

PROTECTING THE WEST, EXCLUDING THE REST: THE IMPACT OF THE AML/CTF REGIME ON FINANCIAL INCLUSION IN THE PACIFIC AND POTENTIAL RESPONSES

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Financial inclusion is an important international policy goal. Remittances promote financial inclusion by contributing almost half a trillion dollars to the economies of developing countries each year and by giving people a strong reason to engage with formal financial services. In the Pacific, remittances represent a significant proportion of many countries' GDPs. The G20 has committed to reducing the global average cost of sending remittances to 5 per cent. At the same time, financial service providers are facing increasingly onerous regulatory requirements to combat the global rise in money laundering and terrorism financing. In Australia, these requirements have led to the bank account closures of many money transfer operators, posing a real risk to financial inclusion, growth and stability in the Pacific. This paper examines the G20's goals for financial inclusion, the role of remittances in achieving these goals for the Pacific region, and the impact of anti-money laundering and counter-terror financing ('AML/CTF') regulations on the Australian remittance industry. A number of solutions are proposed to address the challenges facing the remittance industry in Australia, including the adoption of risk-based regulatory measures such as limiting transfer sums, digitising payments and encouraging greater use of technological innovation to reduce risks.

CONTENTS

I	Introduction.....	2
II	Financial Inclusion and the Work of the G20.....	4
	A The Importance of Financial Inclusion.....	4
	B The G20's Goals.....	5
	C The Role of Remittances	6
III	The Situation in the Pacific.....	8
IV	AML/CTF and the Threat to Financial Inclusion	11
	A International AML/CTF Measures	11
	B Domestic AML/CTF Measures	13
	C The Impact of AML/CTF Measures on the Remittance Industry.....	15
V	Possible Solutions	18
	A Risk-Based Regulation	18
	B Limiting Transfer Sums to Manage Risk.....	20
	C Digitising Payments.....	20

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D Technological Innovation.....	22
VI Conclusion.....	23

I INTRODUCTION

Financial inclusion involves the delivery of financial services at affordable costs to all sections of society.¹ It is increasingly being seen as a significant international policy goal.² The commitment of the Group of Twenty ('G20') to creating a more inclusive global financial system recognises that financial inclusion not only promotes development and reduces poverty, but enhances financial stability and financial integrity as well.³ At the Brisbane Summit in November 2014, the G20 adopted the 2014 Financial Inclusion Action Plan ('FIAP'), which highlights ten action areas considered to be key to the advancement of financial inclusion over the next five years.⁴ One such goal is to reduce the cost of sending remittances.⁵ The G20 affirmed this goal in the High-Level Statement on Remittances, approved at the Antalya Summit in November 2015.⁶

More than 250 million people live outside their country of birth and many migrants choose to send money back to their home country.⁷ These payments are called remittances. The remittance industry plays an important role in furthering financial inclusion because remittances through formal channels require recipients to engage with the financial system and provide them with the means to do so. The amount of money migrants transfer back to developing countries is more than three times the size of official development assistance and, excluding investments made by China, significantly exceeded foreign direct investment flows to developing countries in 2013.⁸ In some developing countries,

¹ Financial Action Task Force, 'FATF Guidance: Anti-Money Laundering and Terrorist Financing Measures and Financial Inclusion' (Report, February 2013) 12 <<https://perma.cc/RN8Y-98Q9>>.

² Financial inclusion has been identified as a key goal of many international organisations, including the Group of Twenty ('G20') and Financial Action Task Force ('FATF'). In April 2015, central bank governors and finance ministers from more than 30 countries across the Group of Twenty-Four ('G24') and Alliance for Financial Inclusion ('AFI') Networks, together with stakeholders such as the International Monetary Fund ('IMF'), World Bank, Financial Stability Board ('FSB'), the Bank for International Settlements, British Bankers' Association ('BBA'), United States Treasury and International Association of Deposit Insurers ('IADI') all met to discuss financial inclusion at the seventh annual G24/AFI Policymakers' Roundtable: Alliance for Financial Inclusion, *G-24/AFI Policymakers Discuss Financial Inclusion and Global Standards: Opportunities and Risks* (30 April 2015) <<https://perma.cc/C63A-MU3V>>.

³ G20, *Financial Inclusion Action Plan* (2010) Global Partnership for Financial Inclusion, 2 <<https://perma.cc/B3K5-YW2T>>.

⁴ G20, *Brisbane Summit: G20 Leaders' Communiqué* (15–16 November 2014) <<https://perma.cc/8FW8-DU6E>>; G20, *2014 Financial Inclusion Action Plan* (2 September 2014) 2 <<https://perma.cc/X46T-UNZF>>.

⁵ G20, *2014 Financial Inclusion Action Plan*, above n 4, 2.

⁶ G20, *High-Level Statement on Remittances* (2015) <<https://perma.cc/P9XQ-Y9A9>>.

⁷ Dilip Ratha et al, 'Migration and Remittances: Recent Developments and Outlook Special Topic — Financing for Development' (Migration and Development Brief No 24, Migration and Remittances Team, World Bank, 13 April 2015).

⁸ Dilip Ratha et al, 'Migration and Remittances: Recent Developments and Outlook Special Topic — Forced Migration' (Migration and Development Brief No 23, Migration and Remittances Team, Development Prospects Group, 6 October 2014) 3.

remittances represent a significant proportion of the country's gross domestic product ('GDP').⁹

In theory, the G20's efforts to advance financial inclusion complement the G20's goal of strengthening the integrity of the global financial system. Expanding access to the formal financial system increases the reach and effectiveness of measures introduced to safeguard the system.¹⁰ However, measures introduced globally to achieve the latter goal are in fact hindering fulfilment of the former. In recent times, large-scale money laundering scandals and the rise of well-financed extremist organisations have highlighted the need to strengthen measures protecting the financial system from abuse.¹¹ Governments worldwide have introduced stringent compliance processes to curb money laundering and the funding of terrorism. Such processes pose a major challenge to the remittance industry worldwide even when the remittances represent scrupulously 'clean' money.

The United States has been the driving force behind the introduction of anti-money laundering and counter-terror financing ('AML/CTF') measures globally.¹² While such measures may be necessary to address problems affecting developed economies, they have unintended and far-reaching consequences that threaten financial inclusion in the developing world. In Australia, compliance with strengthened AML/CTF legislation has led to the bank account closures of many money transfer operators ('MTOs') operating in the Pacific region.¹³ Yet these MTOs do not pose the type of risk that prompted the regulatory push from abroad.

Remittances play a vital role in the Pacific region. In Samoa they are the single most important source of external income, accounting for a fifth of the country's GDP.¹⁴ In Fiji, remittances are the second largest foreign exchange earner after tourism.¹⁵ Studies have found that the impact of remittances extends far beyond the direct recipients and contributes significantly to the alleviation of

⁹ For example, in 2013 remittances represented 49 per cent of Tajikistan's GDP, 32 per cent of the Kyrgyz Republic's GDP, 29 per cent of the GDP of Nepal and 25 per cent of the GDP of Moldova: Ratha et al, 'Financing for Development', above n 7, 5.

¹⁰ Hennie Bester et al, *Implementing FATF Standards in Developing Countries and Financial Inclusion: Findings and Guidelines* (Genesis Analytics, 2008) vi.

¹¹ In the case of HSBC, see Permanent Subcommittee on Investigations, Homeland Security and Government Affairs, 'HSBC Exposed US Financial System to Money Laundering, Drug, Terrorist Financing Risks' (Media Release, United States Senate, 16 July 2012) <<https://perma.cc/NH4D-N43V>>.

¹² This is the case because almost 90 per cent of global foreign exchange transactions involve the US dollar and the majority of these transactions pass through two clearing networks in the US. Under the *Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act* ('USA PATRIOT Act') of 2001, a federal law, all US financial institutions are required to obtain, verify and record information that identifies each person and each legal entity that opens an account. As such, foreign banks are required to comply with US AML/CTF measures in order to clear funds for their customers. See Yalman Onaran, 'Dollar Dominance Intact as US Fines on Banks Raise Ire', *Bloomberg Business* (online), 16 July 2014 <<https://perma.cc/CQ23-DRVG>>.

¹³ Jonathan Capal, 'What Next for Remittances and Money Transfers in the Pacific?' on *Consultative Group to Assist the Poor* (12 June 2014) <<https://perma.cc/UU26-YPE4>>.

¹⁴ Jeannette Francis, 'Remittances Keep Post-Disaster Economies Afloat', *SBS News* (online), 24 December 2012 <<https://perma.cc/D6N3-EXZT>>; Ratha et al, 'Financing for Development', above n 7, 5.

¹⁵ Jeannette Francis, above n 14.

poverty across communities.¹⁶ The impact of AML/CTF measures on the flow of remittances to the Pacific is thus an important social justice issue.

This article seeks to examine the challenge to financial inclusion in the Pacific posed by stricter AML/CTF requirements, and explore possible solutions. The paper has six sections. Following this introduction we outline the G20's goals for improving financial inclusion worldwide and highlight the importance of remittances to achieving this aim. The third section focuses on the Pacific, examining the remittance industry in Australia and the contribution it makes to financial inclusion in the region. The article then analyses the international and domestic AML/CTF regulatory frameworks and discusses the compliance pressures faced by banks. The fifth section explores some of the creative solutions to the challenges facing financial inclusion in the Pacific and the sixth section concludes.

II FINANCIAL INCLUSION AND THE WORK OF THE G20

A *The Importance of Financial Inclusion*

Almost half of the world's adult population — approximately two billion people — do not have access to a formal bank account.¹⁷ The majority of these people are concentrated in developing economies, where banks are often physically inaccessible to parts of the population.¹⁸ One of the greatest barriers to financial inclusion is also affordability.¹⁹ Worldwide, reducing the costs associated with formal banking could enable more than 500 million adults presently without bank accounts to enter the formal financial system.²⁰

Inclusion in the global financial system is fundamental for improving the livelihoods of the poor. Providing people in developing countries with access to financial services such as credit, savings, insurance and payments assists them to manage their financial obligations and build better futures for their families.²¹ The immediate effect of access to finance is that it can help people pay for essential services such as clean water, electricity and housing without taking time off from work to physically pay the bills.²² Longer term, it provides people with

¹⁶ Richard Brown et al, 'Cents and Sensibility: The Economic Benefits of Remittances' in *Pacific Islands at Home and Away: Expanding Job Opportunities for Pacific Islanders through Labor Mobility* (World Bank, 2006) 42, cited in Richard Brown, Gareth Leeves and Prabha Prayaga, 'An Analysis of Recent Survey Data on the Remittances of Pacific Island Migrants in Australia' (Discussion Paper No 457, School of Economics, University of Queensland, 2012) 2.

¹⁷ World Bank, 'Global Financial Development Report 2014: Financial Inclusion' (World Bank, 2014) 2.

¹⁸ Financial Action Task Force, 'FATF Guidance', above n 1, 12.

¹⁹ The expense associated with bank accounts is the second most commonly cited reason globally for not having a bank account. The first most commonly cited reason is a lack of funds: Asli Demirguc-Kunt and Leora Klapper, 'Measuring Financial Inclusion' (Policy Research Working Paper No 6025, World Bank, Development Research Group, Finance and Private Sector Development Team, April 2012) 19.

²⁰ *Ibid* 4.

²¹ Center for Financial Inclusion, *About Financial Inclusion 2020* <<https://perma.cc/P2TD-F95Q>>.

²² World Bank, 'Universal Financial Access Is Vital to Reducing Poverty, Innovation Key to Overcoming the Enormous Challenge, Says President Jim Yong Kim' (Press Release, 2014/132/FPD, 11 October 2013) <<https://perma.cc/RD76-DDD7>>.

a means to save for and invest in their education and health, as well as their own businesses — providing the opportunity to rise out of poverty.²³ Financial inclusion can also allow the poor to insure against unfavourable events to avoid falling deeper into poverty should such an incident occur.²⁴

B *The G20's Goals*

The recent global financial crisis prompted a wide and sweeping range of regulatory responses overseen by the G20.²⁵ The aim of the response has been to build a stable and resilient global financial system that promotes confidence and growth.²⁶ However, the reforms have been based predominantly on the highly developed financial systems of the Northern Hemisphere.

The widespread exclusion of people from the formal financial system in developing countries increases inequality, creates economic distortions and slows economic growth and development.²⁷ Recognising this has driven the G20 to focus on bringing the world's unbanked population into the financial system through a number of measures aimed at advancing financial inclusion.

At the Pittsburgh Summit in September 2009, G20 leaders made a commitment to improve access to financial services for the poor.²⁸ This included establishing the Financial Inclusion Experts Group ('FIEG'), which developed nine principles for innovative financial inclusion that were endorsed by the G20 during the Toronto Summit in June 2010.²⁹ FIEG also recommended the creation of the Global Partnership for Financial Inclusion ('GPMI') to carry forward the G20's commitments on financial inclusion and to maximise the impact of the G20's work through broad stakeholder participation.³⁰

The GPMI was established at the Seoul Summit in November 2010.³¹ At the same time, G20 leaders endorsed the first Financial Inclusion Action Plan.³² In doing so, the G20 recognised that financial inclusion for individuals and organisations should be a key feature of the global growth and development agendas.³³

The G20 made significant progress towards improving financial inclusion during the first three years of the FIAP's implementation. Between 2011 and

²³ Ibid.

²⁴ Christine Lagarde, 'Empowerment through Financial Inclusion' (Speech delivered at the International Forum for Financial Inclusion, Mexico, 26 June 2014) <<https://perma.cc/Z3GE-RSLL>>.

²⁵ See generally Ross P Buckley, 'The G20's Performance in Global Financial Regulation' (2014) 37 *University of New South Wales Law Journal* 63; Kevin Davis, 'Regulatory Reform post the Global Financial Crisis: An Overview' (Report, Melbourne APEC Finance Centre, RMIT University, March 2011) 2 <<https://perma.cc/33AH-CBCX>>.

²⁶ G20, *2014 Financial Inclusion Action Plan*, above n 4, 3.

²⁷ Ibid.

²⁸ G20, *Pittsburgh Summit: Leaders' Statement* (25 September 2009) [41] <<https://perma.cc/UR9K-K533>>.

²⁹ G20 Financial Inclusion Experts Group, 'Innovative Financial Inclusion' (Report, 25 May 2010) <<https://perma.cc/7STW-4H6F>>.

³⁰ G20, *Financial Inclusion Action Plan*, above n 3, 3.

³¹ Alliance for Financial Inclusion, *G20 Principles for Innovative Financial Inclusion* (April 2011) Global Partnership for Financial Inclusion, 7 <<https://perma.cc/GMY2-XWUL>>.

³² G20, *2014 Financial Inclusion Action Plan*, above n 4, 3.

³³ Ibid.

2014, approximately 700 million formerly financially excluded people gained access to financial services, either through bank accounts or mobile money services.³⁴ A review of the GPMI's progress in implementing the original FIAP shows that many of its objectives have been achieved.³⁵ While 'financial inclusion' was a relatively new concept five years ago, the work of the G20 has prompted policymakers worldwide to commit to creating a more inclusive global financial system.

Despite these achievements, substantial work is still required to assist the 2 billion people and over 200 million businesses that remain excluded from the formal financial system. In 2014, the GPMI was tasked with reviewing and updating the FIAP to ensure further progress is made.³⁶

The G20 leaders endorsed the updated FIAP at the Brisbane Summit in November 2014.³⁷ The latest version of the FIAP includes ten action areas which members of the GPMI consider crucial to advancing financial inclusion over the next five years.³⁸ Three of these action items relate specifically to international payment systems:

- 8 Help to analyse and consider ways to address the MTO bank account closure issue
- 9 Reduce the cost of sending remittances
- 10 Expand opportunities for innovative technologies to grow responsible financial inclusion.³⁹

These new FIAP goals recognise that remittances provide an important avenue towards greater financial inclusion.⁴⁰

C The Role of Remittances

Money sent back by migrants assists those in some of the poorest parts of the world to pay for basic needs such as food and shelter, and contributes to poverty alleviation through providing the financial means to access health and education.⁴¹ Remittances also act as a form of insurance for the poor, particularly in times of conflict, political instability or natural disasters.⁴² In Vanuatu, 93 per cent of households reported that remittances were an important part of the recovery following Cyclone Pam in 2015.⁴³ Remittance flows tend to increase

³⁴ The substantial increase in the number of financially included people is not due solely to the actions of the G20, as a trend towards greater use of mobile money was already occurring independently of the G20. Nevertheless, the G20's action plan has made a significant contribution towards promoting financial inclusion: World Bank, 'Massive Drop in Number of Unbanked, Says New Report' (Press Release, 2015/364/DEC, 15 April 2015) <<https://perma.cc/PZ3J-B2NZ>>.

³⁵ G20, *2014 Financial Inclusion Action Plan*, above n 4, annex 2, 14–20.

³⁶ *Ibid* 1 (Executive Summary).

³⁷ G20, *Brisbane Summit: G20 Leaders' Communiqué*, above n 4, 4.

³⁸ G20, *2014 Financial Inclusion Action Plan*, above n 4, 2.

³⁹ *Ibid*.

⁴⁰ G20, *G20 Plan to Facilitate Remittance Flow* (September 2014) Global Partnership for Financial Inclusion, 2–3 <<https://perma.cc/3HLS-GG2M>>.

⁴¹ See generally Global Partnership for Financial Inclusion, 'The Use of Remittances and Financial Inclusion' (Report, September 2015) <<https://perma.cc/JRS6-MRJF>>.

⁴² Ratha et al, 'Financing for Development', above n 7, 5.

⁴³ Shelter Cluster, 'Shelter and Settlements Vulnerability Assessment — Final Report: Cyclone Pam Response' (Report, May 2015) 37 <<https://perma.cc/A28E-AKAS>>.

during times of need.⁴⁴ For example, during the ten days after Cyclone Evan hit Samoa in 2012, the volume of incoming remittances increased by 92 per cent.⁴⁵ These remittance flows have a direct impact on the poor as they go directly to the people and communities who need them most rather than through governments and official agencies, as does development aid money.⁴⁶

Remittance flows to developing countries have increased exponentially in the past thirty years, from US\$22 billion in 1985–89 to an estimated US\$436 billion in 2014.⁴⁷ This figure is projected to grow to reach US\$479 billion by 2017.⁴⁸ Such statistics highlight the growing significance of remittances to aid and development worldwide.

Sending remittances is a costly business. In 2013, the global market cost of transferring money home was US\$37 billion — larger than the combined GDP of most Pacific Island nations.⁴⁹ Globally, migrants pay an average cost of 7.52 per cent to transfer money home.⁵⁰ This figure is down from 10 per cent in 2011.⁵¹ The World Bank estimates that this reduction has resulted in an additional US\$30 billion sent to developing countries from migrants in G20 countries.⁵² As part of its endorsement of the 2014 FIAP, the G20 made a recommitment to further reduce the global average cost of transferring remittances to five per cent.⁵³ During 2015, G20 member states developed National Remittance Plans outlining actions they would take to achieve the five per cent target.⁵⁴ Doing so would save migrants around US\$14 billion per year⁵⁵ — a sum that could make a significant contribution going directly to the intended recipients, rather than to financial intermediaries. Decreasing the cost of remittances is thus an important step for reducing poverty as well as promoting financial inclusion.

⁴⁴ Dilip Ratha, 'The Hidden Force in Global Economics: Sending Money Home' (Speech delivered at TEDGlobal 2014, Rio de Janeiro, October 2014) <<https://perma.cc/6Q26-DLHM>>.

⁴⁵ L Le De et al, 'Remittances in the Face of Disasters: A Case Study of Rural Samoa' (2015) 17 *Environment, Development and Sustainability* 653, 659.

⁴⁶ *Ibid* 657–8.

⁴⁷ T K Jayaraman, Chee-Keong Choong and Ronald Kumar, 'Role of Remittances in Small Pacific Island Economies: An Empirical Study of Fiji' (2011) 3 *International Journal of Economics and Business Research* 526, 527; Ratha et al, 'Financing for Development', above n 7, 3.

⁴⁸ Ratha et al, 'Financing for Development', above n 7, 3.

⁴⁹ Adolfo Brizzi, 'Trends in Global Remittances and Opportunities for Development' (Presentation, United Nations Conference on Trade and Development, Geneva, 20 June 2014) <<https://perma.cc/5DBK-P8H3>>.

⁵⁰ World Bank, 'Remittance Prices Worldwide' (Report, Issue No 15, October 2015) 2.

⁵¹ G20, *High-Level Statement on Remittances*, above n 6.

⁵² *Ibid*.

⁵³ G20, 'G20 Plan to Facilitate Remittance Flows', above n 40, 10.

⁵⁴ Global Partnership Financial Inclusion, *Financial Inclusion Features Prominently in Antalya G20 Communiqué* (18 November 2015) <<https://perma.cc/3MU8-9X6U>>.

⁵⁵ Ratha et al, 'Financing for Development', above n 7, 1.

III THE SITUATION IN THE PACIFIC

The Pacific is one of the least banked regions in the world.⁵⁶ The area is characterised by challenging physical geography, poor infrastructure, widespread poverty and a high proportion of people living a subsistence-based lifestyle.⁵⁷ It is estimated that in some Pacific Island countries ('PICs'), less than 10 per cent of the population has access to basic financial services.⁵⁸ The major barriers to financial inclusion include the physical accessibility of banks, low levels of financial competency and inexperience with using money.⁵⁹

In 2014, the Australian government restructured its aid program so that 90 per cent of all its aid funding is now directed to the Asia-Pacific.⁶⁰ This regional focus reflects the fact that many of Australia's neighbours are politically fragile developing countries whose instability affects Australia's national security.⁶¹ A key goal of Australia's foreign policy is now to 'promote prosperity, reduce poverty and enhance stability' within the Asia-Pacific.⁶² Encouraging financial inclusion is fundamental to achieving these aims.

For a long time Australia has encouraged migrant workers from the PICs through schemes such as the Seasonal Worker Program.⁶³ Within Australia, these migrants remit the highest percentage of their incomes home of any migrant groups in the country.⁶⁴ Payments sent by migrant workers are vital to the economic development and political stability of the PICs.⁶⁵ It is estimated that remittances account for almost a quarter of the GDP of Samoa and Tonga, the two most remittance-dependent countries in the region.⁶⁶

Sending remittances from Australia to the PICs is expensive.⁶⁷ Among G20 countries, Australia has the fourth highest average cost of sending remittances and is above the global average, which was 7.52 per cent in the third quarter of 2015.⁶⁸ Indeed, at the time of writing, the remittance corridor between Australia

⁵⁶ Pacific Financial Inclusion Programme, 'Achieving Financial Inclusion in the Pacific' (Fact Sheet) <<https://perma.cc/T629-7FRT>>.

⁵⁷ Ibid.

⁵⁸ Ibid.

⁵⁹ Ibid.

⁶⁰ Australian Government, Department of Foreign Affairs and Trade, 'Australian Aid: Promoting Prosperity, Reducing Poverty, Enhancing Stability' (Report, June 2014) 4.

⁶¹ Ibid.

⁶² Ibid 1.

⁶³ See Australian Government, Department of Immigration and Border Protection, *Special Program Visa (Subclass 416) for the Seasonal Worker Programme* <<https://perma.cc/4UQJ-KHS2>>.

⁶⁴ Francis, above n 14.

⁶⁵ T K Jayaraman, Chee-Keong Choong and Ronald Kumar, 'Role of Remittances in Small Pacific Island Economies: An Empirical Study of Fiji' (2011) 3 *International Journal of Economics and Business Research* 526, 530.

⁶⁶ World Bank, 'Remittances Growth to Slow Sharply in 2015, as Europe and Russia Stay Weak; Pick Up Expected Next Year' (Press Release, 2015/394/DEC, 13 April 2015) <<https://perma.cc/5YTV-ZZBS>>.

⁶⁷ Julie Bishop, 'Signing of Memorandum of Understanding with Westpac' (Speech delivered at Westpac Place, Sydney, 8 September 2014).

⁶⁸ World Bank, 'Remittance Prices Worldwide Issue No 15' above n 50, 2, 5.

and Vanuatu is the most expensive worldwide, costing migrants an average of 20.61 per cent to send money home.⁶⁹

Australian banks offer migrants two main ways to send money home: bank drafts and electronic transfers using the Society for Worldwide Interbank Financial Telecommunication ('SWIFT') network. Both methods involve fixed fees that are often disproportionate to the value of the remittance sought to be sent.⁷⁰ Additionally, these methods require both the sending and receiving parties to hold a bank account.⁷¹ This requirement is a significant barrier for many migrants wishing to send remittances to the PICs, given the high rate of financial exclusion in that region.

MTOs have traditionally provided migrants with an attractive alternative to the banks. Australia has 5500 registered MTOs, which make about 80 million money transfers each year.⁷² MTOs facilitate quick, inexpensive transfers of money overseas and do not usually require the sender or receiver to hold a bank account. MTOs operate through agents, who often run small businesses as well as handling money transfers. Generally an agent in one country collects the funds to be remitted and informs an agent in the receiver's country, who uses his or her own funds to distribute money to the receiver. At the end of the day, the agent in the home country deposits the collected funds in the MTO's bank account and the next day the MTO transfers this amount to the agent in the receiving country.

Using MTOs to send remittances saves migrants a lot of money. In September 2015, we conducted a comparison of the cost to send AU\$500 from Australia to Samoa using the SendMoneyPacific.org website. This comparison showed that MTOs charged less than half the amount charged by banks. Only two of the four major Australian banks offered remittance services, and both charged fees of more than 13 per cent of the amount transferred.⁷³ Remittances sent via these banks took three to five days to be transferred.⁷⁴ By contrast, four MTOs offered

⁶⁹ Cleoffe Maceda, 'Which Countries Are the Cheapest to Send Money to?', *Gulf News* (online), 8 April 2015 <<https://perma.cc/8YLC-NX34>>.

⁷⁰ The average transfer of money out of Australia is AU\$300 and banks generally charge flat rates of about AU\$30 in addition to any margin they already make on exchange rates: Anthony Klan, 'Industry Fights Back in "Terror" Cash Row', *The Australian* (Sydney), 19 November 2014, 25.

⁷¹ Justin Pritchard, *What is a Bank Draft?* (4 March 2016) About Money <<https://perma.cc/MN86-KP6L>>; Faith Davies, *What Is a SWIFT Money Transfer?*, eHow <<https://perma.cc/U58B-Y2AC>>.

⁷² James Eyers, 'Banks Pull Plug on Sending Money Overseas', *Australian Financial Review* (online), 14 February 2015 <<https://perma.cc/KPQ2-SZ9Z>>; Financial Action Task Force, 'Anti-Money Laundering and Counter-Terrorist Financing Measures: Australia Mutual Evaluation Report' (April 2015) 83 <<https://perma.cc/7TRS-PK7T>>.

⁷³ On 26 September 2015, the total cost for sending AU\$500 from an Australian bank account to a Samoan bank account was AU\$68.78 (13.76 per cent) at Westpac and AU\$84.48 (16.9 per cent) at ANZ. Remittance services were not offered by the Commonwealth Bank of Australia or National Australia Bank: see Send Money Pacific, *Comparison Results* (11 May 2016) <<https://perma.cc/CP24-CF5C>>. It should be noted that ANZ only charged AU\$19.37 (6.4 per cent) to transfer money using the ANZ Pacific Money Transfer Card. However, this required the recipient to have the card, which has an initial issue fee of AU\$24.95.

⁷⁴ See Send Money Pacific, *Comparison Results* (11 May 2016) <<https://perma.cc/CP24-CF5C>>.

same-day money transfers for fees of less than five per cent.⁷⁵ Three of these MTOs offered to transfer remittances in less than an hour.⁷⁶ Furthermore, recipients received the funds in cash so were not required to hold a bank account.⁷⁷

Given that the majority of people in the PICs do not hold a bank account,⁷⁸ the cash-to-cash transfer services offered by MTOs are vital. However, banks still play a key role when migrants use MTOs to send money home. While it is not necessary for those sending and receiving funds to have bank accounts, MTOs and their agents do need to hold accounts in order to facilitate the transfers.

The vast majority of registered remittance providers in Australia have traditionally held bank accounts with the big four banks.⁷⁹ This is no longer the case. Since 2010, these banks, along with Australian branches of foreign banks, have systematically closed the accounts of many MTOs and their agents.⁸⁰ Banks have also refused to open new accounts for MTOs wishing to be banked.⁸¹

This de-risking trend has dramatically increased in the past two years and poses a serious threat to the Australian remittance industry, and consequently to the promotion of financial inclusion in the PICs as well. In 2013, Developing Markets Associates found that nearly 75 per cent of surveyed MTOs operating in Australia had experienced account closures or received threats to close their accounts.⁸² According to the World Bank, seven MTOs went out of business in Australia in the first quarter of 2015.⁸³ It is unlikely to be a coincidence that the average cost of sending remittances from Australia has risen each quarter during the past year, increasing from an average of 8.88 per cent in the third quarter of 2014, to 9.24 per cent in the third quarter of 2015.⁸⁴ By contrast, the global average cost has fallen from 7.9 per cent to 7.52 per cent during the same period.⁸⁵

The primary cause of the account closures has been a convergence of issues related to AML/CTF measures.⁸⁶ These include a decreased risk tolerance as a

⁷⁵ On 26 September 2015 the total cost for sending AU\$500 in cash from Australia to Samoa was AU\$18.81 (3.76%) with Pacific Way Money Transfer, AU\$20.38 (4.08%) with MoneyGram, AU\$21.07 (4.21%) with Xpress Money, AU\$24.17 (4.83%) with IMEX Money Transfer and AU\$27.72 (5.54%) with Western Union: see Send Money Pacific, *Comparison Results* (11 May 2016) <<https://perma.cc/CP24-CF5C>>.

⁷⁶ *Ibid.*

⁷⁷ *Ibid.*

⁷⁸ See generally Pacific Financial Inclusion Programme, above n 56.

⁷⁹ 'Sources say about 75 per cent of registered remitters would have been serviced by the big banks a few years ago, but it is a much smaller percentage today': Evers, above n 72.

⁸⁰ SBS World News, 'Plans to Shut Down Money Transfer Businesses over Terror Fears', 16 November 2015 (Emma Hannigan), available at <http://www.arcpa.org.au/?page_id=298>.

⁸¹ *Ibid.*

⁸² Capal, above n 13.

⁸³ World Bank, 'Remittance Prices Worldwide' (Report, Issue No 13, March 2015) 6.

⁸⁴ World Bank, 'Remittance Prices Worldwide Issue No 15', above n 50, annex table 2.

⁸⁵ *Ibid.*

⁸⁶ Alliance for Financial Inclusion, *G-24/AFI Policymakers Discuss Financial Inclusion*, above n 2.

result of high compliance costs and monetary fines, as well as pressure from foreign banks to comply with international AML/CTF measures.

IV AML/CTF AND THE THREAT TO FINANCIAL INCLUSION

A International AML/CTF Measures

Financial systems are vulnerable to misuse. In the United States, laws designed to protect the financial system from abuse date back to 1970, with the establishment of the *Bank Secrecy Act*.⁸⁷ The integrity of financial systems was predominantly regulated on a domestic level until the 1980s, when organised crime — in particular, the narcotics trade — became increasingly international.⁸⁸ Coordinating financial regulation at an international level then became imperative.⁸⁹

In 1989, the intergovernmental Financial Action Task Force ('FATF') was established to set regulatory standards and to promote the national implementation of measures aimed at safeguarding the integrity of the international financial system.⁹⁰ In 1990, the FATF released the Forty Recommendations.⁹¹ The goal of the original FATF Recommendations was to combat the misuse of financial systems by persons laundering drug money.⁹² The Recommendations were revised in 1996 to include all forms of money laundering, and were further expanded to deal with the issue of terrorist financing after September 11, 2001.⁹³ Endorsed by over 180 countries, the Recommendations are now recognised as the international standard for AML/CTF.⁹⁴

In 2009, the FATF initiated a review of its Recommendations, which resulted in the publication of the second revised Recommendations in February 2012.⁹⁵ While the high-level principles contained in the original remain mostly unchanged, the revisions introduced a number of new elements such as tax offences and financial sanctions related to the proliferation of weapons of mass destruction.⁹⁶

⁸⁷ See *Financial Recordkeeping and Reporting of Currency and Foreign Transactions Act of 1970*, 31 USC § 5311 (2001), commonly referred to as the *Bank Secrecy Act* or *BSA*.

⁸⁸ Basel Committee on Banking Supervision, 'Prevention of Criminal Use of the Banking System for the Purpose of Money Laundering' (Statement, December 1988) 1 <<https://perma.cc/F6BP-7MFE>>.

⁸⁹ *Ibid* 2.

⁹⁰ Financial Action Task Force, 'International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations' (Report, February 2012) 7.

⁹¹ Financial Action Task Force, 'The Forty Recommendations of the Financial Action Task Force on Money Laundering 1990' (April 1990).

⁹² Financial Action Task Force, 'International Standards', above n 90, 7.

⁹³ *Ibid*.

⁹⁴ *Ibid*.

⁹⁵ International Monetary Fund Legal Department, 'Revisions to the Financial Action Task Force (FATF) Standard' (Information Note to the IMF Executive Board, International Monetary Fund, 17 July 2012) 3.

⁹⁶ *Ibid* 4; Financial Crimes Enforcement Network, *FATF Issues Revised Recommendations, The Financial Action Task Force*, United States Department of the Treasury, <<https://perma.cc/6M2Q-65M6>>.

Of particular relevance to financial inclusion is the fact that the updated Recommendations also place an increased emphasis on risk.⁹⁷ The FATF first introduced risk as an element of financial regulation policy in 2003, but limited the concept to specific Recommendations.⁹⁸ For many years the term was not clearly defined, something that the FATF itself acknowledged in 2010.⁹⁹ The new Recommendation 1 promotes a strengthened risk-based approach ('RBA') to AML/CTF, providing that countries should require financial institutions to 'identify, assess and take effective action to mitigate their money laundering and terrorist financing risks'.¹⁰⁰ The RBA requires regulators to apply enhanced measures in areas of high risk, but allows them to take a simplified approach where there are lower risks involved.¹⁰¹ Unfortunately, many banks have introduced stricter rules to manage high-risk customers but have not introduced simplified measures for people who pose a low risk.

Financial inclusion helps to protect the integrity of the global financial system by expanding the reach and effectiveness of AML/CTF regimes, as by definition the financially excluded are beyond the reach of AML/CTF regulation.¹⁰² Promoting financial inclusion has been on the FATF's agenda since 2010.¹⁰³ In 2012, the FATF Ministers noted that financial exclusion poses a real risk to the effective implementation of the revised Recommendations.¹⁰⁴ In light of these concerns, the FATF created a guidance paper, which aims to assist financial regulators to implement an AML/CTF system that aligns with the goal of financial inclusion.¹⁰⁵

The FATF reiterated its commitment to promoting financial inclusion in October 2014, when it warned against wholesale de-risking and encouraged banks to manage customers on a case-by-case basis rather than terminating relationships with certain categories of customers such as remittance providers.¹⁰⁶ The FATF is aware that this global trend of de-risking could lead affected remittance providers to resort to sending money through informal, unregulated channels.¹⁰⁷ Not only would this affect financial integrity, but it would limit the providers' ability to serve as a gateway for broader financial inclusion.

⁹⁷ International Monetary Fund Legal Department, above n 95, 4.

⁹⁸ Louis de Koker, 'Aligning Anti-Money Laundering, Combating of Financing of Terror and Financial Inclusion: Questions to Consider When FATF Standards are Clarified' (2011) 18 *Journal of Financial Crime* 361, 370.

⁹⁹ *Ibid.*

¹⁰⁰ Financial Action Task Force, 'International Standards', above n 90, 11.

¹⁰¹ Financial Action Task Force, 'FATF Guidance for a Risk-Based Approach: Prepaid Cards, Mobile Payments and Internet-Based Payment Services' (Report, June 2013) 27.

¹⁰² Timothy Lyman and Wameek Noor, 'AML/CTF and Financial Inclusion: New Opportunities Emerge from Recent FATF Action' (Focus Note No 98, Consultative Group to Assist the Poor, September 2014) 1 <<https://perma.cc/HL6T-94PT>>.

¹⁰³ Financial Action Task Force, 'FATF Guidance', above n 1, 7.

¹⁰⁴ Financial Action Task Force, *Declaration of the Ministers and Representatives of the Financial Action Task* (20 April 2012) <<https://perma.cc/QU2D-59D4>>.

¹⁰⁵ Financial Action Task Force, 'FATF Guidance', above n 1.

¹⁰⁶ Financial Action Task Force, *FATF Clarifies Risk-Based Approach: Case-by-Case, Not Wholesale De-Risking* (23 October 2014) <<https://perma.cc/2J6Y-F6UF>>.

¹⁰⁷ Global Partnership for Financial Inclusion, 'Global Standard-Setting Bodies and Financial Inclusion: The Evolving Landscape' (White Paper, March 2016) 69–70.

In June 2015, the FATF announced that it was developing guidelines for applying the RBA to MTOs, which will address the issue of access to banking services for MTOs.¹⁰⁸ The FATF also stated that it was undertaking further work on financial inclusion and customer due diligence ('CDD').¹⁰⁹ Work on both these projects should be completed by the FATF in 2016.¹¹⁰

B Domestic AML/CTF Measures

In Australia, many of the FATF Recommendations have been incorporated into the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) ('AML/CTF Act').¹¹¹ This includes implementing an RBA to regulation. When providing services to a customer, reporting entities must assess the risks of potential money laundering or terrorism financing to ensure they meet the minimum standards set out in the *AML/CTF Act* and *AML/CTF Rules*.¹¹²

In June 2014, the *AML/CTF Rules* were amended to include additional CDD requirements.¹¹³ The revised *AML/CTF Rules* place a stronger emphasis on ongoing CDD and expand the factors that banks must consider when determining the money laundering and terrorist financing ('ML/TF') risk of customers.¹¹⁴ Further amendments to the *AML/CTF Rules* are likely to occur in 2016 in response to two reviews: a statutory review required under the *AML/CTF Act* which is currently being undertaken by the Commonwealth Attorney-General's Department and the fourth FATF mutual evaluation which released its findings in April 2015. The latter review found Australia was not compliant with a

¹⁰⁸ Financial Action Task Force, *Drivers for 'De-Risking' Go beyond Anti-Money Laundering/Terrorist Financing* (26 June 2015) <<https://perma.cc/9P44-YJMH>>.

¹⁰⁹ Ibid.

¹¹⁰ Financial Action Task Force, *FATF Takes Action to Tackle De-Risking* (23 October 2015) <<https://perma.cc/STA4-647K>>.

¹¹¹ In 2005, Australia's compliance with the FATF Standards was assessed through a 'mutual evaluation' process. While Australia had implemented many of the original FATF Recommendations, its domestic legislation was not compliant in a number of areas. Notable for the purpose of this article is the fact the FATF recommended that Australia should require all money transfer operators to be licensed or registered, and that AUSTRAC should maintain a comprehensive list of such service providers and their details: Financial Action Task Force, *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: Australia* (14 October 2005) 158. This action has now been taken by Australia, which has required all remittance providers to register with AUSTRAC since November 2011: Australian Transaction Reports and Analysis Centre, *Remittance Sector Register* <<https://perma.cc/G46P-7SVC>>. Australia recently underwent another mutual evaluation process to assess compliance with the revised FATF Recommendations. The report of this process, released in April 2015, revealed that Australia's revised AML/CTF regime is more in line with FATF Standards, though deficiencies remain: Financial Action Task Force, *Anti-Money Laundering and Counter-Terrorist Financing Measures: Australia Mutual Evaluation Report* (April 2015) 9 <<https://perma.cc/496T-9TL9>>.

¹¹² Australian Transaction Reports and Analysis Centre, *AML/CTF Act* <<https://perma.cc/7E4K-6FXJ>>; *Anti-Terrorism Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No 1)* (Cth).

¹¹³ Australian Transaction Reports and Analysis Centre, *Customer Due Diligence* <<https://perma.cc/K5HG-BGKH>>.

¹¹⁴ King & Wood Mallesons, *Getting to Know Your Customer: New Anti-Money Laundering Know Your Customer and Customer Due Diligence Rules* (21 May 2014) <<https://perma.cc/8T8L-ACNB>>.

number of FATF's recommendations.¹¹⁵ The government has also undertaken to review the registration of remittance providers under the *AML/CTF Act* in response to findings released in September 2015 by the Working Group on Remittance Account Closures.¹¹⁶

The *AML/CTF Act* is policed by the federal government agency Australian Transaction Reports and Analysis Centre ('AUSTRAC') which ensures businesses and financial institutions comply with five core obligations:

- (i) enrolment: all regulated businesses need to enrol with AUSTRAC and provide prescribed enrolment details;
- (ii) establishing and maintaining an AML/CTF program: to help identify, mitigate and manage the money laundering and terrorism financing risks a business faces;
- (iii) customer due diligence: identifying and verifying the customer's identity, and ongoing monitoring of transactions;
- (iv) reporting: notifying authorities of suspicious matters, threshold transactions and international funds transfer instructions; and
- (v) record keeping: businesses are required to keep records of transactions, customer identification, electronic funds transfer instructions and details of AML/CTF programs.¹¹⁷

The *AML/CTF Act* and *AML/CTF Rules* give AUSTRAC the power to refuse, suspend, cancel or impose conditions on the registration of remittance providers.¹¹⁸ Since the establishment of the AUSTRAC Remittance Sector Register in November 2011, AUSTRAC has used its powers to cancel the registration of eight MTOs, refuse the registration of seven MTOs, impose conditions on the registration of 17 MTOs and suspend two MTOs from the register.¹¹⁹

According to the FATF, these actions have not been sufficient. The report released by the FATF after the fourth mutual evaluation review in 2015 criticised AUSTRAC's lack of enforcement action, as well as its difficulties in dealing with the remittance sector.¹²⁰ In response to the latter criticism, Australian banks have been cautioned against closing MTO accounts due to fears it will drive the remittance industry underground.¹²¹ However, such requests are unlikely to have any impact unless changes are made to the current regulatory framework to ease the burden on banks.

¹¹⁵ Financial Action Task Force, 'Australia Mutual Evaluation Report', above n 72.

¹¹⁶ Australian Government, Attorney-General's Department, 'Working Group on Remittance Account Closures, Outcomes Statement' (Report, September 2015) <<https://perma.cc/7P6C-5WE3>>.

¹¹⁷ Australian Government, Attorney-General's Department, *Anti-Money Laundering and Counter-Terrorism Financing* <<https://perma.cc/U5NV-CERW>>.

¹¹⁸ Financial Action Task Force, 'Australia Mutual Evaluation Report', above n 72, 87. The power to suspend registration is found in *Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No 1)* (Cth) para 59.4. The power to cancel registration is found in *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) s 75G.

¹¹⁹ Australian Transaction Reports and Analysis Centre, 'AUSTRAC Continues to Stamp Out Rogue Remitters' (Media Release, 5 February 2015) <<https://perma.cc/XGM4-YKZE>>.

¹²⁰ Ben Butler, 'Don't Cut Remitters Off, Banks Cautioned', *The Australian* (Sydney), 22 April 2015, 22.

¹²¹ *Ibid.*

C The Impact of AML/CTF Measures on the Remittance Industry

There is a major ongoing debate about whether the global AML/CTF regime represents a sensible approach to regulating AML/CTF risks, or whether the overzealous application of its rules may well be counter-productive by driving money transfers into informal channels and out of the regulated space altogether.¹²² The strict AML/CTF measures imposed on financial providers, both in Australia and abroad, are having a huge impact on the remittance industry in Australia. Unless changes are made, the current state of affairs poses a serious threat to financial inclusion in the PICs.

For small MTOs, complying with AML/CTF measures can be too onerous. Many MTOs operate by transferring individual remittances together as a lump sum through a single account. However, doing so does not satisfy the enhanced Know Your Customer ('KYC') rules, as the payments cannot be traced to particular individuals. Banks are able to verify individual payments through money transfer software that is often too costly for small businesses to maintain.¹²³ It is particularly costly for MTOs, as they need to purchase software licences for multiple agents.¹²⁴ For small businesses, holding more than one account is also very expensive.¹²⁵

In its recent mutual evaluation report, the FATF noted that small remittance businesses 'lack capacity to implement Australia's complex regulatory requirements and do not implement preventative measures in line with the FATF Standards'.¹²⁶ In particular, the FATF was referring to the regulatory changes Australia made in 2011 to strengthen its monitoring of the remittance sector. These changes required MTOs to perform due diligence on their affiliate, provide agents and affiliates with a compliance program, train agents, monitor agent compliance and monitor transactions across their entire network.¹²⁷ FATF noted the requirements have proven too difficult and expensive for smaller MTOs.

Even larger MTOs have faced difficulties complying with the strengthened due diligence requirements. In January 2015, one of the world's largest MTOs, MoneyGram, was fined AU\$122 400 by AUSTRAC for contravening Australia's AML/CTF laws.¹²⁸ MoneyGram has approximately 800 affiliates in Australia, of which six were found to be unregistered remittance businesses.¹²⁹

¹²² In 2006, Passas noted that overly burdensome regulation might dissuade MTOs from operating through officially regulated channels. This risk remains true today — financial security can be undermined by the very rules and processes designed to strengthen it: Nikos Passas, 'Fighting Terror with Error: The Counter-Productive Regulation of Informal Value Transfers' (2006) 45 *Crime, Law and Social Change* 315, 334.

¹²³ Interview with David Sio, General Manager at Pacific Way Financial Services (conducted by phone, 23 October 2014).

¹²⁴ *Ibid.*

¹²⁵ *Ibid.*

¹²⁶ Financial Action Task Force, 'Australia Mutual Evaluation Report', above n 72, 87.

¹²⁷ *Ibid.*

¹²⁸ Australian Transaction Reports and Analysis Centre, 'MoneyGram, One of the World's Largest Remitters, Fined \$122,400 by AUSTRAC' (Media Release, 21 January 2015) <<https://perma.cc/SH78-R5MX>>.

¹²⁹ *Ibid.*

The AML/CTF regulations also place a heavy burden on banks, particularly in relation to high-risk customers.¹³⁰ The remittance industry has been assessed as 'high risk' due to its susceptibility to exploitation by serious and organised crime.¹³¹ AUSTRAC and the Australian Crime Commission ('ACC') estimate that 10 per cent of the AU\$30 billion transferred across Australia's borders by what AUSTRAC refers to as the 'alternative' remittance sector each year is 'dirty money' — funds that are the proceeds of crime.¹³² As a result, banks are required to spend more time monitoring the accounts of remittance providers.¹³³

In 2013, more than 95 per cent of all international funds transfers in Australia were made by the banking sector.¹³⁴ In terms of value, money transfers made by MTOs accounted for AU\$66 billion — a mere 1.7 per cent of the more than AU\$3.9 trillion transferred internationally.¹³⁵ Given these figures, the costs associated with maintaining MTO accounts and ensuring continued compliance with AML/CTF regulations far exceed the income they generate for banks.¹³⁶ Many banks have thus chosen to close MTO accounts as the level of compliance is too high for such low levels of profits.

Banks also face significant fines and reputational damage if they make poor risk assessments. In 2012, HSBC made the largest bank settlement in US history when it was fined more than US\$1.9 billion for facilitating the transfer of hundreds of millions of dollars from Mexican drug trafficking organisations through the United States.¹³⁷ The transfers occurred as a result of an inappropriate country risk rating and other deficiencies in their approach to identifying AML/CTF risks.¹³⁸

HSBC is just one of a number of banks found to have infringed AML/CTF regulations in recent years. More recently, Commerzbank of Germany was forced to pay US\$1.5 billion and dismiss all employees linked to its failure to comply with US AML/CTF legislation.¹³⁹ BNP Paribas in France was also ordered to forfeit a staggering US\$8.83 billion and pay a fine of US\$140 million

¹³⁰ Louis de Koker, 'Lack of Real Action on Remittances Increases Terrorist Financing Risk', *The Conversation* (online), 1 December 2014 <<https://perma.cc/5HYR-JJ9C>>.

¹³¹ Paul Jevtovic, 'Moving towards a Self-Regulated Alternative Remittance Sector: How Eligo National Task Force is Strengthening the Industry against Money Laundering Exploitation by Serious and Organised Crime' (Speech delivered at the Migration Institute of Australia, Sydney, 31 October 2014).

¹³² *Ibid.*

¹³³ de Koker, 'Lack of Real Action', above n 130.

¹³⁴ Financial Action Task Force, 'Australia Mutual Evaluation Report', above n 72, 83.

¹³⁵ *Ibid.*

¹³⁶ de Koker, 'Lack of Real Action', above n 130.

¹³⁷ United States Department of Treasury, 'Treasury Department Reaches Landmark Settlement with HSBC' (Press Release, 11 December 2012) <<https://perma.cc/KGT6-VYQW>>.

¹³⁸ Homeland Security and Governmental Affairs Permanent Subcommittee on Investigations, above n 11.

¹³⁹ Ben Protess, 'Commerzbank of Germany to Pay \$1.5 billion in US Case', *The New York Times* (online), 12 March 2015 <<https://perma.cc/ZQ88-SD3N>>.

for violating US economic sanctions and disguising the origins of the payments in order to pass the money through the United States.¹⁴⁰

The above examples all occurred in the United States, which is significant as the United States plays a larger role in Australia's remittance industry than many may realise. Remittances are predominantly cleared through US dollars, so Australian banks require a US bank to settle the funds that are transferred.¹⁴¹ Under US law, banks can be held liable for the AML/CTF compliance failure of any foreign bank whose funds they clear.¹⁴² As a result, Australian banks are under pressure from their US counterparts to stop processing remittance transfers. Resisting this pressure could compromise the ability of Australian banks to transact in US dollars for all their customers.¹⁴³ As the General Manager of Westpac Pacific noted in an interview in 2014, Australian banks are 'too far down the line — our reliance on the US dollar means our hands are tied'.¹⁴⁴

For banks, the reputational damage caused by closing the accounts of MTOs trying to serve the world's poor pales in comparison to being found guilty of assisting to fund terrorism.¹⁴⁵ This is particularly true in the United States, where the issue of terrorism has been at the forefront of policy-making since September 2001.

Given pressure from abroad, the costs associated with AML/CTF compliance and the penalties imposed for regulatory breaches, many Australian banks have chosen to leave the remittance sector. Of the big four banks in Australia, Westpac was the last bank to close down the accounts of its remittance customers. The decision to do so in November 2014 came amid pressure from its correspondent bank in the US, JP Morgan Chase, which Westpac uses to clear US dollar transactions.¹⁴⁶ The pressure from the US bank is understandable, as in January 2014, JP Morgan Chase was fined more than US\$2 billion for other unrelated breaches relating to AML/CTF compliance.¹⁴⁷

In November 2014, a group of 24 MTOs formed a class action against Westpac for its blanket ban on dealing with the remittance industry.¹⁴⁸ The Federal Court granted an injunction, preventing Westpac from closing the accounts before a hearing on 23 December 2014. The MTOs argued that the bank's decision to close accounts was unconscionable, but the case settled with

¹⁴⁰ Nate Raymond, 'BNP Paribas Sentenced in \$8.9 Billion Accord over Sanctions Violations', *Reuters* (online), 1 May 2015 <<https://perma.cc/37TU-RA8A>>; United States Department of Justice, 'BNP Paribas Sentenced for Conspiring to Violate the *International Emergency Economic Powers Act* and the *Trading with the Enemy Act*', *Justice News*, 1 May 2015 <<https://perma.cc/XH9Q-ZFFG>>.

¹⁴¹ Interview with Greg Pawson, General Manager, Westpac Pacific and Peter Capell, Head of Compliance, Westpac Pacific (Sydney, 22 October 2014).

¹⁴² *USA PATRIOT Act of 2001*, Pub L No 107-56, 115 Stat 272, § 312.

¹⁴³ Eyers, above n 72.

¹⁴⁴ Interview with Greg Pawson, General Manager, Westpac Pacific and Peter Capell, Head of Compliance, Westpac Pacific (Sydney, 22 October 2014).

¹⁴⁵ Eyers, above n 72.

¹⁴⁶ *Ibid*; Interview with Greg Pawson, General Manager, Westpac Pacific and Peter Capell, Head of Compliance, Westpac Pacific (Sydney, 22 October 2014).

¹⁴⁷ Tracy Kitten, 'JPMorgan Chase Fines Exceed \$2 Billion', *Bank Info Security*, 7 January 2014 <<https://perma.cc/D755-YDHK>>.

¹⁴⁸ Eyers, above n 72; Anthony Klan, 'Transfer Firms Win Temporary Westpac Reprieve', *The Australian* (online), 23 December 2014 <<https://perma.cc/V4AL-79CV>>.

Westpac agreeing to continue to allow international money transfers from the MTOs until 31 March 2015.¹⁴⁹

As a result of the account closures, many small MTOs have been forced to close.¹⁵⁰ Fewer MTOs means less competition and more reliance on banks, which are already increasing the price of sending remittances. The alternative to expensive bank transfers is for remittances to move via informal means, which leaves remitters without consumer protection,¹⁵¹ does nothing for financial inclusion goals and, ironically, may tend to support the very money laundering and other criminal practices that the AML/CTF measures are trying to combat.¹⁵²

The failure of Australia's banks to do more to support the legitimate business operations of MTOs represents a failure by these banks to recognise and accept their social service obligation. A banking licence is a rare privilege, granted to few. Remittances fulfil a vital social need in our region, and legitimate operators deserve the support of their banks as without it they cannot conduct their business. One gains the impression that Australian banks have bowed swiftly and without real complaint to the pressure brought to bear by their US correspondent banks. Once MTOs are driven from the market the beneficiaries are the Australian banks themselves, which stand ready to facilitate these remittances at far higher charges than those of the MTOs. The losers are expatriate workers in Australia, their poor relatives in their countries of origin, and the stability and viability of the nations in the Pacific.

V POSSIBLE SOLUTIONS

During 2015, the average cost of sending remittances to the Pacific region rose and a number of Australian MTOs closed their businesses.¹⁵³ Creative solutions are urgently required to prevent further increases in the cost of sending remittances and to ensure that the remittance industry is not driven underground, which could open a new money-laundering and terrorist-funding ('ML/TF') route that would threaten Australia's security. Relaxing regulation for low-risk customers in the PICs should be a priority so as to prevent AML/CTF measures from stymieing financial inclusion. Limiting transfer sums, promoting the use of digital financial services and encouraging technological innovation are other measures that should also be considered in order to address the challenge currently posed to financial inclusion in the PICs.

A Risk-Based Regulation

In 2015, the Australian government amended the identity documentation required by MTOs so that customers sending money from Australia now only have to meet two identity verification checks rather than three.¹⁵⁴ While this step

¹⁴⁹ Klan, above n 148.

¹⁵⁰ Eyers, above n 72.

¹⁵¹ Capal, above n 13.

¹⁵² Ibid; Clay Lowery and Vijaya Ramachandran, *Unintended Consequences of Anti-Money Laundering Policies for Poor Countries* (Working Group Report, Centre for Global Development, 9 November 2015) 25 <<https://perma.cc/PWL2-RMRP>>.

¹⁵³ World Bank, 'Remittance Prices Worldwide Issue No 13', above n 83, 6.

¹⁵⁴ G20, *National Remittance Plan 2015: Australia* (2015) 3 <<https://perma.cc/2QED-HTJU>>.

should be applauded, further steps could be taken to facilitate increased access to remittance services to the PICs.

The risk-based approach advocated by the FATF Recommendations permits financial institutions to use simplified due diligence ('SDD') measures for customers that are identified as low-risk.¹⁵⁵ In its guidance, the FATF states that such measures would be 'particularly relevant for individuals who rely on remittances from family members living and working away from home'.¹⁵⁶

One example of an SDD measure is the establishment of tiered accounts. This approach would allow undocumented individuals to access very basic accounts such as mobile wallets, with limited functions and low transaction limits.¹⁵⁷ In order to access additional services or increase their transaction limit, customers would need to undergo more extensive identity verification.¹⁵⁸ Such an approach has been adopted in India, where the government amended the AML/CTF regulation to allow banks to provide basic savings accounts for poor customers without sufficient proof of identity. The accounts are subject to strict limitations and are operational for a period of 12 months, after which they can only be renewed if the customer provides evidence that he or she has applied for valid identity documents.¹⁵⁹

Providing flexibility around the identity verification process for low-risk customers is another measure that can be adopted to promote financial inclusion. In many rural or remote parts of the PICs, people do not have formal identification documents. As a matter of practicality, regulations should allow for creativity regarding the type of credible identity documents accepted for KYC purposes. References from employers or existing customers, village chiefs or religious leaders within the customer's community are all examples of alternative forms of identification that could be used.¹⁶⁰

While flexibility is necessary, regulators must ensure that identification verification does not place an additional financial burden on those who are already financially excluded. Louis de Koker has noted that allowing employers or village chiefs to verify identity can increase the power that those people hold over vulnerable members of the community and may lead to corrupt practices such as the imposition of verification fees which may act as a further barrier to financial inclusion.¹⁶¹ For this reason, the more options and flexibility provided to low-risk customers the better.

¹⁵⁵ Financial Action Task Force, 'FATF Guidance', above n 1, 29; Louise Malady, Ross Buckley and Douglas Arner, 'Developing and Implementing AML/CFT Measures Using a Risk-Based Approach for New Payments Products and Services' (CIFR Paper No 028/2014 and University of Hong Kong Faculty of Law Research Paper No 2014/021, 19 June 2014) 2.

¹⁵⁶ Financial Action Task Force, 'FATF Guidance', above n 1, 29.

¹⁵⁷ *Ibid* 28; Lyman and Noor, above n 102, 8.

¹⁵⁸ Lyman and Noor, above n 102, 8.

¹⁵⁹ Financial Action Task Force, 'FATF Guidance', above n 1, 30–1.

¹⁶⁰ Lyman and Noor, above n 102, 8.

¹⁶¹ de Koker, 'Aligning Anti-Money Laundering', above n 98, 369.

B *Limiting Transfer Sums to Manage Risk*

On average, migrants remit US\$200 per month.¹⁶² Placing low transfer limits on remittance accounts could make it difficult for criminals to launder large sums of money, while allowing migrants to continue sending genuine remittances.

Many banks already impose transfer limits based on security or compliance concerns. In the US, transfers to Mexico from Wells Fargo are limited at US\$1500 per day, whereas the bank allows twice that amount to be transferred to Vietnam.¹⁶³ This reflects the fact that Mexico is estimated to be the third largest source of illegal money in the world.¹⁶⁴

These limits are still considerably higher than the average amount remitted by migrants each month. In order to reduce AML/CTF risk while still supporting financial inclusion, regulation could impose a much lower limit. The FATF Recommendations and guidance provide that regulators may significantly reduce the information required for international money transfers valued at less than US\$1000.¹⁶⁵ For transactions of this size, the minimum information required is the name of the sender, the name of the recipient and a unique reference number for the transaction.¹⁶⁶ Providers do not need to verify this information unless the transaction is viewed as suspicious or unusual.¹⁶⁷ Limiting remittance transfers to, say, US\$750 per day would allow migrants to send money home without banks having to fulfil onerous AML/CTF requirements for the transfers.

It is important to note that migrants may sometimes need to exceed such limits, for example in the case of an emergency when they may wish to provide financial aid to friends and family.¹⁶⁸ Policies could allow for flexibility around transfer limits in times of known need, such as following a natural disaster in the receiver country.

C *Digitising Payments*

Digital financial services ('DFS') are globally recognised as an effective means to promote financial inclusion. DFS refers to the technologies available to deliver financial services from a broad range of providers to a wide range of recipients through mobile phones.¹⁶⁹ DFS is particularly well suited to the PICs as mobile technology is inexpensive and already relatively widespread.

¹⁶² Ratha, 'The Hidden Force in Global Economics', above n 44.

¹⁶³ Wells Fargo, *Wells Fargo ExpressSend Transfer Limits* <<https://perma.cc/9AMU-7T7P>>.

¹⁶⁴ Dev Kar and Joseph Spanjers, 'Illicit Financial Flows from Developing Countries: 2003–2012' (Global Financial Integrity, December 2014) <<https://perma.cc/5QWA-HJZJ>>.

¹⁶⁵ Lyman and Noor, above n 102, 10–12.

¹⁶⁶ *Ibid* 12.

¹⁶⁷ *Ibid*.

¹⁶⁸ de Koker, 'Aligning Anti-Money Laundering', above n 98, 364.

¹⁶⁹ Digital Financial Services ('DFS') refers to a range of financial services (including credit, savings, loans, insurance and payments services) accessible via digital remote means (including e-money, mobile money, card payments and electronic funds transfers). This is in contrast to cash payments or traditional financial services accessed through physical means, such as visiting a bank branch. For more terminology definitions, see Mobile Financial Services Working Group, Alliance for Financial Inclusion, 'Mobile Financial Services: Basic Terminology' (Guideline Note No 1, March 2013) <<https://perma.cc/GQ4T-SW74>>.

Encouraging the PICs to transition from cash economies would assist with managing ML/TF risks, but would have many other benefits as well.¹⁷⁰

First, digital payments dramatically reduce the costs associated with transferring remittances. This paper has already highlighted the fee discrepancy between banks and MTOs using the example of sending AU\$500 from Australia to Samoa. In this example, the least expensive cash-to-cash transfer offered by an MTO was for AU\$18.81, or 3.76 per cent of the total amount transferred.¹⁷¹ By contrast, at the time KlickEx Pacific offered instantaneous money transfers via mobile phone for a cost of AU\$1.68, or a mere 0.34 per cent of the money being remitted.¹⁷² Increasing the use of DFS in the PICs would thus provide receiving parties with a much greater proportion of the funds sent to them.

In addition to receiving more money from a digital transfer, recipients may also benefit by not having to take time off work and travel to collect their money from a bank branch. Worldwide, more than 40 per cent of remittances are sent to rural areas.¹⁷³ Recipients in these areas often have to travel considerable distances to collect payments, which can be costly both in terms of transportation expenses and income foregone while travelling.¹⁷⁴ This is particularly true in the PICs, where many people live on remote islands.

Another benefit of sending remittances via digital means is that it increases transparency, which is beneficial for both regulators and the parties involved in the transaction. From a regulatory point of view, transferring money electronically improves the traceability of remittances, which assists banks and MTOs to satisfy AML/CTF compliance requirements.¹⁷⁵ Westpac has highlighted MoneyGram's sophisticated tracing technology as key to its continued relationship with the large MTO, as it enables the bank to satisfy its regulatory requirements.¹⁷⁶

Digital payments provide greater security for senders and receivers of remittances, who are able to track their money online and keep digital records of the amount of money sent and received.¹⁷⁷ This decreases the risk of 'leakage' associated with anonymous cash payments — where payments do not reach the recipient in full.¹⁷⁸ Once received, funds that are stored electronically are also safer than storing cash as they are not at risk of being lost, stolen or destroyed (such as during a natural disaster).

¹⁷⁰ While DFS holds much promise for expanding financial inclusion, there are a number of challenges and potential risks as well. For a discussion of these, see Louis de Koker, 'The 2012 Revised FATF Recommendations: Assessing and Mitigating Mobile Money Integrity Risks within the New Standards Framework' (2013) 8 *Washington Journal of Law, Technology and Arts* 165.

¹⁷¹ Send Money Pacific, above n 74.

¹⁷² Ibid.

¹⁷³ Leora Klapper and Dorothe Singer, 'The Opportunities of Digitizing Payments' (Working Paper No 90305, World Bank Development Research Group, 28 August 2014) 12.

¹⁷⁴ Ibid 4.

¹⁷⁵ MoneyGram, the world's second largest MTO, uses sophisticated in-built technology to trace all its money transfers around the world. In an interview with the Pacific head of compliance at Westpac, Peter Capell, he stated that Westpac had partnered with MoneyGram because its digital systems complied with the 'know your customer' rules.

¹⁷⁶ Interview with Greg Pawson, General Manager, Westpac Pacific and Peter Capell, Head of Compliance, Westpac Pacific (Sydney, 22 October 2014).

¹⁷⁷ Klapper and Singer, above n 173, 3.

¹⁷⁸ Ibid.

Perhaps most importantly, digital payments provide an important incentive for people to engage with DFS technology. Once people have received remittances this way, they are more likely to use DFS to make payments, save money and otherwise participate in the formal financial system through their mobile phone. Remittances can serve as the bridge to better use of DFS.

Recent research by Citigroup and Imperial College London found that a 10 per cent rise in the adoption of mobile money worldwide could bring an additional 220 million people into the formal financial sector.¹⁷⁹ This would result in an estimated US\$1 trillion in net new flows in the formal economy, US\$100 billion in increased tax collections and US\$185 billion in benefits from digitising government benefits.¹⁸⁰

Despite these benefits, only a very small proportion of cross-border transactions currently use mobile money technology. In 2013, the value of international remittances sent through mobile phones was US\$10 billion — less than two per cent of global remittance flows.¹⁸¹ In the Pacific, implementation of DFS is at varying stages and differs in form from country to country. Nations such as Fiji and Papua New Guinea are relatively advanced, having introduced mobile banking services several years ago. By contrast, the availability of DFS in Vanuatu is relatively limited and Timor Leste only introduced its first pilot mobile banking program at the end of 2014.¹⁸²

Currently the way in which AML/CTF regulation is implemented creates a barrier to further development of DFS in the PICs. The implementation of the regulation should be simplified for low-value transfers to assist this useful tool to advance.¹⁸³

D Technological Innovation

The development of mobile banking technology has had a huge impact on financial inclusion worldwide. As technology continues to advance, the development of further innovative solutions for reducing concerns around KYC while promoting financial inclusion should be encouraged.

An example of a creative solution is the possible use of camera phones or voice recognition software to verify the identity of customers in remote, sparsely populated areas within the PICs.¹⁸⁴ This would enable unbanked customers who pose little ML/TF risk to obtain simple bank accounts in scenarios where the cost of conducting conventional face-to-face CDD would normally be prohibitive.¹⁸⁵

The advancement of biometric technology also presents opportunities for verifying the identity of customers, as well as enhancing the security of digital payment systems. The use of biometric authentication mechanisms to authorise mobile payments would increase the transparency of payments and help deter

¹⁷⁹ Citigroup, 'Digital Disruption — How FinTech is Forcing Banking to a Tipping Point' (Report, March 2016) 53 <<https://perma.cc/72XJ-FZNK>>.

¹⁸⁰ Ibid.

¹⁸¹ Ratha et al, 'Forced Migration', above n 8, 13.

¹⁸² Reuben Summerlin, *Timor Leste's First Mobile Money Pilot Launched to Expand Access to Financial Services* (4 December 2014) UN Capital Development Fund <<https://perma.cc/535G-6WKW>>.

¹⁸³ Ratha et al, 'Forced Migration', above n 8, 13.

¹⁸⁴ Lyman and Noor, above n 102, 7.

¹⁸⁵ Ibid.

criminal activity.¹⁸⁶ While the cost may impede adoption of the technology by local DFS providers, introducing the technology at a more central level through a government-led identification project such as that which is currently occurring in India could assist with achieving greater financial integrity as well as financial inclusion.¹⁸⁷

The possible use of cryptocurrencies and block-chain technology is another example of how technological innovation could be used to further financial inclusion.¹⁸⁸ In 2015, three of Australia's big four banks began trialling Ripple's peer-to-peer fiat and cryptocurrency exchange technology.¹⁸⁹ Ripple allows users to transfer in any currency and can provide same or next-day payment, making it a quick, simple and low-cost method of sending small remittances overseas.¹⁹⁰ Furthermore, the technology satisfies AML/CTF obligations because it is able to identify the payment originator for each individual payment.¹⁹¹ The Australian government has announced that it is considering the application of AML/CTF laws to digital currencies as part of its statutory review into the *AML/CTF Act*, which is due to be released in 2016.¹⁹²

VI CONCLUSION

Financial inclusion is vital for the stability and integrity of the global financial system. It also greatly advances the lives of the poor through assisting with community development and the reduction of poverty. The importance of bringing the world's unbanked population into the formal financial system has been recognised by the public and private sector at all levels and has become a priority on the agendas of international bodies such as the G20 and the FATF.

Remittances play an increasingly significant role in promoting financial inclusion. By 2016, remittance flows to developing countries are expected to surpass half a trillion US dollars.¹⁹³ This figure vastly exceeds the amount of

¹⁸⁶ Pierre-Laurent Chatain et al, *Protecting Mobile Money against Financial Crimes: Global Policy Challenges and Solutions* (World Bank, 2011) 50.

¹⁸⁷ Planet Biometrics, *India's Biometric ID Should Be Emulated: World Bank* (14 January 2016) <<https://perma.cc/7BTM-PQKC>>; World Bank, 'World Development Report 2016: Digital Dividends' (2016) 195.

¹⁸⁸ For a discussion on the potential for Bitcoin technology to facilitate remittances and promote financial inclusion, see Brett Scott, 'How Can Cryptocurrency and Blockchain Technology Play a Role in Building Social and Solidarity Finance?' (Working Paper 2016 No 1, United Nations Research for Development, 10 February 2016) ii. The paper also discusses some of the challenges that may hinder Bitcoin from being used freely as a tool for greater financial inclusion. In recent times, Australian banks have taken the same approach to bitcoin accounts as they have to MTO accounts, choosing to close accounts to comply with their obligations under the *AML/CTF Act*. AUSTRAC has spoken in support of bitcoin exchanges and condemned the de-banking of entire industry sectors: see Nathan Lynch, *AUSTRAC Throws Regulatory Lifeline to 'De-Banked' Bitcoin Operators*, UNSW Centre for Law Markets and Regulation <<https://perma.cc/QC9U-6QAL>>.

¹⁸⁹ Paul Smith, 'Westpac, ANZ Trial Ripple Payments, but Big Four Reluctant on Bitcoin', *Australian Financial Review* (online), 9 June 2015 <<https://perma.cc/UU5J-JX54>>.

¹⁹⁰ *Ibid.*

¹⁹¹ *Ibid.*

¹⁹² Australian Government, Treasury, *Government Response to Australia's FinTech Priorities*, <<https://perma.cc/2AMP-T4DS>>.

¹⁹³ Anna Prokhorova, 'Remittances: Statistical Accuracy and Financial Benefits' (World Bank Presentation at the UNECE Capacity-Building Workshop on Migration Statistics, Almaty, Kazakhstan, 31 October–1 November 2013) 4.

official development assistance worldwide. In the PICs, remittances account for a large proportion of many countries' GDPs and are vital for people's livelihoods. Furthermore, these payments can serve to give the poor a reason to engage with the formal financial system by providing them with money that can be placed in a savings account, or used to acquire insurance against death or illness of a breadwinner. Doing so can lay a foundation from which the poor can climb out of poverty.

Around the world, the desire to combat money laundering and the financing of terrorism has seen the introduction of strict financial regulations that impose onerous compliance measures on financial providers. In Australia, such measures have proven too costly or too difficult for many small MTOs, who have been forced to close down. Other remittance providers have had their accounts closed by banks that have decided to exit the industry due to the associated risks and pressure from their US correspondent banks. It is noteworthy that such closures not only minimise risk for banks, but also allow them to profit from a less competitive industry in which the banks charge high rates to facilitate remittances.

The closure of MTO accounts in Australia poses a serious threat to financial inclusion in the PICs. Without MTOs, migrants will be forced to transfer money through banks, which charge significantly higher fees and require recipients to hold bank accounts. Given that the majority of people in the PICs do not hold bank accounts, this is a major problem. Alternatively, migrants may choose to transfer money through informal means. Doing so leaves legitimate remitters without important consumer protections, increases the risk of illicit transfers in Australia and tends to defeat the efficacy of the FATF global regime.

In the first quarter of 2015, a further seven MTOs were forced to close and the average cost of sending remittances from Australia to the Pacific rose slightly while the global average cost decreased.¹⁹⁴ Addressing the issues facing the Australian remittance industry is thus an urgent priority upon which AUSTRAC could, and should, be providing more proactive leadership. This is particularly so given the Australian government's goals of promoting prosperity and stability within our region.

First and foremost, we suggest using a more nuanced, risk-based approach to implementing AML/CTF regulations to accommodate financial inclusion goals. Simplified KYC and SDD measures should be used for lower risk customers, such as those who are very poor and currently unbanked. Other solutions include limiting the amount of funds transferred, digitising payments and encouraging greater use of technological innovation to reduce risks.

¹⁹⁴ World Bank, 'Remittance Prices Worldwide Issue No 13', above n 83, 5.