CHARTERED SECRETARIES
AUSTRALIA

Keeping good companies

23 July 2004

Ms Jan Redfern
Executive Director, Enforcement
Australian Securities & Investment Commission
Level 18, No 1 Martin Place
SYDNEY NSW 2000

Dear Ms Redfern

Re: ASIC Guide on Continuous Disclosure Obligations: Infringement Notices

Chartered Secretaries Australia (CSA) is Australia's peak membership body for corporate governance and compliance with over 8,000 members in Australia representing the majority of public companies listed on the Australian Stock Exchange. Members of CSA regularly deal on a day-to-day basis with the ASX, ASIC, and the ACCC and have a thorough working knowledge of the operations of the markets, the needs of investors and the law and regulation dealing with market practices and independence. In addition, representatives from the ASX, ASIC and the ACCC regularly address members at our seminars and conferences.

While CSA continues to have reservations about the introduction of a penalty regime for continuous disclosure, it believes it is important to provide feedback on the ASIC Guide titled "Continuous Disclosure Obligations: Infringement Notices" released in May 2004.

Joint Parliamentary Committee recommendations – clarity in guide (paras 6.017-6.110)

CSA endorses the following recommendations of the Joint Parliamentary Committee. [1]

- The guide should contain a strong statement that the delegate will maintain his/her independence from the investigation team after being briefed on the suspected breach and that the investigation team and delegate maintain a strict division of responsibility.

- Assurances that, having regard to the subjectivity required in determining whether there has been a breach of the continuous disclosure provisions, the delegates have the expertise and experience necessary to assess the merits of the case effectively.

- Conforming the language of the guide with that of the legislation in relation to "has reasonable grounds to believe" there has been a contravention.

[1] Parliamentary Joint Committee on Corporations and Financial Services, CLERP (Audit Reform and Corporate Disclosure) Bill 2003 – Part 1 – Enforcement, executive remuneration, continuous disclosure, shareholder participation and related matters, June 2004.

In relation to the first point, having regard to section 1317DAD(4), that says that information given to ASIC under the infringement notice regime is not admissible against the entity or a representative of the entity in any proceedings, CSA requests that ASIC clarify in the guide a separation of function between ASIC delegates involved in an infringement notice matter and any decision to bring a proceeding against the entity or its representatives and the conduct of those proceedings.

Application of Infringement Notice Regime

The Explanatory Memorandum (para 5.4.57) to CLERP 9 makes it clear that the infringement notice regime is only to be used in relation to "less serious contraventions of the continuous disclosure regime". The ASIC media release of 20 May 2004 also says the regime is to "address less serious breaches of the continuous disclosure laws". The overview section in the guide says that "The new remedy is intended only to be used for less serious breaches of the obligations". This is not then further discussed in the body of the guide.

It is clear from the report of the Parliamentary Joint Committee that there is widespread concern about the infringement notice regime. In light of this, it is particularly important for there to be clarity about the application of the regime. Reading the body of the guide, in particular para 10, it is not clear what ASIC regards as a less serious breach. For example, looking at the matters identified in para 10, if the information went to the heart of the entity's continued operations or the factual circumstances involve a negligent, reckless or deliberate breach, does this mean the breach is "serious" rather than "less serious" and so will not be subject to the infringement notice regime? Presumably this is not the intention– but, for example, if a breach is deliberate, it is difficult to see how this can be characterised as "less serious"? CSA recommends that ASIC clarify in the guide the interpretation of a "less serious breach".

A related issue to be clarified is the relationship between the infringement notice regime and civil penalty regime. In the guide, ASIC says that if an entity does not comply with the infringement notice, ASIC may begin civil penalty proceedings against an entity under Part 9.4B of the Corporations Act. Under 9.4B, section 1317G(1A) requires a contravention of a financial services civil penalty provision (which includes sections 674(2) and 675(2) – section 1317DA) to meet one of the following criteria before a court will impose a pecuniary penalty:

- it materially prejudices the interests of acquirers or disposers of the relevant financial product,
- it materially prejudices the issuer of the relevant financial products or, if the issuer is a corporation or scheme, the members of that corporation or scheme; or
- it is serious.

Accordingly, the civil penalty regime focus is on more serious or significant breaches, whereas the infringement notice regime is stated to be directed to less serious breaches. CSA requests that the ASIC guide clarify the circumstances in which a "less serious breach" may be regarded as a suitable matter for ASIC to bring proceedings under Part 9.4B.

Publication of Infringements

While it is acknowledged that the publication of notices is permitted by the provisions (section 1317DAJ), CSA believes that ASIC's publication of details of notices of infringement is counterproductive. Given the contentious nature of the disclosure rules and the 'newness' of the penalty regime, listed entities are necessarily concerned at the adverse publicity that will accompany payment of fines without a finding of guilt on the part of the entity. In the event that ASIC discovers later that it was wrong in applying an infringement penalty, it may refund the penalty, but it will not be able to undo the damage caused by ASIC's publication of the infringement. CSA recommends that ASIC not fetter the discretion it is given under the provisions ("ASIC **may** publish details"), in the way set out in para 40 of the guide ("we **will** publish details"), but approach this matter on a case by case basis.

A concern in relation to publicity also identified in the report by the Parliamentary Joint Committee is the risk of follow-on suits (para 6.117). The entity and those involved in the contravention remain exposed to compensation proceedings (s 1317DAF(6)). The publication of compliance with an

infringement notice may potentially be used as a flag for plaintiff lawyers and shareholders, notwithstanding that the breach is "less serious" and compliance does not mean the disclosing entity is to be regarded as having contravened the provision (s 1317DAF(4)).

View of Market Operator

The inclusion of an obligation to consult with the market operator (section 1317DAD) is a development welcomed by CSA. However, CSA is concerned with ASIC's discretion to disregard the views of the market operator given that the operator is in the best position to assess whether a breach has occurred, having regard to its intimate knowledge of the continuous disclosure provisions and the market participants. Potentially this could give rise to a situation where ASIC determines that an entity is in breach of its continuous disclosure obligations even if the market operator believes the entity is not in breach (highlighting the subjective decision-making involved). It is recommended that in this situation, if the two regulators cannot agree, it would be preferable for ASIC not to proceed with an infringement notice, and this should be covered in the guide.

Benefit of Hindsight and Subjectivity

In assessing whether an entity has breached its continuous disclosure obligations CSA believes ASIC should take into account the knowledge the entity had at the time of the alleged breach rather than knowledge available at the time of the investigation. ASIC should recognise that an entity may not be aware of the likely impact of a decision on the price of its securities. Accordingly, it would seem unfair to hold an entity accountable for a decision on the basis of failure to forsee subsequent movements in the price of the securities.

In relation to considering whether a breach warrants action, CSA recommends that the guide include as a factor that should be taken into account, the degree of subjectivity in the decision-making. One of the key concerns identified in the Joint Parliamentary Committee report was the degree of subjectivity required to establish the facts (para 6.31, 6.46, 6.76- 6.84). In cases where it is not clear at the time of the alleged breach that the matter requires disclosure (eg in relation to materiality or the application of a carveout), it is not appropriate to impose a penalty.

Liability of officers and others involved in an alleged contravention

As stated in the Explanatory Memorandum (para 5.492) and guide (para 33), compliance with an infringement notice does not preclude ASIC from taking action under the civil penalty provisions against people involved in alleged contravention. CSA recommends that ASIC clarify the circumstances when this might occur.

Such individuals are placed in a difficult situation, as they are also likely also to be the same people involved in making a decision in relation to the infringement notice. While the interests of the entity should be put first, the exposure of those involved to subsequent action by ASIC may be a deterrent to complying with the notice.

CSA recommends that those involved in a contravention should have the same protection, from future action, as the entity if the entity complies with an infringement notice. CSA acknowledges that legislative amendment is a matter for Treasury, and this submission is copied to Treasury. The Explanatory Memorandum explains the lack of protection for a person involved in the contravention on the basis that the infringement notice is issued to the entity and not to its officers, but this ignores that a corporation can only act through its officers, and that this approach is unlikely to contribute to the efficacy of the regime.

Expert witnesses

The ASIC guide says that the ASIC delegate *may* ask for any independent expert witness (who has prepared a written report for ASIC) to be present to assist at the hearing (para 22). CSA recommends that the ASIC guide state that the witness will be asked to attend if this is requested by the entity. The entity should have an opportunity to raise issues and discuss the views expressed with the expert.

While an entity has a right to legal representation at the hearing, the attendance of other people is at the discretion of the delegate (para 18). CSA recommends that the ASIC guide state that the discretion will be exercised to allow the attendance of any expert witness. This is particularly important if there is an ASIC expert witness, in order to enable the entity's expert to raise issues in relation to the views presented by the ASIC expert.

Joint Parliamentary Committee recommendations –Post Implementation Review (paras 6.134 – 6.135)

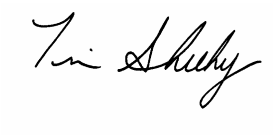
CSA acknowledges that the recommendations relating to post-implementation review are a matter for legislative amendment rather than ASIC, and this letter is copied to Treasury. CSA supports the following recommendations of the Joint Parliamentary Committee.

- The Corporations and Market Advisory Committee should review the effectiveness of the infringement notice provisions in enforcing continuous disclosure two years after they have come into force.

- A three-year sunset clause relating to the infringement notice provisions.

Should you wish to clarify or discuss any of the above please let us know.

Yours sincerely,



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