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## **Tougher breach reporting rules on the way: key items property funds must know**

*Tighter breach reporting rules, accompanied by increased penalties, will include several contentious requirements for property funds.*

ASIC is eager to shake off its “toothless tiger” tag and show it has genuine bite via new breach reporting rules, which intend to introduce new penalties and a more enforceable regime. The changes have been accepted in principle by government, will increase compliance for AFSL holders and could hold a few surprises for unlisted property funds.

The regulator knows breach reporting is one area it can have major impact, and also make an example of license holders who transgress. Most focus has been on the large institutions but all license holders need to analyse their breach reporting and ensure they have the processes to investigate, report breaches, and process any remediation quickly.

Timely reporting is a key focus. The [regulator has emphasised](#) the “serious, unacceptable delays in the time taken to identify, report and correct significant breaches of the law among Australia's most important financial institutions”.

The breach reporting reforms include extending the definition of a “serious breach” to catch a wider set of behaviours. There will be higher penalties for failures to report when required. Maximum recommended penalties include longer jail terms, doubling the maximum imprisonment terms from one year to two years’ imprisonment.

There will also be a new civil penalty in addition to the current criminal penalties – having the civil path available could allow ASIC to pursue a higher number of penalties than previously.

### **Why is the regulator focussed on breach reporting?**

Significant breaches have caused an estimated \$500 million financial loss to consumers, according to ASIC.

The regulator recently examined breach reporting processes among 12 financial services groups, including the big four banks. Excessive time-lag emerged as a persistent problem, with the institutions found to be taking too long from starting an investigation to lodging a breach report: the major banks were averaging more than 4.5 years to identify serious breaches.

Delays in remediation were another issue: it was taking an average of 226 days from the end of an institution’s investigation into the breach before the first payment was made to consumers.

ASIC also found lengthy delays in the time taken from starting an investigation to reporting the breach – major banks were taking an average 150 days from investigation to report. ASIC acknowledges taking a long time to identify breaches is not itself a breach of the reporting requirement, yet has identified these delays as most detrimental to consumers.

The law requires breaches and likely breaches to be reported to the regulator within 10 business days of becoming aware of the breach or likely breach. Yet one in seven significant breaches (110 of 715) were reported later than the 10 business days.

These findings led ASIC Chair, James Shipton, to announce: “Many of the delays in breach reporting and compensating consumers were due to the financial institutions’ inadequate systems, procedures and governance processes, as well as a lack of a consumer orientated culture of escalation.

“Our review found that, on average, it takes over 5 years from the occurrence of the incident before customers and consumers are remediated, which is a sad indictment on the financial services industry. This must not stand.”

Aside from law reform, ASIC will commence a Close and Continuous Monitoring program, which involves placing ASIC staff on site in major financial institutions to closely monitor their breach management, governance and compliance with laws.

### **Law reform on the way**

Changes to the law intend to make breach reporting rules more easily enforceable than previously. These have been accepted in-principle by the government.

ASIC believes previous “ambiguity and subjectivity” in how breaches were identified led to inconsistent decisions, and undermined its ability to take enforcement action against noncompliance.

The law reforms aim to remove these ambiguities by making them stronger, clearer and more enforceable.

The proposed law reforms suggests breaches must be reported if “a reasonable person” would regard them as a significant enough trigger to report. The message is clear – tell ASIC as soon as something happens and then keep them informed.

There is much for property funds to understand, but here are some potentially contentious requirements:

**Extending obligations to report:** This involves licensees reporting matters relating to employees’ and representatives’ conduct. These extended obligations will be particularly onerous regarding costs and resources for licensees. This change extends the breach reporting regime to a whistleblowing-like function, and many property funds will find it challenging to satisfy this requirement without substantial change to their systems, processes and governance.

**Obligation to report 10 days after becoming aware or having suspicion a breach has occurred:** The 10 days’ timeframe is short and burdensome, meaning licensees may be obliged to report compliance concerns before there is any likelihood of a breach occurring. Obligation to report due to suspicion could see huge numbers of breach reports which end up being insignificant or false alarms. PFA asked for this obligation to be extended to 20 days in its submission to ASIC.

**Considering extending the reporting threshold to broader circumstances such as where a licensee “has information that reasonably suggests” a breach has occurred (such as the case in the UK):** This

may also see large numbers of insignificant reports lodged; licensees will need to invest in new systems to quickly identify and analyse potential for breaches; even with systems in place guidance will be needed to demonstrate what kind of information may reasonably suggest a breach.

**ASIC to report breach data at the licensee level:** This requirement puts licensees at risk of significant reputational damage.

#### **What can property funds do?**

Reviewing and updating systems to ensure breaches can be identified, reported, communicated and ultimately rectified will be a major challenge for property funds.

While the new laws are yet to be passed, it's not too early for property funds to consider:

Reviewing their ability to locate breaches, and identifying areas for greatest breach potential

Considering their technological capabilities in locating breaches

Implementing appropriate reporting processes

Liaison with the regulator to identify weak points, and cover off responsibilities and requirements

Reviewing compliance processes and teams

ASIC's findings are consistent with the Royal Commission's expected conclusions regarding abuse of the breach reporting requirement by many financial services organisations, and the poor compliance cultures revealed.

ASIC will now expect breach reporting to be timely, even were the licensee has still yet to investigate the detail. ASIC expects to keep be continuously informed.