



14 February 2020

Manager, Redress and Accountability Unit
Financial Services Reform Taskforce
The Treasury
Langton Crescent
PARKES ACT 2600

By email: FAR@treasury.gov.au

Dear Treasury

Financial Accountability Regime (FAR) Proposal Paper

Thank you for the opportunity to respond to the FAR Proposal Paper dated 22 January 2020. My response is provided as an expert in corporate law and regulation¹ and is not provided on behalf of or endorsed by any of the organisations with which I am professionally affiliated.²

I note that only 23 days has been allowed to formulate and provide this feedback. I also note Treasury's instruction that '[f]eedback should be focussed on how the proposal is best implemented, not whether it should be implemented'. Neither of those things is acceptable in a proper law reform process. The FAR Proposals go much further than Recommendations 3.9, 4.12, 6.6, 6.7 and 6.8 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. The FAR Proposals significantly affect the rights of individuals and for that reason require much more scrutiny than this process allows.

I will keep my feedback brief. I have three substantive objections to the FAR Proposals.

Civil penalties for accountable officers

My first objection is to the imposition of civil penalties on accountable officers under this regime. I note that breach of the accountability obligations under the BEAR do not currently attract civil penalties and this was not a recommendation of the Royal Commission.

The FAR Proposal is that 'individuals will be subject to civil penalties for breaches of their accountability obligations. The maximum civil penalties will be consistent with the newly-introduced

¹ <https://www.business.unsw.edu.au/our-people/pamela-hanrahan>.

² I am a Professor of the UNSW Business School Sydney, a Senior Fellow of the Melbourne Law School, a member of the Centre for Law Markets and Regulation at UNSW Sydney, and an associate of the Centre for Corporate Law at the University of Melbourne. I am a solicitor member of the Law Society of New South Wales and a Fellow of FINSIA. I am a member of the executive board of the Business Law Section (BLS) of the Law Council of Australia and a member of the Corporations Committee of the BLS. I am also a member of the National Corporate Governance Committee of the Australian Institute of Company Directors (AICD).

maximum penalties for individuals under the Corporations Act, ASIC Act, Credit Act and Insurance Contracts Act and any penalties are imposed by a court. The maximum penalties will be the greater of the following: (1) 5,000 penalty units (currently \$1.05 million); or (2) if the court can determine – the benefit derived or detriment avoided because of the contravention, multiplied by three’.

The accountability obligations require affected individuals to: ‘(1) act with honesty and integrity, and with due skill, care and diligence; (2) deal with APRA in an open, constructive and cooperative way (noting that this will not displace legal professional privilege); (3) deal with ASIC in an open, constructive and cooperative way (noting that this will not displace legal professional privilege); (4) take reasonable steps in conducting those responsibilities to prevent matters from arising that would adversely affect the prudential standing or prudential reputation of the entity; and (5) take reasonable steps in conducting their responsibilities as an accountable person to ensure that the entity complies with its licensing obligations’.

Making these obligations civil penalty provisions, without proper consultation, is unacceptable for two reasons. The first is concerns the nature of the accountability obligations themselves, and the second concerns the nature of the civil penalty regime.

Making the accountability obligations civil penalty provisions transforms their legal character from being matters to which APRA may have regard in deciding to disqualify an individual (a decision reviewable by the AAT) into a legal duty attaching the individual concerned. Accountability obligations 1, 4 and 5 expand the existing s 180 of the *Corporations Act 2001* (Cth), both in terms of the classes of persons to whom it applies (who may not all be officers within the meaning of that Act) and by imposing new statutory duties. Obligation 1 imposes a new statutory duty to act with ‘integrity’, an indeterminate concept with no settled legal meaning. Obligation 5 imposes a new statutory duty to ‘take reasonable steps in conducting their responsibilities as an accountable person to ensure that the entity complies with its licensing obligations’. Accountability obligations 2 and 3 put individuals in the position where their capacity to defend themselves in situations where the conduct of their employer has attracted regulatory attention is fatally compromised. This problem is not solved by purporting to protect client legal privilege.

Civil penalty provisions involve the use of the powers and resources of the state to prosecute individuals without those individuals having the benefit of the full rights, privileges and protections provided by the criminal law.³ Very significant penalties – sometimes penalties larger than the fines that can be imposed for similar conduct that is criminal – can result. As the Australian Law Reform Commission’s *Freedoms Inquiry* observed in 2015, ‘A person may be denied their criminal process rights where a regulatory provision is framed as a civil penalty, when it should—given the nature and severity of the penalty—instead have been framed as a criminal offence’.⁴

List of particular responsibilities

The FAR Proposals allow APRA and ASIC, rather than the Parliament, to decide the class of persons to whom the accountability obligations should apply through the ‘particular responsibilities’ power. Therefore, the process by which this occurs is important.

Section 37BA(4) of the *Banking Act 1959* (Cth) currently allows APRA, by legislative instrument, to determine a responsibility for the purposes of s 37BA(2)(b)(ii). A person who has that responsibility becomes an accountable person. This is to be extended; the FAR Proposal is that ‘APRA and ASIC will

³ This issue is discussed in *ASIC Enforcement Review Taskforce* (Final Report, December 2017) 77-9.

⁴ Australian Law Reform Commission, *Traditional Rights and Freedoms— Encroachments by Commonwealth Laws* (Report 129, December 2015) [8.171].

be able to prescribe additional particular responsibilities over time and will also be able to prescribe particular responsibilities in respect of foreign entities subject to the FAR’.

Many of the indicative responsibilities in Annexure B are inappropriate. It is important that this power may only be exercised by disallowable legislative instrument given that the practical effect is to expand the class of individuals to which the regime applies.

Extension to ASIC regulated entities

After the Royal Commission delivered its Final Report, the Government unilaterally decided to extend the executive accountability regime to entities regulated solely by ASIC. The Government’s proposal was that a ‘new ASIC-administered accountability regime will apply to AFSL and ACL holders, market operators, and clearing and settlement facilities’.⁵ These entities are not ipso facto prudentially regulated.

The FAR Proposal is that ‘extension of FAR beyond all APRA regulated entities is proposed to be facilitated by providing the Minister a power to make a legislative instrument that would allow solely ASIC regulated entities to be brought in to the scope of the regime’.

This is a serious reform that will affect many thousands of small businesses and their directors, officers and other executives. Its implications were not considered by the Royal Commission. If it is to happen, it should be the subject of proper Parliamentary debate and scrutiny, not something to be done by the Executive.

The BEAR is narrowly framed specifically to address matters that have the potential to impact on prudential considerations. Those close to the BEAR debate will remember that the Government wanted accountability obligations to embrace conduct as well as prudential matters,⁶ but this was explicitly abandoned (following consultation) in what is now ss 37C(c) and 37CA(1)(c) of the *Banking Act 1959* (Cth). That relevant accountability obligation in BEAR only covers ‘matters ... that would adversely affect the prudential standing or prudential reputation’ of the ADI. The rationale for prudential regulation of some financial sector entities but not others is explained in the Wallis Committee and Murray Committee reports⁷ and reflects the systemic risk caused by financial or non-financial problems in those institutions. It is not clear why the BEAR framework should be untethered from that reasoning. If this is part of a broader push to make ASIC a prudential regulator of AFSL and ACL holders,⁸ which may or may not be appropriate, this should be subject of a proper and principled review. The Minister should not be given the power to extend the regime in this way.

Yours faithfully

Dr Pamela Hanrahan

Professor of Commercial Law and Regulation
UNSW Business School, Sydney

⁵ *Government Response to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (February 2019) 33.

⁶ Treasury, *Banking Executive Accountability Regime Consultation Paper* (July 2017) Ch 5.

⁷ *Financial System Inquiry Final Report* (1996) Ch 8; *Financial System Inquiry Final Report* (2014) Ch 5.

⁸ In the same way that the Financial Conduct Authority in the United Kingdom is a prudential regulator of 50,000 financial firms not regulated by the Bank of England.