



Law Council  
OF AUSTRALIA

3 March 2020

Senior Adviser  
Consumer and Corporations Policy Division  
Treasury  
Langton Cres  
PARKES ACT 2600

By email: [FSRCconsultations@treasury.gov.au](mailto:FSRCconsultations@treasury.gov.au)

Dear Sir/Madam

### Implementation of ASIC Enforcement Review Taskforce – Breach Reporting

1. The Law Council of Australia (**Law Council**) welcomes the opportunity to make a submission to Treasury in relation to the implementation of Financial Services Royal Commission recommendations 1.6, 2.7, 2.8, 2.9 and 7.2 as they relate to reference checking and information sharing, breach reporting and remediation.
2. The Law Council is a peak national representative body of the Australian legal profession. It represents the Australian legal profession on national and international issues, on federal law and the operation of federal courts and tribunals. The Law Council represents 60,000 Australian lawyers through state and territory bar associations and law societies, as well as Law Firms Australia.
3. This submission has been prepared by the Financial Services Committee of the Law Council's Business Law Section (**Financial Services Committee**), and the Superannuation Committee of the Law Council's Legal Practice Section (**Superannuation Committee**). The views of each contributor have been provided separately to ensure clarity of message.

#### Input from the Financial Services Committee of the Law Council's Business Law Section

4. The Financial Services Committee notes that there a number of issues raised by the proposed implementation of recommendations 1.6, 2.7, 2.8, 2.9 and 7.2 of the Financial Services Royal Commission. However, in light of the time allowed for submissions, the Committee has concentrated its response on two issues relating to breach reporting. In particular, the Financial Services Committee is concerned that:
  - the extremely low threshold for reportable breaches, irrespective of circumstances such as the number of customers affected or the impact; and
  - the requirement to report investigations, even if the investigation concludes there is no significant breach;

will significantly increase compliance costs in the financial services sector and have the following effects, amongst others:

- an anti-competitive effect – in particular, the increased cost will act as a barrier to entry and will have a disproportionate adverse effect across financial services participants;
  - a distorted perception of regulatory risk in Australia, having flow-on effects on capital investment, costs of capital and potentially increasing costs to consumers (with little to no corresponding benefit to consumers); and
  - stifling of innovation and growth.
5. The threshold for reporting includes a breach of any civil penalty provision in a range of legislation, including Chapter 7 of the *Corporations Act 2001* (Cth) (**Corporations Act**), the *National Consumer Credit Protection Act 2009* (Cth) (**NCCP Act**) and Division 2 Part 2 of the *Australian Securities and Investments Commission Act 2001* (Cth). It also includes any offence provision that is punishable on conviction by a penalty that may include imprisonment for a maximum period of three months or more (where the offence involves dishonesty) or 12 months or more (in any other case).
  6. The Financial Services Committee notes that the legislation to which those obligations apply is highly prescriptive, setting out an extensive range of highly detailed and specific requirements relating to matters such as the form and content of disclosure, when and how it is to be given, all of which can vary depending upon the circumstances, as well as other conduct matters. Most of these highly prescriptive provisions are civil penalty offence provisions. Accordingly, any breach of them, no matter the number of customers affected, customer detriment or other impact, will be required to be reported under the proposed measures.
  7. As the Australian Securities and Investments Commission (**ASIC**) has acknowledged, occasional and minor breaches do not of themselves mean that compliance arrangements are inadequate and compliance arrangements are unlikely to ensure full compliance with every aspect of the law at all times.<sup>1</sup> Accordingly, notwithstanding the best intentions and efforts of financial services participants, it is highly likely there will be breaches of these provisions. However, there will be a wide spectrum of impacts, which will depend upon the circumstances. At one end of the spectrum, there will be breaches that are very limited and have little or no customer impact. Notwithstanding that, the proposed legislation requires these breaches to be reported. In those circumstances, the cost of establishing and maintaining a compliance regime in relation to breach reporting is likely to be significant.
  8. The Financial Services Committee submits that the issue is compounded by the fact that, under the proposed measures, financial services participants will be required to report not just breaches, but also investigations commenced by a financial services licensee into whether that financial services licensee or a representative of that financial services licensee has breached a core obligation. The issues with this requirement include:
    - the term ‘investigation’ is a potentially very broad term. For example, it may include usual business activities such as audits and quality control assessments; and
    - the utility of the reports may be of marginal utility or will be duplicative. A report of an investigation is likely to be of marginal utility where the outcome of the

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<sup>1</sup> See Australian Securities and Investments Commissions *Regulatory Guide 78: Breach reporting by AFS licensees* (February 2014), 8.

investigation is that there has not been a relevant breach. A report of an investigation will be duplicative where the outcome of the investigation is that there has been a relevant breach because the financial services participant would in any event be required to report that breach.

9. In light of the above, the Financial Services Committee is concerned that these aspects of the proposed measures will have the following significant adverse impacts:
  - it will create additional compliance burdens and will increase costs, which is likely to have the flow on effect of increasing costs to consumers or reducing returns to shareholders (with little to no corresponding consumer benefit). In addition, as there will be a certain level of fixed costs associated with compliance with the provisions, those costs will disproportionately affect smaller participants and act as a further barrier to entry for new participants;
  - it will influence perceptions of risk of the financial services industry in Australia, as a result of the publication of information about reported breaches. In particular, this has the potential to distort investors' perceptions of the investment risk in Australia and adversely impact investor confidence in and willingness to inject capital into the Australian financial services industry, or may lead to higher costs of capital. This, again, would have disproportionate effects across industry participants; and
  - as a consequence of the two points above, innovation and growth in the financial services industry in Australia is likely to be stifled by creating conditions that, essentially, require participants to redirect their resources to compliance as opposed to development and other activities. This will have the detrimental effect of discouraging an inflow of new market players and severely disadvantaging those domestic participants who do not have the resources to meet the new compliance requirements.
10. Accordingly, the Financial Services Committee submits that:
  - the proposed Bill should be amended so that an assessment of significance, which is currently set out in paragraph 912D(1)(b) of the Corporations Act and as proposed in the Bill for subsection 50A(6) of the NCCP Act, is applied to all breaches and likely breaches. The assessment should involve a consideration of whether there are reasonable grounds to believe that the breach or likely breach is significant having regard to those circumstances. If there are, the breach or likely breach should be reported; and
  - the proposed Bill should be amended to remove the requirement to report investigations.
11. Due to the issues set out above, the Financial Services Committee submits that it will be fundamentally important for due consideration to be given to and appropriate consultations engaged in on the consequences that will flow from the regime. The underlying objective should be to achieve a regulatory regime that adequately addresses governance, accountability and transparency goals while promoting competition and growth, and positioning Australia as a frontier for business innovation. As set out above, the Financial Services Committee has concerns that the proposed measures do not achieve this objective.

Input from the Superannuation Committee of the Law Council's Legal Practice Section

12. The Superannuation Committee notes that permitting regulations to add to the list of 'core obligations' would be, on balance, appropriate. There is also reference to other 'additional reportable situations' deemed reportable whether regarded as 'significant' or not, including where aware of serious fraud or conduct constituting 'gross negligence' by licensee or its representative.
13. The Superannuation Committee has queried the differentiation between 'ordinary' negligence and 'gross' negligence – a distinction which is not clearly recognised under current law. 'Serious fraud' is defined under the Corporations Act, so that cross-reference can work.
14. In addition, the Superannuation Committee notes that the publication of breach reporting data could be extremely damaging for licensed operators where news reporting may not have regard to mitigating factors. In publishing such data, and for perspective, the Superannuation Committee submits that it should also be a requirement for ASIC to indicate the extent to which:
  - an organisation has committed to remediate for any direct financial loss arising from the breach – this could be updated progressively as remediation occurs, in accordance with ASIC direction/requirements; or
  - the licensee is acting or not acting in accordance with ASIC directions on remediation required.
15. Finally, the Superannuation Committee submits that no fund identifiable data should be published until it is accepted that 'wrongdoing' has occurred. It is suggested that to do otherwise runs the risk of provoking a 'run on the fund' detrimental to the interests of all members. Self-reporting programs would also be assisted by specified penalty reductions that would ordinarily apply, where good faith reporting occurs.

The Law Council would welcome the opportunity to discuss this submission further with Treasury. In the first instance, please contact [REDACTED]

Yours faithfully

*Margery Nicholl.*

**Margery Nicholl**  
**Acting Chief Executive Officer**