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Committee Secretary
Senate Standing Committee on Economics
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600
AUSTRALIA

Dear Committee Secretary,

Re: *Currency (Restrictions on the Use of Cash) Bill 2019*

I am writing to express my strong opposition to the *Currency (Restrictions on the Use of Cash) Bill 2019* and the associated legislative instrument, the *Currency (Restrictions on the Use of Cash – Excepted Transactions) Instrument 2019.*

About Adams Economics and John Adams

Adams Economics is a private and independent economic research and consulting business. As the founder and Principal Economic Analyst, I have prepared and lodged this submission independent of any external commercial or political relationships/associations and affiliations. This submission reflects my own research and private views regarding the Australian Government's proposed legislation.

For the record, I am not currently a member or associate of any political party or political organisation.

The proposed law is an attack on economic freedom

The proposed law (and associated instrument) are a major affront to and assault on economic freedom in Australia and represents a significant curtailment of Australian civil liberties. The law would punish individual Australians as to how they wish to spend private wealth, including whether:

- they wish to conduct transactions independent of Australia's commercial banking system; and
- they wish to conduct their economic affairs in private.

These concerns have been expressed in other jurisdictions around the world where governments have either implemented or sought to implement Cash Transaction Bans (CTBs) (or described otherwise as Cash Payment Limits). For example, in February 2016, a proposal to implement a CTB of 5,000 euros in Germany was dropped after significant public opposition whereas a 2017 public survey by the European Commission found that 87% of survey respondents believe that *'paying anonymously is an essential personal freedom'*[1].

The proposed law is anti-competitive

Moreover, the proposed CTB is anti-competitive in nature given that cash transactions (irrespective if they include physical or digital forms of currency) are an alternative payment method to using Australia's commercial banking sector.

From an economic regulatory perspective, it is highly improper for the Australian Government to be implementing anti-competitive laws which would effectively force citizens to consume a particular good or service at personal cost offered by a particular industry which, given the recent Hayne Royal Commission into

[1] https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/files/80_limiting.cash.pdf

Banking, has a dubious record in servicing customer interests. The proposed law breaches the principles which have underpinned Australian competition policy in recent decades without sufficient justification.

The Government's Unsubstantiated Claims

The Morrison Government and its instituted Black Economy Taskforce (BET) has made a series of claims regarding:

- the size and nature of Australia's black economy;
- the objectives of the proposed legislation; and
- the benefits that the CTB is anticipated to deliver.

Many of the claims made by the Government relating to the CTB have not been supported by robust empirical evidence. In considering the objectives and potential virtues and vices of the proposed legislation, it is critical that the Senate inquiry examine the Government's main claims and assess whether sufficient robust evidence is available to support these claims.

I will attempt in this submission to catalogue the Government's claims and to address them on a systematic basis.

Size of the Black Economy

According to Chapter 2 of the Black Economy Taskforce Final Report, *Chapter 2 The Size and Trajectory of the Black Economy*[2], the BET stated that:

- according to a 2012 ABS study which relied on data going back to 2001, the size of Australia's black economy was 1.5% of GDP whereas the illicit drug economy was 0.4% of GDP;

- its own work estimated that the size of Australia's *'black economy could be as large as 3% of GDP (or approximately $AUD 50 billion per year in 2015-16 terms) including both cash and criminal or illegal components'*;

- 'O*ur judgement is that important components of the black economy are increasing, owning to a combination of strong incentives, poor transparency and limited enforcement"*; and

- *"We do not believe that countervailing factors, including the falling use of cash, and the fact that black economy participants spend money in the legitimate economy, are offsetting this negative trend."*

The implication of these statements is that the size of Australia's black economy is increasing.

However, the BET did not use a sophisticated empirically robust tested econometric modelling approach to come to their conclusion, whereas the analysis of international experts who did use world leading cutting edge estimation techniques came to the completely opposite conclusion to the BET.

According to international experts Professor Friedrich Schneider and Leandro Medina[3] across multiple papers such as:

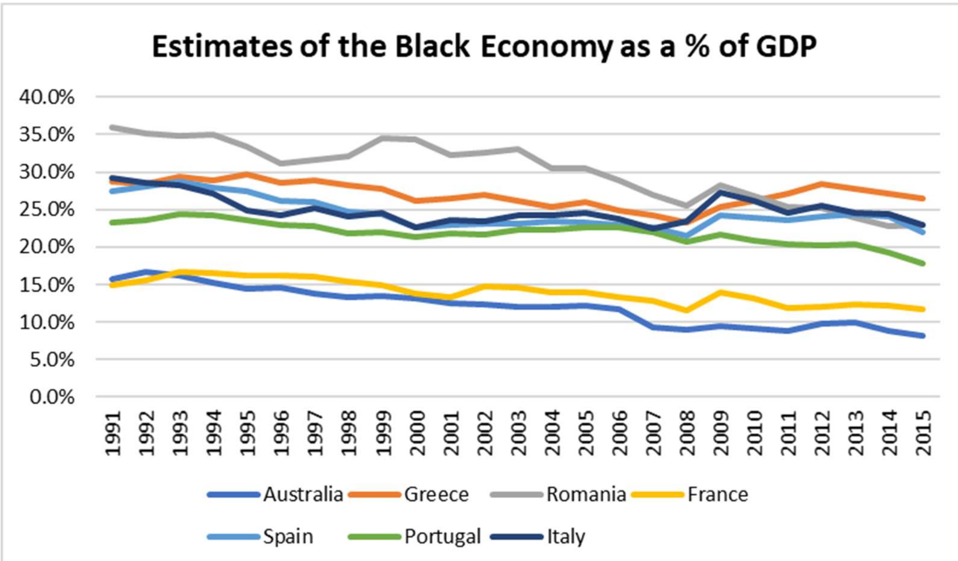
- the International Monetary Fund (IMF) working paper (WP/18/17), *Shadow Economics Around the World: What did we learn over the last 20 years?*[4]; and
- *Shadow Economics around the world; New results from 158 countries over 1991 - 2015*[5]

[2] https://treasury.gov.au/sites/default/files/2019-03/Black-Economy-Taskforce_Final-Report.pdf
[3] Leandro Medina is a Senior Economist with the International Monetary Fund. See the following LinkedIn profile: https://www.linkedin.com/in/leandro-medina-23776b1b/
[4] https://www.imf.org/en/Publications/WP/Issues/2018/01/25/Shadow-Economies-Around-the-World-What-Did-We-Learn-Over-the-Last-20-Years-45583
[5] https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2965972

the size of Australia's black economy actually fell over the period of 1991 to 2015 relative to Australia's GDP using the 'Multiple Indicators Multiple Causes' approach. Although, Schneider and Medina estimates suggest that the size of Australia's black economy is substantially larger than 3% of GDP as estimated by the Australian Government's BET.

Diagram 1 below presents the Schneider and Medina estimates of the size of the black economy for Australia and a select number of the European countries which have the most restrictive CTBs[6] (i.e. the lowest CTB thresholds) for the period of 1991 to 2015.

Diagram 1: Changes in the size of the black economy for the period 1991 - 2015



During this period, the size of the black economy for all these nations reduced in GDP terms. The size of this reduction of the countries shown in Diagram 1 are catalogued in Table 1.

Table 1: The total reduction in the size of the Black Economy for the period 1991 - 2015

	Size of Black Economy in 1991 as % of GDP	Size of Black Economy in 2015 as % of GDP	Size of reduction in the Black Economy as % of GDP
Australia	15.69%	8.10%	7.59%
Greece	28.79%	26.45%	2.34%
Romania	36.03%	22.94%	13.09%
France	14.96%	11.65%	3.31%
Spain	27.49%	22.01%	5.48%
Portugal	23.28%	17.82%	5.46%
Italy	29.14%	22.97%	6.17%

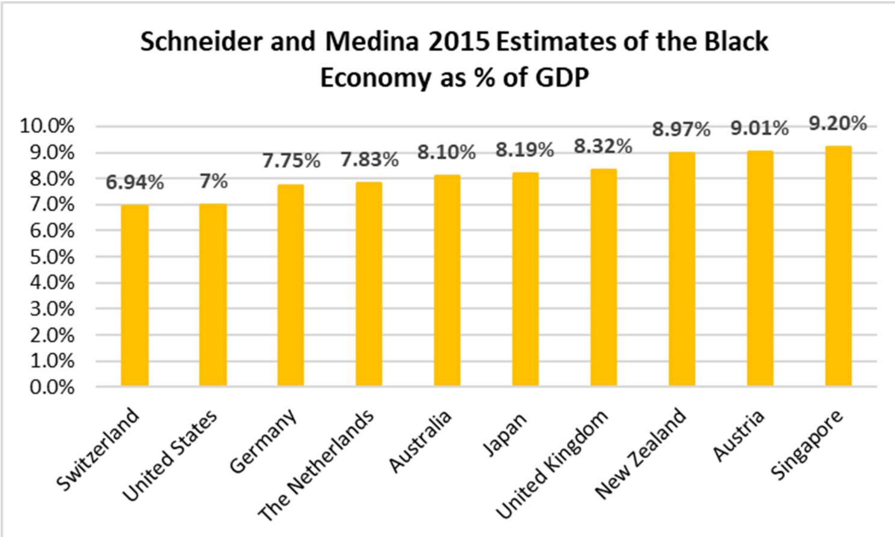
As can be documented in Table 1, Australia which does not have a CTB experienced the second largest reduction in the size of the black economy relative to European countries which do have very restrictive CTBs (the exception being Romania), implying that the CTB as a policy tool is unlikely to have a significant impact in reducing black economy activity and that other policy tools may be more effective in reducing black economy activities.

In addition, it is important to note that Australia, according to Schneider's and Medina's 2015 black economy estimates, has the 5th smallest black economy in GDP terms as shown in Diagram 2 below. These rankings are

[6] Currently, Greece has a CTB of 500 euros, Romania and France 1,000 euros, Spain 2,500 euros and Portugal and Italy 3000 euros.

important given that countries such as Germany[7] and Austria are economies still experience a high cash usage[8] and do not have a CTB, again bringing into question both the need and effectiveness of the Australian Government's proposed $AUD 10,000 CTB.

Diagram 2: Schneider and Medina 2015 estimates of the 10 smallest Black Economies as measured by GDP



Monetary Indicators of the Black Economy

As noted by Schneider and Medina in their papers cited above, one indicator of the black economy as it relates to the use of cash, is the ratio of the different measurements of the monetary supply M0 and M1.

According to Schneider and Medina: *'the larger the shadow economy, the more cash will be used, ceteris paribus'*

To determine whether the influence of cash has grown in the Australian economy, the M0/M1 money supply ratio was calculated using official RBA data and is shown via a time series graph at Diagram 3.

In the Australian context, M0 according to the Reserve Bank of Australia (RBA) is 'currency' whereas and M1 is 'currency + transactional deposits to ADIs'.

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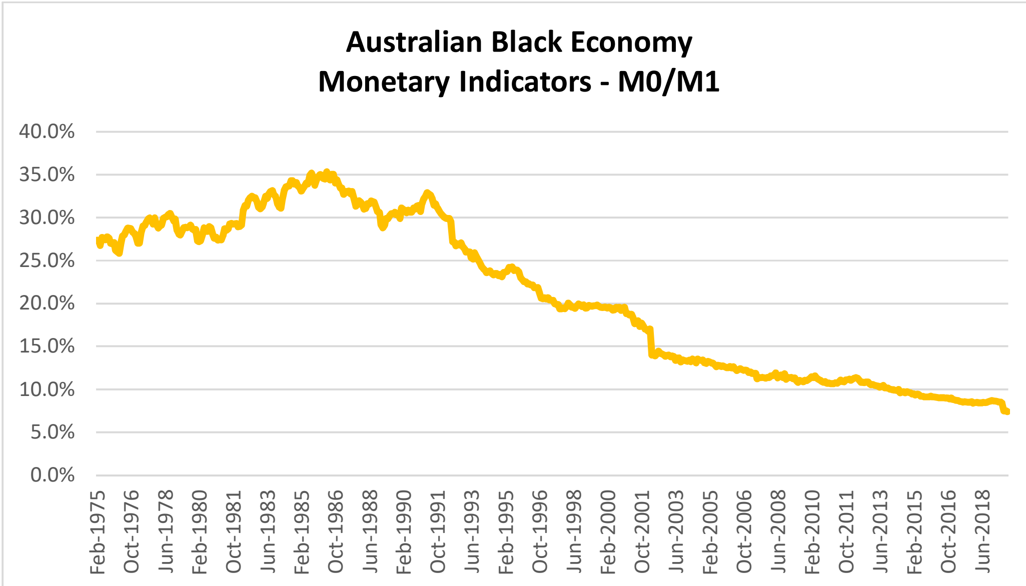
[7] https://www.npr.org/2019/06/09/728323278/for-many-germans-cash-is-still-king

[8] According to a 2017 study by the Austrian National Bank, 82% of all payments in Austria are still settled in cash and 65% of large payments are paid in cash. For more information, see: https://www.ceps.eu/wp-content/uploads/2018/06/final_report_study_on_an_eu_initative_180206.pdf

Diagram 3: A monetary indicator of the Black Economy - M0/M1



As can be shown above, the M0/M1 ratio has significantly fallen from its peak of 35.05% in September 1986 to its current level of 7.42% as of September 2019.

The rapid fall in the M0/M1 ratio indicates that the influence of cash in the Australian economy has significantly diminished in the past 33 years relative to deposits held in Australia's commercial banking system given that government issued M0 has grown by 764% whereas M1 has grown over 3984% over the same period.

This indicator suggests that focusing on cash in efforts to reduce Australia's black economy should not be the highest priority of Australian policy makers and that other policy measures should be considered first, especially as it relates to transactions within the Australian banking system.

Preventing Tax Evasion

According to Section 3 of the *Currency (Restrictions on the Use of Cash) Bill 2019*, the principal objective of the Government's proposed legislation is to:

> *"protect the integrity of the Commonwealth taxation system, by preventing the use of cash in order to avoid scrutiny by the Commissioner of Taxation seeking to enforce the taxation law."*

According to the Federal Treasurer, the Hon. Josh Frydenberg MP, the proposed $AUD 10,000 CTB would reduce the incentive to avoid paying and therefore enhance Commonwealth tax receipts, although according to page 3 of the Explanatory Memorandum to the *Currency (Restrictions on the Use of Cash) Bill 2019*, the *"Bill is estimated to have an unquantifiable impact on revenue over the forward estimates."*

However, according to a 2017 Report by the Centre for European Policy Studies (CEPS), *"Study on an EU initiative for a restriction on payment in cash"*[9], the effectiveness of a CTB in reducing the incidence of tax evasion is highly questionable.

For example, on page 11, the CEPS report states:

[9] https://www.ceps.eu/ceps-publications/study-eu-initiative-restriction-payments-cash/

> *"Even though scientific views differ on the subject cash restrictions may have a (limited) effect on tax evasion. However, it should be noted that in general tax evasion is rather explained by other factors than solely by the use of cash. It also does not capture larger tax evasion schemes, which do not depend on cash at all.*
>
> *"A high ban would not fulfil the purpose of reducing tax evasion. Even a threshold of 1 000 EUR is most likely going to be too high, because the vast majority of tax evasion cases concerns small amounts and would not be affected. The lower the threshold value, the more cash-settled commercial payments are likely to be affected by a cash payment limit. To sum up, to be effective, despite the limitations of the measure, the threshold should be as low as possible."*

Moreover, according to page 150 the CEPS report:

> *"The Austrian National Bank generally considers restrictions of cash payments as ineffective in the fight against tax evasion. They stressed that Austria has a rather low shadow economy compared to other European countries despite its high level of cash usage."*

The implications from the Federal Treasurer's claims vs the available evidence from Europe is that:

- the Australian Government does not have robust empirical evidence that their proposed CTB will have any material beneficial impact on reducing tax evasion in Australia;
- international evidence suggests the CTB will not assist in reducing tax evasion in Australia, especially with a CTB threshold of $AUD 10,000 which is likely to be too high;
- KPMG Australia has also suggested that a CTB of $AUD 10,000 is likely to be ineffective in tackling tax evasion and that a threshold cap of either $AUD 5,000 or $AUD 2,000 should be considered[10];
- the Australian Government is unable to indicate how much additional taxation revenue could be generated from the $AUD 10,000 CTB and has not indicated how much additional cost will need to be incurred in order to enforce the law and generate this revenue; and
- the legislation as currently proposed is likely to fail on delivering on its principal objective.

The Australian Government is not serious about eliminating money laundering

When it comes to tackling money laundering as part of seeking to reduce Australia's black economy, the Australian Government has been heavily criticised by Australian and international experts for lacking the will to pursuing foreign money which is likely being laundered through Australian residential real estate.

For example, according to paragraph 44 of the OECD Anti-Bribery Convention report[11]:

> *"The review team noted the views of J.C. Sharman, an Australian academic and international AML/CFT and anti-corruption expert, on the Australian AML/CFT system's failure to counter the flow of corrupt proceeds from abroad into the Australian real estate sector. Prof. Sharman attributes the gap to a lack of willingness to take action rather than a lack of capacity, stating that Australia has some of the most powerful AML/CFT laws in the world. He provides several examples where banks or AML/CFT authorities have failed to act on suspicious payments, and information from interviews with Australian bankers that believed the Commonwealth Government did not take seriously enough the issue of inward flows of corrupt proceeds."*

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[10] https://www.afr.com/politics/cash-payment-limits-of-5000-or-2000-proposed-in-black-economy-crackdown-20180629-h121r0

[11] http://www.oecd.org/corruption/anti-bribery/Australia-Phase-4-Report-ENG.pdf

Moreover, the Australian Financial Review reported on 11 November 2019 in an article entitled, *'Dirty money spotlight on estate agents'*[12], that the international Financial Action Taskforce which is an inter-governmental body as part of the G7 has stated that:

> *"large amounts are suspected to be laundered out of China into the Australian real estate market".*

The Financial Action Taskforce's 2018 report found that Australia was non-compliant or only partially compliant with 14 of its 40 recommendations.

This lack of will has been recently reflected in the Australian Government's new legislation, the *Anti-Money Laundering and Counter-Terrorism Financing and Other Legislation Amendment Bill 2019*[13] which does nothing to expand the definition of 'designated services'[14] to include real estate agents, accountants and lawyers.

Including real estate agents, accountants and lawyers as a 'designated service' would provide the Australian Transaction Reports and Analysis Centre (AUSTRAC) with additional sources of information that would assist in identifying potential instances of money laundering through the Australian residential real estate sector, especially from mainland China which estimates suggest could be worth billions of dollars.

The lack of will to tackle potential international monetary laundering in the Australian residential real estate brings into question the Australian Government's authenticity in tackling the black economy and also questions whether therefore the CTB should be the highest policy priority, given that the overwhelming majority of large scale transactions occur through Australia's commercial banking system as shown above with the collapse of the M0/M1 money supply ratio over the past 33 years.

Impact of CTB on the Black Economy

With respect to the black economy, the Australian Government and the BET have failed to provide robust empirical evidence that the proposed CTB would have any material impact on the black economy whether from the tax leakage (as noted above) or illicit activities perspective.

An independent 2017 study by Professor Friedrich Schneider, *'Restricting or Abolishing Cash: An Effective Instrument for Fighting the Shadow Economy, Crime and Terrorism"*[15] states that:

> *"Cash has a minor influence on the shadow economy, crime and terrorism, but potentially has a major influence on civil liberties."*

Moreover, Schneider notes that countries such as Sweden, still have sizeable shadow economies even though cash payments have become rare.

Finally, Schneider concludes:

> *"Cash reflects the fundamental relation between citizens or taxpayers and state authorities. Using cash means freedom, independence and personal fulfillment for a citizen who doesn't want a state intervention when using cash. The "voices" calling for the limitation or abolishment of cash argue that tighter and more comprehensive state control over individuals' financial flows and funds will effectively fight crime, shadow economy and terrorism. But in my opinion we have weak empirical evidence."*

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[12] https://www.afr.com/property/residential/dirty-money-spotlight-on-estate-agents-20191107-p538ay

[13] https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bId=r6431

[14] Services which are defined under 'designated services' in the *Anti-Money Laundering and Counter Terrorism Financing Act 2006* include (1) financial services, (2) bullion, (3) gambling services and (4) prescribed services.

[15] http://www.econ.jku.at/papers/2017/wp1708.pdf

Imposition of Negative Nominal Interest Rates

From an economic freedom and wealth preservation perspective, I am concerned that the proposed laws would curtail the abilities of Australians to escape negative nominal interest rates if such a regime were to be imposed by the Reserve Bank of Australia (RBA).

In recent years, there have been a series of international calls from academic and institutional economists as well as elements of the global banking industry for the role of cash to either be significantly reduced or eliminated, given that the use of physical or digital cash outside of the government's control undermines the policy of negative nominal interest rates. This undermining occurs through the process of 'cash hoarding' which has been shown to be prevalent in some economies after the introduction of negative nominal interest rates, such as in Japan[16].

For example, the following papers and blog posts by economic authors at the IMF have argued that the elimination of cash from an economy would enhance the effectiveness of negative nominal interest rates:

- August 2018: *Monetary Policy with Negative Interest Rates: Decoupling Cash from Electronic Money*[17]
- February 2019: *Cashing In: How to Make Negative Interest Rates Work*[18]; and
- April 2019: *Enabling Deep Negative Rates to Fight Recessions: A Guide*[19]

Moreover, the IMF have argued that:

- during an economic recession, interest rates need to be lowered between 3% - 6% in order to stabilise the economy and to allow for economic growth to recover; and

- given that official interest rates are already very low around the world, deep negative interest rates of approximately -4% may be required if a global economic recession or global economic shock were to eventuate.

Given that the Australia's official cash rate currently sits at 0.75%, there is an increasing likelihood that the RBA may be motivated to implement negative nominal official interest rates, among a suite of other unconventional monetary policies, if the Australian economy were to fall into recession or if a global economic shock were to eventuate.

Under such a policy stance, Australians should have the fundamental economic and civil right to protect their private wealth independent of the commercial banking sector that would strip them of their wealth from the imposition of negative nominal interest rates.

Community fears regarding the implications of negative nominal interest rates are well justified given that they are in operation in many jurisdictions around the world including in several European countries as well as in Japan and that commercial banks such as in Denmark[20] are imposing negative nominal interest rates on retail bank deposits.

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[16] https://www.cnbc.com/2015/03/31/japanese-hoarding-300b-under-mattresses.html
[17] https://www.imf.org/en/Publications/WP/Issues/2018/08/27/Monetary-Policy-with-Negative-Interest-Rates-Decoupling-Cash-from-Electronic-Money-46076
[18] https://blogs.imf.org/2019/02/05/cashing-in-how-to-make-negative-interest-rates-work/
[19] https://www.imf.org/en/Publications/WP/Issues/2019/04/29/Enabling-Deep-Negative-Rates-A-Guide-46598
[20] https://www.bloomberg.com/news/articles/2019-08-20/richest-clients-at-jyske-now-face-negative-rate-on-big-deposits

Specific Concerns with the Proposed Law

I have a number of specific concerns in relation to the proposed bill and associated legislative instrument including:

- **Concern 1:** The proposed legislation and associated instrument may only be the first step in a series of escalating measures from the Commonwealth which seeks to infringe on the rights of individual Australians and Australian businesses to engage in commerce independent of the commercial banking sector and the RBA's monetary policy regime (especially if a policy of negative nominal interest rates is introduced in Australia).

- **Concern 2:** The Australian Government has not conducted a cost-benefit analysis of the proposed law and has not demonstrated to the Australian people that the proposed law will deliver verifiable quantitative and qualitative net benefits.

- **Concern 3:** Given that the exemptions to the CTB are defined in a legislative instrument and not in the proposed bill, this gives the Executive Government via the Assistant Treasurer significant flexibility to remove the exemptions without the robust scrutiny of Parliament.

- **Concern 4:** It is unclear how the Commonwealth intends to enforce the proposed CTB. Prior to the proposed law being passed by Parliament, the Government needs to provide clarity as to:

  - what enforcement techniques will the Commonwealth be expecting to use to monitor whether prohibited cash transactions above $AUD 10,000 are not entered into?

  - what operational resources will the Commonwealth be spending (including the dollar amount) in enforcing the proposed law?

  - whether relevant Commonwealth institutions are ready to implement the proposed law if it is enacted in early 2020?

Conclusion

In conclusion:

- the proposed bill and associated legislative instrument should not be enacted by parliament given that they are a gross abuse of Australians' economic and civil rights;

- the claims made by the BET that the size of Australia's black economy has been growing in the past two decades is disputed by international experts;

- economies such as Germany which still heavily rely on cash have smaller black economies as demonstrated by the 2015 black economy estimates by Schneider and Medina;

- economies which do have CTBs have larger black economies than Australia and according to Schneider and Medina have not seen a more rapid reduction in the size of their black economy for the period 1991 to 2015 with the exception of Romania;

- the Commonwealth and the BET have failed to establish robust empirical evidence that the proposed CTB will have any material impact in diminishing tax evasion and other black economy activities, especially given that the proposed cash threshold is $AUD 10,000;

- the lack of willingness by the Australian Government to address money laundering which is occurring through Australia's residential real estate sector (potentially running into the billions of Australian dollars) demonstrates that the Australian Government is not authentic and genuinely committed to tackling the black economy;

- tackling money laundering through Australia's residential real estate sector should take a higher priority by federal policy makers relative to addressing any concerns related to cash transactions;

- the proposed bill and associated legislative instrument make it increasingly difficult for Australians to escape the economic burdens that an official policy of negative nominal interest rates would carry (especially if the proposed exceptions were reversed); and

- there are several legitimate concerns with the proposed bill and associated legislative instrument that have not been adequately address by the Australian Government.

I hope this submission assists the Senate inquiry in adequately assessing the *Currency (Restrictions on the Use of Cash) Bill 2019* and the other associated policy issues.

Yours sincerely,

John Adams