



3 June 2021

Niki De Mel, Strategic Policy Adviser
Strategy Group
Australian Securities and Investments Commission

By email to: BR.submissions@asic.gov.au

Dear Niki,

AIST submission: ASIC CP 340 – Breach reporting and related obligations

In brief: AIST supports the new breach reporting regime and welcomes greater transparency and accountability requirements. We suggest further enhancements to the guidance on what constitutes ‘core obligation’, ‘significance’, ‘material loss or damage’, and requirements relating to ‘investigations’ to provide greater clarity and assist licensees in meeting their new obligations.

AIST also points to the short implementation time given to licensees, noting ASIC’s intention to release final guidance three months prior to the obligations commencing.

The Australian Institute of Superannuation Trustees (AIST) is a not-for-profit organization whose membership consists of the trustee directors and staff of industry, corporate, and public sector superannuation funds.

As the principal advocate and peak representative body for the \$1.5 trillion profit-to-members superannuation sector, AIST play a key role in policy development and is a leading provider of research.

AIST advocates for financial wellbeing in retirement for all Australians regardless of gender, culture, education, or socio-economic background. Through leadership and excellence, AIST supports profit-to-member funds to achieve member-first outcomes and fairness across the retirement system.

Summary

AIST is responding to this submission by addressing questions asked in CP 340 which are pertinent to its superannuation member funds.

AIST welcomes changes to the breach reporting regime to implement Recommendation 7.2 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Sector

(FSRC). We address relevant concerns directly in the questions under each proposal and highlight that overall, there is a need for further guidance on key elements of Draft RG 78.

We welcome the extended reporting timeframe from 10 calendar days to 30 calendar days and acknowledge the intent of introducing a level of objectivity to the breach reporting regime. However, AIST considers there is scope for additional guidance on key themes that will assist AFS licensees meet the breach reporting obligations:

- **On ‘reportable situations’**
- **On requirements relating to investigations**
- **On materiality and what constitutes ‘material loss or damage’**
- **On ‘Significance’**
- **On notifying a reportable situation to an affected client**

Whilst we address specific elements about the detail of the guidance, consultation with member superannuation funds has raised concerns over the timing licensees will have to implement relevant requirements given the short amount of time between the release of the final guidance and when the obligations commence.

Responses to CP 340 – Breach reporting and related obligations

Proposal B1

B1Q1 Do you agree with our proposed approach? If not, why not?

AIST agrees with ASIC’s proposal to provide consistent guidance for AFS licensees on how they can comply with the breach reporting obligation and welcomes implementation of Recommendation 7.2 of the FSRC.

We note that although consistent guidance is important, the depth of the guidance is equally as significant.

Whilst Draft RG 78 provides breadth of guidance, AIST, in consultation with its member superannuation funds, considers AFS licensees would be assisted by the provision of clearer and further guidance on the following themes:

- On reportable situations:
 - Breaches or likely breaches of ‘core obligations’ – the scope is extensive and although the draft guide introduces a level of objectivity, the high-level approach to guidance continues to leave room for subjective assessment of breaches by AFS licensees;

- Additional reportable situations – gross negligence is not defined in the *Corporations Act* and there is no regulatory guidance as to what would constitute gross negligence;
- Reportable situations about other AFS licensees – clarity sought around when the timeframe commences for the AFS licensee being reported
- On requirements relating to investigations:
 - Further clarity on when an investigation starts, including when the investigation is outsourced – the Explanatory Memorandum (EM) and Draft RG 78 still leave an element of subjectivity up to the AFS licensee;
 - There is little guidance on the interaction between a standard complaint investigation that could become an investigation of a (likely) breach, and how this impacts the 30-day requirement to report a reportable situation
- On materiality and what constitutes ‘material loss or damage’:
 - the guidance leaves it up to the AFS licensee to determine material loss or damage, which may include financial loss, but it does not specify the level of financial loss, and leaves out what material loss would be in a non-financial context
- On ‘Significance’:
 - AIST found matters related to ‘significance’ to be broad in scope and further guidance, including case studies or examples, would assist licensees understand their obligations
- On notifying a reportable situation to an affected client:
 - Concerns surround this requirement as the wording in s912EA references four criteria that must be met for the obligation to notify must apply. We highlight that the first criterion states:
 - ‘...the licensee provides or has provided personal advice to the affected client’
 - The wording is explicit in stating that an affected client receives or has received personal advice for the requirement to notify to apply
 - Feedback from member superannuation funds relates to the issue of how ‘provides or has provided personal advice’ is to be interpreted. A ‘reportable situation’ may not be due to personal advice; however, if a member (affected client) has previously received personal advice, this would suggest that the member needs to be notified
 - For example, a reportable situation arises due to a breach of a core obligation resulting from incorrectly overcharged administration fees to 100,000 members over 4 weeks. The licensee determines that material loss or damage has occurred, and so determines a reportable situation has arisen.

- Under s912EA(1)(a) only those members who the licensee 'provides or has provided personal advice' need to be notified. This could be interpreted as the licensee having to notify only those members out of 100,000 who at one point or another received personal advice, even if the incident is unrelated to such advice; all other members impacted would not have to be notified based on the wording outlined above.
- It would assist licensees if clarity could be provided on whether the reportable situation must relate to the provision of personal advice, and broadly outline ASIC's understanding of s912EA in this context.

Proposal B2

B2Q1 Are there any specific issues, incidents, challenges or areas of concern you think we should include as examples, case studies or scenarios? If so, please provide details and explain why they should be included.

AIST welcomes the proposal to include case studies and scenarios to supplement ASIC's general guidance.

Our review of the guidance and feedback from our superannuation fund members highlight the benefit of including (in some cases, additional) case studies or worked examples in relation to the following topics:

- Investigations of reportable situations – AIST acknowledges the two examples set out in Table 6 of Draft RG 78; however, the case studies leave room for clarity on when an investigation would be deemed to have commenced, in particular where there is a complaint involved
- Reportable situations about other licensees – guidance would be enhanced by the provision of examples in the context of superannuation, including clarity on when the 30 days to report to ASIC starts for the licensee being reported, and how an AFS licensee should manage different reporting obligations (for example, when there is a reportable situation to AUSTRAC and this report cannot be provided to the AFS licensee being reported)
- Material loss or damage to members of a superannuation fund – AIST acknowledges the example provided in Table 2; however, additional examples or case studies on what may constitute material loss or damage will assist with guidance, including examples where material loss or damage is not financial in nature

Proposal B4

B4Q1 Do you agree with our proposed approach? If not, why not?

AIST agrees with the provision of guidance to help AFS licensees identify what they must report on. AIST acknowledges the proposed high-level approach; we also welcome how the draft guidance seeks to establish an objective approach to what must be reported to ASIC, such as the introduction of 'deemed significance'.

However, the high-level approach to some key elements in the draft guide create uncertainty in how and what AFS licensees must report to ASIC. There is a risk that a lack of more granular guidance on what must be reported to ASIC may result in licensees inadvertently breaching their obligations as they may interpret guidance differently to how ASIC might do so.

B4Q2 Should we include further guidance on what constitutes a 'core obligation'? if so, please provide details.

The definition of 'core obligation' largely reflects existing obligations in s912A and 912B of the *Corporations Act 2001* (the Act). A breach or likely breach of a core obligation captures a wide range of scenarios and includes any contravention of a civil penalty provision.

Considering the scope of civil penalty provisions and what may amount to trivial breaches, AIST considers that high-level guidance does not provide sufficient objectivity to assist AFS licensees determine if a breach or likely breach of a core obligation is a reportable situation. AIST supports measures that enhance breach reporting but notes that there is scope in Draft RG 78 for additional and targeted guidance on what constitutes 'core obligation'.

B4Q3 Should we include further guidance on how to determine whether a breach or likely breach of a core obligation is 'significant'? if so, please provide details.

AIST supports the provision of further guidance on how to determine whether a breach or likely breach of a core obligation is 'significant'. 'Significance' is not defined, and although we welcome the intent of objectivity by the introduction of 'deemed significance', the broad scope of civil penalty provisions leaves room for specific examples or case studies using one of the many civil penalty provisions outlined in the *Corporations Act*.

For example, Draft RG 78 outlines Example 3(b) for when a 'breach that may be significant under s912D(5) or s50A(5)' occurs. In this example, the licensee has failed to follow disclosed investment mandates. The example is given in regard to ESG but it could be any form of breach. Breach of investment guidelines in Draft RG 78 need to provide greater clarity on what is deemed 'significant' or a 'reportable situation'. For example, is overweight equities versus benchmark, or an incorrectly traded security due to an operational error, considered a reportable situation and/or 'significant'?

In relation to 'deemed significance', we acknowledge its objective application to investigations that take more than 30 days, but would welcome further clarity and guidance on the 'material loss or damage' aspect, in particular more examples of what constitutes 'material loss or damage' both in financial and non-financial terms given that any such loss could result in a breach being deemed significant.

B4Q4 Should we include further guidance on reporting an 'investigation' to ASIC? If so, what should be clarified? Please provide examples of scenarios (where relevant).

AIST has received feedback from member superannuation funds in relation to 'investigations'. In particular, there are only two examples in the draft guidance that outline how investigations are treated. Guidance would be enhanced by providing clarity on when an investigation commences. The term 'investigation' is not defined, and the Explanatory Memorandum (EM) provides only some clarity as to what an investigation is and when an investigation begins.

The EM states that when an investigation commences is "a matter of fact"; however, it is unclear when an investigation into a complaint becomes an investigation into a breach or likely breach.

The wording in the EM is subjective and leaves room for discrepancy as to when ASIC may consider an investigation into a breach commenced or when a licensee does. The EM and draft guidance as written result in a licensee still having to form a view of when the 30 days commenced.

A worked example or case study would assist in providing guidance to licensees.

B4Q5 Should we include further guidance on what constitutes 'material loss or damage'? If so, what examples should be clarified? Please provide examples of scenarios (where relevant).

AIST supports further guidance on what constitutes 'material loss or damage'. Given that it is not a defined term, and there is only one example/case study in the draft guide relating to superannuation, we consider it would assist licensees if further examples were developed to provide guidance. In particular, an expansion of what relevant circumstance a licensee may have to consider other than the financial circumstances of a person.

The draft guide and EM continue to be subjective in the treatment of *material* loss or damage and addressing this subjectivity by providing additional examples would enhance guidance for licensees.

B4Q6 Should we include further guidance on reportable situations involving serious fraud or gross negligence? If so, what are the challenges licensees face in identifying when serious fraud or gross negligence has occurred?

We consider that case studies or examples of gross negligence in the context of a superannuation scenario would assist licensees understand ASIC's approach to gross negligence, noting that, unlike 'serious fraud', it is not a defined term.

B4Q7 Should we include further guidance on reportable situations about other licensees? If so, please provide details.

AIST acknowledges the guidance already provided in relation to reportable situations about other licensees. Further guidance is welcome in relation to when the 30 days within which a report must be lodged with ASIC commences for the licensee being reported on. In addition, clarity is sought on how a licensee would treat a reportable situation that must also be reported to another body, such as AUSTRAC, where a reporting licensee, due to its parallel obligations to such body, may not be able to meet the obligation to give a copy of the report to the licensee being reported on.

Proposal B5

B5Q1 Should we include further guidance to help licensees understand when to report to ASIC? If so, please provide details, including what guidance would be helpful and why.

We consider it would be helpful to include further guidance. In particular, further clarity on the matter of 'knowledge', which we address in B5Q2.

Example 11.2 of the *Financial Sector Reform Bill's* Explanatory Memorandum (EM) usefully outlines a situation where a licensee must report a reportable situation after 30 days of investigation. It goes on to show that the outcome of that investigation must be reported within 10 days. Further clarity on this requirement would be useful. For example, what is the requirement for a licensee if the investigation has not yet concluded after the 10 days?

B5Q2 Should we include further guidance on what may amount to 'knowledge', 'recklessness' and 'reasonable grounds'? If so, please explain what specific guidance would be helpful and why.

AIST acknowledges the guidance around 'recklessness' and 'reasonable grounds'.

In relation to 'knowledge', we highlight paragraphs RG 78.74, RG 78.75 and RG 78.77, which go to the issue of a person's actual or apparent authority when considering who within the licensee 'first knows' or is reckless as to whether there are reasonable grounds to believe a reportable situation has arisen. It is our understanding that a licensee will still have to form a view as to whether a person has actual or apparent authority, and is not necessarily a matter of fact; unless, that is, a licensee specifically ascribes authority in the context of this regime. Further guidance would assist in clarifying this for licensees.

Feedback from member superannuation funds relates to first and second lines of compliance, where the licensee may consider their second line of compliance to be the relevant starting point of the investigation as the relevant body with 'knowledge' of reasonable grounds that a reportable situation exists.

Case study 4 of the draft guide helpfully highlights when the 30 day reporting timeframe commences, but it is unclear from this example when it would commence when considering a front line business unit. Further guidance and case studies on this issue would assist with guidance.

Proposal B6

B6Q1 Do you have any feedback about the types of information we propose must be included in the prescribed form? If so, please provide details, and identify any issues.

AIST generally supports the content outlined in Table 8.

It would be helpful if clarification could be provided where a licensee is aware that it must report a breach or likely breach to ASIC, but has partial information (i.e. 'knowledge' can be ascribed to the licensee or a representative, but the prescribed information required in the form is not fully available).

B6Q2 Should we include any other information in the prescribed form? If so, please provide details.

We have no additional feedback on the prescribed form at this stage.

B6Q3 Do you have any concerns about the types of information in the prescribed form and whether this information can be provided within the prescribed 30-day time period? If so, please provide details?

We have raised our concerns in relation to incomplete information in respect of the prescribed form – see B6Q1.

Proposal B7

B7Q1 Do you agree with our proposed approach? If not, why not?

AIST acknowledges and agrees with the approach to provide high-level guidance on compliance systems for breach reporting.

B7Q3 are there any challenges that you would face in applying our guidance to your specific circumstances (i.e. the nature, scale or type of your business)? If so, please provide details.

AIST has heard feedback from member superannuation funds in relation to the implementation of the proposed guidance. Concerns have been raised particularly in relation to technology solutions (such as a registry system) already in place which have scheduled or designated fixes (or ‘patches’) intended to upgrade or improve said system. These ‘patches’ may not fall within the prescribed period by ASIC, and updating or aligning these patches would prove costly, resource intensive, and with marginal impact to the remediation process. Ultimately, the cost would be borne by members.

Proposal C2

C2Q1 Do you agree with our proposed approach? If not, why not?

AIST supports the intent of the actions outlined in Draft INFO 000 (draft sheet) and supports measures that ensure transparency and accountability on licensees.

We support transparency in reporting and welcome some of the actions listed in the draft sheet; however, AIST and its members have concerns regarding Action 1 and the requirement to notify a client of a potential breach before an investigation into the nature of the breach is completed. This could lead to:

- Poor member experience – premature communication risks misunderstanding;
- Unnecessary distress to the client without having all the information necessary to explain the nature of the breach or likely breach; and
- Triggering complaints that may or may not be necessary, increasing the administrative burden unnecessarily.

Further to these concerns, the licensee may not have all the information available to clearly and concisely communicate the issue with the client.

Action 3 of the sheet states that an AFS licensee must notify affected clients of the outcome of the investigation within 10 days of it concluding. We note that the practicality of meeting this timeframe is contentious, particularly relating to:

- drafting and issuing written client communications; and
- the administrative burden and substantial cost in notifying clients of the outcome of an investigation before a ‘remediation’ solution can be finalised.

We consider that an investigation needs to conclude and identification of a breach of law must occur before any communication to clients commences.

AIST reiterates its support for the intent of the measures being introduced and looks forward to reviewing the final guidance.

For further information regarding our submission, please contact Carlos Lopez, Policy and Regulatory Analyst, at [REDACTED]

Yours sincerely,

[REDACTED]

Eva Scheerlinck
Chief Executive Officer

The Australian Institute of Superannuation Trustees is a national not-for-profit organisation whose membership consists of the trustee directors and staff of industry, corporate and public-sector funds.

As the principal advocate and peak representative body for the \$1.4 trillion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research.

AIST provides professional training and support for trustees and fund staff to help them meet the challenges of managing superannuation funds and advancing the interests of their fund members. Each year, AIST hosts the Conference of Major Superannuation Funds (CMSF), in addition to numerous other industry conferences and events.