

SUBMISSION TO THE VICTORIAN LAW REFORM COMMISSION

USE OF REGULATORY REGIMES IN PREVENTING THE INFILTRATION OF ORGANISED CRIME INTO LAWFUL OCCUPATIONS AND INDUSTRIES.

This is a submission provided to the VLRC in response to the call for submissions on the use of regulatory regimes in preventing the infiltration of organised crime into lawful occupations and industries. This submission is provided following the Roundtable conducted on 30 July 2015 and assumes knowledge of the Consultation Paper (June 2015).

This submission is intended to develop particular points raised in the Paper and discussed at the Roundtable and is not intended to be exhaustive of all matters canvassed in the Paper.

Background.

Underlying this Reference is balancing risk against cost, that is assessing the community's 'risk appetite' for the 'harmful event' against the cost/inconvenience of measures available to ameliorate the risk. This should always be through a prism of the risk vesting, that is the harmful event occurring. The question to be answered is whether the risk management strategy being considered would be accepted by the public or group affected, as being all that was reasonable and acceptable to have been done in the circumstances. Too often risk management analysis proceeds based on a proposition the harmful event can be entirely prevented - *just choose the correct strategy and the event will not happen; if it does happen you have chosen the wrong strategy*. In fact it should proceed on the basis that when the event **does** happen, is the risk treatment that had been used acceptable when now viewed from the standpoint of the event having occurred. The focus has to be on tolerance and appetite – what 'price' you are prepared to pay, what you are prepared to allow happen.

The 'event' in this Reference is infiltration by organised crime. The appetite for allowing this to happen may well vary from occupation to occupation. The interest or incentive for organised crime to infiltrate an occupation will also vary from occupation to occupation, and there is likely be a correlation between those two variables. That is, occupational groups about which there is particular concern about infiltration would likely be the same groups that organised crime would target for infiltration.

The Consultation Paper contains a useful discussion on the purposes of infiltration which is not repeat here, save to observe that the purposes fall broadly into two categories. In the first, the purpose of the infiltration is to enter directly into the occupation or industry to conduct illegal activity within that occupation for profit. This typically involves integrating the illegal activity into the fabric of the legal activity of the business. An example may be running a motor car trading business and dealing in stolen motor vehicles and/or parts, as well as pursuing the usual lawful activities involved in operating such a business. The second is what the Paper describes as 'enabling' of illegal activity by use of the particular occupation. Examples may be lawyers and accountants where the purpose is to have proxies or 'tame' members of the occupation who tend not to be directly involved in illegal activity, but assist through their social standing, specialist knowledge and access to networks of influence in enabling the criminal to protect their criminal enterprise and service their criminal purposes in other ways.

The Consultation paper sets out a range of regulatory responses which can be arranged in ascending levels of intervention and effectiveness. In general, as the level increases so too does the cost and/or administrative burden on the participants in the occupation. Tension generates when regulatory responses of increasing effectiveness are applied to an occupation. The participants often feel that they alone are forced into bearing the related costs and burden, for a benefit that flows to the wider community. This tension grows into resentment if the regulatory

response applied is one towards the top of the range but is then applied inconsistently, or not supported by a competent compliance program. This is evident in the motor car trade where the industry has become increasingly disillusioned with the regulator for these very reasons.

Regulatory Responses to Guard Against Infiltration.

The range of regulatory responses is set out in the Consultation Paper at page 42. Below is some commentary on each:

Positive Licensing (including a 'fit and proper person' test)

Subject to the caveat below, Positive Licensing is the most effective measure because it requires an applicant to meet specified criteria before being permitted to commence in the occupation. Effective Positive Licensing is the security at the door. Licensing controls who gains entry and therefore offers the best option for preventing direct infiltration by criminal elements. In addition it goes some way towards insuring against admission of persons who, though not criminal themselves, may be susceptible to criminal influence once in the industry. Criteria around an applicant's associates are an example of this.

The caveat put on the effectiveness of Positive Licensing is that it cannot be 'tick box licensing'. A genuine Positive Licensing process involves a forensic examination of the application and supporting material, not an afternoon signing session once a week of checklists with all boxes ticked by an administrative officer. The value of positive licensing is the opportunity it gives to subject the applicant to genuine scrutiny, so to surrender that opportunity is to waste the licence application process. If the licensing process is rigorous monitoring and compliance will be less costly as a rigorous admission strengthens the occupation against the risk of infiltration.

However, a genuine licence application process has operating costs 'front loaded' into the admission process as well as taking time to complete, factors that are principally borne by the licence applicants. These are significant burdens upon persons seeking entry into the industry or occupation.

Negative Licensing

Negative Licensing schemes shift responsibility for regulating admission into the occupation to the applicants, making it particularly susceptible to deliberate infiltration. Negative licensing relies for effectiveness upon an active monitoring (and compliance) program, or particular and significant market forces. An example of the latter was Finance Brokers¹. A significant source of work for brokers was the Banks, and for a Finance Broker to receive referrals from the Banks required accreditation with the industry peak body. The peak body's membership rules were a reflection of the negative licensing criteria.

When a person applied for membership (in order to gain access to the lucrative referral work) they would agree to be checked against the criteria and if they failed, membership would be denied. This of course did not absolutely prevent ineligible persons operating as Finance Brokers, however it operated as a significant market force against the ineligible operator.

¹ Regulation of this industry moved to ASIC in 2012. It is worth noting that the Commonwealth's assessment of the industry resulted in abandonment of Negative licensing and moving the sector to positive licensing.

In effect, the peak body performed a *de facto* enforcement function, with the market's requirements (that is the Banks' requirement for membership of the peak body) giving force to that function. If a prospective broker wanted access to a significant portion of the market that was lucrative work, she/he needed to be a member of the peak body; she/he could only be a member if the peak body were satisfied the applicant was eligible under the negative licensing criteria.

The other market force which can give some effect to Negative Licensing is where the 'consumer' or customer group is defined, well organised and powerful. Such a consumer group is in a position to elect not to deal with an ineligible person, or to bring the ineligible trader to the attention of the compliance authority.

Both are examples where market forces giving some effect to an otherwise light touch regulatory model. In general, the absence of a need to obtain a licence clears the path for the dishonest (or ignorant) applicant to commence trading.

Registration Schemes

Registration is merely a list. As a regulatory tool it is low cost and very light touch and as a mechanism to defend an occupation against infiltration it is ineffective.

Other Regulatory Tools

Codes of Conduct have been used in some industries. They are also low cost and light touch (in terms of the involvement of a regulator) and their effectiveness is dependent upon either a strong consumer group who can call the participants to account, or a strong industry group which has significance influence over its industry and a strong presence in the relevant industry.

In this regard the power of a peak industry group should not be overlooked. Although not a formal regulatory tool, a strong peak body or professional group of which all or almost all participants are members can act in defence of its own industry against infiltration by criminal influences. The peak body's incentive is to further the interests of its membership by protecting the occupation or profession's standing in the market place.

Associates and Effective Control

The most difficult areas to address when guarding against infiltration are :

- a. Effective Control, and
- b. Associates.

Regulation is at its most effective when the person to be regulated is identifiable. The applicant for the licence is the subject of examination and is tested or measured against criteria. Some applicants may seek to circumvent this by fraud or dishonesty, thereby testing the integrity of the application process. However, identifying and testing the influence standing in the background is more problematic. This involves trying to uncover links between an applicant and others. These links could be familial, business, employment or social. The existence of a link to a criminal influence does not of itself mean infiltration will take place, but its existence gives rise to the possibility or risk of that happening.

The first step is to identify associates. The next is to determine whether an associate is a criminal element. In recent times we have seen classes of people deemed as criminal, such as the motor cycle gangs. This makes regulation easier as it is not necessary to prove the undesirable or criminal nature of the associate, it is enough to prove membership of the deemed class.

The more usual approach is to have categories of associates, for example an applicant's children, parents, spouse, persons with whom the applicant shares directorships of other companies, and to then examine the associate's background, antecedents and reputation. When there is a forensic examination of the associate's relationship the licensing authority has to determine whether the applicant is susceptible to adverse influence by that associate and what is the risk of influence being exercised. In some schemes, conditions on licences are able to be used to manage the risk. This is a challenging exercise.

Effective Control is closely related. Again the challenge is detecting whether there is someone in the shadows exercising influence over the licensee and who is effectively in control of the business. Effective control is of greater potential reach and more difficult to detect as it is usually dealing with a scenario where there is no apparent link between the licensee, and the shadow. It is particularly challenging because the shadow is likely to have no role at the time of licence application, and to become involved after the licence is in place.

Compliance and Monitoring

This topic was discussed for sometime at the Roundtable. A point made in these submissions is the importance of alignment between a regulatory scheme and the body responsible for compliance and monitoring of the scheme. Regulation is often utilised in the consumer protection space with the primary purpose to protect the interests of consumers. Consumer Affairs Victoria (CAV) is an example of a compliance and monitoring body. In the case of successful compliance bodies there is an alignment between the purpose of the regulations and the values and mission of the compliance body. Where the purpose of the regulations is to protect the interests of consumers the compliance body will view its functions through a prism of the interests of the consumer. The consumer protection compliance body will equip its staff with the skill set appropriate to that regulatory purpose.


In contrast, the Reference is addressed towards criminal conduct, not consumer protection. The appropriate skill set in monitoring criminal matters sits with different agencies, such as Victoria Police and Australian Federal Police.

The importance of correct alignment is illustrated in the history of regulation of the sex work industry. The legislation (now the Sex Work Act, formerly the Prostitution Control Act) is not addressed to consumer issues. The legislation is concerned with legalising a previously illegal industry that was heavily infiltrated by criminal elements. The legislative scheme sought to exclude the criminal element present in the previous illegal industry and protect the fledgling legalised sex work industry from criminal infiltration. The strategy was to focus on who was permitted to own a sex work business and who was allowed to hold operational management positions.

The monitoring function was given to CAV, however this was a problematic decision and CAV's inspectorate was ill equipped to deal with criminality instead of consumer rights. It was a combined 4 Corners / The Age newspaper investigation into the sex work industry which exposed the flaw in that decision. The government response was to have Victoria Police form a specialist unit which utilised Victoria Police's specialist skill set - for example, intelligence gathering resources and investigative expertise - to counter criminal infiltration of the industry, leaving the clipboard compliance/inspection functions² to CAV. CAV and Victoria Police have successfully combined to use their complimentary powers and expertise to 'cover the field'. Monitoring of the industry is now collaborative with other specialist policing bodies included from time to time on an as needed basis. Immigration and Border Protection may be included if there are breaches of visa conditions; Australian Federal Police may be included if there are sexual slavery or human trafficking issues.

² This refers to enforcing regulations dealing with matters such as adequate lighting required in brothels, presence of duress alarms in the rooms, checking there are sufficient condoms and dams in the brothel and that safe sex signage is in each room.

The experience in the sex work industry illustrated the importance of using the appropriately skilled compliance agency to align with the purpose of regulating. Choosing a consumer protection body to conduct anti criminal compliance proved to be inadequate in protecting the legalised industry against crime infiltration.

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11 August 2015