



## REPORTABLE SITUATIONS REGIME (BREACH REPORTING)

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### Key messages

- One of ASIC's key priorities for 2022-23 is undertaking a comprehensive program of work to improve the operation of the reportable situations regime (formerly known as breach reporting).
- ASIC is committed to ensuring the effective operation of the reportable situations regime. The lodgement of reports under this regime provides a critical source of intelligence which allows ASIC to detect significant non-compliant behaviours early, and enables ASIC to identify emerging trends of non-compliance in the industry.
- The reforms also introduced a legislative obligation on ASIC to publish information about reports received on an annual basis. The first of these reports has been recently published (see below).

### Background

- The reportable situations regime imposes obligations on Australian financial services and credit licensees to self-report instances of non-compliance to ASIC. The reforms included a number of changes to the former breach reporting regime, including a change in the 'significance' test to introduce a new category of "deemed significant breaches".
- We have identified a number of challenges associated with the implementation of the regime, including inconsistencies in interpretations and reporting practices.
- ASIC's program to improve the implementation of the regime is well underway. Key milestones so far include:
  - ASIC commenced targeted engagement with industry in September and October 2022. We circulated a Discussion Paper detailing 22 issues identified by ASIC with implementation of the regime and seeking feedback on proposed solutions. We have hosted roundtables with the FSC, ICA and ABA focusing on discussing solutions that could be quickly implemented by ASIC and engaged with other industry associations and licensees, inviting written responses to the Discussion Paper. The proposed solutions can be implemented through supplementary guidance or minor changes to the form in ASIC's Regulatory Portal. It is anticipated that the first tranche of practical solutions to these issues will be delivered by ASIC in early 2023.
  - The development of an API solution to enable licensees to report directly to ASIC's Regulatory Portal through their systems and reduce regulatory burden on licensees. This has now progressed to production in late October. Licensees can now commence development and testing of their own systems to facilitate bulk uploading/system-to-system reporting if they wish to do so.
  - Release of the first publication of key insights from the first nine months of the regime (see below for further detail).
  - Progression of work to improve ASIC's internal processes relating to data collection and analysis of reports.



## Reportable situations publication

- ASIC's first publication provides high-level insights into the trends we observed in the reports lodged by licensees in the reporting period (1 October 2021 - 30 June 2022). Key insights from this publication are below.
- There is a **lower level of compliance** with the regime than expected, with only 6% of the licensees lodging a report (3% of credit licensees, and 9% of AFS licensees). It is important to remember that lodgement of reports reflects the existence of adequate systems to detect and report non-compliance. Failure to detect non-compliance has impacts on rectification of the breaches and remediation of impacted customers.

What is ASIC doing about the low levels of compliance with the regime? As the regime has been in place for over 12 months now, we expect all licensees to be complying with the regime and are concerned by the low levels of compliance. We will be undertaking a range of activities to strengthen compliance with the regime.

**Who has reported the most to ASIC?** Our analysis indicates that the majority of reports were lodged by AFS licensees rather than credit licensees. Further, larger licensees lodged the majority of reports and were also significantly more likely to have lodged a report than smaller licensees. To illustrate that a greater proportion of larger licensees had lodged reports, the data shows that 61% of AFS Licensees with a revenue of \$1,000m or more lodged reports (compared to 5% of licensees with revenue of less than \$50m). To illustrate that these larger licensees lodged proportionately more reports – the data also indicates that these larger licensees only represented 5% of the licensees who lodged reports in total, yet they were responsible for 36% of all lodgements.

- **What was the most common breach reported?** Credit product lines were responsible for the largest subject of breaches and reports (38%), followed by general insurance (19%) and deposit-taking (10%). The products most commonly the subject of a report were home loans (25%) and motor vehicle insurance (13%), which were the primary drivers of credit and general insurance reports respectively.

Is ASIC concerned with the level of reports relating to responsible lending? There are a high level of reports relating to responsible lending but the reports do not point to wholesale non-compliance with the responsible lending regime by licensees. Rather, they reflect the lodgement of separate reports relating to one-off breaches of specific responsible lending obligations.

- **Time to investigate.** One-fifth of reports (18%, 1,567 reports) have indicated that it took the licensee more than one year to start an investigation into an issue after it had first occurred.

What is ASIC doing about the delays in investigation time? Delays in investigation of breaches are of concern to ASIC. Delays in investigations have two likely consequences: 1. A greater number of customers impacted by the conduct because underlying issues have not been rectified, and 2. Impacted customers wait longer to get compensated through remediation. ASIC is considering providing additional guidance to licensees to support improved practices in relation to the identification and investigation of breaches.

- **Remediation/rectification.** The data shows that in many cases remediation is taking licensees too long to complete (over 1 year to finalize compensation after commencement of an investigation in 12% of the reports). Further improvements are needed to licensees' practices towards remediating impacted customers. It is important that where things do go wrong, compensation of impacted customers is prioritised. Even more concerning, in a small percentage



of reports (4%), the licensee indicated they had no intention to compensate customers. It appears some of these were completed in error, but we are considering our regulatory response to the rest of these reports.

Why is the remediation figure so low? The data shows remediation paid to 30 June 2022 is \$51.6 million, yet ASIC has recently stated it has overseen remediation of \$5.6 billion in the last 6 years with \$1.6 billion yet to be paid. The figures in the publication reflect only a subset of the information we have about remediation. Specifically, the figures are only:

- for reports lodged within a specified, short period of time (Oct 21-Jun 22);
- what has been reported as paid by licensees to ASIC as of 30 June 2022;
- cover a subset of the reports lodged during the relevant period (because the reporting requirement only extends to a subset of reports lodged). For example, the publication does not include information or about 'additional reportable situations' such as gross negligence and serious fraud.

- **What was the main root cause of the breaches identified?** 60% of reports identified staff negligence or error as the root cause. However, ASIC has some concerns about whether in all these cases staff negligence was the underlying root cause, or whether there were systems or process issues responsible. This is because staff negligence or error was selected as the sole root cause in 55% of reports where the licensee had reported that there had been previous similar breaches and/or there were multiple breaches grouped into the relevant report.

Appropriately identifying the root cause of a breach is also an important part of a robust breach reporting process. This signals that the licensee has identified the cause of the underlying breach, can take steps to address systemic issues. As part of our broader program of work, we are engaging with industry in relation to the identification of staff negligence as a root cause in these reports. We intend to provide guidance on the circumstances in which it is appropriate to select 'staff negligence or error' as the root cause.

- **Customer impact.** 82% of reports involved impacted customers, financially and non-financially. Types of non-financial impact include distress, inconvenience and confusion. 23% of reports reported financial loss to customers.

Does the low number of financially impacted customers mean that the regime is mainly requiring the reporting of minor breaches? ASIC's view is that financial impact on customers may be understated, as there are indirect impacts that may not be obvious to the licensee (such as the flow-on effects of incorrect information being provided to credit rating agencies). A majority of reports (56%) impacted a single customer. However, around 15% of reports related to conduct that impacted 10 customers or more. A pure focus on financial impact on customers also fails to acknowledge there may be market integrity consequences of a breach.

- **Reporting volumes** have significantly increased under the regime. ASIC received a total of 11,070 reports and updates (under the old regime, ASIC received 2,435 reports and updates). This is in line with expectations of the regime, as is the finding that volume is being driven by "deemed significant" (automatically reportable) breaches (90% of reporting volume).

How many reports lead to a regulatory action of some kind by ASIC? Our enforcement work is informed by reports from a number of sources, including from the public, external administrators, auditors, other government agencies, media and breach reporting, as well as our own intelligence and surveillance activity. We triage and prioritise breach reports using risk-based criteria informed by our strategic and enforcement priorities and designed to help us identify the areas of



greatest harm. Given ASIC's finite resources, choices always have to be made about which of the many matters drawn to our attention can be pursued. We will always look to allocate our resources for maximum public benefit and to help maximise consumer outcomes.

- **Does the data suggest that most of the breaches reported are 'minor' breaches?** The report identifies that a large portion (over 90%) of the reports we received are "deemed significant breaches", with contraventions of misleading and deceptive conduct provisions accounting for over a third of reports that we received (34%). In addition, 73% of reports impacted one (1) customer or less (and as above, 23% involved financial loss to customers). The increase in 'deemed significant' breaches was an expected change as part of the reforms. What is important to note is that purely because a breach is 'deemed significant' does not mean that it has not had an adverse impact on customers or market integrity. Reports received carry regulatory intelligence beyond customer impact. They are also used to detect significant non-compliant behaviours early, and aggregated data from the reports can be used to identify and address emerging trends of non-compliance in industry.
- **Reporting inconsistencies.** The scale of the changes, alongside the principles-based nature of the regime, which applies to a wide array of licensees, has led to some inconsistent reporting practices between licensees.

*How reliable is the information in the report given these reporting inconsistencies?* We have been mindful of these inconsistencies in drafting the publication and accordingly:

- the publication does not name licensees or provide granular data because comparisons between licensees are unlikely to provide meaningful insights, given the current inconsistencies.
- the insights included in the publication should be read in context, taking into account the number and nature of reports received by (and licensees who reported to) ASIC in the reporting period.

Our program of work to address these inconsistencies will assist in our ability to report on a more granular level in future reports (likely 2024 onwards given the time it will take for changes in practices to take effect). We will also consult prior to making any changes regarding licensee level reporting.

- **What information has ASIC received under the new provision for licensees to report about other licensees, and what action has ASIC taken?** Under the reform that came into force on 1 October 2021, licensees have an obligation to lodge a breach report where a reportable situation arises in relation to another licensee, if that other licensee:
  - provides personal financial advice to retail clients about certain financial products (Corporations Act s912AD), or
  - is a mortgage broker (National Credit Act s50C).

During the period between 1 October 2021 and 30 June 2022:

- 121 reports were made to ASIC about another licensee.
- 44 licensees reported about 85 other licensees.
- 55 reports (46%) were about the conduct of representatives, 34 (28%) about both the other licensee and their representatives, and 32 (26%) about the other licensee.

ASIC's consideration of these reports is in line with its processes to identify, triage and respond to all breach reports. This may lead, in some cases, to engagement with the reporting licensee for additional information, surveillance of investigation.



The information is also used for overall regulatory intelligence purposes. It is just one of a number of sources to help us identify the areas of greatest harm.

These reports are not part of the information which ASIC is required to publish annually.

In preparing this first high-level insights publication, ASIC has chosen to focus on the information we are required to report.

- **What are the penalties for a failure to comply with the reportable situations regime?** Failure to report to ASIC when a reportable situation has arisen can attract both civil and criminal penalties. In most cases, the maximum civil penalty is \$11.1million. Criminal penalties may include fines and/or two years imprisonment. A failure to report would always be considered alongside other information ASIC receives or is in possession of in the course of its regulatory activities. ASIC also has a range of other options available to respond to contraventions of the law. This includes restrictions on licensed activity, infringement notices, and court enforceable undertakings. ASIC's approach to enforcement is outlined in INFO 151.
- *Has ASIC taken action against any licensee for a failure to comply with the regime since 1 Oct?* ASIC's focus has been on addressing challenges that licensees have experienced implementing the new regime. The new reportable situations regime differs significantly to the old breach reporting regime and all licensees – large and small – have struggled, to some extent, to comply with the new regime and to put in place the required systems. Licensees are also uncertain about some aspects of the new regime. They are unclear about exactly what is required to comply. For this reason, we are proposing to provide extra guidance. However, if we have evidence of significant failure to comply with the new regime, we will take appropriate enforcement action. Having said this, I note that at this stage we do not have evidence of such a failure. Failure to lodge even a single report with ASIC is not, in itself, evidence of failure to comply with the regime.

#### Attachments

- On the 10<sup>th</sup> of August, ASIC released [22-214MR ASIC's approach to breach reporting: implementation of reportable situations regime](#)
- On the 27<sup>th</sup> of October, ASIC published [REP 740 Insights from the reportable situations regime: October 2021 to June 2022](#) with accompanying media release [22-295MR Breach reporting: ASIC publishes insights from the reportable situations regime](#)