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Submission - ASIC Enforcement Review Taskforce

This submission is made by Herbert Smith Freehills in response to the exposure draft legislation and explanatory memoranda released by Treasury on 11 September 2019 (**Taskforce Legislation**). These relate to implementing recommendations by the ASIC Enforcement Review Taskforce (**Taskforce**) about ASIC's powers in relation to search warrants, access to telecommunications intercept material, licensing and banning orders.

We welcome the opportunity to make a submission about the Taskforce Legislation. Herbert Smith Freehills has acted for many clients in relation to the areas of law that will be amended by the Taskforce Legislation. This submission also reflects client feedback that Herbert Smith Freehills has received.

We have not sought to make submissions on all areas of the Taskforce Legislation. In our view, there are four areas of the Taskforce Legislation which ought to be amended. These are discussed below.

1 Search warrant powers

1.1 Indictable offences

Proposed subsections 39D(3)(b) of the *Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**) and 272B(3)(b) of the *National Consumer Credit Protection Act 2009* (Cth) (**NCCP Act**) (together, **Indictable Offence Provisions**) allow for indictable offences of a broad description in unspecified legislation to give rise to a search warrant.

As recognised by the explanatory memorandum, 'a search warrant is a substantial imposition on individuals' property and personal rights'. Given this, and despite the recommendation of the Taskforce that the search warrant be available for an indictable offence that otherwise falls within ASIC's general power of investigation under section 13(1) of the ASIC Act or section 247(1) of the National Credit Act, in our view the indictable offences which may give rise to such imposition should be clearly articulated in order to avoid unintended consequences or unnecessarily broad application of the search warrant provisions.

To this end, we recommend the Indictable Offence Provisions be amended to:

- exhaustively list the indictable offences, created by legislation other than the corporations legislation, *Retirement Savings Accounts Act 1997* (Cth) and *Superannuation Industry (Supervision) Act 1993* (Cth); or
- alternatively, exhaustively list the legislation which contains the indictable offences,

to which the applied provisions will apply under subsections 39D(1) of the ASIC Act and 272B(1) of the NCCP Act.

1.2 Who may apply for a warrant

Proposed subsections 39F(1)-(4) of the ASIC Act and 272D(1)-(4) of the NCCP Act (together, **Application Provisions**) allow for 'a member, staff member or other person authorised in writing by ASIC for the purposes of this subsection' to apply for a search warrant.

Given:

- the substantial imposition on individual's property and personal rights which arise from the execution of a search warrant;
- the current law in subsections 35(1) of the ASIC Act and 269(1) of the NCCP Action, which limits the making of applications for a search warrant to 'a member or staff member';
- the breadth of the terms 'staff member' which, as defined in the section 5 of the ASIC Act, includes:
  - permanent, temporary and casual staff (ASIC Act, section 120);
  - persons engaged as consultants (ASIC Act, section 121(1)); and
  - seconded staff (ASIC Act, section 122),

our view is that it is inappropriate to further expand the persons entitled to apply for a search warrant as proposed. Consequently, we recommend the Application Provisions be amended to omit the words 'or other person authorised in writing by ASIC for the purposes of this subsection'.

Were this amendment not made, a new subsection should accompany the Application Provisions to list specific and narrow criteria in which ASIC may authorise a person. Our view is that authorisation must be given only:

- by a member of staff who is a 'senior staff member" under a determination made for the purposes of section 122A of the ASIC Act;
- for a specified duration not longer than 1 week; and
- in circumstances where the member or staff member with carriage of the investigation is unexpectedly unavailable for the purposes of the Application Provisions.

1.3 Purposes for which things seized may be used and shared

Proposed subsections 39G(1) of the ASIC Act and 272E(1) of the NCCP Act (**ASIC Purposes Provisions**) allow the use and sharing of 'a thing seized under this Part for the purpose of the performance of ASIC's functions or duties or the exercise of ASIC's powers'. This language does not limit the use or sharing of things seized to the investigation or prosecution of indictable offences in connection with which a search warrant application was made under proposed subsection 39D(1) of the ASIC Act or section 272B of the NCCP Act (respectively). Given ASIC's wide ranging functions and powers, this may, consequently, allow for an overly broad use of things seized on the basis of a search warrant narrowed to a specified indictable offence.

Our view is that the ASIC Purposes Provisions should be amended as to read ' … a thing seized under this Part for the purpose of the performance of ASIC's functions or powers or the exercise of ASIC's powers *in connection with the indictable offence to which the search warrant relates*'.

2 Telecommunications interception information

We consider the proposed amendments to the *Telecommunications (Interception and Access) Act 1979* (Cth) (**TIA Act**) introduced by the *Financial Regulator Reform (No. 1)*

Bill 2019: Access to Telecommunications Interception Information (**Telecommunications Interception Bill**) should include protections in respect to legal professional privilege.

2.1 Overview of amendments

The amendments introduced by the Telecommunications Interception Bill include the insertion into existing section 67, retitled *Dealings for permitted purposes*, to provide that a staff member of ASIC may for a permitted purpose, in relation to ASIC, communicate to another person, make use of or make a record of, lawfully intercepted information or interception warrant information.

Amendments to existing section 68 insert a provision under which the chief officer of an agency may personally, or by an authorised officer, communicate to a staff member of ASIC information which had been intercepted if it relates or appears to relate to a matter that may give rise to an investigation by ASIC of a serious offence or the likely commission of a serious offence.

Related amendments to the definition of *permitted purpose* in section 5 include the insertion of the following, in relation to ASIC,

- the investigation by ASIC of a serious offence or the likely commission of a serious offence;
- a report on such an investigation;
- the making of a decision whether or not to being a prosecution arising from or relating to such an investigation; or
- a prosecution arising from or relating to such an investigation.

2.2 Amendments to sections 67 and 68 of the TIA Act should be made

We consider that any amendments to the access regime in the TIA Act should be appropriately balanced between preventing unreasonable intrusions of privacy and the reasonable requirements of investigating serious criminal offences. The amendments as drafted do not adequately address the risk of abrogation of legal professional privilege.

It is foreseeable that some of the communications that could be intercepted by a warrant issued under the TIA Act might properly be the subject of a claim of legal professional privilege. The TIA Act contains controls on the use that made be made of intercepted information but these are presently inadequate to prevent the abrogation of legal professional privilege and for this reason, access to and use of intercepted material should not be extended to ASIC.

The power to intercept and record communications under the TIA Act has been held to abrogate privilege: *Carmody v MacKellar* (1997) 148 ALR 210. That case considered whether interception of communications in accordance with section 46 allowed interception of communications covered by legal professional privilege and held that it is not a bar to the issue of a warrant that intercepted communications may include privileged communications.

The TIA Act sets out in section 46 what matters are to be considered when deciding whether to issue a telecommunications warrant. An application for such a warrant is made to a judge or an Administrative Appeals Tribunal member. The possibility that the communications may be protected by legal professional privilege is not one of those matters. Since there is an unacceptable risk that privilege could be lost, the access and use of intercepted information should not be extended.

Given the substantial intrusion into human rights which is engendered by telecommunications interception, and the fundamental nature of the protection of legal professional privilege, we recommend that sections 67 and 68 be amended to restrict the ability of ASIC to receive communications or records of lawfully intercepted information or

interception warrant information to the extent that information may be subject to legal professional privilege.

3 Licensing

3.1 Australian financial services (AFS) licenses

(a) Section 912DA *Corporations Act 2001* (Cth) (Corporations Act) should be amended

Section 912DA Corporations Act imposes an obligation on an AFS licensee to lodge a notification with ASIC if "*an entity starts to control, or stops controlling*" the AFS licensee. This notification must be made within 30 business days such a change in control. The AFS licensee will commit an offence of strict liability if the AFS licensee does not comply with the notification obligation.

Our view is that it is inappropriate to impose a strict liability offence on AFS licensees in the manner in the current drafting of proposed section 912DA Corporations Act. Given:

- the expansive definition of "control";
- "control" of an AFS licensee includes direct and indirect control of such a licensee; and
- an AFS licensee may not be itself informed by its controllers when those controllers start to or cease their control of the AFS licensee,

we recommend section 912DA Corporations Act:

- not be a strict liability offence, and instead be based on the *knowledge* of the AFS licensee (taking the meaning of the knowledge fault element from the *Criminal Code*);
- be amended such that strict liability only applies to a particular physical element of section 912DA Corporations Act, such as the failure to notify once the AFS licensee was aware of a change in control; or
- be subject to an objective test, such that an offence would only occur if it was reasonable in all the circumstances for the AFS licensee to have made the notification (such as where the AFS licensee is part of a closely held group).

We note that while the defence of honest and reasonable mistake in section 9.1 of the *Criminal Code* would be available to an offence under section 912DA Corporations Act, this would not address the issues we identified above. This is because the defence of honest and reasonable mistake will not be available where the AFS licensee does not turn its mind to the facts about its control because it is unaware that an entity has started to or ceased to control that AFS licensee.

(b) Section 913B(2) Corporations Act should be amended

Under proposed section 913B(2) Corporations Act, ASIC:

> *must refuse to grant [an AFS licence] application if ASIC is satisfied that … the application for the licence, or any information, audit report or statement lodged with ASIC in accordance with [section 913B(3) Corporations Act] was false in a material particular or materially misleading or there was an omission of material matter from the application, or the information, audit report or statement.*

Given the severe consequences of this provision, and that it is ASIC itself which decides that there has been a materially false matter or omission, we recommend that section 913B(2) Corporations Act be amended to provide that ASIC may refuse to grant a licence if there has been a materially false matter or omission. This would ensure that an AFS licence applicant is not unfairly penalised if, for example, an application is made

which has accidentally omitted information which an ASIC officer considers to be material.

If amendments such as the above were not adopted, we recommend that section 913B(2) Corporations Act be amended to require ASIC to give 14 days' notice of its intention to refuse the application, and for ASIC to be required to give reasons for that intention.

(c) Section 913B(4A) Corporations Act should be omitted

Section 913B(4A) Corporations Act operates together with section 913B(3) Corporations Act, such that if an AFS license applicant does not lodge the information, audit report or statement requested by ASIC within the time specified by ASIC, then the AFS license applicant "*is taken to have withdrawn the [AFS licence] application*". While ASIC is able to extend the time for providing the information, audit report or statement that ASIC requested, it remains that there may be many reasons outside of the control of an AFS licence applicant for why that applicant is not able to provide the information, audit report or statement that ASIC requested within the time which ASIC nominates (e.g. an auditor may not be able to deliver their report as originally anticipated). Our view is that it is unfair for the legislation to provide that an applicant is taken to have withdrawn their application when ASIC may not be willing to give an extension and the AFS licence applicant is not responsible for the delay. This unfairness is compounded by section 913B(4A) Corporations Act providing that the application is *withdrawn* by the applicant, rather than refused by ASIC – this means that the applicant is not entitled to a hearing. The provision should be redrafted to provide for the applicant to be entitled to a hearing.

(d) Section 913BB(m) Corporations Act should be omitted

We note that section 913BB(m) Corporations Act would permit ASIC to consider "*any other matter ASIC considers relevant*" for the purposes of deciding whether a person is "fit and proper" under section 913BA(1) Corporations Act. Given the specificity and extent of the matters set out in sections 913BB(a) – (l) Corporations Act, which already allow ASIC to consider important and relevant matters for the purpose of deciding whether a person is "fit and proper" under section 913BA(1) Corporations Act, in our view it is inappropriate to give ASIC unconstrained latitude to consider other matters for the purpose of section 913BA(1) Corporations Act.

(e) Guidance needed on section 915C(1)(b) Corporations Act ongoing fit and proper requirement

Under section 915C(1)(b) Corporations Act, an AFS licensee will be subject to an ongoing requirement that the licensee, its controllers, and officers of its controllers continue to satisfy the fit and proper test. However, the explanatory materials do not contain any guidance to AFS licensees about the nature and extent of the enquiries that those licensees need to make to comply with this requirement. Our view is that this should not be left to ASIC guidance, and that the explanatory materials should make it clear what AFS licensees need to do to comply with this requirement. In doing so, we recommend the materials do not impose unnecessary compliance burdens on AFS licensees, and recognise that AFS licensees may discharge this requirement by undertaking annual checks using third party information vendors.

3.2 Australian credit licences (ACL)

(a) Section 37(2) NCCP Act should be amended

Section 37(2) NCCP Act provides that ASIC must refuse the application for an ACL if ASIC is satisfied that the ACL application, or any information, audit report or statement lodged in respect to it, was materially false or misleading. Given the severe consequences of this provision, and that it is ASIC itself which decides that there has been a materially false matter or omission, similarly to the case in respect to section 913B(2) Corporations Act, we recommend section 37(2) NCCP Act be amended to provide that ASIC may refuse to grant a licence if there has been a materially false matter

or omission. As above, this would ensure that an AFS licence applicant is not unfairly penalised if, for example, an application is made which has accidentally omitted information which an ASIC officer considers to be material.

(b) Section 37(6) NCCP Act should be amended

This provision seeks to put in place a mechanism (under section 37(5) NCCP Act) by which ASIC may seek information, an audit report or a statement for the purpose of an ACL application and (under section 37(6) NCCP Act) if an ACL applicant does not lodge the information, audit report or statement requested by ASIC within the time specified by ASIC, then the ACL applicant "*is taken to have withdrawn the [ACL] application*". As with the equivalent provision in respect of AFS licenses, there may be many reasons, outside the control of the applicant, why an ACL applicant is not able to provide the information, an audit report or a statement within an extended period of time. Section 37(6) NCCP Act would also operate to mean that an ACL application is withdrawn, rather than being refused by ASIC – this means that the applicant is not entitled to a hearing. Our view is that it is unfair for the legislation to provide that an applicant is taken to have withdrawn their application when ASIC may not be willing to give an extension and the AFS licence applicant is not responsible for the delay. Section 37(6) NCCP Act should be redrafted to provide for the applicant to be entitled to a hearing.

(c) Section 37B(k) NCCP Act should be omitted

Under section 37B(k) NCCP Act, ASIC may consider "*any other matter ASIC considers relevant*" for the purposes of deciding whether a person is "fit and proper" under section 37A(1) NCCP Act. Given the content of sections 37B(a) – (k), which already allow ASIC to consider important and relevant matters for the purpose of deciding whether a person is "fit and proper" under section 37A(1) NCCP Act, in our view section 37B(k) NCCP Act is unnecessary and should be removed.

(d) Guidance needed on section 55(1)(b) Credit Act ongoing fit and proper requirement

This provision seeks to put in place a similar requirement to section 915C(1)(b) Corporations Act. We repeat our submissions above in this respect.

4 Banning

(a) **Section 920A(1A)(j) Corporations Act and Section 80(2)(j) NCCP Act should each be omitted**

Our view is that section 920A(1A)(j) Corporations Act and section 80(2)(j) NCCP Act should each be omitted. Both of these provisions permit ASIC to consider "any other matter ASIC considers relevant" in determining whether to make a banning order. However, each of these sections otherwise contain a comprehensive listing of matters which ASIC may take into account. Given this, section 920A(1A)(j) Corporations Act and section 80(2)(j) NCCP Act are unnecessary and should be omitted.

(b) Sections 920A(1)(l) and (m) Corporations Act should be omitted

Section 920A(1)(l) Corporations Act proposes to enable ASIC to make a banning order under section 920A Corporations Act against a person if:

- one or more banning orders are in force; or
- ASIC is satisfied that it could make a banning order,

against another person who is an officer of the person and who is performing a function involved in the person's financial services business. Section 920A(1)(m) Corporations Act applies similarly in respect to trustees of a trust.

These powers were not referred to in the Taskforce's December 2017 report. We consider these provisions should be omitted because:

1 They have not been the subject of appropriate scrutiny. Until the release of this draft legislation, these powers have not been the subject of the Taskforce consultation process.

2 The provisions lack adequate administrative and judicial safeguards. Allowing the banning power to be used against an entity when another banning order is "in force" against an officer of that entity means that ASIC could make a series of banning orders before administrative or judicial review proceedings have been undertaken in respect of the first banning order, and the only protection against that will be a discretionary stay of the banning order as ordered by the Administrative Appeals Tribunal or a court. The power would also be available in relation to an entity even if ASIC has not made a banning order against an individual officer of that entity, but is merely satisfied that ASIC could have.

3 For section 920A(1)(l) Corporations Act, there is no requirement for a nexus between the alleged conduct giving rise to ASIC's belief that it could obtain a banning order against an officer of the licensee entity and the entity itself, nor is there a requirement that the particular officer's actions be attributable to the entity. Similar comments apply in respect to section 920A(1)(m) Corporations Act.

We understand that the provision permitting an organisation to be banned where an officer could be banned has been included to deal with small financial services businesses where an individual is effectively synonymous with that business (see for example Case Study 1 on page 11 of the Tasksforce's Report – while that was cited in a different context we expect this may be what has driven this proposal). The very different and broader potential scope/implications of the power to an organisation like a major ADI may not have been sufficiently considered. Such a power is not appropriate or needed for large organisations given ASIC's existing banning power, and (subject to court scrutiny) ASIC's ability to seek orders under sections 1101B and 1324 Corporations Act. It would allow ASIC to potentially make a banning order against a whole ADI based on the actions of one officer of that ADI.

Given the reputational effects of a banning order, and the potential impact on an entity's business, the requirement for ASIC to give an entity a hearing prior to making a banning order is an inadequate protection for potentially affected parties against the unfairness which may arise from the exercise of ASIC's powers in section 920A(1)(l) and (m) Corporations Act.

Yours sincerely

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