

**INDUSTRY NEWS**

# ASIC Proposes Reforms to AFSL Breach Reporting Regime

Over the past decade the self-reporting regime for Australian Financial Services Licensees (Licensees), contained within s912D of the *Corporations Act 2001* (the Act), has come under increasing scrutiny.

As part of its Terms of Reference the ASIC Enforcement Review Taskforce (the Taskforce) was asked to review the adequacy of the breach reporting regime. The Taskforce has produced a consultation paper 'Self-Reporting of contraventions by financial services and credit licensees' which identifies concerns within the current self-reporting regime and proposes preliminary reforms to address them. The proposed reforms are broadly outlined below.

**The significance test**

Presently a Licensee is required to self-report to ASIC any significant breaches (or likely breaches) of its obligations as a licensee. The key trigger for the obligation to report being the "significance" of the breach. The subjectivity in determining whether or not a breach is significant has led to inconsistent reporting and uncertainty according to ASIC. For example, the Taskforce noted that while all Licensees have an obligation to self-report, the differing scale, nature and complexity of their respective businesses can mean that larger organisations need to report fewer breaches or less often.

The Taskforce has proposed that the subjective test be amended to provide that significance is to be determined by reference to an objective standard. Effectively a Licensee would be obliged to report to ASIC any breaches "that a reasonable person would regard as significant" and for which "the regulator would reasonably expect notice". Significance is still to be determined with regard to the various factors set out in 912D(1)(b) of the Act. However

these factors may be supplemented by regulatory guidance from ASIC that specifies certain types of breaches it considers should always be reported.

**Obligation to report conduct of Employees and Authorised Representatives**

Currently, the reporting obligation applies to breaches by the Licensee. While Licensees are usually responsible for the conduct of employees and representatives there are occasions where ambiguity can arise as to whether a breach by a representative should be reported to ASIC.

The Taskforce has proposed that the obligation to report be extended to specifically require Licensees to report the misconduct of its employees and representatives. Complimentary reforms are to be proposed to ensure that in these circumstances Licensees will attract qualified privilege to protect them from liability when making reports to ASIC in good faith and accordance with the regime.

**Time to report**

Currently, the period by which a Licensee must report a breach to ASIC is 10 business days. This is taken from the point in time that the Licensee has become aware of the breach and determined that it is of sufficient significance to report.

The Taskforce has suggested that the 10 business day timeframe commence from the point in time where the AFS licensee "becomes aware of, or has reason to suspect a breach has occurred, may have occurred or may occur rather than when the licensee determines that the relevant breach has occurred and is significant".

### **Lack of flexibility for sanctioning**

ASIC's current options for sanctioning a failure to report are limited to a criminal offence and a moderate fine. The Taskforce has suggested that both the existing financial and criminal penalties should be increased to deter deliberate non-compliance by Licensees.

Moreover, it was proposed that ASIC should be given additional powers to sanction non-compliance. These include the introduction of a civil penalty and the authority to issue infringement notices for uncomplicated contraventions that do not involve a deliberate failure to not report.

To encourage a co-operative approach between Licensees and ASIC, where breaches are reported at the earliest opportunity, the Taskforce has proposed the creation of a formal provision expressly allowing ASIC to decide not to take action in respect of a Licensee when they self-report and certain additional requirements are satisfied. These may include the breach having been addressed or remedied to ASIC's satisfaction.

### **Submission and content of reports**

While the Act contains an obligation for the Licensee to provide a self-report, there remains no prescribed structure by which to do so. It is recommended by the Taskforce that a "prescribed form" be adopted and to be submitted to ASIC electronically in machine readable forms.

### **Publication of breach report data**

As part of its annual reports, ASIC currently publishes details about breach reports in an aggregate form. In an effort to promote transparency, the Taskforce has proposed that the annual reporting of breach report data include information at a firm or Licensee level. It is proposed that reporting at this level would be subject to a threshold based on the number of significant breach reports provided by the Licensee for the relevant year.

### **Extension of self-reporting to Credit Licenses**

There is no equivalent obligation for self-reporting under the *National Consumer Protection Act 2009* (Cth). Given the significant overlap between financial services and credit services, there is a strong recommendation to introduce self-reporting regime for credit licensees, equivalent to the regime for Licensees. The increased compliance burden would be offset by making the Compliance Certificates required from credit licensees less onerous to complete.

### **Responsible entities**

Responsible entities of managed investment schemes are obliged to report breaches to ASIC under s912D and s601FC(1)(l) of the Act. In general a breach reported under s601FC(1)(l) will need to be reported under s912D however a breach under s912D will not always need to be reported under s601FC(1)(l).

It is proposed that this unnecessarily complex burden be mitigated by removing the self-reporting obligation under s601FC(1)(l) so that all self-reporting for breaches by responsible entities are absorbed by s912D obligation.