Finance Industry Delegation
Australia

FINANCE INDUSTRY DELEGATION

Submission concerning

ASIC Enforcement Review Position Paper 7

"*Strengthening Penalties for Corporate and Financial Sector Misconduct*"

Introduction

The Finance Industry Delegation, representing 187 Australian Credit Licensees that includes lessors of household goods and small to medium, non-ADI credit providers, considers that this Position Paper is focused on very big business and does not appear to make any concessions as to the realities of small and medium businesses.

Overall, the implied recommendations do not provide encouragement for a person to establish a small business, or attempt to grow a small business into a medium or large business.

We note that no one with small lending or leasing of household goods experience is involved in the management and operation of the ASIC Enforcement Review.

Further, we note that there is no analysis included in "Positions Paper 7" of past non-compliance categories, or levels, within the lending and leasing sectors, which are regulated under the National Consumer Credit Protection Act 2009 regime.

We note that there is no consideration of ASIC's (in)capability to use currently available penalties, or the fact that ASIC has a very poor record of attending to larger non-compliant small and medium amount lenders, particularly if they are public companies or owned by overseas interests, or of ASIC's poor record of adequately attending to larger non-compliant lessors.

Central concerns

This Positions Paper is suggesting that the Government adopt a new penalty regime for the Corporations Act, National Consumer Credit Protection Act and National Credit Code, for ASIC to exploit. If these suggestions proceed, amongst other draconian horrors, the credit provider and lessor supporters of the Finance Industry Delegation will face:

1. a significant increase in the maximum and number of penalties for civil offences in the National Consumer Credit Protection Act and National Credit Code;
2. a significant increase in penalties, including gaol terms, that company directors could face for failing to appropriately undertake their duties as Board members;
3. a significant increase in penalties for non-compliance with an ASIC requirement or defective disclosure;
4. a significant increase in penalties for directors who use their position, or information gained as a director, dishonestly and recklessly, with an intention to gain an advantage for themselves or a third party;
5. the introduction of a highly subjective test for "dishonesty" for company directors;
6. an expansion of ASIC's powers to issue penalty (essentially administrative) notices, making it very easy for ASIC to penalise or effectively blackmail a targeted lender - without investigation; and
7. ASIC to have significant opportunity to confiscate profits as an additional penalty (disgorgement).

We note that Position Paper 7 considers other penalties that are already available - the cancellation of licenses, additional licence conditions, directions to provide ASIC with statements, Enforceable Undertakings and civil prosecutions.

However, the Taskforce erroneously presumes that ASIC cannot fulfil its role without additions to this varied list.

Finance Industry Delegation position

From the Delegation supporters' perspective, the proposed range of new penalties should not be considered for introduction until ASIC can demonstrate timely, equitable and effective use of the existing penalties available - particularly those under the National Consumer Credit Protection Act 2009 and associated National Credit Code.

Response to questions included in the Position Paper 7

The Delegation notes the opportunity to respond to questions and the implied encouragement not to discuss the many issues raised in the often lengthy text included before the questions are presented for consideration.

Penalty levels - Questions 1 and 2

We provide a response to a selection of preliminary comments included in the Position Paper (the numbers relate to the paragraphs in the Paper) -

Para 23.

"*The penalties framework for... financial services... should be transparent and consistent...*".

Under the current ASIC Credit Act regime - it is not. As indicated above, larger credit provider companies are ignored, or receive Enforceable Undertakings, rather than face prosecution. Only smaller credit provider companies of limited means, or larger companies that ASIC already know are unable to pay the prosecution costs or the fines, face very expensive prosecution.

Only directors of small companies face personal prosecution.

Para 24.

"*The taskforce would prefer that the consequences for engaging in different forms of misconduct was always clear from reading the legislation itself...*".

That is largely achieved in the National Consumer Credit Protection Act and therefore the regulated businesses do not need to be thrown into a larger pot of unrelated businesses - in unrelated industries - and be included in the recommendations appearing to emerge from this Position Paper 7.

Para 28.

"*...the Taskforce suggests broad alignment with the ACL penalty regime for civil penalty maximums in the ASIC Act and for individuals in the Corporations Act and Credit Act*".

This is fundamentally unsound. It appears to overlook the extent of the harm that may be caused.

A small company transgressing under the Credit Act frequently has no point of reference, or relevance, to a large publicly listed corporation transgressing under the Corporations Act or ASIC Act. At the personal level, it overlooks the difference between a professional director of listed companies - with their own and the company's substantial access to in-house experts and outsourced experts - in comparison to the small business operator with their lack of any professional staff and limited resources to access generally lesser expertise, via outsourcing.

In chapter 2 - "*Criminal Penalties*", there is no reference to the non-applicability of criminal penalties in the Credit Act.

To the writers' knowledge, in regard to Credit Act regulated companies, ASIC has never attempted to seek a criminal penalty. The Credit Act provides alternative civil penalties every time and the gaol penalties prescribed are so onerous for the "crimes" suggested, that even leading consumer advocates have protested about their inclusion.

To bring these penalties up to some higher amount is ludicrous, when the only justification is to make them similar to other largely non-related legislation.

Page 15.

The tables presented are too simplistic. Valid comparisons with overseas jurisdictions' penalties can only be made when detail is compared to detail. Also, when preparedness to seek imposition of the penalty is compared with local preparedness.

2.1.2

We note that there is no consideration of the Credit Act in the section on false or misleading statements, and remind the Taskforce that the consumer detriment suffered by a credit provider or lessor's transgression in this area is minuscule, compared to the large companies involved with sophisticated financial products and publicly listed company shares, AFSL licenses and major corporate fraud.

On this basis, the current penalty regime in the Credit Act should not be changed.

Question 1:

Is it appropriate that maximum terms of imprisonment for offences in ASIC administered Acts be increased as proposed?

Answer: No.

The presumption that the size of the penalty will deter, so often overlooks the traditional researched assessment that what deters is the fear of being caught. Where the larger companies and the Credit Act are concerned, ASIC is a failure in this regard.

Question 2:

Should maximum fine amounts be set by reference to a standard formula?

Answer: No.

The offences must always attract a flexible approach, for the court to be able to assess the facts of the offence. As almost always happens, place a straight jacket on a court and you discourage conviction, or encourage lesser sentences.

Judges will resent the suggested formula as being an erosion of their necessary judicial discretion.

Question 3:

This question is not applicable to Delegation supporters.

Question 4:

Is the Peter's (ordinary decent people) test appropriate...?

Answer: No.

For the reasons discussed immediately above, it is not appropriate for inclusion in any legislation, because it does not provide any real answer to subjectivity.

2.3.1 Dishonesty test

Para 70.

To propose a test "*according to the standards of ordinary, decent people*" is to propose a test for the judges to decide anyway they want.

Such a test is highly subjective for senior ASIC officers and judges, whose socio-economic position means that they have little chance of contact with "ordinary, decent people" and would have no idea what such people thought.

3. Strict liability offences

Para 2.

We note the mention of the celebrated case of *Proudman v Dayman* and the Taskforce's appropriate recognition of this decision.

It is ironic that a Taskforce concerned about penalties for offences involving honesty and avoiding misrepresentation and deceit, can continue to refer to offences as "*strict liability offences*" whilst being aware of this case.

Para 4.

The assertion that a non-fault penalty/strict liability penalty will encourage people to avoid contravention is nonsense - dreamt up by non-practising lawyers who are isolated from the real world and who just do not understand that the average "person" has no idea what penalty applies to most business offences.

For the ordinary functioning business person, the only time they become aware of the penalty is when ASIC alleges and or charges them with the offence and tells them about the penalty, or their local solicitor looks it up when they seek legal advice.

Para 8.

It is a disgrace that, in 2002, a Senate Committee could recommend that there be no gaol term for strict liability offences - yet this has still not been adopted for all legislation with which ASIC is currently involved.

We note that the Senate Committee's recommendation does apply to the Credit Act.

Para 10.

It is noted with appreciation that the Taskforce agrees with the Senate Committee.

Para 20.

The opportunity for ASIC to issue penalty notices should never be permitted. Such a power encourages ASIC to undertake little or no investigation and to use the concept of a penalty notice to blackmail the target into accepting the notice, as opposed to possibly facing an Enforceable Undertaking or prosecution, with all the consequent, ASIC organised, media publicity.

It should be remembered that providing ASIC with any penalty notice regime is offering ASIC the opportunity to act as an investigator (or rely on a third party auditor approved by ASIC and who reports to ASIC), a prosecutor and a court.

There is already significant delegated power assigned to ASIC, giving it a Parliamentary role - a Penalty Notice then provides a judicial role. The separation of powers is totally overlooked and ASIC acquires a totally unacceptable level of power.

Para 22.

Providing ASIC with the power to issue a penalty notice with half the pecuniary penalty of a prosecution, presumes a prosecution would attract the maximum penalty and introduces a lottery system for the victims. It is noted that no detail has been provided as to who would pay for the associated investigation.

Again, ASIC's powers of blackmail are enhanced and the victim is also pushed to weigh up the cost of defending the allegation in court, as against the potentially less costly and certainly less traumatic penalty of a penalty notice fine.

That is not justice - that is a gamble and a blackmail opportunity.

Question 5:

Should imprisonment be removed from all strict liability offences?

Answer: Absolutely.

Such a penalty is unconscionable and punitive.

Question 6:

Set minimum Corporations Act penalties?

Answer: No.

The judicial system must have the traditional flexibility to impose a range of penalties, only curtailed by the maximum penalty. Conceptually, a maximum must always imply 0 up to the legislated figure.

Question 7:

Introducing ordinary offences.

Answer: "Ordinary offences" involving a gaol term are inappropriate to substitute for a strict liability offence that currently does not attract a gaol term.

It must be remembered that the deprivation of liberty is a very serious punishment and costs the taxpayer a lot of money. Far better to have a pecuniary penalty that primarily involves compensation for the consumer victims and other financial costs for the offender, which can be paid from past or continuing earnings. Gaol does not provide any compensation for the consumer victims.

Question 8:

Extending the penalty notice regime.

Answer: No.

For the reasons outlined above. Penalty Notices are a recipe for encouraging ASIC laziness and incompetence.

4. Civil Penalties

Throughout this section of Positions Paper 7 there appears to be little researched discussion on the effectiveness of the current civil penalty regime.

Again we have the issue of effective and timely investigation, leading to a person being caught and charged, as the major deterrent - not the amount of the penalty, about which almost all laymen have absolutely no idea until charged and ASIC or their lawyers tells them.

The Position Paper attempts to justify a change in the civil penalties because there are different penalty regimes in different Acts and Australia is different to overseas jurisdictions. So what?

Where is the evidence that one regime is better than another. Commonality is not the test for a 'good' penalty regime. Simply because one regime is different does not make it better or more applicable. The Position Paper does not provide any persuasive facts, evidence or research to justify any change - it is all well written nonsense.

If the hard working Taskforce had been given anything other than a sham ASIC Capability Review Report to consider, they may have had the advantage of guidance on this issue.

ASIC has to lift its game before any decision can be made about altering civil penalties.

So far ASIC prosecutions concerning credit providers and lessors have never been about current events, but rather about lender or lessor behaviour from years before, and often since abandoned.

ASIC has to demonstrate that it is prepared to take on the large credit providers and lessors - not only attack the little companies, or near insolvent companies.

ASIC has to prove it can organise prosecutions that do not take years from the start of the investigation to a Federal Court decision and not be constipated by ASIC solicitors exploiting procedural rules. Only then should any change to civil penalties be considered at all.

Questions 9, 10 and 11:

New maximum penalties and alignment between Acts

Answer: For companies under the Credit Act, there should not be any consideration of change to the penalty regime discussed in the Positions Paper until ASIC has lifted its game.

There must be an appropriately consistent approach to prosecutions that considers small and large companies and their directors equally, and does not involve a primary focus on prosecution for actions long since passed and not currently being repeated.

This consistency would then provide a measure as to whether or not it is the fear of prosecution, or the penalty, that has the primary deterrent effect. Understandably, at present there is little fear of any kind in the big companies involved with Credit Act regulated credit activities.

4.4 Disgorgement

We note that the Position Paper does not appear to consider the two important levels of disgorgement -

1. fining the company the gross income from the activity, which will leave the non-compliant company with just their principal, or the leased goods on their return; and
2. fining the company the difference between what would have been the compliant activity income, and the total received by way of the non-compliant activity.

The second opportunity should be available for lesser offences, and more serious offences where some diminution of fault is demonstrated.

Any money collected must first go to compensate the consumers. The current ASIC regime appears to have a major regard for publicity and a minor regard for arranging compensation for the affected consumers.

It is the Delegation's view that any adoption of disgorgement must go hand in hand with the introduction of a new age, where the primary concerns of ASIC are to obtain compensation for the consumer victims, as well as stop the non-compliant behaviour.

This new age could also address previously revealed inequities, such as a class action having to determine compensation for the consumers involved - but ASIC failing to provide a mechanism for the consumers who were not involved to also obtain compensation, given they suffered from the same non-compliance. Further, the new age could address the issue of licensees being found to have overcharged, but not being required to refund the amount overcharged.

Question 12:

Should ASIC be able to seek disgorgement remedies in civil penalty proceedings?

Answer: Yes, but only if it is a substitute for an existing civil penalty and certainly not something that follows the payment of a civil penalty. The current Credit Act preference for consumer compensation must be maintained.

Question 13:

Should the making of the payment and where it is paid be left to the court?

Answer: Legislation should prescribe the priority for disgorgement payments over civil penalty, and consultation between ASIC and the prosecuted company should determine the recipients, with court endorsement by order.

4.5 Priority for compensation

As indicated above, the Delegation supports priority for compensation, over civil penalties and criminal penalties.

Question 14:

Should the Corporations Act expressly provide priority for compensation orders?

Answer: Yes - for the reasons presented above.

4.6 Expanding the civil penalty regime

Para 52.

The Delegation disagrees with the Taskforce's view that any offence involving dishonesty should be criminal.

This opens the way for the consumer victim to be forgotten, while ASIC seeks what is generally a lesser financial penalty in the Credit Act, but with the stigma of a criminal conviction. Stigmas do not generate funds for compensation.

Para 53.

The Delegation is not convinced there is any need for an expansion of civil penalties, except to provide an alternative to a criminal penalty.

Question 20:

Should civil penalties apply to breaches of general licence obligations and to some or all?

Answer: Given the very general nature of the licence obligations under the Credit Act, only civil penalties - and never criminal penalties - should apply.

The current regime has not raised any concerns in regard to any variation in penalties according to the licence obligation. Given that lack of issue, no change is recommended.

5. Credit code provisions

Para 10.

The Position Paper includes a number of broad sweeping statements that sound convincing, but have no basis or support either way. For example, "*…if civil penalty action was available, this could provide a more effective deterrent outcome in appropriate cases*".

No attempt is made to support the words "*could provide*" and no identification of "*appropriate cases*" is attempted. Extending penalties cannot be justified by such vacuous statements.

Para 12.

Discussing the 200% collection of the adjusted credit amount rule, the Taskforce asserts, "*A sanction that only results in the return of funds wrongfully charged is largely ineffective in terms of providing a meaningful deterrent*".

Once again, no evidence has been offered to support this illogical statement.

Further, the writers are aware that, when the issue did arise in the industry sector as being one that ASIC was looking at several months ago, there was general panic in the credit provider industry sector and much checking and repayment of minor amounts of money. A civil penalty was not required to prompt this double check and correction activity.

Question 21:

Should sections 23A(1), 32A(2), 39B(1), 154 and 179U of the Credit Code be given civil penalty provisions?

Answer: Yes, but only to the extent that the civil penalty provision replaces any criminal penalty and any strict liability offence.

We trust that the above assists.

Phillip Smiles LL.B., B.Ec., M.B.A., Dip. Ed.

Lyn Turner MA, Dip. Drama

Co-ordinators

Finance Industry Delegation