

17 December 2021

Senate Standing Committee on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Committee Secretary

Inquiry into the Financial Accountability Regime Bill 2021

Thank you for the opportunity to provide comments to the Senate Economics Legislation Committee (the **Committee**) on the Financial Accountability Regime Bill 2021 (**the Bill**).

The Australian Institute of Company Directors' (**AICD**) mission is to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society. The AICD's membership of more than 47,000 reflects the diversity of Australia's director community, comprised of directors and leaders of not-for-profits, large and small businesses and the government sector.

The AICD supports measures to strengthen governance and accountability practices across financial services industries, including implementing the recommendations of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**).

The AICD has engaged extensively in the consultation on the development of the Financial Accountability Regime (**FAR**), providing submissions on the Exposure Draft (available [here](#)) and the initial Proposal Paper in February 2020 (available [here](#)). The AICD's policy positions on the FAR have been informed by extensive engagement with our members who sit on the boards of Australian Prudential Regulation Authority (**APRA**) regulated entities, including from the AICD's standing policy committee - the APRA Regulated Entities Forum.

1. Executive Summary

1. The AICD welcomes the amendments to the accountable person obligations made to the Bill since consultation on the Exposure Draft. The amendments address the AICD's concerns that the FAR would undermine the important strategic and oversight function of the board and result in a burdensome and unrealistic compliance focus by directors in meeting the accountable person obligations.
2. The AICD supports passage of the Bill in its current form. While the AICD does retain some concerns with certain elements of the Bill, we consider that on balance the FAR will result in accountability improvements across all APRA-regulated entities.
3. The AICD does not support the introduction of civil penalties on accountable persons within the FAR regime. The Bill as currently drafted is already beyond what was contemplated in the recommendations of the Royal Commission, in the AICD's view. To introduce direct personal liability would be inconsistent with the Royal Commission and unnecessary given the existing extensive enforcement and penalty powers available to APRA and ASIC.

4. The AICD recommends the Committee consider whether minor amendments to the Bill can be made to clarify how the regulators will exercise powers and jointly administer the regime.
5. The AICD encourages the Committee to communicate an expectation to the Government and regulators that comprehensive practical guidance is needed for FAR entities and accountable entities to meet the FAR obligations in a manner consistent with the objectives of the regime.

2. General comments

6. The AICD recommends the Committee assess any submissions that call for significant amendments to the Bill in the context of the recommendations of the Royal Commission. Notably recommendation 6.8 of the Financial Services Royal Commission final report was to “extend” the Banking Executive Accountability Regime (**BEAR**):

*Over time, provisions modelled on the BEAR should be **extended** to all APRA-regulated financial services institutions. APRA and ASIC should jointly administer those new provisions.*¹

7. As detailed in our submission on the Exposure Draft, the Bill represents a material divergence from the BEAR and what was contemplated under the Royal Commission recommendations. The FAR is in effect a new accountability regime with expanded obligations on entities and accountable persons, such as the provisions in s.21(1)(d) that is a new accountable person obligation that is not present under the BEAR.
8. Expansion of the BEAR, rather than extension, is contrary to the recommendations of Commissioner Hayne:

*I do not otherwise consider there to be a need for the obligations in the BEAR to be expanded, although consequential changes may be necessary in light of what I have said above.*²

9. The AICD urges that the Committee approach with caution any consideration of further departure from the recommendations of the Royal Commission. The FAR that is contemplated under the Bill will introduce a broad accountability regime that will apply to all APRA-regulated entities and ensure that increased number of executives are subject to accountability obligations for the first time, including deferred remuneration requirements. Importantly it will be a regime that is jointly administered by two well-resourced regulators in APRA and ASIC that will be equipped with broad powers and sanctions to appropriately drive improvements in accountability practices across the financial system.
10. Accordingly, it would not be appropriate to impose further obligations when these matters have already been comprehensively examined by Commissioner Hayne and the subject of explicit recommendations.

3. Civil penalties - accountable persons

11. The AICD would not support changes to the Bill to introduce new, direct civil penalties on accountable persons for breaches of accountability obligations under the FAR. Instead, we note

¹ Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, page 39.

² Ibid, page.466

that, mirroring the approach taken in other regulatory settings, that directors of FAR entities can be held liable where they have acted as an accessory to an entity's breach (see further below).

12. The Royal Commission did not recommend the introduction of civil penalties under the BEAR or its extension to all APRA-regulated entities. Treasury consulted on this issue as a component of its Proposal Paper in January and February 2020. The AICD was one of many industry participants that raised significant concerns with the proposal, and it was subsequently not included in the Exposure Draft.
13. As set out in our submissions on the Proposal Paper and the Exposure Draft, directors in Australia are already exposed to a unique civil penalty regime for directors' duties contraventions. In 2020, the AICD commissioned the law firm Allens to research the frameworks for imposing criminal and civil liability on directors in Australia and comparative jurisdictions (the UK, New Zealand, Canada, Hong Kong and the USA). Allens concluded that Australia's director liability environment is unique - and in many regards, uniquely burdensome - as compared with other jurisdictions. Of note, Australian courts may impose civil fines on directors for breaches of the Corporations Act that rival criminal fines in other jurisdictions.³ Perhaps more importantly, and unlike some comparable jurisdictions, directors are subject to general directors' duties, such as the duty of care and diligence, which are enforceable by the corporate regulator ASIC (see further below).
14. In addition to director duties under the *Corporations Act 2001* (**Corporations Act**), directors of APRA-regulated entities face specific penalty regimes based on the relevant industry act (e.g. *Banking Act 1959*) and the APRA prudential standards that apply to the entity. Further, the Bill will provide both APRA and ASIC with extensive powers and penalties in respect of any accountability failing or breach by an accountable person, including disqualification of an accountable person.
15. Civil penalties on accountable persons would be a punitive and unnecessary step in the context of the existing director liability environment and the new powers available to the regulators.

Accessorial liability and stepping stone liability

16. The AICD notes that the Bill does provide for accessorial personal liability for accountable persons under section 81. Essentially this provision increases the liability risk faced by accountable persons who aid, abet or are knowingly concerned in a contravention by an entity.
17. The presence of accessorial liability coupled with the trend of ASIC utilising 'stepping stone liability' to pursue directors for breaches of the general director duties under the Corporations Act means that the Bill already provides for personal liability on directors.
18. Stepping stone liability, is a 'two-step process', whereby 'directors and officers may be personally liable for failure to prevent contraventions of law by their corporation.'⁴ In the case of the FAR, stepping stone liability would be where a director as an accountable person is alleged by ASIC to have failed to comply with one of their accountability obligations, or the accountable entity itself fails to comply with its accountability obligations, and is charged by ASIC for breaching a directors' duty under the Corporations Act.

³ Allens research is available [here](#).

⁴ Jennifer Hill, 'Legal Personhood and Liability for Flawed Corporate Cultures' (European Corporate Governance Institute (ECGI)-Law Working Paper 431, 2018) 27.

19. Stepping stone liability is a unique feature of the Australian director liability environment because similar jurisdictions utilise private, rather than public, civil enforcement of directors' duties. Regulators in these jurisdictions are not able to 'step' from an enforcement action against a company to a civil penalty application against a director in the manner ASIC can, as such, stepping stone liability creates a unique liability risk for Australian directors.
20. We recommend the Committee assess calls for the imposition of direct civil penalties on accountable persons within the context of the genuine risk of personal liability that accountable persons face already via the accessorial liability provision and ASIC's approach of pursuing directors via stepping stone liability. We would also reiterate our point above that Commissioner Hayne did not make any recommendation that accountable persons be subject to direct, as opposed to accessorial, liability.

5. Accountable person obligations

21. The AICD welcomes the amendments to the accountable person obligations made since consultation on the Exposure Draft.
22. The AICD had expressed significant concerns with the use of the word "ensure" in subsections 19(1)(d) and 20(d) of the Exposure Draft (subsection 21(1)(d) and section 22 of the Bill) as they related to the role of directors as accountable persons. Our concerns were grounded in the distinction between the respective roles of directors and management. The AICD considered that requiring directors as accountable persons to guarantee compliance or ensure that certain management functions occur would result in a blurring of the line between the board and management.
23. We argued in our submission that this approach to drafting was also inconsistent with the observations of Commissioner Hayne:

*Boards cannot, and must not, involve themselves in the day-to-day management of the corporation. Nothing in this Report should be taken to suggest that they should. The task of the board is overall superintendence of the company, not its day-to-day management.*⁵

24. We also made the broader observation that it is an extraordinarily high bar to require an accountable person (either a director or executive) to guarantee compliance or make certain it occurs.
25. Subsection 21(1)(d) has been amended to replace 'ensure' with an accountable person taking reasonable steps to prevent matters from arising that would (or would be likely to) result in a material contravention by the entity under the relevant financial services laws. The 'ensure compliance' subsection under section 22 has now sensibly been deleted.
26. The drafting changes to the accountable person obligations better reflect the role of directors and the oversight function of the board. While we continue to consider the additional obligation from those under the BEAR – subsection 21(1)(d) – to still be extremely broad and duplicative of other legislation, the amendments have mitigated our concerns about the potential liability on directors of APRA regulated entities who act in good faith and take reasonable steps to meet the FAR obligations.
27. Based on these important amendments, the AICD supports passage of the Bill in its current form. While we do consider there is an opportunity for clarification, through minor amendments, on regulator

⁵ Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, page 400.

powers and joint administration, discussed below, these issues should not be a barrier to passage of the Bill.

6. Regulator powers

28. The AICD maintains its concerns with how some of the regulator powers are drafted and the uncertainty of how the regulators will jointly administer the FAR. We encourage the Committee to assess whether minor amendments to the Bill or further detail in the Explanatory Memorandum would assist in resolving industry uncertainty in these areas.
29. As detailed further in our submission on the Exposure Draft, our concerns are focused in two areas:
 - a) the obligation on an accountable person to deal with the regulator in an 'open, constructive and cooperative' way (subsection 21(1)(b)); and
 - b) the extensive directions powers available to the regulators under section 64.
30. The obligation to deal with the regulator in an 'open, constructive and cooperative' way exists under the BEAR and will be extended to ASIC under the Bill. ASIC as a conduct regulator with an explicit focus on enforcement under its mandate has historically had a greater prosecutorial focus than APRA, which has a supervision led focus on prudential matters and system stability. Requiring an entity or an individual to be "co-operative" with a regulator attempting to prosecute them, potentially restricts their ability to mount a robust defence and may deny them procedural fairness.
31. On the current drafting, it is unclear whether this provision would require an accountable person to provide to the regulator material that is subject to legal professional privilege. However, we understand that the policy intent is not to over-ride legal professional privilege. Accordingly, we recommend that such a clarification be made in the Bill under section 89. We would also welcome further detail from the regulators regarding the joint administration arrangement (section 37) and supporting guidance on expectations on accountable persons for meeting these obligations.
32. Our submission on the Exposure Draft highlighted the lack of a stated policy rationale for the broad and unfettered directions powers available to the regulators under section 64. APRA already has access to identical directions powers under the relevant industry acts (e.g. section 11CA of the Banking Act). Additionally, the Bill provides the regulators with an extensive toolkit of investigatory and enforcement powers that appear to negate the need for sweeping directions powers.
33. The AICD encourages the Committee to consider whether additional drafting that clearly sets the parameters and a higher threshold for use of directions powers under section 64 is needed. We would also welcome further detail from the regulators on how they will utilise their directions powers, and under what scenarios, in the joint administration arrangement under section 37 and in supporting guidance.

7. Joint administration arrangement and regulator guidance

34. A key component of the successful implementation of FAR will be the Government and regulators providing all FAR entities with comprehensive guidance on the expectations for meeting the new obligations. As discussed above, our view is that FAR will represent a new broad accountability regime and with that will come significant challenges for smaller entities, particular RSE licensees and insurers, in interpreting the obligations.

35. Feedback from our members who sit on the boards of ADIs is that they currently operate without a clear understanding of APRA's expectations on the BEAR. APRA to date has released very limited public guidance on its expectations for meeting the BEAR requirements and this has increased the burden and uncertainty that ADIs and accountable persons face in complying with the obligations. We would be very concerned if this approach was replicated with the FAR, particularly given its much broader application.
36. While we welcome the requirement for the regulators to reach a joint administration arrangement under section 37, this document needs to be sufficiently detailed. An arrangement that is brief and solely principles based is unlikely to provide sufficient insight to entities and accountable persons. We encourage the Committee to consider whether further detail on what the arrangement should cover could be included in section 37.
37. We also encourage the Committee to recommend the two regulators provide comprehensive practical guidance to industry. This guidance would cover key areas of interpretation, such as 'reasonable steps' and how to deal with the regulators in a 'cooperative' manner. We note that the potential misalignment between the FAR deferred remuneration obligations and APRA's new prudential requirements under *Prudential Standard CPS 511 Remuneration* continues to cause concern for entities and accountable persons and this area should be a priority for regulator guidance.

8. Next Steps

We hope our submission will be of assistance. If you would like to discuss any aspects further, please contact Simon Mitchell, Senior Policy Adviser at smitchell@aicd.com.au, or Christian Gergis, Head of Policy, at cgergis@aicd.com.au.

Yours sincerely,



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