

EXPLANATORY STATEMENT

Issued by authority of the AUSTRAC CEO

Anti-Money Laundering and Counter-Terrorism Financing Act 2006

*Anti-Money Laundering and Counter-Terrorism Financing Rules Amendment
Instrument 2021 (No. 2)*

AUTHORITY

Section 229 of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (**AML/CTF Act**) provides that the AUSTRAC CEO may, by legislative instrument, make Anti-Money Laundering and Counter-Terrorism Financing Rules (**AML/CTF Rules**). The AML/CTF Rules are set out in the *Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No. 1)*.

PURPOSE AND OPERATION OF THE INSTRUMENT

The *Anti-Money Laundering and Counter-Terrorism Financing Rules Amendment Instrument 2021 (No. 2)* (the **Amendment Instrument**) is a legislative instrument for the purposes of the *Legislation Act 2003*.

Details of the Amendment Instrument are set out in [Attachment A](#).

A Statement of Compatibility with Human Rights (the **Statement**) is at [Attachment B](#). The Statement has been completed in accordance with the *Human Rights (Parliamentary Scrutiny) Act 2011*. The overall assessment is that the Amendment Instrument promotes the realisation of human rights, and as such, is compatible with them.

Background

1. Litigation funders partly or wholly fund the costs of litigation in return for a portion of the proceeds if the action is successful. A litigation funding scheme is an arrangement where a group of plaintiffs, a law firm and a litigation funder collaborate to pursue a class action. Since 2009, this type of arrangement has been understood to constitute a managed investment scheme (MIS).
2. Until 2020, the *Corporations Regulations 2001* (**Corporations Regulations**) specified that:
 - a person providing financial services for litigation funding schemes was exempt from the requirement to hold an Australian Financial Services Licence (AFSL) (if they maintain and apply adequate practices for managing conflicts of interest), and
 - litigation funding schemes were exempt from being a MIS or a credit facility.
3. Amendments to the Corporations Regulations have removed these exemptions. Consequently, most litigation funding schemes entered into on or after 22 August 2020 must be registered as MISs under the *Corporations Act 2001* (**Corporations Act**).

4. As a MIS, the issuing of an interest in a litigation funding scheme is a designated service for the purposes of Item 35 of Table 1 in subsection 6(2) of the AML/CTF Act (issuing or selling a security or derivative).
5. The regulation of litigation funding schemes under the AML/CTF framework is an unintended consequence of changes made to the Corporations Regulations 2001 in 2020. The purpose of the amendments to the Corporations Regulations was to give effect to the Government's announcement on 22 May 2020 that litigation funders would be required to hold an AFSL and comply with the managed investment scheme regime, generally requiring the scheme to be registered with ASIC.
6. The ML/TF risks associated with the provision of services to general members of a litigation funding scheme is low (negligible). General members, who are usually individuals who are party to a class-action suit, are issued a share in the litigation fund scheme at a price of \$nil. General members also do not receive any money directly from the litigation funding scheme, which exists only to fund the legal proceedings. General members are paid a share of the resolution sum (less legal fees and the share owed to the funder) directly by the defendant of the litigation proceedings.
7. Section 247(3) of the AML/CTF Act allows the AML/CTF Rules to specify circumstances in which the AML/CTF Act does not apply to the provision of a designated service. Chapter 21 currently specifies four circumstances in which the issue or sale of securities or derivatives, which includes interests in managed investment schemes, are exempt from the operation of the AML/CTF Act.
8. The Amendment Instrument amends Chapter 21 of the AML/CTF Rules to exempt the issuing of an interest in a litigation funding scheme from the operation of the AML/CTF Act when the person issuing the interest holds an AFSL and the litigation funding scheme is either registered with the Australian Securities and Investments Commission or under subsection 601ED(2) of the Corporations Act, not required to be registered.
9. For the purposes of the AML/CTF Rules, 'litigation funding scheme' has the meaning given by regulation 7.1.04N(3) of the Corporations Regulations.

CONSULTATION

10. Draft AML/CTF Rules were released on 30 July 2021 for a four-week period of public consultation. Ongoing consultation with industry was undertaken following the public consultation period.

REGULATION IMPACT STATEMENT

11. The Office of Best Practice and Regulation has advised that a Regulatory Impact Statement (**RIS**) is not required as the amendments to the AML/CTF Rules do not have a regulatory impact.

Anti-Money Laundering and Counter-Terrorism Financing Rules Amendment Instrument 2021 (No. 2)

Section 1—Name

This section provides that the name of the Instrument is the *Anti-Money Laundering and Counter-Terrorism Financing Rules Amendment Instrument 2021 (No. 2)*.

Section 2—Commencement

This section provides for the commencement of each provision in the Instrument, as set out in the table in subsection 2(1).

The amendments in Schedule 1 commence on the day after registration.

Section 3—Authority

This section provides that the Instrument is made under section 229 of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006*.

Section 4—Schedules

This section provides that the instrument specified in Schedule 1 is amended as set out in the applicable items in that Schedule.

Schedule 1—Amendments

Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No. 2)

Notes on items

Item 1—Chapter 21

This item inserts a new paragraph 21.3(5) of the AML/CTF Rules.

Paragraph 21.3(5) specifies the conditions that must be met so an issue of an interest in a litigation funding scheme is exempt from the operation of the AML/CTF Act.

Item 2—Chapter 21

This item inserts a new paragraph 21.4(4A) of the AML/CTF Rules.

Paragraph 21.4(4A) specifies the term litigation funding scheme has the meaning given by Regulation 7.1.04N(3) of the *Corporations Regulations 2001*.

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

Australian Human Rights Commission Regulations 2019

This Disallowable Legislative Instrument (the **Instrument**) is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Instrument

The Instrument amends the *Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No. 1)* to exempt the issue of an interest in a litigation funding scheme from the operation of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (AML/CTF Act)* on the basis that these services present a low risk of money laundering and terrorist financing.

Human rights implications

The *Human Rights (Parliamentary Scrutiny) Act 2011* requires that Statements of Compatibility must be made by the rule-maker with regard to disallowable legislative instruments, and must contain an assessment of whether the legislative instrument is compatible with the rights and freedoms recognised in the seven core international human rights treaties that Australia has ratified.

The Instrument engages the right to privacy in Article 17 of the International Covenant on Civil and Political Rights (**ICCPR**) by excluding customers of litigation funding schemes from the customer due diligence, record keeping and reporting obligations of the AML/CTF Act.

Article 17 of the ICCPR provides that no one shall be subjected to arbitrary or unlawful interference with their privacy, family, home or correspondence. The use of the term ‘arbitrary’ means that any interference with privacy must be in accordance with the provisions, aims and objectives of the ICCPR and should be reasonable in the particular circumstances. The United Nations Human Rights Committee has interpreted ‘reasonableness’ to imply that any limitation must be proportionate and necessary in the circumstances. The right to privacy can be limited by necessity in a democratic society in the interests of national security or public order.

As a result of the amendments, customers of litigation funding schemes will no longer be required to undergo an applicable customer identification procedure under the

AML/CTF Act. In doing so, the amendments preserve the right to privacy by ensuring that personal information is only collected when a designated service, that is not the subject of an exemption, is being provided. This ensures that the required collection of personal information under the AML/CTF Act remains reasonable, necessary and proportionate.

Conclusion

The Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in the definition of ‘human rights’ in subsection 3(1) of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

[signed]
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