

9 April 2021

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The Manager  
Regulatory Powers and Accountability Unit  
Financial System Division  
The Treasury  
Langton Crescent  
PARKES ACT 2600

Dear Sir/Madam

## **BREACH REPORTING REGULATIONS**

The Stockbrokers and Financial Advisers Association (SAFAA) is the professional body for the stockbroking and investment advice industry. Our members are Market Participants and Advisory firms that provide securities and investment advice, execution services and equity capital-raising for Australian investors, both retail and wholesale, and for businesses. Practitioner Members are suitably qualified professionals who are employed in the securities and derivatives industry.

Thank you for the opportunity to provide feedback on the changes to regulations that support the breach reporting rules in Schedule 11 of the *Financial Sector Reform (Hayne Royal Commission Response) Act 2020* that amend the Corporations Act (the Act).

### **Civil penalty provisions that are not taken to be significant if contravened**

SAFAA provided a submission to Treasury on the exposure draft of the bill on 28 February 2020 expressing concerns about the changes to the breach reporting regime around the 'significance' threshold.

We consider that a consequence of 'deeming' a contravention of a civil penalty provision to be a significant breach is a large increase in breach reports for minor, technical or inadvertent breaches that would not otherwise be significant. In particular the extra volume of breach reports will result in:

- an increase in the amount of 'noise' given that many breaches will relate to trivial failures, thus making ASIC's job harder; and
- considerable rise in resource costs both to individual firms and across the industry in ensuring that the additional reporting is carried out within the timetable imposed.

We pointed out in our submission that the draft bill would result in a minor matter such as sending a Financial Services Guide (FSG) to a client a day late would trigger a requirement to lodge a breach report.

We support the provision of a regulatory carve-out to prescribe civil penalty provisions that are not taken to be significant (and therefore may not be reportable) under the relevant breach reporting regime, as a sensible solution to the problem we previously highlighted.

SAFAA agrees that:

- failure by a licensee to give an FSG when providing a financial service to a person as a retail client
- failure by an authorised representative to give an FSG when providing a financial service to a person as a retail client
- failure to give a Product Disclosure Statement (PDS) when giving personal advice recommending a particular financial product
- failure to give a PDS in situations relating to the offer and issue of financial products
- failure to give a PDS in situations relating to the sale of financial products
- giving a defective disclosure document or statement (including a defective PDS or supplementary PDS)

should not be taken to be significant for the purposes of paragraph 912D(4)(b) of the Act. We are pleased that the point we made about minor technical breaches such as the late provision of an FSG has been taken into account when drafting the regulations.

We note that such a breach may still be significant and reportable under the breach reporting regime if one of the other circumstances in the deemed significance test in subsection 912D(4) apply, or if the breach is otherwise significant under the test in subsection 912D(5) of the Act.

SAFAA considers that in addition to the matters in Item 8 there are other civil penalty provisions in the Act that should be carved out from being deemed significant breaches and thereby subject to breach reporting requirements. We set these out below.

## **Market Integrity Rules**

A matter of particular concern for our members is the incorporation (by reference) of the *ASIC Market Integrity Rules (Securities Markets) 2017* (Market Integrity Rules) into the list of 'Core Obligations' to which the 'deeming' provision applies. SAFAA assumes that this result was not intended by Parliament. This will have a significant impact on SAFAA members as even minor breaches of the Market Integrity Rules will be required to be reported to ASIC as a significant matter. We are not aware of other markets where breaches of market integrity rules are automatically required to be reported to the regulator.

We note that section 912D(3) of the Act lists all of the '*core obligations*'. Section 912D(3)(b) provides that section 912A(1)(c) (the general licence obligation to comply with financial services laws) is a '*core obligation*' so far as the financial services law relates to the specified paragraphs of the definition in section 761A (our emphasis highlighted below):

- (3) Each of the following is a *core obligation*:
- (a) an obligation under section 912A or 912B, other than the obligation under paragraph 912A(1)(c);
  - (b) the obligation under paragraph 912A(1)(c), so far as it relates to provisions of this Act or the ASIC Act referred to in paragraphs (a), (b), (ba) and (c) of the definition of *financial services law* in section 761A;
  - (c) in relation to financial services, other than traditional trustee company services provided by a licensed trustee company—the obligation under paragraph 912A(1)(c), so far as it relates to Commonwealth legislation that is covered by paragraph (d) of that definition and that is specified in regulations made for the purposes of this paragraph;
  - (d) in relation to traditional trustee company services provided by a licensed trustee company—the obligation under paragraph 912A(1)(c), so far as it relates to Commonwealth, State or Territory legislation, or a rule of common law or equity, that is covered by paragraph (d) or (e) of that definition.

The definition of ‘financial services law’ in Section 761A includes ‘a provision of this Chapter’ (meaning Chapter 7 of the Act).

*financial services law* means:

- (a) a provision of this Chapter or of Chapter 5C, 5D, 6, 6A, 6B, 6C, 6D or 8A; or
- (b) a provision of Chapter 9 as it applies in relation to a provision referred to in paragraph (a); or
- (ba) a provision of the Passport Rules for this jurisdiction; or
- (c) a provision of Division 2 of Part 2 of the ASIC Act; or
- (d) any other Commonwealth, State or Territory legislation that covers conduct relating to the provision of financial services (whether or not it also covers other conduct), but only in so far as it covers conduct relating to the provision of financial services; or
- (e) in relation to a financial services licensee that is a licensed trustee company (in addition to paragraphs (a) to (d))—any rule of common law or equity that covers conduct relating to the provision of financial services that are traditional trustee company services (whether or not it also covers other conduct), but only in so far as it covers conduct relating to the provision of such services.

One of the provisions within Chapter 7 is section 798H (the obligation on participants of licensed markets to comply with the Market Integrity Rules).

## 798H Complying with market integrity rules

(1) The following entities must comply with the market integrity rules:

- (a) operators of licensed markets;
- (b) participants in licensed markets;
- (c) entities prescribed by the regulations for the purposes of this paragraph.

Note: This subsection is a civil penalty provision (see section 1317E). For relief from liability to a civil penalty relating to this subsection, see section 1317S.

(2) Subsection (1) does not apply in relation to a financial market the operator of which is licensed under subsection 795B(2) (overseas markets).

(3) If there is an inconsistency between the market integrity rules and the derivative transaction rules or the derivative trade repository rules, the market integrity rules prevail to the extent of the inconsistency.

As section 798H is a civil penalty provision, a breach of that section (and therefore a breach of the Market Integrity Rules) is automatically deemed to be significant under new section 912D(4).

(4) For the purposes of this section, a breach of a core obligation is taken to be *significant* if:

- (a) the breach is constituted by the commission of an offence under any law and the commission of the offence is punishable on conviction by a penalty that may include imprisonment for a maximum period of:
  - (i) if the offence involves dishonesty—3 months or more; or
  - (ii) in any other case—12 months or more; or
- (b) the breach is constituted by the contravention of a civil penalty provision under any law, other than a civil penalty provision prescribed by the regulations for the purposes of this paragraph; or
- (c) the breach is constituted by a contravention of subsection 1041H(1) of this Act or subsection 12DA(1) of the ASIC Act (misleading or deceptive conduct in relation to a financial product or a financial service); or
- (d) the breach results, or is likely to result, in material loss or damage to:
  - (i) in the case of a managed investment scheme—a member or members of the scheme; or
  - (ii) in the case of a superannuation entity—a member or members of the entity; or
  - (iii) in all cases—a person or persons to whom the financial services licensee or a representative of the financial services licensee provides a financial product or a financial service as a wholesale or retail client; or
- (e) any other circumstances prescribed by the regulations for the purposes of this paragraph exist.

The Market Integrity Rules already include a reporting regime. Market participants are required to notify ASIC about various matters under the Market Integrity Rules such as trust account reconciliation breaches and suspicious activity reports. The obligation to report suspicious conduct under Rule 5.1.1 of the Market Integrity Rules is in addition to the breach reporting obligations under section 912D and is a distinct obligation. Market Participants must also report significant breaches of the Market Integrity Rules to ASIC.

SAFAA recommends that the Market Integrity Rules be added to item 8 to ensure that they are explicitly carved out from being deemed significant breaches and subject to breach reporting requirements under section 912D. Breaches of the Market Integrity Rules are often minor, technical or inadvertent and would not otherwise be significant. They are remedied quickly, have low impact and occur in the context of large volumes of trading. Including them as reportable breaches will increase the regulatory burden on firms as well as on ASIC and will impact on the cost of providing financial services. As noted above, significant breaches of the Market Integrity Rules are required to be reported to ASIC in any event.

### Statements of advice

SAFAA considers that breaches of the statement of advice provisions are in the same category as breaches of the FSG provisions in the context of the breach reporting regime. This is because:

- a breach of these provisions may be minor, technical or inadvertent in nature;
- given the frequency with which these documents must be provided, it is possible minor, technical or inadvertent breaches (that would not otherwise be significant) would result in a large regulatory burden if they were deemed automatically significant; and
- more material breaches of these provisions would be captured by the other limbs of the deemed significant test in subsection 912D(4) or by the test in subsection 912D(5) of the Act.

We note that breaches of the FSG provisions are included in the regulation as not being significant for the purposes of paragraph 912D(4)(b) of the Act.

SAFAA recommends that the following provisions of the Act be included in the regulation as items not deemed to be significant breaches:

- failure to provide a client with a statement of advice (section 946A (4))
- giving a defective statement of advice (section 952 E (9))
- failure to ensure an authorised representative gives a statement of advice (section 952 H (3)).

### Conclusion

SAFAA is happy to discuss any issues arising from these comments, or provide any further material that may assist. Should you require any further information, please contact Michelle Huckel, Policy Manager by way of the contact details in the covering email.

Kind regards



Judith Fox  
Chief Executive Officer