



Strengthening Penalties for Corporate and Financial Sector Misconduct

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About Financial Counselling Australia

FCA is the peak body for financial counsellors in Australia. We support financial counsellors and provide a voice on national issues. We advocate on behalf of the clients of financial counsellors for a fairer marketplace that will prevent financial problems in the first place.

What Financial Counsellors Do

Financial counsellors provide advice to people experiencing financial difficulty about how to overcome current issues and prevent recurring problems. Working in community organisations, their services are free, independent and confidential.

Financial counsellors need knowledge of a wide range of areas of law and policy, including consumer credit law, debt enforcement practices, the bankruptcy regime, industry hardship policies and government concession frameworks.

Financial counsellors also document their experiences and highlight issues that have a negative impact on their clients. Either individually, or through FCA, they consult with industry, government and other stakeholders and to encourage practices that prevent financial and consumer problems in the first place.

The main causes of financial difficulty are unemployment, illness and relationship breakdown. Financial counsellors also assist many people trying to make ends meet on very low incomes.

1 OVERVIEW

1.1 Our Interest in this Area

Because of the work they do in assisting people experiencing financial hardship, financial counsellors come across examples of poor or exploitative behaviour by individuals and companies involved in financial services. Financial services can be complex and unscrupulous operators take advantage of this. These behaviours sometimes cause financial hardship in the first place or can make a bad situation even worse.

1.2 Overall Views

It is important to the integrity of the financial system and an effective market that there are adequate penalties for misconduct. FCA therefore supports the proposals in “Positions Paper 7” to increase and/or adjust the various penalty regimes for offences relating to the financial system. We make three overarching points about the proposed changes.

First, serious breaches of consumer protection laws should attract significant sanctions. The community expects that contraventions of consumer protection and corporate law should result in penalties that provide a substantial deterrent and encourage compliance. A penalty should not be seen as a cost of doing business. Financial counsellors have observed that the penalties for corporate misconduct in the years following the GFC have been much lower in Australia compared to comparable jurisdictions. The proposed changes will go some way to address the problem of low penalties.

Second, the regulator should have a wide-range of regulatory tools to ensure it is able to respond in a flexible way to misconduct. This should include criminal penalties (both jail time and financial penalties), civil penalties and remedies such as disgorgement of profits. Noting that corporations cannot be jailed, criminal financial penalties should be substantial to reflect the criminality involved. Infringement notices are an important part of the regulator’s toolkit which allow it to respond quickly to more minor infractions.

Third, the penalty regime between various pieces of consumer protection legislation should be consistent. In particular, it would make sense for the civil penalties in the National Consumer Credit Protection Act and the financial services chapters of the Corporations Act to align with those in the ASIC Act and the Australian Consumer Law.

2 SPECIFIC COMMENTS

2.1 Criminal penalties

FCA supports Position 1, that the maximum imprisonment penalties for criminal offences in ASIC-administered legislation should be increased. Fraudulent or dishonest conduct should be met with tough penalties. This is due to the fact that it can be challenging to identify and prosecute these offences. White collar criminals can use canny means to avoid detection, including hiding or destroying evidence. The penalty needs to be set at a level that not only punishes, but also deters similar conduct. FCA notes the proposal to increase the maximum prison time to ten years for many offences and welcomes this. We also note that table on page 15 of the position paper which indicates that the maximum penalty for similar offences in the US is 20 years. A longer maximum prison time would give the courts more flexibility to award longer penalties in appropriate cases.

FCA also supports Position 2, which proposes to increase the maximum pecuniary penalties for all criminal offences. While we support a standard formula relating to the relevant maximum prison term being adopted, FCA considers that the penalties could be higher. Again, we note that pecuniary penalties for similar criminal offences in the US are higher.

FCA supports Position 3, that is, to increase the maximum penalty for corporate fraud and breach of section 184 of the Corporations Act. It makes little sense for the corporate fraud provisions to be inconsistent between federal and state laws, so increasing the penalty as proposed is appropriate. FCA notes that financial counsellors sometimes help clients affected by mortgage fraud, where a broker fraudulently assists a borrower obtain the loan, driven by commissions. In this case, vulnerable borrowers may not come forward for fear of prosecution against them. Given the harm is caused by the broker, FCA is of the view that the fraud penalties in this circumstance should be similarly increased to ensure there is appropriate deterrence.

FCA does not have a strong view about Position 4 and the appropriate legal test for dishonesty, but supports consistency across the various legislation.

2.2 Strict and absolute offences

Position 5 proposes to remove imprisonment as a possible sanction to strict and absolute offences. This is a step backwards, and does not align with a key principle of the position paper to strengthen penalties.

FCA supports the introduction of an ordinary offence to complement a number of strict and absolute liability offences as proposed by Position 6. This would give the regulator flexibility to take the appropriate action depending upon the misconduct. For the same reason, FCA supports Position 8 which would apply an infringement or penalty notice regime to strict and absolute liability offences.

FCA also supports increasing the maximum pecuniary penalties for strict and absolute liability offences as proposed by Position 7.

2.3 Civil Penalties

FCA supports position 9 that maximum civil penalties be increased. Civil penalties are commonly sought by regulators in consumer protection cases, and should be set at a sufficient level to encourage compliance.

FCA provided submissions to the review of the Australian Consumer Law (ACL), and strongly endorsed the proposal to increase the maximum civil penalties for contraventions of the ACL. We note that the Commonwealth Government has endorsed this proposal, and is developing legislation to increase the maximum penalty for corporations to the greater of \$10 million, three times the value of benefits obtained or 10% of annual turnover.

FCA considers that similar misconduct should attract similar penalties. For that reason, we consider that the civil penalties for contraventions of the ASIC Act, the National Consumer Credit Protection Act and the financial services chapters of the Corporations Act should be aligned with that of the ACL. There is no reason for the penalties for breaches of the latter two pieces of legislation to be set at a lower level compared with the ASIC Act, as is being proposed by the Taskforce. These laws cover important areas of consumer protection, including credit products such as payday lending, consumer leases and also the important area of financial advice. Financial counsellors unfortunately see many clients who have been harmed by exploitative lending or poor financial advice. In the case of consumer leases and payday loans, individual loans may be relatively small. But for individuals on low

incomes, the impact can be devastating. In aggregate, these kind of breaches add up to significant amounts.

The risk to consumers should these laws be contravened is therefore high, and the penalty should be set at a level to ensure compliance. It sets the wrong message for the civil penalties for these areas to be lower than in the general consumer law.

FCA strongly supports Position 10. Disgorgement should be an available remedy in civil penalty proceedings brought by ASIC under the Corporations, Credit and ASIC Acts. This remedy ensures that a firm or individual does not profit from their misconduct.

FCA also strongly supports Position 11 that priority should be given to consumer compensation when a wrongdoer has insufficient financial resources to both pay fines and compensation. It is very important that the harm to the individual be prioritised – this ensures community confidence in the regulatory regime.

Noting the importance of civil penalties in incentivizing compliance, FCA supports Position 12 to expand civil penalties to a wide range of ASIC-administered contraventions. It can be challenging to prove intent to the criminal standard, so civil penalty actions provide the necessary flexibility for the regulator to respond to legal contraventions. FCA supports the lists at both Table 6 and Table 7 of the position paper being made civil penalty provisions.

Table 7 in particular includes certain Credit Code provisions and provisions which require financial service providers to comply with ASIC directions. The Credit Code provisions are important and particularly impact vulnerable and disadvantaged groups, including the prohibitions on harassment (s 155 and s 179V), the prohibition on visiting premises (s 156(1)), and the provisions relating to business purpose declarations (s 13(6) and s 172(6)) and consumer lease disclosure (s 174(3)). There has been a history of problematic practices relating to credit providers mis-using business purpose declarations,¹ as well as harmful practices by consumer leases providers.² It is very important that ASIC has a flexible regulatory toolkit to deal with contraventions of these provisions, so civil penalties should be available in addition to criminal penalties.

¹See for example - <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2012-releases/12-19mr-federal-court-finds-loan-brokers-engaged-in-unconscionable-conduct/>

² ASIC Repor 447, Cost of Consumer Leases for Household Goods, September 2015, <http://asic.gov.au/regulatory-resources/find-a-document/reports/rep-447-cost-of-consumer-leases-for-household-goods/>

Similarly, it is imperative that ASIC has the capability to ensure compliance. The ability of the regulator to require individuals and firms to comply with its directions or provide information on request is essential. Extending civil penalties to these provisions should enhance the flexibility of ASIC to take action in these circumstances, and would not require ASIC to prove intent.

FCA also strongly supports civil penalties attaching to the prohibited monetary obligations for small amount credit contracts, the provisions relating to entering contracts in excess of the interest rate cap, and the provisions that limit the amount that may be recovered if there is default under a small amount credit contract. Small amount credit contracts, or payday loans, are very harmful products that can lead to debt spirals for low-income clients of financial counsellors. FCA believes that the caps and limits that apply to these contracts are currently too high, but it is important that the regulator has flexibility to enforce the existing price and default caps. The payday lending sector has a long history of avoiding these provisions, so it is important that the regulator has a flexible toolkit to respond to any avoidance. The threat of civil penalties in this case can encourage compliance, and relieve the regulator of having to prove intent to secure a prosecution.

Finally, FCA supports section 154 and 179U of the Credit Code being civil penalties. These provisions are commonly used to prosecute dishonest brokers and, as noted above, borrowers can be particularly vulnerable where a broker acts fraudulently. Again, it is important for the regulator to have flexibility to ensure compliance.

2.4 Insurance Contracts Act

FCA supports civil penalties being extended to insurers that breach the duty of utmost good faith and the requirement to provide a key facts sheet (Position 14). At the moment, ASIC has limited regulatory oversight over insurance claims handling³, and the proposal could contribute to ASIC's regulatory toolkit. The duty of utmost good faith covers a range of conduct, including requiring insurers to administer claims efficiently and without delay, to investigate claims in a reasonable manner, and to not use inappropriate reasons to deny

³ The Corporations Regulations specifically exclude 'handling insurance claims' from the definition of a financial service in the Corporations Act and as such ASIC is somewhat precluded from using its administrative powers in relation to claims handling.

claim. Attaching a civil penalty to this provision would enhance ASIC's powers.

2.5 Infringement notices

As noted above, FCA supports the inclusion of infringement notices in the regulator's toolkit which enables it to respond flexibly to more minor contraventions. Considering the resource intensiveness of regulator court actions and even enforceable undertakings, many minor infractions may go un-remedied if ASIC did not have option to issue an infringement notice. For this reason FCA strongly endorses Position 15.

2.6 False and misleading misrepresentations

FCA supports the extension of section 12DB of the ASIC Act to cover additional misleading representations. While FCA's preferred approach is for the general prohibition on misleading and deceptive conduct to be an offence and a civil penalty provision, in the absence of that it is important that misleading representations of the kind articulated in the position paper are able to specifically prosecuted by ASIC.