

**Submission to the Senate Standing Committees on Economics**

**Australian Securities and Investments Commission Investigation and  
Enforcement**

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**Introduction**

This submission addresses the questions raised in the Terms of Reference regarding the Review of Australian Securities and Investments Commission Investigation and Enforcement. The aim of this submission is to provide informed commentary on the Australian Securities and Investments Commission's role in the regulatory sphere.

If any part of this submission requires or invites further explanations, please contact Associate Professor Marina Nehme at the University of New South Wales, Sydney, The Faculty of Law and Justice at [REDACTED]

**General Observation**

The observations made in this submission can be summarised in the following manner:

- Dispute resolution and compensation schemes play a critical role in ensuring consumers are protected in case of misconduct. The operation of the schemes should not distort efficient markets, but should enhance trust in the sector. Regulatory action should not be impacted by the availability of these schemes as such action has a different objective which is centred on protecting the public and deterrence. The scheme's objective is compensating affected consumers for losses suffered due to misconduct.
- Reaching the right regulatory balance between promoting entrepreneurship, protection of consumers and enforcement is important to ensure that our corporate regulatory regime does not impose unreasonable expectations on businesses as 'unreasonable expectations' may have a negative impact on compliance with the law.
- In the past two years ASIC has been subjected to a range of internal and external reviews. It is important to provide the regulator with time to assess all the recommendations and implement them. Afterward an appropriate time, a review may be conducted to ascertain

whether the regulator's implementation of previous recommendations has led to improvements in the way the system operates. Constant reviews of the regulator may divert ASIC's limited resources to dealing with reviews and may prevent ASIC from implementing much needed internal changes in its regulatory approach.

- A wider review of the legislative scheme is needed to remove and/or limit regulatory duplication.
- ASIC should enhance its reporting in the enforcement sphere and clarify how its data is collected to ensure transparency and accountability in the system.

#### **a. The potential for dispute resolution and compensation schemes to distort efficient market outcomes and regulatory action**

Dispute resolution and compensation schemes are essential to ensure consumers are protected in case of misconduct and can find relatively (relative to seeking legal redress for wrongs) quick and effective remedies for losses they may have suffered from breaches of corporate law. As such, the potential for dispute resolution and compensation schemes to distort efficient market and regulatory action outcomes is negligible. They instead improve the efficiency of the market and free up the court system.

Regulatory action serves a different purpose than compensating consumers for losses they may have suffered. The key mandate of a regulator taking action in instance of breach of the law is the protection of consumers by preventing and deterring misconduct from occurring in the future. Accordingly, regulatory action is not a replacement for, nor a substitute to, dispute resolution and compensation schemes. Neither negate the other. Having access to both and the potential for quick redress for consumers will maintain public confidence in corporations, markets and regulators.<sup>1</sup>

The operation of efficient markets is not impacted by the use of dispute resolution and compensation schemes holding offenders liable for their poor conduct. They in fact raise the level of accountability in the system and this, in turn, leads to a greater confidence in the regulatory scheme.

The only instance where a distortion of efficient market outcome may occur is in instances where compensation schemes fail to achieve their mandate as they may result in a burdensome expectations of Industry participants when those participants are complying with the letter as well as the spirit of the law.<sup>2</sup>

Furthermore, imposing a levy on the financial services industry to run a compensation scheme may be problematic in that it may negatively effect, and lead to resentment by good corporate citizens.

#### **b. The balance in policy settings that deliver an efficient market but also effectively deter poor behaviour**

Balancing policy settings is one key consideration that should be taken into account when introducing or assessing regulatory schemes as will be demonstrated below.

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<sup>1</sup> For a discussion on importance of dispute resolution and compensation schemes and their limitations, see Commonwealth of Australia et al, *Review of the Financial System External Dispute Resolution and Complaints Framework* (Final Report, 2017).

<sup>2</sup> For a paper considering this issue, see for example: Fanci Cantatore and Brenda Marshall, 'A Step too far in Consumer Credit Protection: Are External Dispute Resolution Schemes Wielding the Sword of Damocles?' (2012) 40 *Australian Business Law Review* 322.

A move toward more aggressive and legalistic enforcement of corporate law has its advantages, making regulation more effective in some respects. When regulated entities know that harsher penalties may be applied this generally induces compliance with the law, leading in turn to a reduction in the number of unlawful acts.<sup>3</sup> However, overly complex regulation may also impose unreasonable compliance costs on those being regulated. Stringent regulation is designed to cope with 'bad apples' and unusually hard cases which, in reality, constitute a minority of all the problems in the domain of regulatory supervision. Most firms, being 'good apples', will accordingly, be subjected to an unreasonable burden of regulation. If this population ('good apples') is large, such burdensome regulation will appear even more unreasonable because it raises the costs of business, leading to lost opportunities for the progress of the 'good apples' businesses.<sup>4</sup>

This was illustrated by Bardach and Kagan when they observed that inspectors generally tended to look at the complete set of rules listed in the regulation and expected them to be followed. However, those rules might not be the most pertinent rules for preventing poor behaviour and thus the inspector's attention was diverted to trivial or immaterial matters. The rules may also be expensive to implement and not very relevant to preventing poor behaviour.<sup>5</sup> This could lead the inspector to fail to observe a source of potential harm that may not be explicitly covered by the rule. This blindness could also afflict the regulated entity, whose management may concentrate on the set of rules listed in the regulation and in so doing, fail to devote time and money to serious potential problems.<sup>6</sup> Greater communication between the regulators and the regulated entities is required, because such excessive legalism can lead to resentment on the part of the regulated entities, ultimately tending to destroy their cooperation with the regulators.

Furthermore, resentment and hostility from regulated entities can cause the following vicious cycle:

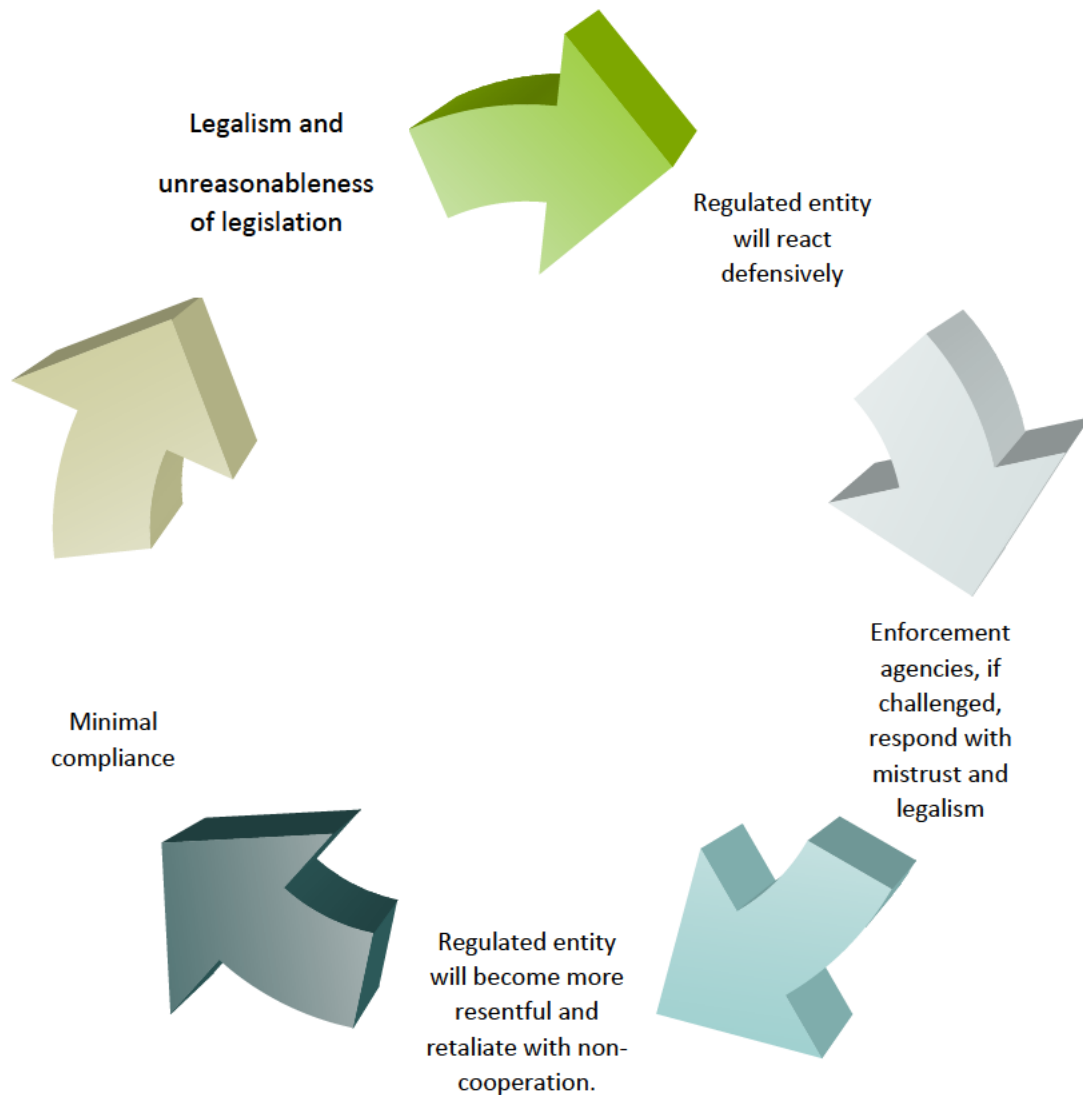
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<sup>3</sup> Ian Ayres and John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (Oxford University Press, 1992), 36.

<sup>4</sup> Bardach and Kagan, Eugene Bardach and Robert Kagan, *Going by the Book: The Problem of Regulatory Unreasonableness* (Temple University Press, 1982) 92–3.

<sup>5</sup> The rules in general cannot be detailed enough to cover all the different situations and dangers that may emerge from technological changes and human interaction.

<sup>6</sup> Bardach and Kagan, (n 4) 105.



Resentment towards the regulator can be fostered if a regulated entity believes that the rules imposed are unreasonable or excessively legalistic. For instance, if regulated entities have a fine imposed on them when they believe they have acted responsibly, the result may be counterproductive. Some business managers may respond by taking the position that they will act no more responsibly than the regulatory agency's rules require them to. This will lead to minimal compliance and more legalistic and unreasonable legislation.<sup>7</sup>

This once again highlights the importance of having a balanced set of policies in place that protects investors and consumers while at the same time allowing innovation in the market.

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<sup>7</sup> Bardach and Kagan, (n 4) 105.

**c. Whether ASIC is meeting the expectations of government, business and the community with respect to regulatory action and enforcement.**

**f. Resourcing allocated to ensure investigations and enforcement action progresses in a timely manner.**

Challenges may arise when considering whether ASIC meets the expectations of its stakeholders especially as expectations from government, business and community may vary and may even be competing. Accordingly, a robust empirical review should be undertaken to assess the views of stakeholders and how those views match with ASIC's mandate. This brings us back to a basic regulatory question raised by Black: What do we want to achieve with regulation?<sup>8</sup>

Furthermore, in terms of allocation of resources and meeting expectations, it is important to remember that ASIC has been the subject of several reviews in the past two years the latest being this one. In addition to this review, a few other reviews are ongoing and that may directly impact on ASIC's operations and may require the regulator to divert scarce resources to contribute to these reviews:

- Review of the Australian Securities and Investments Commission Industry Funding Model (ongoing)<sup>9</sup>
- Inquiry into Financial Services Legislation (ongoing)<sup>10</sup>
- Review of the Australian Securities and Investments Commission Annual Report 2021 (ongoing)<sup>11</sup>

Other reviews ASIC has been subjected of in the past two years include:

- PwC to review ASIC's infrastructure (2022)<sup>12</sup>
- Effectiveness and capability review of the Australian Securities and Investments Commission (2022)<sup>13</sup>
- Oversight of ASIC (2022)<sup>14</sup>
- The Thom Review on ASIC Governance (2021)<sup>15</sup>

The reviews that have already occurred have resulted in changes within ASIC's operation. However, it takes time to measure and assess the impact of the changes as a strategy needs time to take effect. The fact that ASIC is once more subject to a review means that resources may again be diverted to answer queries for the review and this may be counterproductive to ASIC's operation. It may be time to give ASIC a few years to absorb the impact and deal with the results of the recent reviews to see

<sup>8</sup> Julia Black, 'Critical Reflection on Regulation' (2002) 27 *Australian Journal of Legal Philosophy* 1.

<sup>9</sup> Department of Treasury (Cth), *Review of the Australian Securities and Investments Commission Industry Funding Model* (2022-Ongoing).

<sup>10</sup> Australian Law Reform Commission, *Inquiry into Financial Services Legislation* (2021-ongoing).

<sup>11</sup> Standing Committee on Economics, *Review of the Australian Securities and Investments Commission Annual Report 2021* (2022- ongoing)

<[https://www.aph.gov.au/Parliamentary\\_Business/Committees/House/Economics/ASICAnnualReport2021](https://www.aph.gov.au/Parliamentary_Business/Committees/House/Economics/ASICAnnualReport2021)>.

<sup>12</sup> Financial Regulator Assessment Authority, *Effectiveness and Capability Review of the Australian Securities and Investments Commission* (July 2022); See Australian Securities and Investments Commission, *ASIC Annual Report 2021-22* (Report, 14 October 2022) 12 [https://download.asic.gov.au/media/10dg0aqv/asic-annual-report-2021-22\\_full.pdf](https://download.asic.gov.au/media/10dg0aqv/asic-annual-report-2021-22_full.pdf)

<sup>13</sup> See Australian Securities and Investments Commission, *ASIC Annual Report 2021-22* (Report, 14 October 2022) 12 [https://download.asic.gov.au/media/10dg0aqv/asic-annual-report-2021-22\\_full.pdf](https://download.asic.gov.au/media/10dg0aqv/asic-annual-report-2021-22_full.pdf)

<sup>14</sup> Parliamentary Joint Committee on Corporations and Financial Services, *Oversight of ASIC, the Takeovers Panel and the Corporations Legislation* (2022); Australian Securities and Investments Commission, *ASIC Annual Report 2021-22* (Report, 14 October 2022) 11 [https://download.asic.gov.au/media/10dg0aqv/asic-annual-report-2021-22\\_full.pdf](https://download.asic.gov.au/media/10dg0aqv/asic-annual-report-2021-22_full.pdf).

<sup>15</sup> See Australian Securities and Investments Commission, *ASIC Annual Report 2020-21* (Report, 1 October 2021) 6 <https://download.asic.gov.au/media/2aaomxuz/asic-annual-report-2020-21-full-1.pdf>

whether the changes that have been incorporated over the last few years as a result of the reviews are making the ASIC a more effective regulator.

**d. the range of use of various regulatory tools and their effectiveness in contributing to good market outcomes;**

**e. the offence from which penalties can be considered and the nature of liability in these offences**

ASIC has a range of tools at its disposal that may allow it to take action to deal with misconduct. While ASIC does not have unlimited resources and is not able to take legal action against all offenders, it does have an arsenal of sanctions that, at different stages, may allow it to stop and even deter misconduct.

ASIC should have an understanding of the strength and weaknesses of each sanction and the role it can play in the regulator's enforcement strategy. Accordingly, sanctions at all levels should be used to enhance compliance of entities with the law.

**g. opportunities to reduce duplicative regulation**

Reducing duplicative regulation is very important however it is easier said than done as the statutes themselves, in a number of occasions, lead to duplicative regulation. Consequently, the *Corporations Act 2001* (Cth) needs to be reviewed and reassessed to deal with these duplications.<sup>16</sup>

Additionally, charities who are operating as companies limited by guarantee are subjected to a red tape as they have a range of obligations imposed by both the ACNC and ASIC. However, duties for directors in these charitable companies are currently suspended and as such directors of charities do not have these duties applying on them. That is a problem as under the current regime these directors may escape liability for breaching of their duties.

**h. Any other matter**

ASIC needs to improve its reporting on enforcement matters. Enforcement strategies need to be detailed and more in depth. Currently, the reporting is mediocre. For instance, contradictions between different ASIC reports are rife. A more consistent approach to reporting is needed.

**Conclusion**

While reviews are always welcomed, this review into ASIC's capacity and capability timing may be problematic as ASIC has been subjected to a number of reviews in the past years and it needs time to articulate and implement the changes it has done based on the recommendation of the different Inquiries. A review of the Corporations Act (not just a part of it) would be a positive action to ensure that the legislation is still fit for purpose. The current Corporations Act is a monolithic, clumsy collection of rules and a comprehensive review of the legislation should be undertaken to simplify this regime. Simplification of our legislation may have a positive impact on compliance, consumer protection and enforcement.

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<sup>16</sup> See discussion on this by the Australian Law Reform Commission, *Inquiry into Financial Services Legislation*.

If you have any queries, please do not hesitate to contact me at [REDACTED]

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27/02/2023