



## Parliamentary Joint Committee on Corporations and Financial Services

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Report on the 2014-2015 annual reports of bodies  
established under the ASIC Act

May 2016

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## Duties of the Committee

Section 243 of the *Australian Securities and Investments Commission Act 2001* sets out the Parliamentary Committee's duties as follows:

- (a) to inquire into, and report to both Houses on:
  - (i) activities of ASIC or the Panel, or matters connected with such activities, to which, in the Parliamentary Committee's opinion, the Parliament's attention should be directed; or
  - (ii) the operation of the corporations legislation (other than the excluded provisions); or
  - (iii) the operation of any other law of the Commonwealth, or any law of a State or Territory, that appears to the Parliamentary Committee to affect significantly the operation of the corporations legislation (other than the excluded provisions); or
  - (iv) the operation of any foreign business law, or of any other law of a foreign country, that appears to the Parliamentary Committee to affect significantly the operation of the corporations legislation (other than the excluded provisions); and
- (b) to examine each annual report that is prepared by a body established by this Act and of which a copy has been laid before a House, and to report to both Houses on matters that appear in, or arise out of, that annual report and to which, in the Parliamentary Committee's opinion, the Parliament's attention should be directed; and
- (c) to inquire into any question in connection with its duties that is referred to it by a House, and to report to that House on that question.



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# Abbreviations

AAT	Administrative Appeals Tribunal
AASB	Australian Accounting Standards Board
ACCC	Australian Competition and Consumer Commission
ANAO	Australian National Audit Office
APRA	Australian Prudential Regulation Authority
APX	Australia Pacific Exchange
ASIC	Australian Securities and Investments Commission
ASIC Act	<i>Australian Securities and Investments Commission Act 2001</i>
ASX	Australian Securities Exchange
AUASB	Auditing and Assurance Standards Board
CALDB	Companies Auditors and Liquidators Disciplinary Board
CAMAC	Corporations and Markets Advisory Committee
CAMAC Bill	Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014
CIO	Credit and Investments Ombudsman
Corporations Act	<i>Corporations Act 2001</i>
CSEF	Crowd Sourced Equity Funding
EU	Enforceable Undertakings
FOS	Financial Ombudsman Service
FRC	Financial Reporting Council
FSI	Financial System Inquiry
IASB	International Accounting Standards Board
IAASB	International Auditing and Assurance Standards Board
IFRS	International Financial Reporting Standards
PGPA Act	<i>Public Governance, Performance and Accountability Act 2013</i>
SMSF	Self-Managed Super Fund
The Panel	Takeovers Panel



## **List of recommendations**

### **Recommendation 1**

**4.20** The committee recommends that the government consider the suggestions that ASIC has made in relation to reforms of section 631 of the Corporations Act.

### **Recommendation 2**

**4.41** That the government consider strengthening the register by enabling the inclusion of retrospective data on banned and disqualified financial advisers on the Financial Advisers Register.



# Chapter 1

## Scrutiny of annual reports

1.1 The Parliamentary Joint Committee on Corporations and Financial Services (the committee) is established by Part 14 of the *Australian Securities and Investments Commission Act 2001* (the ASIC Act). This report is prepared in fulfilment of the committee's duties under subsection 243(b) which is:

to examine each annual report that is prepared by a body established by this Act and of which a copy has been laid before a House, and to report to both Houses on matters that appear in, or arise out of, that annual report and to which...the Parliament's attention should be directed.<sup>1</sup>

1.2 The ASIC Act establishes nine bodies which are listed below:

- Auditing and Assurance Standards Board (AUASB);
- Australian Accounting Standards Board (AASB);
- Australian Securities and Investments Commission (ASIC);
- Companies Auditors and Liquidators Disciplinary Board (CALDB);
- Corporations and Markets Advisory Committee (CAMAC);
- Financial Reporting Council (FRC);
- Office of the Australian Accounting Standards Board (Office of the AASB);
- Office of the Auditing and Assurance Standards Board (Office of the AUASB); and
- The Takeovers Panel (the Panel).<sup>2</sup>

1.3 Collectively, these bodies form the 'administrative organs' of the national financial services regulatory scheme established by the ASIC Act and the *Corporations Act 2001* (Corporations Act).<sup>3</sup>

1.4 While nine bodies are established under the ASIC Act, only six annual reports have been prepared for 2014–15. The ASIC Act directs that one annual report will cover both the AASB and the Office of the AASB. Similarly, the AUASB is required to prepare an annual report that addresses its activities and the activities of the Office

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1 *ASIC Act 2001*, s. 243 (b).

2 *ASIC Act 2001*, Parts 2, 9–12.

3 The Hon Lionel Bowen MP, Attorney-General, House of Representatives Hansard, Second Reading Speech, Australian Securities Commission Bill 1988, 25 May 1988, p. 2991. The ASIC Act predominantly replicates the administrative structure established in the Australian Securities and Investments Commission Act 1989. Section 261 of the ASIC Act 2001 directs that bodies established under the Australian Securities Commission Act continue in existence as if they had been established under the ASIC Act 2001.

of the AUASB. CAMAC did not prepare an annual report for 2014–15 as it has ceased operations pending passage of the Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014.<sup>4</sup> Accordingly, this report examines the 2014–15 annual reports of the AASB, the AUASB, ASIC, CALDB, the FRC and the Takeovers Panel.

1.5 The committee notes that the annual reports of bodies established under the ASIC Act are also the subject of scrutiny by the Senate Economics Legislation Committee. Senate Standing Order 25(20) requires the Economics Committee to:

- (a) Examine each annual report referred to it and report to the Senate whether the report is apparently satisfactory.
- (b) Consider in more detail, and report to the Senate on, each annual report which is not apparently satisfactory, and on the other annual reports which it selects for more detailed consideration.
- (c) Investigate and report to the Senate on any lateness in the presentation of annual reports.
- (d) In considering an annual report, take into account any relevant remarks about the report made in debate in the Senate.
- (e) If the committee so determines, consider annual reports of departments and budget-related agencies in conjunction with examination of estimates.
- (f) Report on annual reports tabled by 31 October each year by the tenth sitting day of the following year, and on annual reports tabled by 30 April each year by the tenth sitting day after 30 June of that year.
- (g) Draw to the attention of the Senate any significant matters relating to the operations and performance of the bodies furnishing the annual reports.
- (h) Report to the Senate each year whether there are any bodies which do not present annual reports to the Senate and which should present such reports.

1.6 Therefore, in conducting its review of the annual reports of bodies established under the ASIC Act, the committee will focus on operational matters of interest and raise other matters that in the committee's opinion Parliament should consider. Chapter two examines the annual reports of the bodies established under Parts 9–11 of the ASIC Act: CALDB and the Takeovers Panel. Chapter three examines the annual reports of the three agencies established by Part 12 of the ASIC Act to oversee the financial reporting framework: the AASB, the AUASB and the FRC. Chapter four examines ASIC's annual report.

1.7 In reviewing the annual reports, the committee also considers whether there are opportunities to strengthen the operation of the corporations legislation, however the committee is not proposing any changes in this report.

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4 For detail on the status of CAMAC please see Chapter 2 of this report.

## Chapter 2

### Bodies established under Parts 9–11 of the ASIC Act

2.1 This chapter considers the 2014–15 annual reports of the:

- Companies Auditors and Liquidators Disciplinary Board (CALDB); and
- The Takeovers Panel (the Panel).

2.2 This chapter also discusses the status of the Corporations and Markets Advisory Committee (CAMAC).

#### Companies Auditors and Liquidators Disciplinary Board

2.3 CALDB was first established as an independent statutory body in 1989 and is currently established by Part 11 of the ASIC Act. Its primary purpose, in the administration of Australia's financial services system, is to hear applications and consider cancellation or suspension of a liquidator's or auditor's registration. The Board's casework is not self-generated as it holds no powers to instigate applications. Rather, applications are brought by either ASIC or the Australian Prudential Regulation Authority (APRA) for the Board's adjudication.<sup>1</sup> Accordingly, the Board operates as an expert disciplinary body for auditors and liquidators in Australia.

2.4 CALDB's 2014–15 annual report states:

The responsibilities conferred on CALDB by the Corporations Act are intended to provide an incentive to registered auditors and liquidators to maintain high professional standards. CALDB's jurisdiction to cancel or suspend the registration of an auditor or liquidator also has a public protective and educative role.<sup>2</sup>

#### *Annual report of CALDB*

2.5 The ASIC Act directs that the annual report is to 'describe the operations' of CALDB for the relevant financial year.<sup>3</sup> New applications received by CALDB are categorised as either 'administrative' or 'conduct'. There were two new applications to CALDB by ASIC in 2014–15. Both of these applications were conduct matters. No administrative applications were received. One of the matters received related to auditors, and one related to liquidators.<sup>4</sup> During 2014–15 three matters were heard, leading to orders being issued for suspension of registration in one matter and the board issuing an admonishment in another. The decision for the third matter will be delivered in 2015–16.<sup>5</sup>

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1 *Corporations Act 2001*, Part 9.2, Division 3.

2 CALDB, *Annual Report: 2014–15*, p. 4.

3 *ASIC Act 2001*, s. 214.

4 CALDB, *Annual Report: 2014–15*, p. 7.

5 CALDB, *Annual Report: 2014–15*, pp 8, 23.

2.6 An analysis of data provided in previous annual reports indicates that the Board's case load has significantly declined since 2004–05 (see Figure 2.1). During 2014–15 there was also a decline in the hearings workload from 71 to 26 person days and this contributed to a decrease in member's fees, from \$456,000 in the previous year to \$349,000 in 2014–15. The committee notes that for this reporting period the Board has operated without its full complement of 14 members.<sup>6</sup>

**Table 2.1: Number of cases referred: 2003–04 to 2014–15<sup>7</sup>**

Financial Year	Auditors	Liquidators
2014–15	1	1
2013–14	2	2
2012–13	1	4
2011–12	5	2
2010–11	2	1
2009–10	0	0
2008–09	11	1
2007–08	5	0
2006–07	7	0
2005–06	9	3
2004–05	23	12
2003–04	32	1

2.7 During the 2014–15 financial year, two applications for decisions made by CALDB were referred to the AAT. The first application was still the subject of proceedings before the AAT at the time of reporting. The outcome of the second application was unsuccessful with CALDB's decision to suspend the registration of a registered auditor affirmed by the AAT.<sup>8</sup> No applications for judicial review were made during this period.<sup>9</sup>

2.8 The committee considers that CALDB has fulfilled its regulatory and reporting responsibilities during the 2014–15 financial year.

6 CALDB, *Annual Report: 2014–15*, pp 1, 7, 10.

7 CALDB, *Annual report: 2014–15*, p. 7; CALDB, *Annual report: 2013–14*, p. 6; CALDB, *Annual report: 2012–13*, pp 7–8; CALDB, *Annual report: 2011–12*, p. 13; CALDB, *Annual report: 2010–11*, p.13; CALDB, *Annual report: 2009–10*, pp 14–15; CALDB, *Annual report: 2008–09*, pp 13–14; CALDB, *Annual report: 2007–08*, pp 13–14; CALDB, *Annual report: 2006–07*, pp 13–14; CALDB, *Annual report: 2005–06*, p. 11; CALDB, *Annual report: 2004–05*, p. 11; CALDB, *Annual report: 2003–04*, p. 10.

8 CALDB decisions, <http://www.caldb.gov.au/decisions/caldb-decisions/> (accessed 4 April 2016)

9 CALDB, *Annual Report: 2014–15*, pp 10, 12.

## The Takeovers Panel

2.9 The Takeovers Panel (the Panel) was established by Part 10 of the *Australian Securities and Investments Commission Act 2001* as a peer review body largely comprised of takeover experts, whose main purpose is the resolution of takeover disputes. During a takeover bid, the Panel is able to declare unacceptable circumstances with respect to the public interest in relation to the affairs of a company, in addition to establishing orders to remedy those circumstances.<sup>10</sup>

2.10 The Panel is also able to review decisions made by ASIC<sup>11</sup> and maintains its operations with a rule making power.<sup>12</sup> The Panel's annual report states that:

The Panel improves the certainty, efficiency and fairness of Australia's takeovers market by:

- resolving disputes in a fair, timely, consistent, informal and sound manner; and
- publishing clear, well-developed guidance.<sup>13</sup>

2.11 As at 30 June 2015, the Panel had 38 members, up from 37 at 30 June 2014.<sup>14</sup> Members are nominated by the Minister and appointed by the Governor-General.<sup>15</sup> Members are chosen so that there is a mix of expertise, geographical representation and gender.<sup>16</sup>

### *Annual Report of the Takeovers Panel*

2.12 Since the committee last reported on the Takeovers Panel, the *Corporations Legislation Amendment (Deregulatory and Other Measures) Act 2014* was enacted. This amended sections 184 and 188 of the ASIC Act to allow:

- Panel members to participate in proceedings whether or not they are physically located in Australia; and
- the President to give a direction about the members who are to constitute the Panel whether or not the President is physically located in Australia.<sup>17</sup>

2.13 During the 2014–15 financial year, the Panel received 20 applications. This was below the yearly average of 30 applications and below the 26 applications received in 2013–14. It is the same number as those received in the 2012–13 year.<sup>18</sup>

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10 *Corporations Act 2001*, s. 657A.

11 *Corporations Act 2001*, s. Part 6.10, Division 2.

12 *Corporations Act 2001*, s. 658C.

13 Takeovers Panel, *Annual Report 2014–15*, p. 7.

14 Takeovers Panel, *Annual Report 2014–15*, p. 4; Takeovers Panel, *Annual Report 2013–14*, p. 4.

15 *ASIC Act 2001*, s. 172.

16 Takeovers Panel, *Annual Report 2014–15*, p. 12.

17 Takeovers Panel, *Annual Report 2014–15*, p. 24.

18 Takeovers Panel, *Annual Report 2014–15*, pp 5, 20; *Annual Report 2013–14*, p. 3.

2.14 The Panel declined to conduct proceedings for 60 per cent of the applications it received.<sup>19</sup> Over the previous decade, the proportion of applications for which the Panel declined to conduct proceedings has grown steadily from 6% in 2001 to 60% in 2014–15.<sup>20</sup> In its annual report, the Panel indicates that when determining whether to conduct proceedings it gives weight to:

Whether the circumstances complained of would give rise to a declaration of unacceptable circumstances if established, given the strength of the evidence, and the remedies that might be available.<sup>21</sup>

2.15 Three declarations and/or orders were issued in 2014–15, however no undertakings were requested. The Panel conducted proceedings with three cases in which unacceptable circumstances were deemed to be present. Proceedings were withdrawn in one case throughout the 2014–15 year.<sup>22</sup> The issues raised in applications included association/breach of section 606, rights issues, disclosure, contravention of the substantial holding provisions, frustrating action and disclosure and voting in relation to a scheme of arrangement.<sup>23</sup>

2.16 The annual report indicates a decrease of time between a Panel decision and its publication of reasons. The average number of calendar days between a decision and the publication of reasons was 11.8 days for 2014–15, down from 12.1 days in 2013–14. This is also below the average of 36.8 calendar days since March 2000. The time between receipt of an application and a decision also decreased, with an average of 11.3 days, down from an average of approximately 15 days since March 2000.<sup>24</sup>

2.17 In the annual report the Panel notes the fact that it has increasingly declined to conduct proceedings but also notes that it has made more declarations of unacceptable circumstances when it has conducted proceedings, stating '...that this reflects the developing maturity in Panel decision making and the ability of the Panel to make quick and commercial decisions.'<sup>25</sup>

2.18 The committee notes that the Panel executive has issued an index of past decisions for future guidance. *The Australian Government Takeovers Panel Index of Reasons 2000–2014* is ordered by topic and by legislation. It was published on the Panel's website on 8 April 2015.<sup>26</sup>

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19 Takeovers Panel, *Annual Report 2014–15*, p. 5.

20 Ian Ramsay, *The Takeovers Panel and Takeovers Regulation in Australia*, Melbourne University Publishing Ltd, December 2010, p. 25.

21 Takeovers Panel, *Annual Report 2014–15*, p. 20.

22 Takeovers Panel, *Annual Report 2014–15*, pp 5, 20.

23 Takeovers Panel, *Annual Report 2014–15*, p. 22.

24 Takeovers Panel, *Annual Report 2014–15*, p. 5.

25 Takeovers Panel, *Annual Report 2014–15*, p. 3.

26 Australian Government Takeovers Panel, *Index of Reasons*, [http://www.takeovers.gov.au/content/index\\_of\\_reasons/default.aspx](http://www.takeovers.gov.au/content/index_of_reasons/default.aspx), (accessed 3 March 2016)

2.19 The Panel was subject to one judicial review regarding Queensland North Australia Pty Limited. An appeal was lodged with the Full Federal Court on 25 June 2014. On 22 May 2015 the appeal was allowed, however, during this reporting period the Full Federal Court had not made final orders. The Panel did not use its rule making power, nor were any matters referred from the court during the financial year.<sup>27</sup>

2.20 The Panel maintains contact with the Australian Securities Exchange (ASX), the Australian Competition and Consumer Commission (ACCC) and with ASIC, with which the Panel has a Memorandum of Understanding. The annual report notes the Panel may refer matters to ASIC because aspects of the application might give rise to concerns under the Corporations Act or the Panel wants ASIC to consider whether to make an application. The latter occurred once during 2014–15.<sup>28</sup> The report also indicated that the Panel was not subject to any reports by the Australian National Audit Office (ANAO) in 2014–15.<sup>29</sup>

#### *Committee view*

2.21 The committee considers that the Panel has fulfilled its regulatory and reporting responsibilities during the 2014–15 financial year. The committee has previously commented on the increasing proportion of applications for which the Panel has declined to conduct proceedings and will continue to monitor the trend. The committee commends the panel for continuing to publish reasons for decisions in a timely manner.

### **Corporations and Markets Advisory Committee**

2.22 The Corporations and Markets Advisory Committee (CAMAC) was first established in 1989 and was subsequently established by Part 9 of the *Australian Securities and Investments Commission Act 2001*. CAMAC's role in the administration of Australia's financial services system is to provide informed and expert advice to the Minister about the content, operation and administration of the corporations legislation, corporations, financial products and markets. On its own initiative or at the Minister's request, CAMAC may provide advice or recommendations about any matter connected with:

- a proposal to make corporations legislation, or to make amendments of the corporations legislation;
- the operation or administration of the corporations legislation;
- law reform in relation to the corporations legislation;
- companies or a segment of the financial products and financial services industry; or
- a proposal to improve the efficiency of the financial markets.

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27 Takeovers Panel, *Annual Report 2014–15*, p. 24.

28 Takeovers Panel, *Annual Report 2014–15*, p. 26.

29 Takeovers Panel, *Annual Report 2014–15*, p. 33.

### ***Proposal to abolish CAMAC***

2.23 In March 2014, the National Commission of Audit considered that CAMAC's functions could be consolidated into the Department of the Treasury.<sup>30</sup> In May 2014 the Commonwealth Government, as part of the budget, announced its decision to abolish CAMAC and its Legal Committee during the 2014–15 financial year.<sup>31</sup> On 24 September 2014, the government released an exposure draft of legislation to abolish CAMAC.<sup>32</sup> The Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014 (the CAMAC Bill) was introduced into the House of Representatives on 4 December 2014. The CAMAC Bill was passed by the House of Representatives on 2 March 2015 and introduced into the Senate on 3 March 2015. The Bill lapsed when Parliament was prorogued on 15 April 2016.<sup>33</sup>

2.24 On 12 February 2015, the Senate referred the provisions of the CAMAC Bill to the Senate Economics Legislation Committee for inquiry and report by 16 March 2015.<sup>34</sup> While the Economics committee recognised that CAMAC had contributed extensively to the development of reforms to corporations law in Australia, it supported the passage of the bill.<sup>35</sup>

2.25 The committee will continue to monitor developments in relation to CAMAC.

2.26 The committee will continue to monitor developments in relation to the ongoing effectiveness of the development of reforms to corporations law in Australia.

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30 The National Commission of Audit was established by the Commonwealth government in October 2013 as an independent body to review and report on the performance, functions and roles of the Commonwealth government. It reported in February - March 2014; Commission of Audit, *Towards Responsible Government - The Report of the National Commission of Audit, Phase One*, February 2014, p. 216; Commission of Audit, *Towards Responsible Government: Appendix to the Report of the National Commission of Audit*, Volume 3, March 2014, p. 171.

31 Budget 2014–15, *Budget Measures*, Budget Paper No. 2, 2014–15, p. 71.

32 Treasury, *Cessation of the Corporations and Markets Advisory Committee (CAMAC)*, exposure draft, <http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/CAMAC>, (accessed 3 March 2016)

33 Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014, [http://www.aph.gov.au/Parliamentary\\_Business/Bills\\_Legislation/Bills\\_Search\\_Results/Result?bId=r5386](http://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bId=r5386), (accessed 28 April 2016).

34 *Journals of the Senate*, No. 78, 12 February 2015, p. 2156.

35 Senate Economics Legislation Committee, *Australian Securities and Investments Commission Amendment (Corporations and Markets Advisory Committee Abolition) Bill 2014 [Provisions]*, March 2015, p. 12.

## Chapter 3

### Bodies established under Part 12 of the ASIC Act

3.1 This chapter considers the 2014–15 annual reports of the:

- Financial Reporting Council (FRC);
- Australian Accounting Standards Board (AASB); and
- Auditing and Assurance Standards Board (AUASB).

#### Financial reporting framework

3.2 Part 12 of the *Australian Securities and Investments Commission Act 2001* (the ASIC Act) establishes Australia's financial reporting system. As outlined in section 224 of the ASIC Act, the objectives of the financial reporting system include:

- facilitating the Australian economy;
- maintaining investor confidence in the Australian economy;
- developing accounting standards that require the provision of information that is relevant, reliable, easy to understand, allows investors to make and evaluate financial decisions, and assists directors to fulfil their statutory financial reporting obligations; and
- developing auditing and assurance standards that provide Australian auditors relevant and comprehensive guidance in determining whether financial reports comply with statutory requirements, and require auditors' reports to be reliable and capable of being readily understood by investors.<sup>1</sup>

3.3 Three agencies are established under Part 12 of the ASIC Act as the administrative arms of the financial reporting system; namely, the FRC, the AASB and the AUASB. All three bodies are required to advance and promote the object of Part 12 of the ASIC Act.<sup>2</sup>

3.4 ASIC is also involved in the administration of the financial reporting system. ASIC's role in oversighting auditor independence is set out under division 5A of the ASIC Act, which covers 'Audit deficiency notifications and reports'.<sup>3</sup> During the 2014–15 financial year, ASIC conducted an inspection of one Australian audit firm jointly with the United States Public Company Accounting Oversight Board.<sup>4</sup>

3.5 The FRC annual report is required to include an analysis of its achievements against the objects of the financial reporting system.<sup>5</sup> The Chairs of AASB and

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1 *ASIC Act 2001*, s. 224.

2 *ASIC Act 2001*, s. 225, s. 227, s. 227B.

3 *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, Schedule 2.

4 ASIC, *Annual Report 2014–15*, p. 169.

5 *ASIC Act 2001*, s. 235B.

AUASB must, as soon as practicable after the end of each financial year, prepare and give to the Minister, for presentation to the Parliament, reports of the operations of the AASB, the AUASB and their respective offices.<sup>6</sup>

### ***Coordination between the FRC, the AASB and the AUASB***

3.6 The ASIC Act requires interaction between the FRC, the AASB and the AUASB. Accordingly, the FRC's specific accounting standards functions and specific auditing standards functions also include oversight of certain activities of the AASB and the AUASB. The FRC is required to:

- appoint members of the AASB and the AUASB, other than the Chair;
- determine the broad strategic direction of the AASB and AUASB;
- advise the AASB and the AUASB on the Boards' priorities, business plans and procedures;
- monitor the effectiveness of the Boards' consultative arrangements; and
- advise the Office of the AASB and the Office of the AUASB on the offices' budgets and staffing arrangements.<sup>7</sup>

3.7 The ASIC Act also sets out restrictions on the FRC's oversight of the AASB and the AUASB:

The FRC does not have power to direct the AASB in relation to the development, or making, of a particular standard.

The FRC does not have power to veto a standard made, formulated or recommended by the AASB.

The FRC does not have power to direct the AUASB in relation to the development, or making, of a particular auditing standard.

The FRC does not have power to veto a standard made, formulated or recommended by the AUASB.<sup>8</sup>

### *Committee view*

3.8 The committee notes the recommendation by the National Commission of Audit to merge the AASB and the AUASB and/or their offices.<sup>9</sup> At the time of drafting this report no action has been taken in regards to the recommendation, however, the committee will continue to monitor any developments.

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6 ASIC Act 2001, s. 235J, s. 236DG.

7 ASIC Act 2001, s. 225(2–2D).

8 ASIC Act 2001, s. 225(5–8).

9 National Commission of Audit, *Towards Responsible Government*, Appendix Volume 2, February 2014, pp 170, 179.

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## The Financial Reporting Council

3.9 The FRC was established in 1989 and operates pursuant to Part 12 of the ASIC Act 2001.<sup>10</sup> The FRC's role in the operation of Australia's corporations law includes:

- providing broad oversight of the processes for setting accounting standards and auditing standards in Australia; and
- advising the Minister on these matters.<sup>11</sup>

3.10 The ASIC Act also confers on the FRC 'specific accounting standards functions' and 'specific auditing standards functions'. The *Corporations Legislation Amendment (Audit Enhancement) Act 2012* added provisions conferring 'specific auditor quality functions' on the FRC.<sup>12</sup>

3.11 The FRC's specific auditor quality functions direct the FRC to give the Minister strategic policy advice and reports on the quality of audits conducted by Australian auditors. In undertaking this function, the FRC is to advise the Minister on:

- systems and processes used by Australian auditors and professional accounting bodies in overseeing auditors;
- the procedures and outcomes of reviews;
- investigations and disciplinary procedures applied to Australian auditors;
- the adequacy of audit legislation;
- standard and codes of conduct; and
- the teaching of professional and business ethics.<sup>13</sup>

3.12 The FRC's specific accounting standards functions and the specific auditing standards functions recognise the position of Australia's financial system within the international economy.<sup>14</sup> The functions also reflect the object in section 224 of the ASIC Act which is 'facilitating the Australian economy by enabling Australian entities to compete effectively overseas'.<sup>15</sup> Accordingly, the FRC is required to:

- monitor developments in international accounting standards and auditing standards;
- further the development of a single set of accounting standards and auditing standards for world-wide use; and

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10 Section 261 of the ASIC Act directs that bodies established under the *Australian Securities and Investments Commission Act 1989* continue in existence as if they had been established under the *ASIC Act 2001*

11 *ASIC Act 2001*, ss. 225(1).

12 *Corporations Legislation Amendment (Audit Enhancement) Act 2012*, schedule 2.

13 *ASIC Act 2001*, ss 225 (2B–C).

14 *ASIC Act 2001*, ss 225(2), ss 225(2A).

15 *ASIC Act 2001*, paragraph 224(b)(ii).

- promote the continued adoption of international best practice accounting standards and auditing standards if doing so would be in the best interests of the private and public sectors of the Australian economy.<sup>16</sup>

### *Annual report of the FRC*

3.13 As detailed in the 2014–15 annual report, the FRC's view of its purpose and functions reflects its statutory responsibilities:

Under Part 12 of the ASIC Act one of the FRC's functions is to provide broad oversight of the processes for setting accounting and auditing standards in Australia and to give the Minister reports and advice about these processes. Specific accounting and auditing standard setting functions for which the FRC was responsible in 2014–15 are contained in subsections 225(2) and (2A) of the ASIC Act. The activities of the FRC in executing these functions and responsibilities can be grouped as follows:

activities in relation to the standards setting boards in Australia;

activities in relation to audit quality;

activities in relation to developments in Australia; and

activities in relation to international developments.<sup>17</sup>

3.14 Although the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board ceased formally working together on convergence during 2014–15, the FRC noted in its annual report that this does not detract from Australia's decision to adopt the International Financial Reporting Standards (IFRS).<sup>18</sup>

3.15 The FRC continued to actively monitor ongoing international developments in relation to financial reporting and audit and assessed their potential impact on, and usefulness for, Australian practitioners and the financial reporting industry. In the annual report the FRC noted that the current Australian accounting and audit standards, and their respective standard-setting processes, are relevant and appropriate but that it would continue to maintain 'a watching brief' on developments. It also noted that the Australian financial reporting framework continued to be robust during the reporting period and that it was not necessary to propose changes at this time.<sup>19</sup>

3.16 During 2014–15 the FRC's Financial Report Taskforce (the Taskforce) delivered its report into the current financial reporting regime in Australia. This report found that the legislative requirements for the preparation of financial reports significantly differed and/or overlapped between government jurisdictions and different types of organisations. The Taskforce noted that the requirements were not

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16 ASIC Act 2001, ss 225(2), ss. 225 (2A).

17 FRC, *Annual Report 2014–15*, p. 5.

18 FRC, *Annual Report 2014–15*, p. 26.

19 FRC, *Annual Report 2014–15*, pp 1, 9.

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often related to risk profiles or accountability and should be the focus of sustained reform efforts.<sup>20</sup>

3.17 The Taskforce made a number of recommendations to assist in reducing the noted complexity in the financial reporting framework and the FRC in conjunction with the AASB are in the process of considering how a number of these recommendations can be progressed.<sup>21</sup> The committee will continue to monitor the adoption and implementation of the Taskforce recommendations.

3.18 The FRC highlighted in its annual report that, as part of the government's deregulation agenda, it had provided advice during 2014–15 in relation to determining deregulation priorities and identified future deregulation initiatives in the financial reporting sphere.<sup>22</sup>

#### *Committee view*

3.19 The committee considers that FRC has fulfilled its regulatory and reporting responsibilities during the 2014–15 financial year.

3.20 The committee will continue to monitor deregulation initiatives in relation to financial reporting standards.

### **The Auditing and Assurance Standards Board**

3.21 The AUASB is established under Subdivision C, Division 1, Part 12 of the ASIC Act. The AUASB's responsibilities include facilitating an Australian financial reporting system that provides guidance to auditors about auditing standards and requirements.<sup>23</sup> The AUASB formulates auditing standards, in the form of legislative instruments, which operate under the *Corporations Act 2001* (the Corporations Act).<sup>24</sup>

3.22 Consistent with the object in section 224 to 'enable Australian entities to compete effectively overseas', the AUASB is required to contribute to the 'development of a single set of auditing standards for world-wide use.'<sup>25</sup> The ASIC Act also establishes the Office of the AUASB, which provides technical services and administrative support to the AUASB.<sup>26</sup>

#### ***Annual report of the AUASB***

3.23 The AUASB's statutory responsibilities are reflected in the Board's mission statement as contained in the 2013–14 annual report:

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20 FRC, *Annual Report 2014–15*, pp 1, 21.

21 FRC, *Annual Report 2014–15*, pp 1, 21.

22 FRC, *Annual Report 2014–15*, pp 1, 22.

23 *ASIC Act 2001*, s. 224, s. 227A, s. 227B.

24 *ASIC Act 2001*, s. 227B; *Corporations Act 2001*, s. 336.

25 *ASIC Act 2001*, s. 227B.

26 *ASIC Act 2001*, s. 227AB.

The mission of the AUASB is to develop, in the public interest, high-quality auditing and assurance standards and related guidance, as a means to enhance the relevance, reliability and timeliness of information provided to users of audit and assurance services.

Sound public-interest oriented auditing and assurance standards are necessary to reinforce the credibility of the auditing process for those who use audited financial and other related information.

The AUASB contributes to public confidence in the financial reporting and corporate governance frameworks by issuing auditing standards, which are legally enforceable for audits and reviews of financial reports required under the Corporations Act 2001, other auditing and assurance pronouncements and related guidance.

The role of the AUASB also extends to liaison with other national standard setters and participating in standard setting initiatives of the IAASB to develop a single set of auditing standards for worldwide use. Such involvement seeks to contribute ultimately to the quality of AUASB pronouncements.<sup>27</sup>

3.24 The main activities of the AUASB during 2014–15 included promoting enhanced auditor reporting and other initiatives to promote audit quality. In line with this approach, revised assurance standards were issued on various topics including:

- controls engagements;
- auditing grant acquittals and multi-scope engagements;
- auditing prudential reporting requirements of life companies;
- audit reports under the Franchising Code of Conduct; and
- auditor's use of the work of management experts.

#### *Global developments*

3.25 The annual report indicates that the AUASB continued to contribute to the setting of international standards. This involved participating in International Auditing and Assurance Standards Board (IAASB) international taskforces, making submissions to the IAASB on exposure drafts, participating in National Standard Setters meetings and harmonising Australian and New Zealand Auditing standards.

3.26 Following the completion of the IAASB's Auditor Reporting project in late 2014 the new and revised Auditor Reporting Standards were released by the IAASB in late 2014 and early 2015. Following the release of exposure drafts on the proposed changes for auditor reporting and auditing disclosures, new and revised Australian standards were issued by AUASB at the end of 2015. The AUASB annual report noted that:

A key change in the auditor reporting related standards is the requirement for placement of the auditor's opinion at the front of the report for all

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27 AUASB, *Annual Report: 2014–5*, p. 21.

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entities, and for listed entities to provide details of matters of most significance to the audit, Key Audit Matters (KAM), and how these were addressed by the auditor.<sup>28</sup>

3.27 During 2014–15 the AUASB released an exposure draft of the revised International Auditing Standard ISA 720, *The Auditor's Responsibilities Relating to Other Information*. The revised standard will seek to clarify the nature and extent of 'other information' in an entity's annual report that an auditor is responsible for considering.<sup>29</sup>

#### *Local developments*

3.28 During 2014–15 the AUASB issued a new assurance engagement standard on controls which requires the 'assurance practitioner to conclude on the suitability of the design of controls to achieve identified control objectives for these engagements.'<sup>30</sup>

3.29 The AUASB worked closely with a number of regulatory bodies during the reporting period, including the Clean Energy Regulator and the Department of Environment whom they advised on requirements for assurance under the newly introduced Emission Reduction Fund (ERF).<sup>31</sup>

3.30 The AUASB continued to monitor and facilitate the implementation of the Clarity Auditing Standards (referred to in the current annual report as the Auditing Standards) as one of its ongoing activities. The committee previously requested that an assessment of the impact of the standards be included in AUASB annual reports.<sup>32</sup> In addition to noting the AUASB's efforts to provide guidance and information on the implementation and use of the Clarity Auditing Standards the committee welcomes the following AUASB assessment in the 2014–15 annual report that the Auditing Standards:

- have been properly incorporated into legislation;
- conform to the International Standards on Auditing;
- are used by auditors and other assurance practitioners, where required; and
- contribute positively to promoting relevant and reliable auditor reports as well as to the quality of audit generally.

#### *Committee view*

3.31 The committee considers that the AUASB has fulfilled its regulatory and reporting responsibilities during the 2014–15 financial year.

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28 AUASB, *Annual Report: 2014–15*, p. 12.

29 AUASB, *Annual Report: 2014–15*, p. 13.

30 AUASB, *Annual Report: 2014–15*, p. 14.

31 AUASB, *Annual Report: 2014–15*, p. 15.

32 Parliamentary Joint Committee on Corporations and Financial Service, *Report on the 2010–11 annual reports of bodies established under the ASIC Act*, March 2012, p. 48.

## **The Australian Accounting Standards Board**

3.32 The AASB was first established in 1989 and is currently established by Subdivision B, Division 1, Part 12 of the ASIC Act 2001.<sup>33</sup> The AASB's role is to develop a conceptual framework by which to evaluate proposed accounting standards and international standards as well as formulating and making accounting standards. The AASB also contributes to the development of 'a single set of accounting standards for world-wide use'.<sup>34</sup> The ASIC Act also establishes the Office of the AASB, to provide the AASB with administrative and technical support.<sup>35</sup>

### ***Annual report of the AASB***

3.33 As detailed in the 2014–15 annual report, the AASB's mission statement has been revised following the development of the AASB Strategy 2015-2019.

The mission of the AASB is to:

- create principle-based external reporting standards for Australia that meet user needs; and
- contribute to the development of international external reporting standards.<sup>36</sup>

3.34 The annual report indicates that the AASB completed a review of its five-year strategic plan with the development of the AASB Strategy 2015–2019.<sup>37</sup> This review confirmed five key strategic directions for the AASB:

- Use IFRS and transaction-neutrality as a starting point, taking into account cost/benefit considerations and user needs;
- Take leadership role in shaping the Australian Financial Reporting Framework;
- Enhance international influence with respect to International Accounting Standards Board (IASB) and International Public Sector Accounting Standards Board (IPSASB) outcomes;
- Facilitate and encourage active stakeholder participation in developing standards; and
- To maintain relevance, investigate expanding the scope of activities to cover external reporting rather than just financial reporting.<sup>38</sup>

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33 Section 261 of the ASIC Act directs that bodies established under the *Australian Securities and Investments Commission Act 1989* continue in existence as if they had been established under the *ASIC Act 2001*

34 *ASIC Act 2001*, s. 227

35 *ASIC Act 2001*, s. 226A

36 AASB, *Annual Report: 2014–15*, p. 11.

37 AASB, *Annual Report: 2014–15*, pp 7, 11.

38 AASB, *Annual Report: 2014–15*, pp 7, 11–17.

3.35 The committee will continue to monitor the implementation of AASB's new strategic plan.

3.36 During 2014–15, the AASB issued Australian versions of two key international standards, on Financial Instruments and Revenue from Contracts with Customers, largely completing the IASB's work program from the Global Financial Crisis.<sup>39</sup>

3.37 The AASB indicated in its annual report that the implementation process of IFRS in Australia, which began in 2005, will be reviewed by the AASB during 2015–16. This review will include the 'implications for future directions regarding transaction neutrality.'<sup>40</sup>

3.38 During 2014–15, the AASB continued to have influence internationally making thirteen submissions to the IASB, two submissions to the IPSASB and one submission to the International Value Standards Council (IVSC). The AASB also assisted the IASB with its disclosure initiative project.<sup>41</sup>

3.39 During 2014–15, the AASB commenced work on projects in relation to the:

- Australian Financial Reporting Framework – the project aims to clarify and simplify the Australian Financial Reporting Framework, so that objective criteria determine which entities would be required to prepare General Purpose Financial Statements (GPFS) and the level of the reporting requirements; and
- Reduced Disclosure Requirements Framework – the project aims to determine if the principles for determining reduced disclosure requirements should be changed and, if so, what those principles should be.<sup>42</sup>

3.40 Another key focus for the AASB during 2014–15 was the not-for-profit (NFP) sector with twenty-three of the forty-two standards and two of the fourteen issued by the AASB having specific NFP or public sector specific requirements/modifications. Additionally a number of proposals and exposure drafts on several projects of high priority to NFP entities were released including those relating to fair value disclosures, service concession arrangements, residual values for infrastructure assets and service performance reporting (SPR).<sup>43</sup>

#### *Committee view*

3.41 The committee considers that the AASB has fulfilled its regulatory and reporting responsibilities during the 2014–15 financial year.

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39 AASB, *Annual Report: 2014–15*, pp 7, 12.

40 AASB, *Annual Report: 2014–15*, pp 7.

41 AASB, *Annual Report: 2014–15*, pp 7, 11–17.

42 AASB, *Annual Report: 2014–15*, p. 13–14.

43 AASB, *Annual Report: 2014–15*, pp 7, 11–17.



## Chapter 4

### ASIC's 2014–15 annual report

4.1 This chapter discusses the 2014–15 annual report of ASIC. Under Senate Standing Order 25(20),<sup>1</sup> annual reports of bodies established under the ASIC Act are subject to scrutiny by the Senate Economics Legislation Committee which noted the following in relation to ASIC:

- an eight percent increase in the revenue raised for the Commonwealth, by ASIC, through fees and charges;<sup>2</sup>
- a ten percent reduction in appropriation revenue which was correlated with the ten percent reduction in expenditure driven by a general reduction in staff and supplier expenditure;<sup>3</sup>
- the steps taken by ASIC in response to the Senate's inquiry into ASIC's performance including:
  - the establishment of an Office of the Whistleblower;
  - the redesign of ASIC's webpage to make it more user-friendly and accessible; and
  - the updating of its guidance on enforceable undertakings.<sup>4</sup>
- ASIC's outcomes for the year including:
  - the launch of the Financial Adviser's Register;
  - 321 funds management surveillances, including a review of risk management practices; and
  - 54 instances where potentially misleading or deceptive promotional material was withdrawn or amended.<sup>5</sup>

4.2 The Senate Economics Legislation Committee considered that ASIC met its reporting obligations and the annual report is apparently satisfactory, well-presented and comprehensive.<sup>6</sup> Therefore, in conducting its review of the 2014–15 ASIC annual report, the committee will focus on the statutory requirements under the ASIC Act and other operational matters.

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1 The Senate, *Standing Orders and other orders of the Senate*, August 2015, p. 30.

2 Senate Economics Legislation Committee, *Annual reports (No. 1 of 2016)*, March 2016, p. 31.

3 Senate Economics Legislation Committee, *Annual reports (No. 1 of 2016)*, March 2016, p. 32.

4 Senate Economics Legislation Committee, *Annual reports (No. 1 of 2016)*, March 2016, p. 33.

5 Senate Economics Legislation Committee, *Annual reports (No. 1 of 2016)*, March 2016, p. 33.

6 Senate Economics Legislation Committee, *Annual reports (No. 1 of 2016)*, March 2016, pp 33–34.

### *Statutory requirements*

4.3 Statutory requirements for the ASIC annual report are set out in section 136 of the ASIC Act and Section 46 of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) cover tabling, distribution and the contents of the annual report.

#### *Tabling and distribution*

4.4 The 2014–15 ASIC annual report was provided to the Minister on 15 October 2015, and tabled in the Senate and the House of Representatives on the next available sitting day, 9 November 2015. As a result, the legislative requirements as set out below were satisfied:

- Section 46(1), PGPA Act: After the end of each reporting period for a Commonwealth entity, the accountable authority of the entity must prepare and give an annual report to the entity's responsible Minister, for presentation to the Parliament, on the entity's activities during the period.; and
- Section 46(2), PGPA Act: The annual report must be given to the responsible Minister by: the 15th day of the fourth month after the end of the reporting period for the entity; or the end of any further period granted under subsection 34C(5) of the Acts Interpretation Act 1901.

4.5 Section 136(4) of the ASIC Act requires that 'the Minister must cause a copy of each annual report to be sent to the Attorney-General of each State and Territory as soon as practical after the Minister receives the report'. ASIC advised the committee that copies had been provided to the Attorney-General of each state and territory in line with this requirement.<sup>7</sup>

#### *Contents of the annual report*

4.6 In addition to the requirements for annual reports as approved by the Joint Committee of Public Accounts and Audit, ASIC is subject to statutory requirements for the contents of the ASIC annual report as set out in sections 136(1)(a–e) and 136(2A) of the ASIC Act. It should be noted that changes to section 136(1) and 136(2) of the ASIC Act were imposed by the *Public Governance and Resources Legislation Amendment Act (No. 1) 2015* which sought to align annual report requirements, where possible, with the PGPA Act.<sup>8</sup> Table 4.1 lists where in the 2014–15 ASIC annual report the current requirements in the ASIC Act are met.

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7 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

8 *Public Governance and Resources Legislation Amendment Act (No. 1) 2015*, Revised Explanatory Memorandum, p.13-14 of 25  
[http://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r5402\\_ems\\_126da0a5-fac4-4fa7-989e-acfc994bec58/upload\\_pdf/500599.pdf;fileType=application%2Fpdf](http://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r5402_ems_126da0a5-fac4-4fa7-989e-acfc994bec58/upload_pdf/500599.pdf;fileType=application%2Fpdf) , (accessed 8 March 2016)

**Table 4.1- Statutory requirements for the ASIC annual report**

Section	Reporting requirement (ASIC Act)	2014–15 Annual Report
136(1)(a)	Exercise of ASIC's powers under Part 15 of the <i>Retirement Savings Accounts Act 1997</i> and under Part 29 of the <i>Superannuation Industry (Supervision) Act 1993</i>	Page 169
136(1)(b)	ASIC's monitoring and promotion of market integrity and consumer protection	Pages 28–31 Pages 34–63
136(1)(c)	In relation to ASIC's functions under subsection 11(14), and each agreement or arrangement entered into by ASIC under that subsection, information about the activities that ASIC has undertaken during the period in accordance with that agreement or arrangement	Page 169
136(1)(d)	Operation of the <i>Business Names Registration Act 2011</i>	Pages 64–68
136(1)(e) 136(2A)	Information relating to the exercise by ASIC, members of ASIC, or staff members, of prescribed information-gathering powers.	Pages 175–176

***Operational matters identified in the annual report.***

***Enforcement***

4.7 In the annual report ASIC indicates that 631 enforcement outcomes were achieved in 2014–15, including criminal and civil litigation, administrative action and enforceable undertakings. This was an increase on the 596 enforcement outcomes in 2013–14.<sup>9</sup> The annual report enforcement outcome data shows a notable increase in:

- the dollar value of fundraising where ASIC required additional disclosure<sup>10</sup>;
- the dollar value of civil penalties under Priority One;<sup>11</sup> and

9 ASIC, *Annual Report 2014–15*, p. 164; ASIC, *Annual Report 2013–14*, p. 158.

10 ASIC indicated that the growth in the dollar value of fundraisings is as a result of market factors as opposed to any deterioration of disclosure quality or changes to ASIC policy regarding disclosure. Additionally comparatively large deals requiring additional disclosure influenced the increase in the 2014–15 total e.g. MYOB Group Limited, Estia Health Limited and Perpetual Equity Investment Company Limited all conducted large fundraisings which required disclosure. These deals alone amounted to \$2.1 billion (of the 2014–15 total of \$10.6 billion). ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

11 ASIC, *Annual Report 2014–15*; ASIC has adopted three strategic priorities and has structured its annual report according to achievements in these three areas. These are as follows:

Priority 1 – Promote investor and financial consumer trust and confidence.

Priority 2 – Ensure fair, orderly, transparent and efficient markets.

Priority 3 – Provide efficient and accessible registration.

- the total number and dollar value of infringement notices issued.<sup>12</sup>
- 4.8 In contrast, the enforcement outcome data shows a notable decrease in:
- the percentage of civil litigations completed under Priority Two;<sup>13</sup> and
  - the amount of compensation or remediation secured for investors and financial consumers.<sup>14</sup>
- 4.9 The annual report also notes that the number of investigations commenced and completed under Priority One have decreased whereas the number of investigations under Priority Two have increased.<sup>15</sup>
- 4.10 In 2013–14 it was noted that there was a decline in the number of illegal schemes that had been shut down, from 39 to zero. There was no data available in the 2014–15 annual report in relation to this trend but in recent correspondence ASIC has informed the committee that no illegal schemes were shut down in 2014–15.<sup>16</sup>
- 4.11 In 2014–15 ASIC completed its Evidence Management System (EMS) Ringtail project. The system enables ASIC to handle large amounts of electronic evidence and has reduced evidence processing times.<sup>17</sup>
- 4.12 ASIC has advised the committee that it is seeking to publish monthly enforcement statistics that will complement the more detailed six-monthly report that focuses on key themes that have been identified from the enforcement data for the preceding period.<sup>18</sup>

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The increase in the value of penalties is largely attributable to the penalty awarded against Cash Store Pty Ltd – totalling \$18.975 million. This was the largest civil penalty obtained by ASIC. ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

- 12 In 2013–14, 20 infringement notices were issued to 12 entities. In 2014–1, 70 infringement notices were issued to 12 entities with one entity (BMW Australia Finance), alone, being issued with 36 infringement notices. ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016); ASIC, *Annual Report 2014–15*, pp. 6–9; 161–164; 167.
- 13 ASIC, *Annual Report 2014–15*; The significant decrease in the percentage of civil litigations which had been completed successfully during 2014–15 was largely due to the matter of Mariner Corporation Limited – see discussed of Mariner matter in this report and Appendix 2. ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).
- 14 ASIC, *Annual Report 2014–15*, pp 6–9, 161–164, 167.
- 15 ASIC, *Annual Report 2014–15*, pp 6–9.
- 16 ASIC, *Annual report 2013–14*, p. 7; *Committee Hansard*, 20 March 2015, pp 17–18; ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).
- 17 ASIC, *Annual Report 2014–15*, p. 43.
- 18 Mr Greg Tanzer, Commissioner, Australian Securities and Investments Commission, *Committee Hansard*, 16 October 2015, p. 12; Mr Greg Medcraft, Chairman, Australian Securities and Investments Commission, *Committee Hansard*, 16 October 2015, p. 12.

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*Mariner matter*

4.13 The significant decrease in the percentage of civil litigations which had been completed successfully during 2014–15 (noted above), was largely due to the legal action taken by ASIC in the Federal Court (the court) against Mariner Corporation Limited (Mariner) in April 2014.<sup>19</sup>

4.14 This matter concerned an announcement by Mariner on 25 June 2012 that it was making a takeover bid for Austock Group Limited at a price of 10.5 cents per share.<sup>20</sup> At the time of the bid, however, Mariner did not have concluded financing arrangements in place. This was contrary to the 'objective' standards for 'funding arrangements for the cash component of consideration under a takeover' articulated in the Takeovers Panel's *Guidance Note 14: Funding Arrangements* (GN14).<sup>21</sup>

4.15 Following the Takeover Panel's declaration of 'unacceptable circumstances'<sup>22</sup> ASIC took the matter to the Federal Court alleging that Mariner was reckless as to whether it could perform its obligations in relation to the bid because at the time the bid was announced it did not have the financial resources, or any pending funding that could finance the bid.<sup>23</sup> Consequently ASIC alleged that Mariner had contravened section 631(2)(b) of the *Corporations Act 2001* (Corporations Act).<sup>24</sup> In undertaking

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19 *Australian Securities and Investments Commission v Mariner Corporation Limited [2015] FCA 589*. Appendix 3 contains a summary by ASIC as to the background of the matter, the issues of construction raised by the matter and the possibilities for legislative reform in relation to s631(2) (b) of the *Corporations Act 2001*.

20 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

21 The importance of ensuring there is sufficient funding at the time a bidder makes a takeover bid is highlighted in the Takeovers Panel's *Guidance Note 14: Funding Arrangements* which indicates that the inadequacy of a bidder's funding arrangements may give rise to 'unacceptable circumstances'. The guidance note in place at the time of the takeover bid can be located via this link:

[http://www.takeovers.gov.au/content/DisplayDoc.aspx?doc=guidance\\_notes/superseded/014a.htm&pageID=&Year](http://www.takeovers.gov.au/content/DisplayDoc.aspx?doc=guidance_notes/superseded/014a.htm&pageID=&Year). This particular policy advice is generally supported by ASIC and utilised when regulating takeover transactions in Australia. This guidance note is now superseded by a revised policy implemented in November 2015, largely as a result of the outcome in this court matter. It can be located via the following link

[http://www.takeovers.gov.au/content/DisplayDoc.aspx?doc=guidance\\_notes/current/014.htm](http://www.takeovers.gov.au/content/DisplayDoc.aspx?doc=guidance_notes/current/014.htm). ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

22 According to the Takeovers Panel's *Guidance Note 14: Funding Arrangements*, unacceptable circumstances may arise if a bidder does not have funding in place, or a reasonable basis to expect that it will have funding in place, to pay for all acceptances when its bid becomes unconditional.

23 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

24 CORPORATIONS ACT 2001 - SECT 631

(2) A person must not publicly propose, either alone or with other persons, to make a takeover bid if:

(a) the person knows the proposed bid will not be made, or is reckless as to whether the proposed bid is made; or

this behaviour ASIC alleged that Mariner had also contravened s1041H (misleading and deceptive conduct) and section 180 (director's duty of care and diligence) of the *Corporations Act 2001*.<sup>25</sup>

4.16 Prior to the Mariner matter section 631(2)(b) of the *Corporations Act 2001* had never been the subject of judicial consideration.<sup>26</sup> In deciding the Mariner matter the court opined on a number of aspects of the construction of section 631(2), notably:

- the test of whether a person is 'reckless', and whether this is a subjective or objective test; and
- the question of what is meant by a 'substantial proportion of the offers'.<sup>27</sup>

4.17 In handing down its findings the court disagreed with ASIC's submission that section 631(2)(b) is an objective test.<sup>28</sup> It also found that the concept of 'substantial proportion of the offers' was unclear and took the approach of assuming in particular case that this meant 'no less than' 50% of the shares that are the subject of the offer.<sup>29</sup> The matter was resolved in the favour of Mariner on 19 June 2015, with Beach J summarising:

(a) The test for “reckless” under s 631(2)(b) is a subjective test. Applying that test, Mariner was not “reckless”.

(b) Alternatively, if the test for “reckless” under s 631(2)(b) is an objective test, Mariner was not “reckless”.

(c) Mariner did not engage in any conduct in contravention of s 1041H in relation to the price representation or the funding representation.

(d) Alternatively, if Mariner did engage in any misleading or deceptive conduct concerning the price representation, on no reasonable view would it be entitled to any relief. I express no view on whether relief would go if, alternatively, Mariner engaged in misleading or deceptive conduct concerning the funding representation.

(e) No director contravened s 180, whether or not Mariner contravened s 631(2)(b) or s 1041H.

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(b) the person is reckless as to whether they will be able to perform their obligations relating to the takeover bid if a substantial proportion of the offers under the bid are accepted.

*Australian Securities and Investments Commission v Mariner Corporation Limited [2015] FCA 589*

25 *Australian Securities and Investments Commission v Mariner Corporation Limited [2015] FCA 589*

26 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

27 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016); *Australian Securities and Investments Commission v Mariner Corporation Limited [2015] FCA 589*.

28 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016); *Australian Securities and Investments Commission v Mariner Corporation Limited [2015] FCA 589 at [248,249]*.

29 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016); *Australian Securities and Investments Commission v Mariner Corporation Limited [2015] FCA 589 at [312]*.

(f) Alternatively, even if Mr Olney-Fraser contravened s 180, neither Mr Christie nor Mr Fletcher contravened s 180 given their reasonable reliance upon the information provided to them by Mr Olney-Fraser and their ability to invoke s 189.<sup>30</sup>

4.18 Following this finding, ASIC indicated a number of possibilities for legislative reform in relation to section 631(2)(b) of the *Corporations Act 2001*:

ASIC would generally support a review of s631(2) to consider amendments aligning the requirements of the provision with the broader regulatory policy settings discussed in GN 14. This would potentially include:

amending s631(2)(b) to require that a bidder have an objectively reasonable basis that it will be able to comply with its funding obligations under a bid; and

addressing the uncertainty arising from the reference in the provision to a 'substantial proportion of offers' by clarifying that funding is required to pay for all securities to which the proposed bid relates.<sup>31</sup>

4.19 ASIC also indicated that it may be 'appropriate' to reconsider whether section 631(2)(b) of the *Corporations Act 2001* should 'continue to require funding for only some, rather than all, of the securities the subject of the announced bid.'<sup>32</sup> It also expressed concerns about the criminal operation of section 631(2), particularly in terms of its lack of 'harmony' with the *Criminal Code* and the high degree of uncertainty in terms of its operation when a defence under section 670 of the *Corporations Act 2001* is presented.<sup>33</sup>

## Recommendation 1

**4.20 The committee recommends that the government consider the suggestions that ASIC has made in relation to reforms of section 631 of the Corporations Act.**

### *Enforceable undertakings*

4.21 Following a recommendation from the Senate Economics References Committee inquiry into the performance of ASIC,<sup>34</sup> the Australian National Audit Office (ANAO) conducted a performance audit of ASIC's use of Enforceable Undertakings (EU). The audit was undertaken during the reporting period and the report, issued on 2 June 2015, made two recommendations:

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30 *Australian Securities and Investments Commission v Mariner Corporation Limited [2015] FCA 589 at [5]*.

31 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

32 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

33 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

34 Economics References Committee, *Performance of the Australian Securities and Investments Commission*, June 2014, p. xxviii.

### Recommendation 1

To assess the effectiveness of enforceable undertakings as an appropriate regulatory tool and their contribution to ASIC achieving its compliance objectives, the ANAO recommends that ASIC:

- (a) develops appropriate performance measures to monitor the effectiveness of enforceable undertakings in addressing non-compliance, and regularly reports against these measures; and
- (b) periodically assesses, and reports on, the effectiveness of enforceable undertakings in contributing to improved levels of voluntary compliance.

### Recommendation 2

To strengthen decision-making and support the transparency of, and quality assurance over enforceable undertakings, the ANAO recommends that ASIC:

- (a) reinforces to staff the need for key documents and decisions relating to enforceable undertakings to be appropriately recorded in accordance with ASIC policies and procedures; and
- (b) formalises the processes for obtaining enforceable undertaking approvals.<sup>35</sup>

4.22 ASIC noted in its response to the ANAO report and in the 2014–15 annual report that it agreed with both recommendations and indicated that they would be implemented.<sup>36</sup>

4.23 Following the release of the ANAO report the Parliamentary Joint Committee on Corporations and Financial Services expressed concerns in relation to ASIC being able to assess the effectiveness of EUs, particularly in terms of measuring them against Key Performance Indicators. The committee also had concerns about ASIC's ability to provide assurances that EUs were having the desired regulatory or compliance outcomes.<sup>37</sup>

4.24 The committee notes that when compared to the 2013–14 annual report the 2014–15 annual report contains more information and commentary in relation to how ASIC monitors enforceable undertakings, and their effectiveness in terms of improved compliance, with a number of case studies documented to illustrate a variety of outcomes.<sup>38</sup> The committee also notes that the annual report includes information about the fact that in the reporting period ASIC:

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35 ANAO, *Audit Summary - Administration of Enforceable Undertakings*, June 2015, p. 6; ASIC, *Annual Report 2014–15*, p. 170.

36 ANAO, *Audit Summary - Administration of Enforceable Undertakings*, June 2015, p. 6; ASIC, *Annual Report 2014–15*, p. 170.

37 *Committee Hansard*, 14 August 2015, pp 9–10, 21–22; *Committee Hansard*, 16 October 2015, pp 4–5; *Committee Hansard*, 19 November 2015, pp 16–17, 19–20.

38 ASIC, *Annual Report 2014-15*, pp 14, 46, 61.

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- had issued new public guidance in relation to enforceable undertakings to include information on independent experts and publicity for enforceable undertakings;
  - accepted 20 enforceable undertakings during the reporting period; and
  - had commenced public reporting on compliance with undertakings given on or after March 2015.<sup>39</sup>

4.25 The committee considers that further improvement regarding the measurement, assessment, and reporting of EUs should be implemented and the committee will monitor the content regarding the use of EUs in future enforcement and annual reports.

### *Surveillance*

4.26 The annual report indicates that the number of high-intensity surveillances completed by ASIC decreased during the reporting period. Across Priority One and Two, 1,016 high-intensity surveillances were conducted in 2014–15, down from 1,767 in 2013–14.<sup>40</sup> ASIC states in its annual report that a reduction in resources has reduced the level of random sampling-based surveillance and that alternatively a risk-based approach to targeted operations that have the greatest market impact is being implemented.<sup>41</sup> The committee will continue to monitor the number of high-intensity surveillances and the allocation of resources for surveillance activities.

4.27 During the reporting period the annual report notes that ASIC's surveillance was proactive, risk-based surveillance focused on areas such as financial benchmarks, retail OTC derivative trading, fundraising disclosure, financial reporting, auditors and registered liquidators.<sup>42</sup> In October 2014 ASIC set up a specialist wealth management project, utilising risk-based surveillance, to focus on the conduct and compliance of large financial advice firms with the aim of lifting advice standards.<sup>43</sup>

4.28 Surveillance by ASIC also targeted retail life insurance advice with a review of such advice in October 2014 finding that 37% of life insurance advice did not comply with the required standards in the Corporations Act.<sup>44</sup> This review resulted in the industry commissioned Trowbridge Report in March 2015, and the Commonwealth Government was presented with what was described as an 'industry led reform package' in mid-2015.<sup>45</sup> Following further consultations, on 6 November 2015, the Minister for Small Business and Assistant Treasurer,

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39 ASIC, *Annual Report 2014-15*, pp 6–9, 46.

40 ASIC, *Annual Report 2014–15*, pp 6, 8.

41 ASIC, *Annual Report 2014–15*, pp 36, 52.

42 ASIC, *Annual Report 2014–15*, p. 6, 8.

43 ASIC, *Annual Report 2014–15*, p. 37.

44 ASIC, *Annual Report 2014–15*, p 12, 37.

45 ASIC, *Annual Report 2014–15*, p 12, 37.

the Hon Kelly O'Dwyer, announced a package of reforms, which are scheduled to commence on 1 July 2016.<sup>46</sup>

4.29 On 3 December 2015, the Government released draft legislative amendments to the *Corporations Act 2001* which would remove the current exemption in the Corporations Act from the ban on conflicted remuneration for benefits paid in relation to certain life risk insurance products. The amendments would give ASIC the power to:

make a legislative instrument to permit benefits in relation to life risk insurance products to be paid, provided certain requirements are met. These requirements relate to the quantum of allowable commissions and to 'clawback' arrangements, where a certain portion of the upfront commission is paid back to the life insurer by the financial adviser in the event that the life insurance policy is cancelled or the premium is reduced.<sup>47</sup>

4.30 ASIC had begun processing feedback from life insurers, Australian financial services (AFS) licensees and their representatives, and consumers on proposals to implement and monitor the impact of the retail life insurance industry reforms, as contained in a consultation paper released in December 2015.<sup>48</sup> However, on 15 April 2016, the Bill lapsed due to the prorogation of the Parliament.<sup>49</sup>

4.31 During 2014–15 ASIC continued to undertake surveillance on credit licensees and the banking, credit and insurance industry to ensure compliance with responsible lending obligations and to address the sale of inappropriate products to consumers. This included reviews and reports on payday lending, 'low doc' loans, interest only loans, home building and motor vehicle insurance and add-on insurance products.<sup>50</sup>

4.32 In March 2015 ASIC reviewed the files of 13 payday lenders who are responsible for more than 75% of the payday loans in Australia. This review and its consequent report found that some lenders were not meeting responsible lending

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46 The Hon. Kelly O'Dwyer, MP, Minister for Small Business and Assistant Treasurer, *Government announces significant improvements to life insurance industry*, Media Release, 6 November 2015, <http://kmo.ministers.treasury.gov.au/media-release/024-2015/> (accessed 8 March 2016).

47 *Corporations Amendment (Life Insurance Remuneration Arrangements) Bill 2016*, Explanatory Memorandum, p. 3, [http://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r5611\\_ems\\_82e13b89-08d8-493e-88fa-6d8eef045ba6/upload\\_pdf/16010EM.pdf;fileType=application%2Fpdf](http://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r5611_ems_82e13b89-08d8-493e-88fa-6d8eef045ba6/upload_pdf/16010EM.pdf;fileType=application%2Fpdf) (accessed 8 March 2016).

48 ASIC, *Consultation Paper 245: Retail life insurance advice reforms*, December 2015, <http://download.asic.gov.au/media/3490655/cp245-published-15-december-2015.pdf> (accessed 8 March 2015).

49 Parliamentary Business, Bills and Legislation, *Corporations Amendment (Life Insurance Remuneration Arrangements) Bill 2016*, [http://www.aph.gov.au/Parliamentary\\_Business/Bills\\_Legislation/Bills\\_Search\\_Results/Result?bld=r5611](http://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bld=r5611) (accessed 27 April 2016).

50 ASIC, *Annual Report 2014-15*, pp 38–39.

obligations. A follow up investigation led to ASIC pursuing the lender and loan funder in the Federal Court who found there had been a systemic failure by both the lender and loan funder to comply with consumer lending laws and awarded a record \$19 million in penalties.<sup>51</sup>

4.33 In 2014–15 ASIC completed the implementation of the Market Analysis and Intelligence (MAI) system – the first of four deliverables of ASIC's Flexible Advanced Surveillance Technologies (FAST) program. The MAI system is a real-time market surveillance system that provides sophisticated data analytics to identify suspicious trading in real time and across markets. It also enables ASIC to interrogate very large data sets and increases the ability of ASIC to detect insider trading.<sup>52</sup> The annual report states:

MAI helps us to adapt to increased message traffic, new technologies and trading techniques. It also helps us handle the increase in trading messages generated by high frequency trading.<sup>53</sup>

#### *International cooperation*

4.34 ASIC has identified globalisation as an emerging issue with cross border activity and integration of international markets, reform of over the counter derivative markets and involvement in the International Organisation of Securities Commissions as key activities for ASIC in a more integrated, complex and competitive environment.<sup>54</sup>

4.35 Cross-border regulatory issues were highlighted in the annual report with ASIC making 330 international cooperation requests and receiving 424 requests during the reporting period. To further facilitate these efforts in international regulation and enforcement, ASIC entered into six memoranda of understanding with various services and commissions in Korea, Gibraltar and the United States.<sup>55</sup>

4.36 ASIC also noted the provision of technical assistance to the Department of the Treasury for the purposes of developing and negotiating the Asia Region Funds Passport. The Passport is being developed with the aim of providing a 'multilaterally agreed framework to facilitate the cross border marketing of managed funds across participating economies in the Asian region.'<sup>56</sup>

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51 ASIC, *Annual Report 2014–15*, p. 39; Mr Greg Medcraft, Chairman, Australian Securities and Investments Commission, *Committee Hansard*, 20 March 2015, p. 2.

52 ASIC, *ASIC's next generation market surveillance system commences*, Media Release, 25 November 2013, <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2013-releases/13-316mr-asics-next-generation-market-surveillance-system-commences/> (accessed 4 April 2016)

53 ASIC, *Annual Report 2014-15*, p. 53.

54 ASIC, *Annual Report 2014-15*, pp 3, 43, 47, 62–63.

55 ASIC, *Annual Report 2014-15*, pp 20–21.

56 ASIC, *Annual Report 2014-15*, p. 47.

4.37 The committee notes the potential impact that increases in cross-border compliance, industry driven requests for assistance and requirements under international agreements could have on ASICs resources.<sup>57</sup> The committee will continue to monitor the capacity of ASIC to recover costs in these areas.

#### *Financial advisers register*

4.38 In March 2015 ASIC launched the Financial Advisers Register, which at the end of the reporting period had 22,000 financial advisers listed and had been searched more than 200,000 times.<sup>58</sup> The register:

...contains details of persons employed or authorised – directly or indirectly – by AFS licences to provide personal advice on 'relevant financial products' to retail clients.<sup>59</sup>

4.39 The Financial Advisers Register was updated in May/June 2015 to also include information about the qualifications, training and professional memberships of financial advisers.

4.40 Following the implementation of the Financial Advisers Register the committee raised concerns about financial advisers who have been banned not appearing on the Financial Advisers Register.<sup>60</sup> This has led to questions by the committee about:

- the ability of ASIC to incorporate information from the banned and disqualified person's register in the Financial Advisers Register so as to facilitate having publicly accessible information about financial advisers in a single location;<sup>61</sup> and
- the restrictions placed on ASIC, by the regulations for the Financial Advisers Register, in terms of their ability to capture retrospective data in relation to advisers who had ceased practising prior to 31 March 2015.<sup>62</sup>

### **Recommendation 2**

**4.41 That the government consider strengthening the register by enabling the inclusion of retrospective data on banned and disqualified financial advisers on the Financial Advisers Register.**

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57 *Committee Hansard*, 20 March 2015, p. 21–24.

58 ASIC, *Annual Report 2014–15*, p. 68.

59 ASIC, *Annual Report 2014–15*, p. 68.

60 *Committee Hansard*, 16 October 2015, pp 2–5.

61 *Committee Hansard*, 16 October 2015, pp 2–5; 19 November 2015, pp 4–5.

62 *Committee Hansard*, 16 October 2015, pp 2–5; 19 November 2015, pp 4–5.

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*Other registers*

4.42 The annual report notes that during the reporting period the government announced a competitive tender process to test the capacity of a private sector operator to upgrade and operate the ASIC registry.<sup>63</sup>

4.43 During 2014–15 ASIC redesigned its website and continued to digitise its registry services. In its annual report ASIC noted this has provided a more contemporary service for customers with corresponding increases in:

- the online submission of registry lodgements;
- the online submission of lodgements to the companies register;
- the number of online searches of the ASIC register, up almost 10 million searches from 2013–14; and
- a significant increase in followers on social media channels such as ASIC Connect Facebook (up by 74%) and ASIC Connect Twitter (up by 47%).<sup>64</sup>

4.44 The ASIC annual report indicates that the number of authorised financial markets operating in Australia increased from 40 in 2013–14 to 43 in 2014–15, a marginal increase compared to the doubling of the figures from 2012–13 to 2013–14.<sup>65</sup> The continued increase is in line with ASIC's indication in early 2015 that the increase is due to the increasing fragmentation of markets because of technology and the effect of Australian Pacific Exchange (APX) coming into the market in 2013–14.<sup>66</sup>

4.45 The ASIC annual report notes that in 2014–15 there was a halving of the number of Self-Managed Super Fund (SMSF) auditor registrations, which reached a total of 123, down from 240 in 2013–14 and 7,194 in 2012–13.<sup>67</sup> The drop in registrations is indicative of the slow down expected once SMSF auditors had complied with the new mandatory registration requirements in the last half of 2013 but is still below the expected 200–300 registrations per year.<sup>68</sup> The committee will continue to monitor the trend in the number registrations.

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63 ASIC, *Annual Report 2014–15*, p. 64.

64 ASIC, *Annual Report 2014–15*, p. 65.

65 ASIC, *Annual Report 2014–15*, p. 167.

66 Ms Cathie Armour, Commissioner, Australian Securities and Investments Commission, *Committee Hansard*, 20 March 2015, p. 18; Mr Greg Medcraft, Chairman, Australian Securities and Investments Commission, *Committee Hansard*, 20 March 2015, p. 18.

67 ASIC, *Annual Report 2014–15*, p. 68; *Annual report 2013–14*, p. 55.

68 Mr Greg Tanzer, Commissioner, Australian Securities and Investments Commission, *Committee Hansard*, 20 March 2015, p. 20.

### *Culture and whistleblowing*

4.46 In an effort to promote good conduct and shift the banking and financial sector culture in the right direction, the ASIC annual report indicates that the number of consultations with domestic stakeholders, under Priority Two – Fair, orderly, transparent and efficient markets, has increased, with the number of meetings with domestic stakeholders increasing to 876, up from 487 in 2013–14.<sup>69</sup>

4.47 In response to recommendations from the Senate Economics References Committee inquiry into the performance of ASIC, during 2014–15 ASIC established an Office of the Whistleblower and adopted a centralised monitoring procedure for whistleblower complaints. The new office will 'monitor the handling of all whistleblower reports, manage staff development and training, and handle the relationship with whistleblowers on more complex matters.'<sup>70</sup>

### *Education and financial literacy*

4.48 ASIC released the National Financial Literacy Strategy 2014–17 in August 2014. As the annual report indicates the strategy sets out a national direction for financial literacy and provides a practical framework for action built around five strategic priorities:

1. Educate the next generation, particularly through the formal education system
2. Increase the use of free, impartial information, tools and resources
3. Provide quality targeted guidance and support
4. Strengthen coordination and effective partnerships
5. Improve research, measurement and evaluation.<sup>71</sup>

4.49 In line with the aim of providing education and tools to help the community with their financial decisions, the annual report notes that ASIC's MoneySmart website provides free, impartial and comprehensive investor and consumer information on money matters. During the reporting period there were 5.4 million unique visits to website, an increase of 15% from 2013–14. Follow-up research has also shown that 89% of users 'took action on their finances after visiting the site.'<sup>72</sup>

4.50 ASIC's MoneySmart Teaching program also expanded with 3185 schools engaged during the reporting period compared with 396 for 2013–14.<sup>73</sup> Over 76,000 teaching resources for the program were also distributed.<sup>74</sup>

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69 ASIC, *Annual Report 2014–15*, p. 50; ASIC, *Annual report 2013–14*, p. 38.

70 ASIC, *Annual Report 2014–15*, p. 14.

71 ASIC, *Annual Report 2014–15*, p. 41.

72 ASIC, *Annual Report 2014–15*, pp 41, 161.

73 ASIC, *Annual Report 2014–15*, p. 6.

74 ASIC, *Annual Report 2014–15*, pp 42, 161.

4.51 During 2014–15 Australia was one of a select group of countries to contribute to the Organisation for Economic Cooperation and Development (OECD) handbook on the implementation of national strategies for financial education.<sup>75</sup>

#### *Regulatory guidance*

4.52 A total of 22 new or revised regulatory guides were published by ASIC during the reporting period. These included guides on superannuation forecasts, responsible lending, digital disclosure, cyber resilience and the resignation, removal and replacement of company auditors.<sup>76</sup>

4.53 Following feedback from an FRC survey of directors and financial reporting professionals on the financial literacy of company directors, conducted in 2012, ASIC launched a financial reporting quiz in December 2014 to help directors test their knowledge of financial reporting and to direct them to additional resources that may assist in improving their knowledge.<sup>77</sup> During the reporting period this quiz has been completed by more than 2000 directors and responses have been collected by a third party provider.<sup>78</sup> ASIC seeks to use this information to assist them and other organisations, such as the Australian Institute of Company Directors and the Institute of Public Accountants 'in considering ways to assist in educating directors in the future.'<sup>79</sup> The committee will monitor the outcomes of this initiative.

#### *Professional, ethical and education standards in the financial services industry*

4.54 Following a recommendation by the Senate Economics References inquiry into the performance of ASIC, the Parliamentary Joint Committee on Corporations and Financial Services resolved on 14 July 2014 to inquire into proposals to lift the professional, ethical and education standards in the financial services industry (standards inquiry).<sup>80</sup> ASIC provided a submission to this inquiry and notes in its annual report that it supported many of the report's recommendations.<sup>81</sup>

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75 ASIC represents Australia in the Organisation for Economic Cooperation and Development (OECD); ASIC, *Annual Report 2014–15*, p. 43.

76 ASIC, *Annual Report 2014–15*, pp 6, 8, 57–58.

77 Financial Reporting Council, *FRC survey on Financial Literacy of Australian Directors*, September 2012, <http://www.frc.gov.au/files/2013/12/Paper-survey-financial-literacy-2013.pdf> (accessed 8 March 2016).

78 ASIC, *Annual Report 2014–15*, p. 58; ASIC, *Financial reporting quiz for directors*, <http://asic.gov.au/regulatory-resources/financial-reporting-and-audit/directors-and-financial-reporting/financial-reporting-quiz-for-directors/> (accessed 8 March 2016); ASIC, answer to question on notice, 9 March 2016 (received 19 April 2016).

79 ASIC, *Answer to question on notice*, 9 March 2016 (received 19 April 2016).

80 Economics References Committee, *Performance of the Australian Securities and Investments Commission*, June 2014, p. xxx1–xxxiii ; Parliamentary Joint Committee on the Corporations and Financial Services, *Inquiry into proposals to lift the professional and ethical and education standards in the financial services industry*, December 2014, p. 2; ASIC, *Annual Report 2014–15*, p. 13.

81 ASIC, *Annual Report 2014–15*, p. 13.

4.55 Following extensive consultations on the recommendations contained in the standards inquiry report the government decided to incorporate its response to the standards inquiry in its response to the Financial System Inquiry (FSI).<sup>82</sup> At the time of preparing this report the government has agreed to develop legislation that supports a number of the report's recommendations, including the requirements for financial advisers to:

- hold a degree qualification;
- undertake a professional year;
- undertake ongoing professional development;
- pass a registration exam; and
- subscribe to a code of ethics.<sup>83</sup>

4.56 It is of note that until these measures are implemented, financial product advisers will still be required to meet the minimum training standards as set out in RG146. At the time of preparing this report more than 2000 new financial advisers have been added to the register following completion of the training requirements.<sup>84</sup> In response to the committee's concerns about the adequacy of RG146, ASIC indicated that within the financial advice industry there is a recognition about changing standards of education and professionalism and many firms have already sought to have their advisers improve their qualifications.<sup>85</sup> ASIC also indicated that it will continue to undertake surveillance and provide feedback in relation to licensees' obligations to provide adequate training for their advisers.<sup>86</sup>

4.57 The committee will continue to monitor the adequacy of current training requirements for financial advisers.

#### *External dispute resolution*

4.58 Following a recommendation by the Senate Economics References inquiry into the performance of ASIC, the annual report contains commentary on the work of the financial services and consumer credit external dispute resolution (EDR) schemes.<sup>87</sup> The 2014–15 annual report notes the significant issues the two EDR schemes, the Financial Ombudsman Service (FOS) and the Credit and Investments

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82 The Government response to the FSI was released in October 2015.

83 Australian Government, *Improving Australia's Financial System: Government Response to the Financial System Inquiry*, October 2015, p. 21.

84 *Committee Hansard*, 16 October 2015, p. 10.

85 Ms Louise Macaulay, Senior Executive Leader, Financial Advisers, Australian Securities and Investments Commission, *Committee Hansard*, 19 November 2015, p. 5.

86 *Committee Hansard*, 19 November 2015, pp 5–7.

87 Economics References Committee, *Performance of the Australian Securities and Investments Commission*, June 2014, p. xxiii-xxiv.

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Ombudsman (CIO), have raised in their reports to ASIC and action taken by ASIC in relation to these issues.<sup>88</sup>

4.59 During the reporting period the FOS and CIO reported on 93 definite systemic issues and 25 cases of serious misconduct. ASIC was able, where appropriate, to use information from these reports to inform new and current investigations.<sup>89</sup>

4.60 During the reporting period the FOS implemented many of the recommendations from its 2013 independent review and engaged with ASIC in relation to changes to its terms of reference, many of which came into effect on 1 January 2015.<sup>90</sup>

### *Deregulation*

4.61 In line with the deregulation focus articulated in the government's Statement of Expectations, ASIC has continued to seek ways to reduce red tape and lower compliance costs. ASIC notes the following achievements in this area:

- reaching \$119.6 million in compliance savings for business which was in excess of the target set by the Government;
- the establishment of the Innovation hub;<sup>91</sup>
- the continuation of ASIC's Business Names Register;<sup>92</sup> and
- the establishment of the Market Entity Compliance system.<sup>93</sup>

### *Other emerging issues*

4.62 In its annual report ASIC identified a number of issues that it sees as its key challenges in the long-term. In an environment of advancing technology, digital disruption and cyber resilience were highlighted as becoming increasingly important and complex. In response to these emerging issues ASIC has noted in its annual report the following developments during the 2014–15 reporting period:

- issuing guidance and information reports in relation to assisting the sector to understand emerging risks in an era of fast paced technological change;

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88 ASIC, *Annual Report 2014–15*, pp 14, 58.

89 ASIC, *Annual Report 2014–15*, p. 58.

90 ASIC, *Annual Report 2014–15*, p. 48.

91 The Innovation Hub is an ASIC initiative for new financial technology businesses that are developing innovative financial products or services. Through the Innovation Hub eligible financial technology startup businesses can receive informal assistance to help them navigate ASIC's regulatory system; see <http://asic.gov.au/for-business/your-business/innovation-hub/>

92 The market entity compliance system (MECS) is an online regulatory compliance portal that provides market entities with tools and information to assist them in complying with a number of their regulatory obligations; see <http://asic.gov.au/online-services/register-for-online-access/market-entity-compliance-system/>

93 ASIC, *Annual Report 2014–15*, pp 12–13.

- the development of an Innovation Hub to help financial technology start-ups understand the regulatory system;
- the development of a Cyber Resilience Model to better understand how investment banks manage cyber resilience;
- the issuing of a cyber-resilience report to help financial markets and the financial system manage all aspect of a cyber-attack; and
- the establishment of a Digital Finance Advisory Committee to help ASIC monitor and understand developments in the digital sphere including digital platforms that enable crowd sourced funding and market place lending, digital currencies and 'blockchain technology'.<sup>94</sup>

4.63 It is also of note that in the reporting period that ASIC continued to respond to emerging developments and opportunities such as:

- globalisation;
- complexity driven by financial innovation;
- structural change driven by superannuation;
- conduct risk and the balance between a free market-based system and investor and financial consumer protection;
- digital currencies;
- high frequency trading; and
- dark liquidity (dark pools).<sup>95</sup>

#### *Inquiries and reviews*

4.64 The ANAO have noted that a key area of attention during 2015–16 will be the regulatory functions of Australian Prudential Regulation Authority (APRA), ASIC and the Australian Competition and Consumer Commission (ACCC).<sup>96</sup>

4.65 ASIC noted in its annual report a number of areas that had been identified during the course of inquiries, reviews and hearing as in need of review and reform. These included:

- the need for an industry funding model;
- the need for a 'more flexible regulatory toolkit' which would include product intervention powers;
- the need for adequate penalties; and
- continued work towards lifting professional, ethical and education standards in the financial advice sector.

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94 ASIC, *Annual Report 2014–15*

95 ASIC, *Annual Report 2014–15*, pp 2–3, 50–51.

96 ANAO, *Audit Work Program, July 2015*, p. 127.

4.66 The annual report forecasts that there will also be ongoing developments in these and other areas during 2015–16 as a result of recommendations and proposals that result from the completion of:

- ASIC's four-year corporate plan;
- the government response to the Financial System Inquiry (FSI); and
- the capability review into ASIC.<sup>97</sup>

4.67 The Capability Review found that many of ASIC's regulatory capabilities are in line with global best practice. However, the review recommended additional measures to support ASIC in delivering its mandate and ensuring it is fit for the future. The Capability Review found there were aspects of strategy, governance, IT, data infrastructure, management information systems and ASIC's approach to stakeholder engagement that required improvement.<sup>98</sup>

4.68 On 20 April 2016 the Commonwealth government released the ASIC Capability Review and the government response. The government also announced that five of the Capability Review recommendations would be implemented and that it expected ASIC to provide an implementation plan for the other 29 recommendations.<sup>99</sup> The committee welcomes and will monitor the implementation of the announcements including:

- a user pays industry funding model to deliver \$127m in additional funding;
- deepening the surveillance and enforcement capability of ASIC with a specific focus on investigating financial advice, responsible lending and life insurance;
- enhancing data analytics and surveillance capabilities as well as modernising data management systems;
- strengthening ASIC's powers;
- the appointment of an additional ASIC commissioner with experience in the prosecution of crimes in the financial services industry;
- bringing forward law reforms recommended by the Financial System Inquiry, including product intervention powers, product distribution obligations, strengthening consumer protection for electronic payments and a review of ASIC penalties and the enforcement regime.<sup>100</sup>

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97 ASIC, *Annual Report 2014–15*, p. 5.

98 Australian Government Factsheet, *Improving Consumer Outcomes in Financial Services*, 20 April 2016, p. 1.

99 Australian Government Factsheet, *Improving Consumer Outcomes in Financial Services*, 20 April 2016, p. 1.

100 Australian Government Factsheet, *Improving Consumer Outcomes in Financial Services*, 20 April 2016, p. 1; The Hon Scott Morrison MP, Treasurer, joint media release with the Hon Kelly O'Dwyer MP, Minister for Small Business, Assistant Treasurer, *Turnbull Government bolsters ASIC to protect Australian Consumers*, 20 April 2016.

*Committee view*

4.69 The committee notes that the recommendation it made in its examination of ASIC's 2012–13 annual report relating to the compliance index has been adopted in ASIC's 2014–15 annual report. The committee also notes that the recommendation it made in its examination of ASIC's 2012–13 annual report relating to the provision of more longitudinal data has been incorporated in ASIC's reporting on key outcomes in its 2014–15 annual report.

4.70 The committee notes that whilst the 2014–15 annual report does contain more information in relation to EUs than in previous years, it will continue to monitor ASIC's response to the ANAO audit recommendations and the information provided by ASIC on EUs in enforcement and annual reports.

4.71 The committee notes that the annual report confirms that ASIC has implemented or is working to implement many of the recommendations from the Senate Economics References Committee inquiry into the performance of ASIC and the Parliamentary Joint Committee on Corporations and Financial Services inquiry into proposals to lift professional, ethical and education standards in the financial services industry.

4.72 The committee considers that ASIC has fulfilled its annual reporting responsibilities during the 2014–15 financial year. The committee notes that ASIC is continuing to address significant changes to its mandate and the environment in which it operates as a result of global trends, emerging issues and recent reviews and inquiries. The committee will continue to use annual reports and other mechanisms to monitor ASIC's performance and ability to adapt appropriately.

4.73 The committee thanks ASIC for its contributions at hearings, responding to questions on notice, and the timely provision of information to the committee.

**Senator David Fawcett**  
**Chair**

# **Appendix 1**

## **Submissions**

1. Professor Jean Du Plessis and Associate Professor Anil Hargovan, Corporate Law Teachers Association
2. Associate Professor Gill North, Corporate Law Teachers Association
3. Associate Professor Christopher Symes, Associate Professor Colin Anderson and Mr Jason Harris, Corporate Law Teachers Association
4. Professor Paul Redmond, Corporate Law Teachers Association

## **Tabled Documents**

1. Opening Statement of Mr Greg Medcraft, Chairman, Australian Securities and Investments Commission
2. Update on ASIC's progress in implementing relevant recommendations of the Senate inquiry into the performance of ASIC
3. Cognitive Task Analysis of financial advisers for the Australian Securities and Investments Commission
4. Cognitive Task Analysis of financial advisers report summary
5. Letter to Mr Medcraft from Industry Associations regarding ASIC's review of training standards
6. Opening statement of Mr Greg Medcraft, Chairman, Australian Securities and Investments Commission provided on 20 March 2015.
7. Opening statement of Mr Greg Medcraft, Chairman, Australian Securities and Investments Commission provided on 14 August 2015
8. ASIC Strategic Framework Map, provided on 14 August 2015
9. ASIC Regulatory Transformation - Capture Share Use, provided on 14 August 2015
10. Opening statement of Mr Greg Medcraft, Chairman, Australian Securities and Investments Commission provided on 19 November 2015

## **Additional information received by the committee**

1. City Pacific background information provided by ASIC on 16 June, 2015
2. Applications for Property Possession provided by APRA on 26 May, 2015

3. ASIC response to the Parliamentary Joint Committee on Corporations and Financial Services in regard to its investigation of ASTARRA and TRIO Capital, provided on 19 June 2015
4. ASIC response to the Parliamentary Joint Committee on Corporations and Financial Services in regard to the Financial Advisors Register, provided on 19 November 2015
5. Answers to Questions on Notice: Presented to ASIC on 28 November 2014 and provided 30 January 2015.
6. Answers to Questions on Notice: Presented to ASIC on 20 March 2015 and provided 30 April 2015.
7. Answer to Questions on Notice, provided by ASIC and received on 13 May 2015.
8. Answer to Questions on Notice, provided by ASIC and received 11 August 2015.
9. Answer to Questions on Notice asked at a public hearing on 14 August 2015, received from ASIC on 20 August 2015.
10. Answers to Questions on Notice asked at a public hearing on 14 August 2015, received from ASIC on 8 October 2015.
11. Answers to Questions on Notice asked at a public hearing on 14 August 2015, received from ASIC on 14 October 2015.
12. Answer to Questions on Notice asked at a public hearing on 16 October 2015, received from ASIC on 18 November 2015.
13. Answers to Questions on Notice asked at a public hearing on 19 November 2015, received from ASIC on 4 February 2016.
14. Answers to Questions on Notice, provided by ASIC and received on 19 April 2016.

## **Appendix 2**

### **Public hearings and witnesses**

#### **Canberra, 28 November 2014**

*Australian Securities and Investments Commission*

Mr Greg Medcraft, Chairman

Ms Cathie Armour, Commissioner

Mr Adrian Brown, Senior Executive Leader, Insolvency Practitioners

Mr Warren Day, Senior Executive Leader, Assessment and Intelligence

Mr Peter Kell, Deputy Chairman

Mr Greg Kirk, Senior Executive Leader, Strategy Group

Ms Louise Macaulay, Senior Executive Leader, Financial Advisers

Mr Tim Mullaly, Senior Executive Leader, Financial Services

Mr John Price, Commissioner

Mr Chris Savundra, Senior Executive Leader, Markets Enforcement

Mr Greg Tanzer, Commissioner

#### **Sydney, 20 March 2015**

*Australian Securities and Investments Commission*

Mr Greg Medcraft, Chairman

Ms Cathie Armour, Commissioner

Mr Warren Day, Senior Executive Leader, Assessment and Intelligence

Mr Peter Kell, Deputy Chairman

Mr Greg Kirk, Senior Executive Leader, Strategy Group

Ms Louise Macaulay, Senior Executive Leader, Financial Advisers

Mr John Price, Commissioner

Mr Greg Tanzer, Commissioner

#### **Canberra, 14 August 2015**

*Australian Securities and Investments Commission*

Mr Greg Medcraft, Chairman

Mr Warren Day, Senior Executive Leader, Stakeholder Services

Regional Commissioner

Mr Peter Kell, Deputy Chairman

Mr Greg Kirk, Senior Executive Leader, Strategy Group

Ms Louise Macaulay, Senior Executive Leader, Financial Advisers

Mr Tim Mullaly, Senior Executive Leader, Financial Services

Mr John Price, Commissioner

Mr Michael Saadat, Senior Executive Leader, Deposit Takers and Insurers and Credit Services

Mr Chris Savundra, Senior Executive Leader, Markets Enforcement

Mr Greg Tanzer, Commissioner

### **Melbourne, 16 October 2015**

*Australian Securities and Investments Commission*

Mr Greg Medcraft, Chairman

Ms Cathie Armour, Commissioner

Mr Warren Day, Senior Executive Leader

Mr Peter Kell, Deputy Chairman

Ms Louise Macaulay, Senior Executive Leader

Mr Tim Mullaly, Senior Executive Leader, Financial Services Enforcement

Mr John Price, Commissioner

Mr Michael Saadat, Senior Executive Leader

Mr Greg Tanzer, Commissioner

### **Brisbane, 19 November 2015**

*Australian Securities and Investments Commission*

Mr Greg Medcraft, Chairman

Ms Cathie Armour, Commissioner

Mr Warren Day, Senior Executive Leader, Assessment and Intelligence

Ms Louise Macaulay, Senior Executive Leader, Financial Advisers

Mr Tim Mullaly, Senior Executive Leader, Financial Services Enforcement

Mr John Price, Commissioner

Mr Michael Saadat, Senior Executive Leader, Deposit Takers and Insurers and Credit Services

Mr Greg Tanzer, Commissioner

**Canberra , 16 March 2016**

*Australian Securities and Investments Commission*

Mr Greg Medcraft, Chairman

Ms Cathie Armour, Commissioner

Ms Joanne Bird, Senior Executive Leader, Financial Advisers Group

Mr Warren Day, Senior Executive Leader, Assessment and Intelligence

Mr Peter Kell, Deputy Chairman

Mr Greg Kirk, Senior Executive Leader, Strategy Group

Mr David McGuinness, Senior Executive Leader, Financial Services

Mr John Price, Commissioner

Mr Michael Saadat, Senior Executive Leader, Deposit Takers and Insurers and Credit Services

Mr George Stogdale, Senior Executive Leader, Market Integrity

Mr Greg Tanzer, Commissioner



# Appendix 3

## Summary of Mariner Matter

### Background to the Mariner matter

In April 2014, ASIC brought legal action in the Federal Court of Australia against Mariner Corporation Limited (*Mariner*) and three of its then current and former directors.<sup>1</sup> The action was concerned with Mariner's public announcement on 25 June 2012 of an off-market takeover bid for Austock Group Limited at a price of 10.5 cents per share.

ASIC alleged that Mariner was reckless as to whether it could perform its obligations in relation to the announced bid because, at the date of the announcement, Mariner did not itself have the financial resources necessary to the fund the bid, nor any commitment or assurance from another party to provide funding for the bid.

Specifically, ASIC alleged that in making the public announcement Mariner had contravened s631(2)(b) of the *Corporations Act 2001* (**Act**). Subsection 631(2) provides that:

*"A person must not publicly propose, either alone or with other persons, to make a takeover bid if:*

- (a) the person knows the proposed bid will not be made, or is reckless as to whether the proposed bid is made; or*
- (b) the person is reckless as to whether they will be able to perform their obligations relating to the takeover bid if a substantial proportion of the offers under the bid are accepted."*

Section 631 of the Act was enacted in its current form as part of amendments to the takeover provisions made by the *Corporate Law Economic Reform Program Act 1999* (**CLERPA**) in March 2000. Subsection 631(2) had not been the subject of judicial consideration prior to the *Mariner* matter.

In addition to s631(2), ASIC alleged that the making of the public announcement in the circumstances also gave rise to contraventions of s1041H (misleading and deceptive conduct) and s180(1) (director's duty of care and diligence) of the Act.

#### *The policy underlying the requirement to have funding for a bid*

The predecessor provisions to subsection 631(2) date back to the early 1970s. Their genesis is the 1969 Eggleston Committee Report<sup>2</sup> which set out a number of key principles that still underpin takeovers laws today.

As with its predecessors, subsection 631(2) seeks to address the concern that takeover bids should not be announced where a proposed bidder either does not in fact have any intention to proceed with a bid, or does not have reasonable grounds to expect that they will be able to pay the consideration offered under the bid.<sup>3</sup> It is an important market integrity provision which recognises that the announcement of a takeover bid will often have a significant effect on the market for target securities even before offers are made.

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<sup>1</sup> *Australian Securities and Investments Commission v Mariner Corporation Limited* [2015] FCA 589

<sup>2</sup> The *Second Interim Report* of the Company Law Advisory Committee to the Standing Committee of Attorneys-General, (Parliamentary Paper No. 43), February 1969.

<sup>3</sup> See para 37 of the Eggleston Committee Report

The importance of ensuring bidders have sufficient funding is also highlighted in the Takeovers Panel's (**Panel**) *Guidance Note 14: Funding Arrangements (GN 14)* which discusses when the inadequacy of a bidder's funding arrangements may give rise to 'unacceptable circumstances'. Since it was first published in 2004, the Panel's guidance has noted that unacceptable circumstances may arise if a bidder does not have funding in place, or a *reasonable basis* to expect that it will have funding in place, to pay for *all acceptances* when its bid becomes unconditional. GN 14 seeks to outline the standard of funding certainty necessary to give effect to the principles underlying the takeover provisions set out in section 602 of the Act—in particular the objective of ensuring that the acquisition of control of an entity takes place in an efficient, competitive and informed market. ASIC generally supports the policy settings in GN 14 and applies them in its day to day role regulating takeover transactions in Australia.

#### Prior Takeover Panel proceedings

At the time of Mariner's proposed bid, the Panel had cause to consider Mariner's funding arrangements as a result of Mariner itself applying for a declaration of unacceptable circumstances from the Panel in relation to Austock's announcement that it had agreed to sell its property funds management business to a third party. Prior to Mariner's application ASIC had made inquiries regarding the company's funding arrangements. ASIC subsequently raised concerns with Mariner that it did not have adequate arrangements in place and indicated that it was minded to make a separate application to the Panel in relation to its concerns. Following this Mariner announced that would not be proceeding with the proposed bid.

The Panel ultimately made a declaration of 'unacceptable circumstances' in relation to Mariner's announced bid on the basis that it appeared to the Panel that Mariner had not had a reasonable basis to expect that it would have funding in place to pay for all acceptances in the event the bid became unconditional and that the market was not sufficiently informed regarding the circumstances of Mariner's bid.<sup>4</sup>

In making the declaration the Panel noted that Mariner's intention was to obtain bridging finance that was to be repaid from the proceeds of selling off Austock's businesses, but that Mariner had acknowledged that it did not have concluded financing arrangements to this effect in place. The Panel commented that, in its view, the bid should not have been announced, or allowed to proceed at all, unless and until finance had been arranged and that the announcement was likely to have had an adverse effect on Austock and its shareholders.<sup>5</sup>

#### **Issues of construction raised by the *Mariner* matter**

In deciding the *Mariner* matter, the Court opined on a number of aspects of the construction of s631(2). The two principal issues of interpretation discussed by the court were:

- (a) the relevant test of when a person is 'reckless', and in particular, whether this is a subjective or objective test; and
- (b) the question of what is meant by a 'substantial proportion of the offers'.

#### Recklessness

The court disagreed with ASIC's submission that s631(2)(b) is an objective test. Rather the court found that the question of whether a person is 'reckless' requires the application of a subjective test of recklessness, such as the test set out in Section 5.4 of Ch 2 of the *Criminal Code* or a similar common law test. To meet a test of this kind the Court stated that it is necessary to show that:

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<sup>4</sup> *Austock Group Limited* [2012] ATP 12

<sup>5</sup> *Austock Group Limited* [2012] ATP 12, [60].

- 
- (a) the person alleged to be reckless was aware there was a substantial risk that they may not be able to perform their obligations under the bid if a substantial proportion of offers were accepted; and
  - (b) on the basis of what was known to the person, it was unjustifiable to take that risk (or that the person went ahead in conscious disregard of, or indifference to, the risk).<sup>6</sup>

The court, after examining the evidence regarding the state of mind of the directors of Mariner, concluded that it had not been shown that Mariner was actually aware of the substantial risk that Mariner would not be able to perform its obligations under the bid.<sup>7</sup> The court also found that, even if Mariner's actual awareness of the risk had been established, it had not been demonstrated that the risk was unjustifiably taken.<sup>8</sup>

The Court also opined on whether, if s631(2)(b) had an objective element, Mariner had reasonable grounds to believe it would be able to perform its obligations under the bid. The Court was prepared to accept that in the specific circumstances of the Mariner case, notwithstanding that Mariner did not have sufficient funding itself, or sufficient commitments or assurances from external parties to fund the bid, the 'arbitrage opportunity' reflected in the difference between Austock's market capitalisation and the value of Austock's assets that could be realised on a break-up of Austock supported a case that there was reasonable grounds to believe that the requisite funding could be sourced.<sup>9</sup>

#### 'Substantial proportion of offers'

In considering the application of s631(2)(b), it was also necessary for the Court to construe the level of funding required if 'a substantial proportion of offers' under the proposed Mariner bid were accepted.

This aspect of the provision raises two difficulties in particular:

- (a) while s631(2)(b) requires a bidder to consider their obligations if a substantial proportion of 'offers' are accepted, the offers under a bid are made to registered shareholders who generally hold different quantities of shares in the company. The amount of funding required is a function of the number of shares held by those shareholders who decide to accept the offers; and
- (b) it is unclear what percentage of offers (or shares the subject of offers) constitutes a 'substantial' proportion.

The Court noted that the concept was potentially unclear on both of these points, and with some hesitation, decided that the most appropriate approach to take was to assume that the concept required funding for *at least* 50% of the shares in Austock.<sup>10</sup>

### **Possibilities for legislative reform**

In response to the decision in *Mariner*, the Takeovers Panel consulted on proposed amendments to GN 14. The amendments were designed to clarify that GN 14 is based on the general principles in s602(a) and (c) of the Act and, consistent with those principles, to confirm the existing requirements in GN 14. ASIC supported the Panel's update of the guidance note.

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<sup>6</sup> *Mariner*, [248]-[279]; [334]-[341].

<sup>7</sup> *Mariner*, [340] and [370].

<sup>8</sup> *Mariner*, [369]-[374].

<sup>9</sup> *Mariner*, [375]-[387]. The court did however comment that it was not without some hesitation that it had come this view: see [377].

<sup>10</sup> *Mariner*, [311].

ASIC would generally support a review of s631(2) to consider amendments aligning the requirements of the provision with the broader regulatory policy settings discussed in GN 14. This would potentially include:

- (a) amending s631(2)(b) to require that a bidder have an objectively reasonable basis that it will be able to comply with its funding obligations under a bid; and
- (b) addressing the uncertainty arising from the reference in the provision to a '*substantial proportion of offers*' by clarifying that funding is required to pay for all securities to which the proposed bid relates.

As previously noted, s631(2) is a key market integrity provision that recognises the announcement of a bid will often have a significant effect on the market for a target entity's securities. It is also the principal provision in the regulatory framework for takeovers imposing a direct obligation on a bidder to have a level of certainty in relation to funding the cash component of a takeover bid.

The requirement for an objectively reasonable basis for funding was a feature of each of the predecessor provisions to s631.<sup>11</sup> As such the objective standard, reflected in the principles based policies of ASIC and the Panel, has represented market practice in relation to takeover bid funding since the revamp of Australia's takeover laws in response to the Eggleston Committee Report.

Moreover, we note that the importance of ensuring an announced bidder has adequate funding is a feature of takeovers regulation internationally. Specific requirements in connection with the announcement of cash offers is common to most comparable jurisdictions. Reasonableness appears, in one way or another, to be a factor in each—with some even requiring independent verification as to funding at varying stages of the offer. The table below outlines some of the requirements in comparable overseas jurisdictions.

### Requirements regarding funding of cash bids in comparable jurisdictions

Jurisdiction	Requirements at announcement
UK	<p>An offeror should announce a <b>firm intention</b> to make an offer only after the most careful and responsible consideration and when <b>the offeror has every reason to believe that it can and will continue to be able to implement the offer...</b><sup>12</sup> Where the offer is for cash, or includes an element of cash, the announcement <b>must include confirmation by the financial adviser or another third party</b> that sufficient resources <b>are available</b> to satisfy <b>full acceptance</b> of the offer.<sup>13</sup></p> <p>There is no requirement in the code to discuss funding in connection with announcement of a possible offer (which triggers the 28-day 'put up or shut up' rule).<sup>14</sup></p>

<sup>11</sup> See for example s746 of the *Corporations Law*, as it stood prior to the CLERPA amendments.

<sup>12</sup> Panel on Takeovers and Mergers (UK), *City Code on Takeovers and Mergers*, rule 2.7(a). This rule reflects one of the six general principles on which the code is based: '*An offeror must announce a bid only after ensuring that he/she can fulfil in full any cash consideration, if such is offered, and after taking all reasonable measures to secure the implementation of any other type of consideration*' (General Principle 5).

<sup>13</sup> Panel on Takeovers and Mergers (UK), *City Code on Takeovers and Mergers*, rule 2.7(d). The offer document for cash offer must also include confirmation from third party that resources are available to the offeror sufficient to satisfy full acceptance of the offer Panel on Takeovers and Mergers (UK), *City Code on Takeovers and Mergers*, rule 24.8. The UK Panel's Practice Note 10 also specifies that where an offer is proposed to be financed by new securities, the offer must be made subject to any condition required, as a matter of law or regulation, in order to validly issue those securities (including shareholder approval).

<sup>14</sup> Panel on Takeovers and Mergers (UK), *City Code on Takeovers and Mergers*, rule 2.6.

Jurisdiction	Requirements at announcement
Hong Kong	<p>The announcement of a <b>firm intention to make an offer</b> should be made only when an offeror has <b>every reason to believe</b> that it <b>can and will continue to be able to implement the offer</b>. Responsibility in this connection also rests on the financial adviser to the offeror.<sup>15</sup></p> <p>Preliminary announcements may be made however before this time (for example in the case of a leak), and sometimes will need to be made prior to approaching parties to seek financing.<sup>16</sup> Prior to a binding 'firm intention' statement being made, only a brief announcement is required that the offeror is considering an offer.<sup>17</sup></p>
Singapore	<p>When a <b>firm intention</b> to make an offer is announced, if the offer is for cash or involves an element of cash, the announcement should include an <b>unconditional confirmation</b> by the financial adviser or by another appropriate third party that the offeror has sufficient resources available to satisfy full acceptance of the offer.<sup>18</sup></p>
EU (Directive)	<p>As a general principle, an offeror must announce a bid <b>only after ensuring</b> that he/she <b>can fulfil in full</b> any cash consideration, if such is offered.<sup>19</sup></p>
New Zealand	<p>Takeovers Code notice announcing an intention to bid must include <b>confirmation</b> by the offeror <b>that resources will be available</b> to the offeror <b>sufficient to meet the consideration to be provided on full acceptance</b> of the offer and to pay any debts incurred in connection with the offer.<sup>20</sup></p>

Given the emphasis placed on the importance of ensuring adequate funding arrangements in announced takeovers generally, it may also be appropriate to re-examine whether the provision should continue to require funding for only some, rather than all, of the securities the subject of the announced bid.

ASIC is also aware that some market participants have supported reform to bring the requirements of s631(2) into line with ASIC and the Panel's regulatory policy position following the *Mariner* decision.<sup>21</sup>

## Criminal Liability

While the *Mariner* case was a civil action, ASIC also considered the criminal operation of s631(2) and discussed this with the CDPP.

<sup>15</sup> Securities and Futures Commission (HK), *The Code on Takeovers and Mergers and Share Buy-backs*, rule 3.5. This is consistent with one of the general principles underpinning the code: An offeror should announce an offer only after careful and responsible consideration. The same applies to making acquisitions which may lead to an obligation to make a general offer. In either case the offeror and its financial advisers should be satisfied that it can and will continue to be able to implement the offer in full (General Principle 4). An offeror must proceed with a 'Firm intention' offer subject only to announced conditions: rule 5. The offer document for cash offers must include confirmation by a financial adviser or another appropriate independent person that resources are available sufficient to satisfy full acceptance: Sch I, cl 11.

<sup>16</sup> *The Code on Takeovers and Mergers and Share Buy-backs* (HK), rule 3.1

<sup>17</sup> *The Code on Takeovers and Mergers and Share Buy-backs* (HK), rule 3.6

<sup>18</sup> *Singapore Code on Take-overs and Mergers*, rule 3.5. See also rule 1.3 and General Principle 6.

<sup>19</sup> Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on Takeover Bids, Art 3, General Principle (e).

<sup>20</sup> *Takeovers Code Approval Order 2000* (NZ). Rule 41, 41A, 42, Sch 1 cl 9(1).

<sup>21</sup> See submission dated 26 October 2015 from Herbert Smith Freehills, Takeovers Panel, Public Consultation Response Statement (26 November 2015). See also <http://herbertsmithfreehills.com/insights/legal-briefings/takeover-funding-requirements-cast-adrift-by-federal-court-decision> and [https://www.ashurst.com/page.aspx?id\\_Content=12151](https://www.ashurst.com/page.aspx?id_Content=12151).

A difficulty with s631(2) is that it has not been harmonised with the general principles of physical and fault elements in Chapter 2 of the *Criminal Code*. There are potentially a number of interpretations of how the section would operate in a criminal prosecution. This would require judicial interpretation in any prosecution, and creates uncertainty for the regulators, prosecutors and the regulated community.

In addition, the defence in s670 presents some difficulties. The defence provides that:

*"A person does not commit an offence under subsection 631(1) or (2), and is not liable under s670E for a contravention of those subsections if the person proves that they could not reasonably have been expected to comply with those subsections because:*

- (a) at the time of the proposal or announcement, circumstances existed that the person did not know of and could not reasonably have been expected to know of; or*
- (b) after the proposal or announcement, a change in circumstances occurred that was not caused, directly or indirectly, by the person."*

While the offence in s631(2) applies at the time of the public proposal, the defence in s670(b) purports to apply retrospectively to circumstances that occur after the public proposal. The operation of a defence in this matter is arguably inappropriate and again adds to the uncertainty surrounding the operations of these provisions.

ASIC, answer to question on notice, 9 March 2016 (received 19 April 2016).