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Dear Sirs

ASIC's power to ban senior officials in the financial sector

Clifford Chance welcomes the opportunity to make submissions in relation to ASIC Enforcement Review Position and Consultation Paper 6 dated 6 September 2017, on enhancing ASIC's banning power to enable it to take appropriate action to ban senior managers from managing financial services businesses.

Clifford Chance

We are one of the world's pre-eminent law firms, with more than 3,300 lawyers across 5 continents led by a single integrated partnership.

We have significant experience working with global banking and financial services clients in relation to individual accountability regimes, including the FCA Approved Persons regime and the Senior Managers and Certification Regime (SMR) in the United Kingdom, and Hong Kong Manager-in-Charge Regime. We have also prepared joint submissions on behalf of global banks to regulators in relation to the SMR and assisted regulators (via secondees) with drafting proposed rules and consultation papers.

Submissions

Our views and recommendations expressed below are confined to the Australian commercial and jurisprudential context. Further, the content of our submissions are not intended to be exhaustive nor do they constitute legal advice.

In addition to addressing the questions in the Consultation Paper, we have raised some further matters for consideration.

1. *Is it appropriate that ASIC's power to ban individuals be broadly cast? If not, how should the power be framed? If limited to a ban from managing financial services business how should the term 'management' be defined?*

In our view, any power to ban an individual should be cast in such a way as to ensure that any ban is reasonable and proportionate to the severity of the risk posed by the individual. By its very nature, therefore, the power to ban should only apply to functions which risk significant harm to the financial services business or its customers if performed improperly. The individuals performing these functions will often fall within the definition of officers or senior managers in the Corporations Act 2001 (Cth) (**Corporations Act**).

Reasonableness and proportionality also dictates that any banning power should include a range of bans, such as the three levels of ban proposed by the Taskforce in its preliminary position 1. However, it must be recognised that the options proposed vary in their severity and will therefore be subject to differing threshold jurisdictional considerations. An individual's suitability to perform a function – whether that suitability is to be adjudged by reference to fitness and propriety or some other quality – will need to be measured against the circumstances of each case, the range of functions which the individual performs, the nature of the financial services business and the risks posed by the individual.

There will be circumstances in which it might be reasonable and proportionate to ban an individual from performing a specific function for which they are insufficiently qualified or otherwise unfit to perform, but it would not be appropriate or necessary to ban the individual from taking any part in the management of a financial services business. We submit that only in the rarest of circumstances would it be reasonable and proportionate to ban an individual not only from providing a financial service or being involved in a *specific function* or in the *management* of a financial services business, but from performing *any function at all* in the business.

2. *Is it appropriate that these expanded powers to ban also apply in respect of credit businesses?*

If it is proposed that the expanded powers also be available in respect of credit businesses, then the above principles should also apply to the exercise of those powers in respect of credit businesses, i.e.:

- such powers should be cast in such a way as to ensure that any ban is reasonable and proportionate to the severity of the risk posed by the individual;

- such powers should only apply to functions which risk significant harm to the credit business or its customers if performed improperly; and
- there should be a range of bans varying in their severity, which are subject to differing threshold jurisdictional considerations.

3. *Should the 'good fame and character' test in section 920A of the Corporations Act be replaced by a 'fit and proper person' test?*

If ASIC is to be granted a power to ban individuals from performing specific functions, or from being involved in any function, in a financial services business, then in our view ASIC's banning power should be based on a fit and proper test rather than a good fame and character test, so as to ensure that it is not subject to any lesser jurisdictional threshold than APRA's disqualification powers.

However, since fitness and propriety are broader concepts than good fame and character, they are prone to more subjective interpretation. In the financial services context, they have their roots in principles-based regulation in the UK and elsewhere, but are largely untested in Australia. APRA has recognised this and has developed detailed prudential standards (CPS 520) setting out minimum requirements for APRA-regulated institutions in determining the fitness and propriety of individuals to hold positions of responsibility. The UK Financial Conduct Authority (FCA) has also issued detailed guidance on how fitness and propriety is to be assessed (see the FCA Handbook, FIT), covering such matters as the circumstances to be taken into account and the qualities to be considered (including the individual's honesty, integrity, reputation, competence, capability and financial soundness, among other criteria).

More – and, importantly, consistent – guidance would be needed both from ASIC and APRA, to ensure that financial services businesses and individuals are clear on the standards required. Without proper guidance and a clear framework for assessing fitness and propriety, there is a strong risk that the test will be applied inconsistently and inequitably. It is critical for the stability of the financial sector generally that financial services businesses are able to assess the suitability of candidates, including their fitness and propriety, by reference to clear and practical guidance and a proper framework.

4. *Should the positions outlined above, so far as they relate to senior officials, adopt the current definitions of 'officer' and 'senior manager' in the Corporations Act? Or should some other definition/s be used?*

We consider the current definitions of "officer" and "senior manager" to be adequate. However, these terms encompass a variety of functions and the suitability of

individuals to perform a particular function will need to be assessed against each function separately, according to each function's own suitability criteria. Hence, any power to ban should include (or be restricted to) the power to ban an individual from performing a particular function, rather than banning an individual from being an "officer" or "senior manager" per se.

5. *Is it appropriate that ASIC have power to ban individuals involved in phoenixing activity and are the positions outlined [in the consultation paper] appropriately cast? Should this ground be limited to phoenixing activity within a certain period and should the banning period for phoenixing activity be capped (as it is for director disqualifications under section 206F of the Corporations Act)?*

In our view, it is unnecessary to single out phoenixing activity as a basis upon which an individual may be banned. Rather, phoenixing activity should be considered as a matter which may be relevant in assessing an individual's fitness and propriety to continue to perform a specific function, insofar as it may cast doubt on an individual's honesty and integrity, and financial soundness.

It would be improper to conclude that a person is unfit to perform a specific function simply on the basis that the person was involved in phoenixing activity. The fit and proper test is an inherently forward-looking test, and natural justice dictates that an investigation would be necessary to determine whether and to what extent past conduct, including involvement in phoenixing activity, is conclusive of ongoing suitability to perform the function in question. It would be necessary to take into account all matters relevant to assessing the individual's honesty and integrity, and financial soundness. These are the same principles which underpin the requirements of section 206F(b) and (c) of the Corporations Act.

As to whether a time limitation should apply, we submit that any assessment of a person's fitness and propriety to undertake a particular function by reference to their past conduct should take into account how long ago that conduct occurred. It is inherently unlikely that phoenixing activity which occurred in the very distant past will of itself be conclusive of a person's unfitness in the present. However, if it is proposed that there be a separate power to ban based on the person's involvement in phoenixing activity, then we submit this power should be consistent with the power in section 206F of the Corporations Act 2001, including incorporating a time limit.

6. *Should ASIC be able to impose a ban based on a breach by an individual of a duty under sections 181, 182 or 183 of the Corporations Act? What would be the implications of allowing ASIC to ban based on a breach of section 180?*

In our view, breach of a directors' duty is not in and of itself a sound basis for banning an individual. However, a breach of a directors' duty may be relevant in assessing an individual's fitness and propriety to continue to perform a specific function. For example, a breach of section 180 may cast doubt on the individual's competence and capability to perform the function in question, but the conclusion that the individual is incompetent or incapable of continuing to perform the function does not necessarily follow. Natural justice dictates that an investigation would be necessary to determine whether and to what extent past conduct is conclusive of ongoing suitability to perform the function in question. Similarly, a breach of the section 181 duty to act in good faith and for a proper purpose, or the sections 182 and 183 duties not to misuse a position, may cast significant doubt on the person's honesty or integrity, but again it would be improper to reach this conclusion without investigating the question further and taking into account all matters relevant to assessing the individual's honesty and integrity.

Thank you for considering our submission in relation to Consultation Paper 6.

If you wish to discuss our submission, please contact Angela Pearsall, Partner at angela.pearsall@cliffordchance.com, Jenni Hill, Partner at jenni.hill@cliffordchance.com, Kirsten Scott, Counsel at Kirsten.scott@cliffordchance.com or Jason Oliver, Senior Associate at jason.oliver@cliffordchance.com.

Yours faithfully



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