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Australian Law Reform Commission
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Via email: corporatecrime@alrc.gov.au

Dear Commission

ALRC review into Australia's corporate criminal responsibility regime

Thank you for the opportunity to respond to the Australian Law Reform Commission (**ALRC**) Corporate Criminal Responsibility Discussion Paper 87 (the **Discussion Paper**) released in November 2019. This response is my own views given as an expert in corporate law and regulation¹ and is not provided on behalf of or endorsed by any of the organisations with which I am professionally affiliated.²

I flag at the outset that I have significant concerns about Proposals 5, 8, and 9. In my view, these Proposals should not be recommended to Government.

This is not because I am naïve or unconcerned about illegal, unethical or unsustainable behaviour by business or not-for-profit (NFP) corporations. Nor am I an apologist for wealthy or powerful corporate insiders – whether owners or donors, directors or managers – who enjoy the upside of unlawful or sharp corporate practice but go spectacularly missing when it is exposed. Principled, dynamic and efficient corporate regulation requires constant effort and must respond to changing conditions and expectations. The impact of corporations – both in traditional and new businesses and as contracted providers of social and human services for the state – on the lives of individuals and the sustainability and prosperity of the communities and environments in which they operate is profound. Their impact has been magnified this century by the expectation that corporations will step up to solve long-term social and economic problems that seem increasingly beyond the scope,

¹ <https://www.business.unsw.edu.au/our-people/pamela-hanrahan>.

² I am a Professor of the UNSW Business School Sydney, a Senior Fellow of the Melbourne Law School, a member of the Centre for Law Markets and Regulation at UNSW Sydney, and an associate of the Centre for Corporate Law at the University of Melbourne. I am a solicitor member of the Law Society of New South Wales and a Senior Fellow of FINSIA. I am a member of the executive board of the Business Law Section (BLS) of the Law Council of Australia and a member of the Corporations Committee of the BLS. I am also a member of the National Corporate Governance Committee of the Australian Institute of Company Directors (AICD).

capacity or ambition of governments. Ensuring corporations and their insiders are, and are seen to be, appropriately accountable for their actions is essential to the legitimacy of liberal democracies and the rule of law in capitalist and mixed economic systems.

This Inquiry focuses on the way in which the state should respond when there is failure by a corporation or its insiders to comply with existing substantive laws or to take reasonable steps to achieve compliance with existing substantive laws. It focuses on the imposition of criminal or civil penalties by the state on a corporation or individual, rather than what corporations ought to be required (by those substantive laws) to do or not do. It responds to growing community mistrust that corporations can be made (by law enforcement or otherwise) to behave lawfully, and that government and its agencies are willing and able to make them do so. The Inquiry and its focus are timely. As Commissioner Hayne observed in the Interim Report of the Royal Commission into Misconduct in the Banking and Financial Services Industry, ‘breaches of existing law are not prevented by passing some new law that says, “Do not do that”’.³ We need to find some more effective way of making corporations comply with existing laws and norms.

Any changes to the corporate criminal responsibility regime are therefore best understood as being directed at making the substantive federal laws that govern the conduct of corporations more effective (in the sense of being more likely to be complied with). The changes proposed should also engender or enhance warranted community trust and confidence in federal regulation. The ALRC’s task is to examine the use of the Commonwealth criminal law to deter and punish corporate misconduct and the cultures and behaviours within corporations that are thought to contribute to that misconduct, to promote these twin goals. The extent to which corporate non-compliance with law is attributable to other causes – including badly designed substantive laws, inadequate supervision or enforcement by relevant federal agencies, and a lack of adequate scrutiny and oversight of lawmakers and regulators – is largely left for another day.

The Discussion Paper includes proposals that, if adopted, are far-reaching and would have the effect of increasing the exposure of individuals and corporations to state sanctions across a range of domains. I believe that any change to the law that increases exposure to state sanctions should be closely scrutinised; ultimately it is for the state to make the case for legislating in this way, not for those potentially affected to resist it. Where proposals further encroach on what the terms of reference for the ALRC’s Freedoms Inquiry referred to as ‘traditional rights, freedoms and privileges’,⁴ including by reversing the legal burden of proof in favour of the state, these encroachments should occur only if and to the extent that they are necessary and proportionate.⁵

In conducting the Inquiry, the ALRC must ‘aim at ensuring that the laws, proposals and recommendations it reviews, considers or makes: (a) do not trespass unduly on personal rights and liberties or make the rights and liberties of citizens unduly dependent on administrative, rather than judicial, decisions; and (b) are, as far as practicable, consistent with Australia’s international obligations that are relevant to the matter’. In formulating recommendations, it must ‘have regard

³ *Royal Commission into Misconduct in the Banking and Financial Services Industry* (Interim Report, October 2018), 290.

⁴ ALRC, *Traditional Rights and Freedoms— Encroachments by Commonwealth Laws* (Report 129, December 2015).

⁵ *Ibid*, [1.15]. ‘Proportionality is used to test limits on constitutional rights by the High Court and by constitutional courts and law makers around the world. This involves considering whether a given law that limits rights has a legitimate objective and is suitable and necessary to meet that objective, and whether—on balance—the public interest pursued by the law outweighs the harm done to the individual right. The use of proportionality tests suggests that important rights and freedoms should only be interfered with reluctantly—when truly necessary.’

to the effect that the recommendations may have on: (a) the costs of getting access to, and dispensing, justice; and (b) persons and businesses who would be affected by the recommendations (including the economic effect, for example).⁶

The decision to initiate the Inquiry, the formulation of the terms of reference for the Inquiry and the limited time allowed for the Inquiry's work were driven by political considerations outside the ALRC's control. This is acknowledged. But the Discussion Paper is limited in its analysis. It does not always provide theoretical or normative foundation for key proposals, nor does it engage with the literature in relevant fields such as criminology, regulatory theory, economics, or management or behavioural science. It provides no compelling rationale for some of the proposals and no empirical or doctrinal basis for concluding that the changes proposed would, if adopted, help to improve corporate conduct or restore trust in regulation. Nor does it address the key question of whether more or more draconian law, rather than more strategic and effective public enforcement of existing law, is required.

Again, to be clear, I do not raise these concerns because I want to protect the powerful or the status quo by delaying or diverting necessary reform. Commissioner Hayne pointed out that reform is difficult and often opposed for the wrong reasons. He said that, 'Those who oppose change will appeal to real or supposed difficulty in altering present arrangements. Reference will be made to change bringing "unintended consequences". That argument is easily made because it has no content; the "consequences" feared are not identified.'⁷ I agree that knee-jerk conservatism and naked self-interest, including of industry incumbents in maintaining special protections or regulatory barriers to entry, must be resisted. But so must political opportunism.

Key proposals in the Discussion Paper have broader implications (that is, beyond the immediately context) touching on the nature of the relationship between individuals and the state, and between the state and the private and third sectors. These implications should be explicitly identified and acknowledged, and the case for the change clearly made. This includes demonstrating how and why the changes are both necessary and likely to improve corporate conduct and restore warranted trust in the regulatory system. Bad law that works is bad enough; bad law that does not work is even worse.

The following comments relate specifically to Chapters 4, 6 and 7 of the Discussion Paper.

Chapter 4 – Regulation of Corporations

Chapter 4 includes Proposal 1 for reorganising federal regulation into three categories – criminal offences, civil penalty proceeding provisions, and civil penalty notice provisions. There may be some merit in this approach, particularly if it gets rid of dual-track regulation (see [4.19] – [4.21]) and infringement notices (see [4.22] and [4.23]). But I note that regulatory agencies will probably fight to keep both, so this may be challenging to achieve.

There are two likely difficulties with Proposal 1, which are identified in the Discussion Paper but not really resolved. The first concerns the decision about when to make contravening conduct a criminal offence, and follows from the approach suggested in [4.29] to 'leave it open to the framer of the legislation to consider what features of the conduct or its consequences may make a contravention deserving of denunciation such that a deterrent effect of a civil penalty is insufficient, and that the additional deterrence and condemnation provided by the criminal law is required'. It is precisely

⁶ *Australian Law Reform Commission Act 1996* (Cth), s 24.

⁷ *Royal Commission into Misconduct in the Banking and Financial Services Industry* (Final Report, February 2019) 4.

because that decision has been left to the framers in the past that we have the current incoherence in the regulatory stock. There is existing principled guidance, provided by the Attorney-General's Department, but as the Discussion Paper points out it is routinely ignored by legislators. The second difficulty is related and is the subject of Proposal 7. Again, experience (including with the use of Regulatory Impact Statements⁸) suggests that Proposal 7 is unlikely to result in greater legislative discipline in the absence of some form of independent discipline or oversight or formal program of regulatory stewardship.

I also note that the approach put forward in Chapter 4 might shift the balance in regulation of corporate (as distinct from individual) conduct even more towards the use of civil penalty provisions. Unlike many people, I do not consider the expansion of civil penalties in federal regulation an unalloyed good. They involve the use of the powers and resources of the state to prosecute business or NFP corporations (of all sizes) without those defendants having the benefit of the full rights, privileges and protections provided by the criminal law.⁹ Very significant penalties – sometimes penalties larger than the fines that can be imposed for similar conduct that is criminal – can result. As the ALRC's Freedoms Inquiry observed, 'A person may be denied their criminal process rights where a regulatory provision is framed as a civil penalty, when it should—given the nature and severity of the penalty—instead have been framed as a criminal offence'.¹⁰ A hard question, not asked in the Discussion Paper, is about the trade-offs involved in an approach that allows the state to seek very large (potentially over \$500 million in some situations) pecuniary penalties in civil court. This includes the risk to defendants of drawn-out and overlapping regulatory proceedings.¹¹ The trade-offs, particularly in dealing with corporate rather than individual defendants,¹² may be acceptable but they should at least be recognised.

Chapter 4 also includes Proposal 5 that would criminalise a 'repeated or flagrant' contravention of a civil prohibition. As flagged, I do not support this proposal. The example given in [4.48] is about increasing the fine for subsequent offending, not about making a civil contravention into a criminal one. As for 'flouting or flagrant disregard', perhaps this introduces a novel fault element the effect of which is to create a different prohibition that falls into the first category in Proposal 1. It is difficult to tell, and the example given in [4.50] is not apposite.

Chapter 6 – Attribution

I have agreed elsewhere with the proposition in [6.1] and Proposal 8 that there is a need for and benefit in rationalising the attribution rules across the general body of federal regulation.¹³ But I have reservations about the single method in Proposal 8.

The Discussion Paper represents a missed opportunity to consider why the attribution rules in Part 2.5 of the Commonwealth *Criminal Code* (discussed in [5.33] – [5.77]) have not been adopted in legislation controlling corporate conduct (see [3.41]) or tested by regulators or prosecutors. Despite their limited use, the attribution rules in the *Criminal Code* have positively influenced corporate

⁸ Pamela Hanrahan, 'Improving the Process of Change in Australian Financial Sector Regulation' (2008) *Economic Papers* 6-23.

⁹ This issue is discussed in *ASIC Enforcement Review Taskforce* (Final Report, December 2017) 77-9.

¹⁰ ALRC (n 4) [8.171].

¹¹ *Australian Securities and Investments Commission v Helou* [2019] FCA 1634.

¹² This is discussed in P Hanrahan, 'Deterring White-Collar Crime: Lessons from Australia's Insider Trading Penalties Regime' (2017) 11(2-3) *Law and Financial Markets Review* 61-74.

¹³ Pamela Hanrahan, 'Fundamental Attribution Error?' 36(1) *Company Director* 24-5 (February 2020).

governance by creating an awareness in corporations of the need for a ‘culture of compliance’.¹⁴ This is a wider concept than due diligence.

If the existing Part 2.5 is to be abandoned, then a cleaned-up version of the TPA Model (discussed in [5.78] to [5.84]) would appear to be a better option than a new provision that reverses the burden of proof in favour of the state. A cleaned-up version would remove the variations identified in [5.82] and adopt the statutory attribution provisions as a code to the exclusion of the general law (see [5.80]). This would be less disruptive, but this solution is rejected at [6.11].

While generalising is difficult, in many situations the single method in Proposal 8 would expand the circumstances in which a corporation can be made criminally liable for conduct engaged in by its ‘associates’. The Discussion Paper says at [6.36] that Proposal 8 ‘both widens the actors from whom the physical elements can be attributed to a corporation and also potentially reduces liability because of the availability of a defence of due diligence’. For the reasons explained in my introductory comments, this requires careful thought, particularly as it is to be applied across the board and departs from internationally accepted practice (which is to impose liability for failure to prevent, rather than to impose liability unless the defendant can prove due diligence).

Chapter 7 – Individual Liability for Corporate Conduct

As drafted, Proposal 9 is flawed and dangerous. If adopted, it would trespass unduly on personal rights and liberties of affected officers, and there is no reason to conclude it would be effective to improve corporate compliance. It should not form part of the ALRC’s final recommendations to Government.

Chapter 7 begins with the proposition that ‘Where corporate officers have clear responsibilities to prevent corporate misconduct, and where the relevant individuals fail to take reasonable measures to do so, they should be personally liable’. But Proposal 9 goes far beyond this. On its face, it imposes liability on any officer ‘who was in a position to influence the conduct of the body corporate in relation to the contravention’. This is a far wider class of potential defendants than persons who had clear duties or responsibilities to, or even the capacity to, prevent corporate misconduct.

The Proposal then requires the individual officer to prove, if they can, that they took ‘took reasonable measures to prevent the contravention’. Proposal 9 thereby reverses the legal burden of proof in favour of the state. In the Freedoms Inquiry, the ALRC said, ‘Offences that reverse the legal burden of proof on an issue essential to culpability arguably provide the greatest interference with the presumption of innocence, and their necessity requires the strongest justification’.¹⁵ This is true also for civil penalties.¹⁶

The stated intention at [1.64] is to ‘enhance corporate compliance by simplifying the individual liability regime, which would promote and reward efforts at genuine compliance’. The Proposal is also said to ‘assist regulators in the detection and prosecution of individuals who abuse the corporate vehicle’. However, any attempt to justify such a fundamental attack on any citizen’s rights on the basis that it simplifies the law or makes it easier for regulators to produce heads on sticks is wholly inadequate. A person who, among many others, is in a position to influence the

¹⁴ *ASIC; Re Chemeq Ltd v Chemeq Ltd* (2006) 234 ALR 511; [2006] FCA 936 (French J). Professor Bob Baxt AO wrote extensively on this issue: see Pamela Hanrahan, ‘On Compliance’ in P Hanrahan and A Black (eds) *Contemporary Issues in Corporate and Competition Law: Essays in Honour of Professor Robert Baxt AO* (LexisNexis Butterworths, 2018).

¹⁵ ALRC (n 4) [9.64].

¹⁶ *Ibid* [9.111].

behaviour of a corporation but cannot prove they took reasonable measures to prevent the contravention is hardly abusing the corporate vehicle.

Nothing in the criminology or regulatory theory literature supports the assertion that Proposal 9 would promote and reward efforts at genuine compliance. Unlike the BEAR, discussed below and in the ALRC's supplementary note,¹⁷ it does not require the corporation itself to map functional responsibilities, clarify reporting and decision lines, and make hard decisions about how best to allocate its resources to achieve lawful, ethical and sustainable corporate behaviour. Unlike an officer affected by the BEAR, a person covered by Proposal 9 may have had no explicit discussion with their employer about the scope of responsibilities or how far their authority extends. Instead, the Discussion Paper proposes a form of 'functional managerial liability, in which any senior officer who was in a position to influence misconduct in practice may be civilly liable unless they can prove that they took reasonable measures to prevent the misconduct'.

What is required instead is a principled discussion of whether, and if so why, the existing accountability mechanisms are inadequate. The fact that regulators have failed to enforce the existing law is not a reason to expand it. There are a range of ways in which corporate officers can be held to account in connection with offences committed by their corporations.¹⁸ These include accessory liability, and liability for breach of the statutory duty of care.

Under general principles of criminal law, any person who aids, abets, counsels or procures the commission of an offence by another person – including a corporation – is taken to have committed that offence and is punishable accordingly. The existing statutory duty of care is a civil penalty provision that applies to all corporate officers (as defined). Breach of the duty of care can attract a substantial civil penalty even if the failure to take care did not cause a loss to the corporation itself. Australian courts have consistently interpreted the duty as requiring officers to take reasonable care to avoid exposing their corporation to a foreseeable risk of harm, such as the harm that would result from a criminal conviction. Their duty to protect the corporation's interests is not limited to its financial interests; as Edelman J pointed out in *ASIC v Cassimatis (No 8)* [2016] FCA 1023 they include 'its interests which relate to compliance with the law'.

Senior executives of authorised deposit-taking institutions, including banks, have a further layer of accountability through the BEAR. If they are identified by the bank as an 'accountable person', they are required to take 'reasonable steps' in conducting their identified responsibilities 'to prevent matters from arising that would adversely affect the prudential standing or prudential reputation' of the bank. Failure to do so can result in them being disqualified by the regulator, but does not result in individual civil penalty liability. The expanded accountability of officers in prudentially regulated institutions was justified on the basis of the systemic risks that misconduct in those institutions may cause.

There may be a case for expanding the class of persons to whom a statutory duty to take reasonable care to prevent corporate offending is applied. It may also be time to revisit the debate about whether accessory or involvement liability might be extended to a person who 'actively participates

¹⁷ ALRC, *The Banking Executive Accountability Regime: an alternative model of individual liability for corporate fault* (19 December 2019).

¹⁸ These are explored in detail in Tim Bednall and Pamela Hanrahan, 'Officers' liability for mandatory corporate disclosure: Two paths, two destinations?' (2013) 31 *Company & Securities Law Journal* 474 and Justice Ashley Black, 'Directors' statutory and general law accessory liability for corporate wrongdoing' (2013) 31 *Company & Securities Law Journal* 511.

in the contravention if they do something to bring it about or if they fail to do something that they ought to have done to prevent it'.¹⁹

Yours faithfully

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¹⁹ Ibid.