According to a paper *Summary of the Main Difference between the Revised Exposure Draft Bill 2006 and the Introduction Bill* issued by the Attorney General's Department.

from BAC's deficiencies in handling foreign money service business clients and AML controls; and

- in December 2005 ABN AMRO agreed to pay US\$80 million in fines and penalties for various defects, including AML internal controls and failures to identify, analyse, and report suspicious activity;
- in the UK:
  - in 2005 the FSA imposed financial penalties of £175,000 on Investment Services UK Limited and £30,000 on its managing director; and
  - in 2004 it imposed fines of £1,250,000 and £375,000 on the Bank of Scotland and Bank of Ireland respectively.
- in Japan:
  - in September 2004 the Japanese financial authorities ordered Citibank NA Japan to suspend its private banking operations for a number of violations including some relating to anti-money laundering.

## CONCLUSION

Although AUSTRAC has indicated that it intends to work in cooperation with the financial services sector to implement and regulate the new AML/CTF regime, there is no reason to doubt they will take enforcement action if they consider a serious contravention has occurred and there is also no reason to suggest that the courts will hesitate to impose significant pecuniary penalties.

The Act and explanatory material can be found at <http://www.ag.gov.au/aml>.

If your business operates in the financial services sector you need to assess your AML/CTF risk and start planning now for compliance with the Act. AAR's team of AML experts will provide you with clear advice on the Act and its ramifications for your business.

## CONTACTS

**Peter Jones**  
Partner, Sydney  
Ph: +61 2 9230 4987  
[Peter.Jones@aar.com.au](mailto:Peter.Jones@aar.com.au)

**Catherine Parr**  
Partner, Sydney  
Ph: +61 2 9230 4994  
[Catherine.Parr@aar.com.au](mailto:Catherine.Parr@aar.com.au)

**Anna Lenahan**  
Partner, Sydney  
Ph: +61 2 9230 4132  
[Anna.Lenahan@aar.com.au](mailto:Anna.Lenahan@aar.com.au)

**Judy Maguire**  
Senior Associate, Sydney  
Ph: +61 2 9230 4835  
[Judy.Maguire@aar.com.au](mailto:Judy.Maguire@aar.com.au)

**Craig Phillips**  
Partner, Melbourne  
Ph: +61 3 9613 8938  
[Craig.Phillips@aar.com.au](mailto:Craig.Phillips@aar.com.au)

**Stephen Spargo**  
Partner, Melbourne  
Ph: +61 3 9613 8861  
[Stephen.Spargo@aar.com.au](mailto:Stephen.Spargo@aar.com.au)

**John Beckinsale**  
Partner, Brisbane  
Ph: +61 7 3334 3520  
[John.Beckinsale@aar.com.au](mailto:John.Beckinsale@aar.com.au)

**Steven Cole**  
Partner, Perth  
Ph: +61 8 9488 3743  
[Steven.Cole@aar.com.au](mailto:Steven.Cole@aar.com.au)

*Have your details changed?*

*If your details have changed or you would like to subscribe or unsubscribe to this publication or others, please go to [www.aar.com.au/general/subscribe.htm](http://www.aar.com.au/general/subscribe.htm) or email [Publications@aar.com.au](mailto:Publications@aar.com.au)*



Bangkok  
Beijing  
Brisbane  
Hong Kong  
Jakarta  
Melbourne  
Perth  
Phnom Penh  
Port Moresby  
Shanghai  
Singapore  
Sydney