FBAA

Your Choice, Your Voice

ASIC Enforcement Review
Financial Systems Division
The Treasury
Langton Crescent
PARKERS ACT 2600

12 May 2017

ASICenforcementrev ew@treasury.gov.au

Positioning and Consultation Paper 1
Self-Reporting of Contraventions by Financial Services and Credit Licensees

FBAA Response to each Position in the paper

Framing Statement
The FBAA generally supports the introduction of mandatory breach self-reporting obligations for credit licensees.

The current requirement for credit licensees to report significant breaches annually at the time of renewing the credit license through lodging an annual compliance certificate is not effective.

The objectives of timely breach reporting are identified in the position paper as being aimed at enhancing ASIC's ability to:

1.1. Monitor the extent and severity of non-compliance and commence surveillances and investigations where necessary;
1.2. Take law enforcement and regulatory action where warranted, including administrative action to protect consumers of financial products and services; and
1.3. Identify and respond to emerging risks and trends within the financial services industry.

The FBAA is concerned to ensure any proposed obligations remain meaningful and manageable for licensees. Excessive reporting merely loads up licensees with additional obligations and leads to ASIC being inundated with information it cannot use and does not need.

Please see as follows as submitted on behalf of the FBAA, the leading national professional association to finance and mortgage brokers.

Yours faithfully

Peter J White CPFB FMDI MAICD
Executive Director

t: 1300 130 514 f: 07 3041 0350
Level 1, 116 Ipswich Road, Woolloongabba Qld 4102
PO Box 234, Stones Corner Qld 4120
www.fbaa.com.au ABN: 22 094 784 040

Position 1: The 'significance test' in section 912D of the *Corporations Act 2001* (Cth) should be retained but clarified to ensure that the significance of breaches is determined objectively.

Questions against Position 1

1.1 Would a requirement to report breaches that a reasonable person would regard as significant be an appropriate trigger for the breach reporting obligation?
1.2 Would such a test reduce ambiguity around the triggering of the obligation to report?

FBAA Response

We recognise that this question is framed around s912D of the Corporations Act and relates to financial services, however we see parallels with consumer credit that make a response to this question equally relevant for credit licensees.

Licensees should report a breach to ASIC any time there is any doubt about whether a breach is reportable or not. This is already made clear in RG78.

Licensee conduct is more likely a cause of breaches not being reported to ASIC than any ambiguity over which breaches to report, although we recognise there are some legitimate situations where it may be unclear. Further regulation needs to balance the genuine need for further clarity against the desire to make recalcitrant licensees more accountable. Those intent on shirking their obligations will respond better to a stronger penalty regime than from imposing further obligations which impact the entire regulated population.

The FBAA supports retaining the 'significance' test and introducing objective measures to support the 'significance' test.

The current structure favors large licensees because the impact of specific breaches is less likely to materially impact their ongoing viability. Licensees who under-report place more emphasis on this than other elements identified in s912D of the Act namely:

- the number or frequency of similar previous breaches;
- the impact of the breach or likely breach on the AFS licensee's ability to provide the financial services covered by the licence;
- the extent to which the breach or likely breach indicates that the AFS licensee's arrangements to ensure compliance with those obligations is inadequate;
- the actual or potential financial loss to clients of the AFS licensee, or the AFS licensee itself, arising from the breach or likely breach; and
- any other matters prescribed by regulations made for the purposes of section 912(1)(b).

We recommend setting objective reporting criteria around conduct issues and financial thresholds.

The example provided at paragraph 23 of the consultation paper describes a situation where an individual adviser has misappropriated $1m from a single client. In our view this would always be a reportable breach regardless of the financial impact on the licensee. The purpose of reporting this is to provide ASIC with information on which it can take action to remove the adviser from the industry. The client has remedies against the licensee through IDR, EDR and court and ASIC would be unlikely to individually resource an action aimed at recovering for one client.

For the above example, objective criteria that could be added to the obligation to report a breach include:

- A requirement for a licensee to notify ASIC about all conduct matters that result in an adviser being dismissed or otherwise leaving the licensee; and
- A requirement to notify ASIC for any client losses exceeding a particular dollar threshold. The amount should be open for further discussion.

The FBAA does not consider that introducing a requirement to notify ASIC of matters that a "reasonable person would regard as significant" will provide any more clarity than the existing regime. It remains subjective.

FBAA does not support mandatory breach reporting obligations being written into ASIC regulatory guidance. Regulatory guidance is not law and should not be used as a lawmaking instrument. Regulatory guidance is of itself subjective and its open to the interpretations of the staff within ASIC at any given time. In the credit space, one need look no further than RG209. Despite not having changed significantly since 2009 when it was first written, ASIC's enforcement attitude and approach has changed markedly. There remains a great deal of ambiguity in the interpretation and application of responsible lending laws despite RG209.

Position 2: The obligation for licensees to report should expressly include significant breaches or other significant misconduct by an employee or representative.

The FBAA strongly supports extending the breach reporting requirement for licensees to report on matters involving the conduct of an employee or representative where such matters involve:

- fraud
- concerns about propriety (good fame and character) of a representative
- concerns about a representative's competency where they are unwilling or unable to demonstrate improvement, leading to their dismissal.

We do not support mandatory reporting to ASIC where a representative becomes an insolvent under administration unless it goes to their competency to discharge their duties in the specific role. For example, it would not be a matter for ASIC if their insolvency comes about due to marital breakdown or other situation that is not relevant to their licensed activities.

Question against Position 2

2.1 What would be the implications of this extension of the obligation of licensee's to report?

Licensees would be required to notify all representatives to ASIC where there is a belief or suspicion about that representative's integrity or competency. This is a positive outcome that reduces instances of bad apples remaining in the industry.

Position 3: Breach to be reported within 10 business days from the time the obligation to report arises.

Questions against Position 3

3.1 Would the threshold for the obligation to report outlined above be appropriate?
3.2 Should the threshold extend to broader circumstances such as where a licensee "has information that reasonably suggests" a breach has or may have occurred, as in the United Kingdom?
3.3 Is 10 business days from the time the obligation to report arises an appropriate limit? Or should the period be shorter or longer than 10 days?
3.4 Would the adoption of such a regime have a cost impact, either positive or negative, for business?

The FBAA agrees the obligation to report a breach should be an objective threshold from when the licensee first becomes aware of the breach or ought reasonably to have become aware. We support the 30 calendar day reporting period as used in the FINRA model in the US.

We do not consider it necessary to adopt broader wording such as having information that "reasonably suggests" a breach. "Becomes aware or ought reasonably to have become aware" is sufficiently detailed.

We believe 10 days is too short. The US model of requiring a report 'promptly and not later than 30 calendar days' would seem more reasonable. Breaches are often not clear cut and licensees will sometimes become aware of a potential breach from just a small amount of information. This can often mean a licensee requires a reasonable period of time to gather all of the relevant facts and information before making an informed decision. Whilst licensees can strive to gather all relevant information within a 10 day period, it will often be difficult. In many cases for credit providers it may entail making inquiries and asking for information from third parties.

We have no information before us that indicates any detriment would be caused by a 30-day breach reporting ceiling rather than 10. Licensees would make more complete and better informed reports to ASIC with the benefit of the additional time. Changing from 10 business days to 30 calendar days can lead to increases of as little as 16 days in the reporting time limit ceiling.

Licensees have always been able to elect to report within a shorter timeframe than the stipulated maximum. Licensees regularly provide ASIC with an initial breach report and provide further information as it comes to hand.

Inevitably all regulatory imposts have a negative cost impact on business. This will be particularly true for credit licensees who are currently not required to monitor breaches for the purposes of near real-time reporting (they must currently only notify significant breaches at the time of completing their annual compliance certificate. Whilst this still requires credit licensees to monitor for breaches and remedy them once identified, the immediacy of monitoring and reporting is not present as it is with financial services licensees.) Credit licensees will need to adopt new systems and processes to be able to monitor and report breaches in near real time.

Position 4: Increase penalties for failure to report as and when required.

Our response to Positions 4 through 7 is provided under Position 7 below.

Position 5: Introduce a civil penalty in addition to the criminal offence for failure to report as and when required.

Our response to Positions 4 through 7 is provided under Position 7 below.

Position 6: Introduce an infringement notice regime for failure to report breaches as and when required.

Our response to Positions 4 through 7 is provided under Position 7 below.

Position 7: Encourage a co-operative approach where licensees report breaches, suspected or potential breaches or employee or representative misconduct at the earliest opportunity.

Questions against Positions 4 - 7

4.1 What is the appropriate consequence for a failure to report breaches to ASIC?
4.2 Should a failure to report be a criminal offence? Are the current maximum prison term and monetary penalty sufficient deterrents?
4.3 Should a civil penalty regime be introduced?
4.4 Should an infringement notice regime be introduced?
4.5 Should the self-reporting regime include incentives such as that outlined above? What will be effective to achieve this? What will be the practical implications for ASIC and licensees?

FBAA Response

Failure to report material breaches to ASIC should attract a penalty where such failure to report is intentional or recklessly indifferent. We support a criminal and civil penalty regime.

Infringement Notice Regime

We are concerned with the concept of introducing a mandatory, near real-time breach reporting obligation coupled with an infringement notice regime. We note the financial services laws do not have an infringement notice regime whereas the infringement notice regime is already being used in the consumer credit space. Any penalty regime must be applied equally to financial services and consumer credit. Credit licensees should not be subject to any additional sanctions or penalties merely because the infringement notice regime already exists under the credit legislation.

It is essential that there be safe harbours for licensees reporting breaches in good faith. If an infringement notice regime is further explored, FBAA would suggest that the issuance of an infringement notice would only occur where a licensee cannot satisfy the safe harbour requirements. We recognise that self-reporting breaches should not grant immunity to a licensee from prosecution or civil penalty, and that some breaches, if significant, may require penalties to be imposed. Significant further work is needed to identify an appropriate threshold.

In addition to, or as an alternative to the matters listed in paragraph 68 of the Consultation Paper, safe harbour requirements could require a licensee to demonstrate that it had adequate measures in place to detect and report breaches, that the measures led to the breach being reported and that it proposes a reasonable remedy for the breach (or is working through the issues to determine the scope and severity).

FBAA does not support the suggestion in paragraph 70 of allowing an 'uplift' or 'discount' in the penalty based on the cooperation of the licensee. This introduces too much discretion and would not be transparent.

Position 8: Prescribe the required content of reports under section 912D and require them to be delivered electronically.

Questions against Position 8

5.1 Is there a need to prescribe the form in which AFS licensees report breaches to ASIC?
5.2 What impact would this have on AFS licensees?

FBAA Response

Yes. The form for licensees to report breaches to ASIC should be prescribed. It provides certainty and clarity for licensees.

Position 9: Introduce a self-reporting regime for credit licensees equivalent to the regime for AFS licensees under section 912D of the Corporations Act.

Questions against Position 9

6.1 Should the self-reporting regime for credit licensees and AFS licensees be aligned?
6.2 What will be the impact on industry?

FBAA Response

The FBAA supports introducing self-reporting for the credit industry and agrees the regime should be aligned with the financial services regime.

As indicated in our response to Position 8, we want to ensure there is moderation in the issuance of infringement notices where licensees self-report breaches. Further work is required to develop this.

Imposing any new regulatory obligations on businesses will have an impact. There will be considerable time cost as well as financial cost for licensees to establish a breach reporting framework and to educate their staff.

We recommend a reasonable transition period be given to credit licensees if a self-reporting regime is introduced.

Position 10: Ensure qualified privilege continues to apply to licensees reporting under section 912D.

The FBAA makes no submission on this Position.

Position 11: Remove the additional reporting requirement for responsible entities.

The FBAA makes no submission on this Position.

Position 12: Require annual publication by ASIC, of breach report data for licensees.

Questions against Position 12

8.1 What would be the implications for licensees of a requirement for ASIC to report breach data at the licensee level?

8.2 Should ASIC reporting on breaches at a licensee level be subject to a threshold? If so, what should that threshold be?

8.3 Should annual reports by ASIC on breaches include, in addition to the name of the licensee, the name of the relevant operational unit within the licensee's organisation? Or any other information?

FBAA Response

We agree with the Taskforce that reporting of individuals based on breach reports would be inappropriate.

We do not support publishing breach data at a licensee level. The purpose of breach reporting is to enhance ASIC's regulatory functions. It is not to embarrass or tarnish the name of a licensee. Reporting at a licensee level would potentially penalise the more vigilant or those licensees that err on the side of caution and over-report.

If, as a result of the breach report, ASIC conducts further investigations that lead to public outcomes then the licensee can be named. ASIC can, at the time of making this information public, reference the fact that the matter commenced through a breach report. There is no public interest element served by naming licensees solely for information passed through via breach reports.

Concomitantly, any proposal to introduce licensee level breach reporting introduces further complexity in attempting to determine materiality thresholds for reporting. We do not believe this is necessary and the notion should be abandoned.

End.