Allens › ‹ Linklaters

Allens: Submission to Australian Law Reform Commission review of corporate criminal responsibility

31 January 2020

1 Introduction

We welcome the Australian Law Reform Commission (***ALRC***) review of corporate criminal responsibility and the thoughtful and detailed *Discussion Paper, Corporate Criminal Responsibility (DP 87)* (***Discussion Paper***) it has published. We welcome the opportunity to make this submission on its proposals.

Allens' disputes and investigations practice and anti-bribery & corruption practices are recognised as 'Band 1.'[1] We have a long history of representing many of Australia's largest companies in regulatory investigations, civil penalty proceedings and criminal prosecutions. We also have extensive international experience of corporate criminal regimes in other jurisdictions, most notably in the United States and the United Kingdom.

The Discussion Paper makes a number of proposals, the majority of which, if adopted, would help achieve a simpler, more balanced and more effective Australian corporate criminal responsibility regime.

Our submission focusses on a few areas raised in the Discussion Paper where we think there are important issues the ALRC should consider before finalising its proposals in its final report. Those areas are:

- the methods for attributing conduct and states of mind to a company (Chapters 5 and 6 of the Discussion Paper);
- individual liability for corporate misconduct (Chapter 7 of the Discussion Paper);
- whistleblower protections (Chapter 8 of the Discussion Paper);
- deferred prosecution agreements (Chapter 9 of the Discussion Paper); and
- sentencing (Chapter 10 of the Discussion Paper).

We preface those more detailed comments with some general observations about:

- the scope of the review;
- the proposal to recalibrate all civil penalty provisions and offence provisions to align with the regulatory pyramid (Chapter 4 of the Discussion Paper); and
- Proposal 5 concerning a new criminal offence for repeated or flagrant breaches of civil penalty provisions.

2 Prefatory comments

2.1 The scope of the review

We acknowledge the ALRC considers the process by which criminal offences are investigated and prosecuted to be outside the scope of its Review, and consider it unfortunate that the Terms of Reference for the Review did not extend to a review of these matters.

Commissioner Hayne made clear in both the interim and final reports of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industries (***Royal Commission***) that:

> …almost all of the conduct identified and criticised in that Report contravened existing norms of conduct and that the most serious conduct broke existing laws. Notwithstanding that, the law was too often not enforced at all, or not enforced effectively.[2]

[1] Chambers Asia Pacific 2020 law firm rankings.
[2] Royal Commission Final Report p 413.

The premise for many of the proposals in the Discussion Paper is that change is necessary because there has been a lack of enforcement or perceived difficulties or challenges to enforcement.[3] However, without a parallel review of the investigation and enforcement process, it is impossible to determine whether this failure is because of a deficiency or difficulty in the laws or whether the issues arise from the approach to investigation and enforcement.

We have recently seen a paradigm shift in ASIC's and APRA's approaches to investigation and enforcement. There is every reason to believe that similar shifts in approach to investigation and enforcement within the corporate criminal sphere would address many of the perceived challenges and difficulties with current laws.

We endorse the ALRC's comment at 1.40 of the Discussion Paper that an inquiry into criminal investigative processes would be appropriate, including any lessons that can be gleaned from other jurisdictions, including the United States and the United Kingdom. We think such an inquiry should be a formal recommendation of the ALRC's review on the basis that the rationale for changes to the laws for corporate criminal responsibility cannot be properly tested, and may be ineffective, without an inquiry of this kind.

In **Schedule 1** we set out some issues we think should be considered in such an inquiry.

2.2 Recalibrating criminal liability

We support the proposal to review and recalibrate Commonwealth penalties into a three-tier regime comprising criminal penalties, civil penalty proceeding provisions and civil penalty notice provisions.

We agree that the current proliferation of criminal offences for conduct that is 'not criminal in any real sense'[4] is contrary to principled regulation and creates incoherence in the law.[5]

We would add that criminal prosecution can have disproportionate collateral consequences for companies. Not only does a criminal prosecution carry with it the denunciation identified in the Discussion Paper, but it can also have more practical consequences:

- Criminal prosecutions (and convictions) can place at risk statutory licences to operate. For example, a conviction for a minor record-keeping obligation by a financial services company in Australia may prejudice a company's ability to obtain and retain licences to provide any financial services in foreign jurisdictions, with flow-on effects for the market and innocent stakeholders.
- Criminal prosecutions (and convictions) frequently need to be disclosed in any corporate due diligence. Counterparties, particularly in foreign jurisdictions, will tend to interpret a prosecution as indicative of serious misconduct (even if that characterisation is unwarranted), which can have significant and disproportionate commercial implications.
- Convictions can lead to compulsory or discretionary debarment from tendering for government contracts in certain jurisdictions.
- Relatedly, a finding of criminal conduct can effectively deprive a company of the opportunity to successfully rehabilitate, even if the conviction is overturned (a seminal example being Arthur Andersen).

2.3 Repeat or flagrant offending

Proposal 5 envisages that repeated or flagrant breaches of civil penalty provisions should be criminal offences. We have concerns that the scope and application of this proposal is

[3] See eg 1.32, 3.56, 6.63, 12.12
[4] *Sherras v De Rutzen* [1895] 1 QB 918, 922.
[5] Discussion Paper Chapter 4.

insufficiently certain as a basis for criminal liability and that it is not necessary to ensure a proportionate response to repeated or flagrant breaches.

- Ordinary principles for determining penalties consider recidivism and the seriousness of breaches.
- The amount of maximum penalties, particularly where there are numerous breaches and particularly since the enactment of the *Treasury Laws Amendment (Strengthening Corporate and Financial Sector Penalties) Act 2019* (Cth) (***Penalties Act***), is more than capable of providing effective deterrence and punishment in the appropriate circumstances.
- The Penalties Act introduced a tiered system for specified offences where there is a distinction between strict liability and 'fault-based' breaches of obligations. It would be preferable to build on this approach to provide appropriate denunciation of intentional or reckless breaches rather than introducing a different framework for much the same purpose. Having different mechanisms to achieve the same purpose does not assist with simplicity or clarity.
- There is tension between Proposals 1-4, which seek to establish a principled distinction between civil and criminal regulation and Proposal 5 which breaks down that distinction.
- There is uncertainty about key concepts in Proposal 5 that is undesirable in a provision creating criminal liability. In particular, when would a breach be sufficiently 'flagrant' that it ceases to be civil and becomes criminal? What number or length of time between 'repeated' breaches would attract criminal rather than civil liability?
- The concern over the uncertainty of when 'repeated' breaches might become criminal rather than civil is particularly pointed in the context of 'general' penalty provisions that can encompass entirely unrelated and distinct issues. For example, section 912A(1)(a) of the *Corporations Act 2001* (Cth) (***Corporations Act***) requires financial services licensees to do all things necessary to ensure that financial services covered by the licence are provided efficiently, honestly and fairly. This can encompass entirely different types of conduct in entirely different business units that would not be indicative of recidivism. Similarly, there could be 'repeated' breaches of section 1311 of the Corporations Act, which creates an offence where a person contravenes any provision of the Corporations Act, where in substance there is no element of repetition in the underlying conduct.

3 Attribution

3.1 Summary

The ALRC has proposed that there be a single method for attributing conduct and states of mind to corporations for all Commonwealth offences. The key features of the proposed 'single method' are that:

- the conduct of any 'associate' of a body corporate will be deemed to be conduct of the body corporate;
- there will be a broad definition of 'associate' which will include employees, officers, agents, contractors, subsidiaries and controlled bodies;
- the state of mind of any 'associate' who engaged in the conduct will be the state of mind of the company and a company will also be at fault if it authorised or permitted the offence; and
- there will be a due diligence defence.

3.2 A single attribution method?

We agree with the observations by the ALRC that the multitudinous mechanisms by which criminal responsibility can be attributed to corporations at the Commonwealth level are inconsistent and that, in many cases, there is no apparent rationale for particular mechanisms that have been adopted. In those circumstances, we agree that some consolidation and simplification of mechanisms of attribution is desirable for the sake of consistency and simplicity.

However, there may be unintended collateral consequences from applying a 'single method' of attribution for *all* offences.

Special rules

There are a number of 'special rules'[6] of attribution representing a carefully worked-through policy position that should not be overturned without careful consideration. For example, the twin requirements for continuous disclosure under section 674 of the Corporations Act and the prohibition on insider trading under section 1043A are fundamental to the operation of informed and fair securities markets within Australia. Those provisions are underpinned by a 'special rule' of attribution in section 1042G of the Corporations Act, which deems a company to possess information that is possessed by an officer and which came into his or her possession in the course of performance of their duties as an officer.[7] That 'special rule' also grounds the requirements for continuous disclosure under section 674 of the Corporations Act through ASX Listing Rule 3.1 and the definition of 'aware' in Listing Rule 19.[8]

Changing the attribution method as proposed by the ALRC would radically alter the obligation.

- It would become more onerous in the sense that information possessed by any 'associate' would be information known to the company for the purposes of those provisions. If applied to continuous disclosure (and an alignment between continuous disclosure and insider trading is an important feature of the current regime), that form of attribution would make already onerous laws unworkable.
- It would become less onerous for insider trading because companies would only be liable if the act of trading securities was done by the particular individual or individuals who possessed the information and because there would be a due diligence defence.

Similarly, the rules for attribution in the context of fundraising documents (eg section 710(3) of the Corporations Act) represent an important 'special rule' adapted for a very particular context.

Companies have built sophisticated systems and processes based on the existing attribution regime for these provisions. There would likely be significant compliance costs if there was a change to the current position as to what information a company possesses and there may be implications also for the operation of markets. There are likely to be other 'special rules' of attribution that are also delicately poised and where change will have significant economic consequences. We submit that those special rules should continue to prevail over any general rule for attribution until specific consideration is given to whether the general rule for attribution should replace the specific rule.

Which offences are applicable to corporations?

Secondly, Proposal 8, as framed on page 129 of the Discussion Paper, changes the nature of corporate criminal responsibility from a system in which certain conduct or mental states are *attributed* to the company, to a system where the corporate is *deemed* to have engaged in

[6] *ABC Developmental Learning Centres Pty Ltd v Joanne Wallace* (2006) 161 A Crim R 250, [2006] VSC 171 [8], citing Lord Hoffmann in *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 AC 500, 3 All ER 918507E
[7] There are also particular exceptions, eg s1043I.
[8] The definition of 'aware' in Listing Rule 9 is based on section 1042G of the Corporations Act.

conduct (and to have states of mind) of its 'associates.'[9] On its face, this has the effect that companies would be *deemed* to be liable for offences which could currently only be committed by natural persons. For example, section 184 of the Corporations Act (criminal breach of director duties) can only be committed by a natural person because only natural persons can be directors. However, if the conduct and state of mind of a director is 'deemed' to be the conduct and state of mind of the company of which they are a director, then the company would be 'deemed' also to have committed the offence.

Some possible resolutions of these issues include:

- Proposals 1-7 contemplate a review of Commonwealth offences to recalibrate criminal and civil liability. That review could also determine:
  - whether the offence should be applicable to a corporation; and
  - if so, whether the proposed 'single method' for attributing criminal (and civil) liability should apply to it.
- In relation to the second issue, the proposed redraft of Part 2.5 could replace the 'deeming' language with the words 'may be attributed'.

3.3 Perceived issues with Part 2.5 of the Code

Part 2.5 of the Code was intended to fill the function of a single 'general' rule of attribution for Commonwealth offences (although, as noted by the ALRC, it has not had the breadth of application that would be expected). We welcome the prospect of this forming the basis for the proposed 'single method' of attribution (subject to the comments above).

However, we question whether it is otherwise necessary or desirable to change Part 2.5. In our view, the perceived challenges with enforcement under Part 2.5 are an illustration of the issue identified in section 2.1 above: a reticence on behalf of enforcement agencies to utilise the available tools, rather than a deficiency in the tools themselves. In particular, the three-limbed approach to establishing corporate fault in section 12.3 of the Code provides prosecutors with ample means by which to establish corporate liability, including by reference to:

- the role of the Board;
- the involvement of a 'high managerial agent'; or
- the existence of a deficient corporate culture in the company or a failure to create and maintain a corporate culture that required compliance (we comment further on the corporate culture limb in section 3.9 below).

In the balance of section 3 of this submission we outline comments in relation to the proposed amendments to Part 2.5.

3.4 Vicarious liability

We acknowledge that a vicarious liability model for corporate criminal attribution is not a foreign concept and already exists under certain current Commonwealth laws, including under Part 7 of the Corporations Act and the 'TPA'[10]. However, as outlined by the ALRC, the rationale for vicarious liability in many of those laws is not articulated.

The Proposal is informed by the 'failure to prevent bribery' offence under the UK Bribery Act, and is proposed for introduction in Australia in the Crimes Legislation Amendment (Combatting Corporate Crime) (***CLACCC***) Bill 2019. The justification in the explanatory materials for the

[9] There is some inconsistency of language in the Discussion Paper. For example, page 10 uses the phrase 'is attributable', whereas page 129 uses the phrase 'is deemed'.
[10] As outlined in the Discussion Paper,

CLACCC Bill 2019 for introducing a model that makes companies liable for failing to prevent offences by its 'associates' is founded in issues particular to the offence of foreign bribery; in particular, the harm that it causes, requirements under international conventions to which Australia is a party and peculiar challenges to enforcement of an offence that is characterised by the use of third party agents, issues with the availability of evidence and instances of wilful blindness by senior managers.[11]

The proposal is implicitly (but not expressly) contingent on there being a major reduction in the number of criminal offences under Proposals 1-7 so that there is only criminal liability for the most serious conduct.

In our view, the appropriateness and implications of seeking to impose vicarious liability unless they can prove their blamelessness should be assessed once the review contemplated by Proposals 1-7 has occurred. At that stage it may be possible to assess which offences (or categories of offences) the 'single method' should be applied to. For example, it may be most appropriate to initially adopt this approach for offences that already have a vicarious liability method of attribution and then progressively add other categories of offence once the justifications and implications of doing so have been fully considered in relation to the particular offence.

3.5 Scope of 'Associate' – drafting comments

As stated above, Proposal 8 would deem conduct (and state of mind) of any 'associate' to be conduct (and state of mind) of the corporation. The definition of 'associate' and the operation of that definition are therefore of critical importance. The ALRC has deliberately chosen a broad definition of 'associate', including officers, employees, agents or contractors, subsidiaries and controlled bodies. We have two comments on the proposed definition of 'associate' and its operation in Proposal 8. We further comment in section 3.6 below on the implications of this broad definition when combined with the proposed model of vicarious liability.

First, there is tension between, on the one hand, the proposed drafting of the definition of 'associate' and the proposed redraft of section 12.2 of the Commonwealth Criminal Code (***Code***) and, on the other hand, the narrative underpinning those proposed changes:

- The proposed drafting is an inclusive list, such that every officer, employee, agent, contractor, subsidiary or controlled body is an 'associate' such that their conduct is deemed to be conduct of the corporation, even if the conduct is entirely disconnected from the performance of their duties or any corporate benefit. Under the proposed redraft of section 12.2 of the Code, *any* conduct engaged in by an 'associate' is deemed to have been engaged in by the body corporate (that is, regardless of whether the conduct was engaged in for or on behalf of the body corporate).
- By contrast, the language in paragraph 6.20 of the Discussion Paper suggests that the intention is that the focus be on the substance of whether the associate is acting 'for or on behalf of' the company.

We submit that, at the very least, the definition of 'associate', together with section 12.2 of the Code, should limit the conduct attributed to the corporation to conduct engaged in 'for or on behalf of the company'. From a drafting perspective, this limitation should be within any proposed redraft of section 12.2 of the Code. Consistently with the current form of section 12.2, this should attribute to the body corporate 'any conduct engaged in by one or more associates of a body corporate *for or on behalf of the body corporate'* (not just any conduct engaged in by the associate).

[11] Explanatory Memorandum to the CLACCC Bill 2019 paragraphs 5 to 7.

Secondly, the Discussion Paper proposes changing the language of the current Code, which attributes conduct of an employee, agent or officer *acting within the actual or apparent scope of his or her employment* to focus on conduct engaged in *for or on behalf of* the corporate. The rationale and intended scope of this change is not addressed in the Discussion Paper. For example, it is not clear whether the term *for or on behalf of* is intended to align with concepts of agency as is suggested in paragraph 5.98, or the much broader concept of *in the course of the body corporate's affairs or activities*, as may be suggested in paragraph 5.81.

As above, we do not consider it appropriate that a corporation should be criminally liable for the actions of associates acting outside the scope of their actual or apparent authority. Further, the ALRC should consider limiting liability to circumstances where the conduct was intended to benefit the body corporate (or at least be favourable to its interests):

- That would be consistent with the *respondeat superior* doctrine in the United States,[12] which requires both that the conduct be within the scope of authority *and* intended in part for the benefit of the corporation (or is at least favourable to the interests of the company, even if the individual's primary motive was personal gain). The ALRC has identified the vicarious liability approach of the United States as being generally too low a bar for the corporate liability in Australia and we submit that the requirements for vicarious liability in Australia should not be any lower than the US regime in this respect.
- It would also be consistent with the proposed 'failure to prevent bribery' offence in the CLACC Bill 2019 (Cth) which makes corporations liable for conduct of associates 'for the profit or gain' of the corporation.

3.6 Vicarious liability for contractors, subsidiaries and controlled entities

We further submit that it is unnecessary and/or inappropriate to include contractors, subsidiaries and controlled bodies within the definition of 'associate' in circumstances where a company will have 'deemed' criminal liability for the conduct (and state of mind of) its associates:

- It may be unnecessary because the definition already includes 'agents'. The principles of agency are well developed and can include contractors, subsidiaries and controlled bodies where this is warranted on close examination of how the relationship in fact operated.[13] The ALRC states that the words 'for or on behalf of' in Proposal 8 are intended to focus on the substance of the relationship rather than formal titles.[14] If, as may be suggested by paragraph 5.98 of the Discussion Paper, this is intended to align with concepts of agency, then the inclusion of contractors, subsidiaries and controlled bodies (to the extent that they act 'for or on behalf of' a company) is unnecessary.
- It is inappropriate to extend vicarious liability beyond the circumstances in which the substantive relationship between the parties would give rise to a relationship of agency. Outside of those circumstances, the company does not have sufficient control over the ways in which the contractor, subsidiary or controlled body conducts itself such that it should be vicariously liable. For example, a non-operating joint venture participant may have a level of ownership of shares in a joint venture company to make that company a subsidiary, but may not have a degree of operational control such that it should have vicarious criminal liability for the joint venture company's conduct. The uncertainties as to the scope and operation of a due diligence defence, and the practical implications of

[12] Summarised at 5.16 of the Discussion Paper.
[13] Indicia for agency within corporate groups are usually traced back to six features identified by Lord Atkinson in *Smith, Stone & Knight Ltd v Birmingham* Corporation [1939] 4 All ER 116 at 121.
[14] Discussion Paper paragraph 6.2.

casting the onus on the parent company to prove it exercised due diligence, would not adequately ameliorate this issue, as outlined below.

3.7 Vicarious liability and due diligence as the 'single method'

The Discussion Paper justifies a transition to vicarious liability as the 'single method' for attribution on the basis that there will also be a due diligence defence and that corporate 'blameworthiness' will be established if the company is unable to prove it exercised due diligence to prevent the commission of the offence.

There are policy and practical implications of this reversal of onus, including:

- **Uncertainty** – reasonable minds may differ significantly as to what 'due diligence' requires. This is exacerbated in circumstances where:
  - it will be a jury (rather than a judge) determining whether the company exercised due diligence. Not only are there greater difficulties in predicting what a jury might determine, there will also not be any reasons given by a jury to guide the development of the law and industry practice; and
  - there is necessarily a temptation to analyse with hindsight such that the fact that conduct occurred will place companies at a significant disadvantage in proving they exercised due diligence to prevent it.
- **Meaningful guidance is challenging** – that uncertainty could be mitigated to some degree by detailed guidance, produced in consultation with industry, as to what due diligence requires. However, to meaningfully achieve that objective, the guidance would need to be tailored to each offence that the proposed 'single method' applies to, to particular industries, to different sizes of companies etc. The broad application of the Foreign Corrupt Practices Act (US) and introduction of the 'failure to prevent bribery' offence in the United Kingdom has driven the progressive development of guidance on anti-bribery programs that is gradually providing that level of granularity (and is progressively enhancing the prevention of bribery as it does).[15] However, this has taken a considerable amount of time. Extrapolating that across all categories of offence, industry and company, there may be a lengthy period during which there is no guidance that is sufficiently targeted to provide meaningful certainty.
- **Practical burden** – the combination of vicarious liability and a due diligence defence can create an incentive towards 'red-tapism' and invasive interventions into how counterparties go about performing their duties so that companies can have the documentary evidence to discharge the onus placed on them. This comes at a cost. Smaller companies and individuals may also struggle to deliver the systems, processes and paperwork demanded by larger and more sophisticated organisations (placing them at a competitive disadvantage). The burden and costs related to proving steps were taken to prevent the offence must be weighed against justifications for the offence itself.

3.8 Due diligence defence

We are supportive of the introduction of a due diligence defence for criminal and civil liability for the reasons stated in the Discussion Paper. In effect, a company is not blameworthy (and should not be liable) where a rogue employee or agent has engaged in misconduct despite the company taking reasonable steps to prevent this.

[15] The CLACCC Bill has been the occasion for publication of draft guidance in Australia also.

However, the proposal in the Discussion Paper[16] suggests that the due diligence defence will apply only in relation to the conduct element(s) of any offence. In our view, it should apply so that a company is not liable if it exercised due diligence to prevent the commission of the offence as a whole (rather than just applying to the conduct element(s)).

The parsing of offences into separate physical and fault elements can be complex and there can be significant differences of opinion as to what falls within the conduct, as opposed to the fault elements of an offence. Many conduct elements, on their own, are not things that any company should be seeking to prevent. For example, it would be unfortunate if financial services companies sought to prevent their employees engaging in conduct in relation to financial products or financial services (a physical element of section 1041G of the Corporations Act). The application of the due diligence offence should not be contingent on technical arguments as to whether key concepts are part of the conduct or the fault element of the offence. Rather, it should apply to due diligence to prevent the commission of the offence as a whole.

3.9 Corporate culture and authorisation or permission

The Discussion Paper proposes to remove section 12.3(2) of the Code, which sets out some of the ways a company may be held liable for 'authorising or permitting' an offence, including the 'corporate culture' provisions in sections 12.3(2)(c) and (d). The rationale given for removing these provisions is that they are unnecessary and the concept of 'corporate culture' is said to be uncertain and not to have aided in prosecutions.

We comment on those reasons as they relate to the 'corporate culture' provisions:

- The meaning of 'culture', what it requires of companies and how the culture can give rise to the authorisation or permission of offences is coming of age, as evidenced by Chapter 6 of the Final Report of the Financial Services Royal Commission, APRA's Prudential Inquiry into the CBA, ASIC's Corporate Governance Taskforce and APRA's revised approach to supervision.[17] Understanding and acceptance of the drivers of corporate culture has reached a level of maturity over recent years such that the criticism of culture being 'uncertain' no longer has force. Part 2.5 of the Code defines 'corporate culture' to mean an 'attitude, policy, rule, course of conduct or practice existing within the body corporate generally or in the relevant part of the body corporate…'. That definition, which encompasses not only formal 'polic[ies] or rule[s]' but also an 'attitude', a 'course of conduct' and a 'practice' is broad enough to encompass the matters articulated in the reports set out above.
- The emphasis that regulators including ASIC and APRA have placed on culture in recent years (and the focus that corporate culture is receiving from senior managers and boards) means that a failure to create and maintain a corporate culture that requires compliance is a far more appropriate reference point for corporate blameworthiness than the looser and more general concept of due diligence.
- There is normative power in having an express pathway to criminal liability if a corporate culture requiring compliance is not created and maintained.
- The fact that enforcement agencies have not found 'corporate culture' to have aided them in prosecutions may speak more to the issue raised in 2.1 above as to the enforcement agencies themselves rather than the utility of the laws.

[16] Discussion Paper page 129.
[17] As articulated in APRA *Information Paper: Transforming governance, culture, remuneration and accountability: APRA's approach* (19 November 2019).

On that basis, we submit that section 12.3(2) should be retained. It could further be supplemented by statutory guidance, adopting themes emerging from the resources referred to in the first bullet point above, as to what corporate culture requires and how it can give rise to corporate authorisation or permission of offences.

Given the above, we also submit that the ALRC should consider whether corporate culture is preferable as the reference point for the defence addressed in section 3.8 above. Some considerations in that regard include:

- Proof of 'due diligence' to prevent particular offences would, as outlined above, tend towards the 'red-tapism' of checklists, reviews, certifications etc, whereas 'corporate culture' encompasses more general steps to instil ethical norms of behaviour and reinforce them through top-level commitment, appropriate governance, remuneration frameworks, consequence management etc.
- Taking section 1041G of the Corporations Act (dishonest conduct in relation to financial products or financial services) as an example, a 'due diligence' defence would tend to require a company to prove it had in place checks to prevent all the multifarious and unpredictable ways in which 'associates' might engage in dishonest conduct. By contrast, 'corporate culture' would tend to encompass steps to reinforce the importance of acting with honesty and integrity and the means by which those norms of conduct are reinforced through various frameworks. A company unable to articulate and prove how it created and reinforced desirable norms of behaviour is more aptly characterised as blameworthy than a company that did not foresee and put in place some procedure to prevent a particular form of dishonesty.
- Many institutions, particularly in the financial services sphere, have already undertaken self-assessments against the issues identified APRA's Prudential Inquiry into CBA and have had close engagement with APRA and ASIC about these issues. Accordingly, corporate culture would be starting from a far more certain baseline than a new 'due diligence' defence.

3.10 Aggregation

The Discussion Paper gives some consideration to aggregation.[18] However, it is not clear from Proposal 8 how the ALRC intends for the proposed 'single method' for attribution to deal with aggregation.

The language of the proposed redraft of Part 2.5 may suffer from the vice identified in *Commonwealth Bank of Australia v Kojic* (referred to in paragraph 5.87 of the Discussion Paper). Where the conduct of 'one or more associates' is attributed to the body corporate and the state of mind of each of those associates is separately attributed to the body corporate, that could create a situation where two or more different (and innocent) states of mind are each attributed to the body corporate to create a different (guilty) state of mind. We submit that states of mind should only be aggregated in the circumstances identified in *Kojic*, that is, where there was some duty for information to be passed from one 'associate' to another.

It is also unclear how aggregation is intended to apply in circumstances where the actions of one or more 'associates' constitute the conduct element for an offence, however, only one associate had the relevant (guilty) state of mind. For example:

- an 'associate' may direct another 'associate' to effectuate a payment, in circumstances where the second associate is unaware the payment is intended by the first associate to be a bribe – in those circumstances it may be appropriate for the company to be liable

[18] Discussion Paper paragraphs 5.85 to 5.93.

because the associate with the innocent state of mind was acting under the direction of first associate;

- however, it would be a different situation entirely if the acts of the only 'associate' with a guilty state of mind were inconsequential and had no substantive impact on whether the payment was made.

We recommend the position on aggregation be further considered and clarified.

4 Individual liability for corporate conduct

4.1 Summary

The Discussion Paper proposes a single deemed liability model 'that would replace (and streamline) the various provisions [imposing individual liability for corporate offences] under current law'.[19] Specifically, the ALRC's:

- Proposal 9 is that '[t]he *Corporations Act 2001* (Cth) should be amended to provide that, when a body corporate commits a relevant offence, or engages in conduct the subject of a relevant offence provision, any officer who was in a position to influence the conduct of the body corporate in relation to the contravention is subject to a civil penalty, unless the officer proves that the officer took reasonable measures to prevent the contravention'; and
- Proposal 10 is that '[t]he *Corporations Act 2001* (Cth) should be amended to include an offence of engaging intentionally, knowingly, or recklessly in conduct the subject of a civil penalty provision as set out in Proposal 9'.

While we strongly support the Discussion Paper's proposal that laws imposing individual liability for corporate conduct should be recalibrated to realistically reflect the governance role of directors on the one hand and the managerial role of senior managers on the other hand, we do not support the Discussion Paper's proposed model for senior manager liability in its present form.

4.2 Liability of directors

The Discussion Paper observes that directors are exposed to several provisions imposing individual liability for corporate offences, and that 'directors may not be the most appropriate target where the objective is to ensure corporate compliance at all levels of a corporation, across all lines of business, in the course of day-to-day operations'.[20]

We strongly agree that laws regarding individual responsibility for corporate conduct should realistically reflect that directors 'have a governance role rather than a managerial one'.[21] We consider that existing laws too readily expose non-executive directors who are not involved in the day-to-day management of corporations to legal liability, and that legal liability for day-to-day contraventions of corporations' compliance obligations should be shifted away from non-executive directors.

4.3 Deemed liability of senior managers

The Discussion Paper proposes a single model for individual civil liability for corporate conduct, based on capacity to influence the conduct of a corporation, whereby an officer who was in a position to influence corporate conduct that is the subject of a relevant offence provision is subject to a civil penalty.

[19] Discussion Paper paragraph 7.70.
[20] Discussion Paper paragraph 7.83.
[21] Ibid.

In addition, the Discussion Paper proposes a new offence, whereby an officer who was in a position to influence corporate conduct that is the subject of a relevant offence provision, and intentionally, knowingly or recklessly failed to do so, is subject to a criminal penalty, even though they were not knowingly involved in the contravention.[22]

We make the following observations regarding these proposals, and we do not support them in their present form.

(a) Justification for a deemed liability model

The Discussion Paper proposes a deemed liability model. Deemed liability is a particularly burdensome form of liability, given it imposes liability on an individual based on their role within a corporation, rather than on their involvement in corporate misconduct. Consequently, we consider that deemed liability should not be utilised absent a compelling justification.

The Discussion Paper justifies deemed liability as an appropriate liability mechanism on the basis that 'the current regime setting out individual liability for corporate conduct provides too many opportunities for senior executives to evade personal liability.'[23]. It notes that '[u]nclear obligations and an assortment of (often untested) statutory liability provisions enable corporate executives to create opaque reporting structures and shield themselves from liability'.[24]

We disagree with this rationale for the following reasons.

- The Discussion Paper does not consider the efficacy of direct or accessorial liability mechanisms as alternatives to a deemed liability mechanism.
- The Discussion Paper's premise that the adoption of a deemed liability mechanism is necessary because there are perceived difficulties or challenges to enforcement should be examined carefully to determine whether the issue arises from the approach to enforcement, rather than the current regime setting out individual liability.[25]
- Indeed, as set out in Appendix I to the Discussion Paper (which surveys current provisions imposing individual liability for corporate offences), many statutory provisions imposing individual liability for corporate conduct already utilise deemed liability mechanisms, indicating that the approach to enforcement may be a primary reason for a lack of prosecutions.
- Generally, larger organisations having complex reporting structures is more likely reflective of the size, scale and complexity of those organisations, than of an attempt to shield corporate executives from liability.

We are unable to support the proposal absent a clearer justification for deemed individual criminal and civil liability for corporate conduct.

(b) Availability of a 'reasonable measures' defence

The Discussion Paper recognises the need for individual protections against the unfair operation of deemed liability mechanisms,[26] and acknowledges that its proposed model would lower the burden for establishing civil liability in some instances by removing the fault element and imposing a reverse onus for a contravention.[27]

The Discussion Paper provides that its proposed model protects individuals who have 'behaved appropriately by providing a clear avenue to avoid any personal liability'[28] - a 'reasonable

[22] Discussion Paper paragraph 7.132.
[23] Discussion Paper paragraph 7.33-34.
[24] Discussion Paper paragraph 7.33.
[25] See section 2.1 above.
[26] Discussion Paper 7.27.
[27] Discussion Paper paragraph 7.89.
[28] Discussion Paper 7.85.

measures' defence, pursuant to which an officer who proves they took appropriate reasonable measures to prevent a corporate contravention' is not liable. The Discussion Paper provides little indication as to what steps an officer must take to avail themselves of the 'reasonable measures' defence and considers that it may be preferable for regulatory (rather than statutory) guidance to be provided on the matter.[29]

We make the following observations in relation to the 'reasonable measures' defence.

- Because the concept of 'reasonable measures' is undefined, it is difficult to assess the extent to which the defence protects individuals against the unfair operation of the proposed deemed liability mechanism.
- It also is difficult to assess the compliance implications of the proposal. For example, the proposal and any accompanying regulatory guidance could have the effect of mandating diligence standards and compliance procedures for companies. In general, we consider that large organisations are in the best position to assess their own diligence and compliance needs, and mandated diligence could significantly increase their compliance burdens without commensurate compliance gains.
- Though the ALRC considered whether an approach modelled on the Banking Executive Accountability Regime (***BEAR***),[30] it did not pursue this option because 'the regime is relatively untested' and in light of reservations expressed by consultees.[31] Should Proposal 9 be adopted, we see merit in aligning the concept of 'reasonable measures' with the obligation to 'take reasonable steps' inherent in BEAR (and its proposed extension through a *Financial Accountability Regime*).[32]

We are unable to support the proposal without a clearer understanding of the operation of a reasonable measures defence.

(c) Category of offences to which the model applies

The Discussion Paper does not identify the offences to which the proposed model should apply. While Appendix I identifies 26 potentially relevant offences across 18 Acts, the ALRC has not yet determined which of those provisions should be replaced by the proposed model.[33]

We make the following observations in relation to the offences to which the proposed model should apply.

- The proposal aims 'to harmonise the current law, rather than impose any radical change'.[34] Accordingly, the proposal should not be implemented in a way that exposes officers to individual liability in relation to forms of corporate misconduct to which individual liability presently does not attach.
- The proposal forms part of a package of reforms, which includes a recalibration of corporate regulation and a likely significant reduction in the number of corporate criminal offences[35]. Accordingly, the proposal should not be adopted absent this recalibration and rationalisation of corporate criminal offences.

[29] Discussion Paper 7.88.
[30] *Banking Act 1959* (Cth) Part IIAA. See also Department of Treasury Proposal Paper *Implementing Royal Commission Recommendations 3.9, 4.12, 6.6, 6.7 and 6.8 – Financial Accountability Regime* (22 January 2020).
[31] Discussion Paper paragraph 7.75.
[32] *Banking Act 1959* (Cth) s 37C.
[33] Discussion Paper paragraph 7.126.
[34] Discussion Paper paragraph 7.82.
[35] *See generally* Discussion Paper Chapter 4

- As the Discussion Paper acknowledges, 'there may be important justifications for retaining distinctive formulations in some legislation based on the scope and purpose of that legislation'.[36]

We are unable to support the proposal without a clearer understanding of the offences to which the model would apply.

(d) Category of persons who may be liable

The Discussion Paper provides that the proposed model's application to 'officers in a position to influence the conduct of a corporation' is an attempt provide clarity and certainty as to the category of persons who may be liable, without adopting an unduly restrictive formulation.[37]

We make the following observations in relation to the category of persons who may be liable.

- The qualifying concept of 'influence' is undefined, and while the Discussion Paper asserts it is already 'appropriately suited and understood in this context',[38] we have not identified clear guidance on what constitutes a position of 'influence' in Australian legislation or case law that we have reviewed.
- Accordingly, it is uncertain how the concept of influence might apply to an officer with very broad compliance responsibilities, such as a Chief Executive Officer, Chief Compliance Officer or General Counsel.
- Should Proposal 9 be adopted, we see merit in aligning the concept of a 'reasonable position to influence' with the concept of 'accountable persons' in BEAR.[39]

We also consider that the proposed model's application may have negative practical implications for corporations, including the following.

- The proposal might have a chilling effect on compliance culture and reporting by encouraging senior executives to view their accountabilities narrowly and act less vigilantly than they otherwise would to avoid suggestion that they occupy a position to influence the conduct of a corporation.
- The proposal might result in an increase in premiums for D&O insurance or reduce the availability of D&O insurance, by causing a perception that senior executives are exposed to heightened liability

We are unable to support the proposal without a clearer understanding of the category of persons to whom the model would apply.

5 Whistleblower protections

5.1 Guidance that effective corporate whistleblower protection policy is a relevant consideration as to whether a corporation has exercised due diligence

We acknowledge it is in the best interests of companies and the public that large proprietary and public companies have effective corporate whistleblower protection policies and it would be helpful to recognise companies that have implemented an effective whistleblower policy.

We also agree with the Discussion Paper that any guidance provided should be limited to the entities that are subject to the whistleblower policy requirement under section 1317AI of the Corporations Act (being public companies, large proprietary companies and proprietary

[36] Discussion Paper paragraph 7.126.
[37] Discussion Paper paragraph 7.110.
[38] Discussion Paper paragraph 7.116.
[39] *Banking Act 1959* (Cth) s 37A.

companies that are trustees of a registrable superannuation entity) and not smaller companies or those not currently required by law to have a whistleblower policy.

5.2 Compensation scheme for whistleblowers

We support the right to compensation and other civil remedies where a whistleblower or any other person is the subject of detrimental conduct. The whistleblower protections currently contained in the Corporations Act and *Taxation Administration Act* provide for a right of compensation to whistleblowers and other persons who fall victim of detrimental conduct. Given the whistleblower reforms are relatively recent (commencing from 1 July 2019), we support there being an ability to revaluate the sufficiency of whistleblower compensation once these provisions have operated for a period of time (eg two or three years).

5.3 Extraterritorial application of whistleblower protections

In our view, it is arguable the whistleblower laws already apply extraterritorially in respect to conduct that impacts upon the Australian market or an Australian person. Clarification of the extraterritorial reach of existing whistleblower laws would be a useful undertaking.

6 Deferred Prosecution Agreements

The ALRC's Discussion Paper revisits the concept of Deferred Prosecution Agreements (***DPAs***) by asking:

> *Should a deferred prosecution agreement scheme for corporations be introduced in Australia, as proposed by the Crimes Legislation Amendment (Combatting Corporate Crime) Bill 2017, or with modifications?*

An Australian DPA scheme has been the subject of lengthy discussions since the Attorney-General's Department first consulted the public on this topic in early 2017.[40] That consultation resulted in the Federal Government's introduction of the proposed scheme in the CLACC Bill 2017 (***2017 Bill***). On 2 December 2019, the Australia Government introduced the CLACCC Bill 2019 (***2019 Bill***), which retains the key features of the 2017 Bill (described in our 2017 report), with some notable differences.[41]

We prepared submissions in response to the Australian Government's initial consultation on the introduction of DPAs in the 2017 Bill.[42] We continue to fully support the Australian Government's commitment to expanding the enforcement options for serious misconduct and we consider that DPAs can serve an important role under the ALRC's new proposed framework. We also propose that the offences to which the DPA regime applies should be aligned with the offences to which the ALRC's new model of attribution applies (at a minimum), with other offences to be considered on a case by case basis.

We highlight some of the observations we have made with respect to the 2017 and 2019 Bills that may assist in the ALRC's consideration of a DPA regime:

- **Clear guidance** - Certainty and transparency will be central to the success of any DPA scheme introduced. Clear, detailed and publicly available guidance to which the CDPP will have regard throughout the DPA process will, therefore, be vital. We consider the

[40] Commonwealth of Australia, Attorney-General's Department, *Improving Enforcement Options for Serious Corporate Crime: A Proposed Model for a Deferred Prosecution Agreement Scheme in Australia* (March 2017). See, for example: Commonwealth of Australia, AUSTRAC, *Submission on extending deferred prosecution agreement scheme to AML/CTF offences* (May 2017); BHP Billiton, *Combatting bribery of foreign public officials and enforcement options for serious corporate crime: Submission to the Attorney-General's Department* (10 May 2017); and Law Council of Australia, *A Proposed Model for a Deferred Prosecution Agreement Scheme in Australia* (3 May 2017).

[41] Read our report on the 2017 Bill here.

[42] Allens, *Submission to the Consultation on Improving Enforcement Options for Serious Corporate Crime: A Proposed Model for a Deferred Prosecution Agreement Scheme in Australia* (May 2017).

Draft Guidance on the steps a body corporate can take to prevent an associate from bribing foreign public officials released by the Attorney-General's Department in respect of the 2019 Bill to be a useful starting point in this regard.

- **Availability of DPAs** - We recognise the desire to only have DPAs made available to companies. We note, however, that the absence of availability of DPAs for individuals may impact upon the willingness: (i) of individuals implicated in wrongdoing to come forward (ie disincentivising whistleblowing), and (ii) of companies to self-report the conduct of their directors, officers and/or employees. Accordingly, we support there being an ability under the 2019 Bill to reassess the scope of availability of DPAs two years after the introduction of the scheme.
- **Approval** - We agree that the test applied in the UK — that the terms of the DPA are in the interests of justice and are fair, reasonable and proportionate — is an appropriate test. However, it is our strong preference that this test be applied by a sitting, as opposed to retired, judge.

  It is our view that a retired judge would not have sufficient public confidence, or resources, to preside over this scheme. While we recognise that the constitutional separation between courts and the executive is a potential issue for the introduction of a DPA regime involving judicial oversight, we do not consider this issue to necessarily be insurmountable. First, as the UK Government observed, the judiciary's role in the DPA regime is not to try an offence, nor sentence an organisation, but rather to consider the terms upon which prosecution is proposed to be deferred. Second, the court will not be 'rubber-stamping' penalties; rather it will be deciding whether the terms of the DPA are in the interests of justice and are fair, reasonable and proportionate.

7 Sentencing

7.1 Sentencing factors

We agree with the observations by the ALRC that there is lack of clarity around the purposes and principles of sentencing, and that there would be value in having a statutory statement of relevant sentencing factors.

We generally endorse Proposals 12-14 which would bring greater clarity to the factors that courts are required to consider when sentencing a corporate or imposing civil penalty orders on a corporation.

In relation to Proposal 12, we think the principles of sentencing that were proposed by the ALRC in 2006 can be further developed to expressly refer to the 'course of conduct' principle. This principle has particular significance in the sentencing of corporate offenders, where one error in establishing a system or process can lead to many thousands of contraventions. The application of this principle is an important aspect of both 'proportionality' and 'parsimony' (and is distinct from the application of the 'totality' principle that is already referred to in Proposal 12).

7.2 Non-monetary penalties

Proposals 15 and 16 canvass the potential amendment of the *Crimes Act 1914* (Cth) and the Corporations Act to provide for a range of non-monetary penalty sentencing options for corporations that have committed a Commonwealth offence, including:

- orders disqualifying the corporation from undertaking specified commercial activities; and
- orders dissolving the corporation.

While we do see merit in the introduction of certain non-monetary penalty options, we maintain some concerns about the proposed breadth of non-monetary penalties being proposed.

Penalties such as those listed above are of a very serious nature. Orders to disqualify a corporation from undertaking specified commercial activities could have the potential to irreparably damage the functioning of a corporation, with the many attendant consequences of such an outcome. We would caution against the introduction of such orders, or if they are introduced, would encourage the introduction of clear guidance that only permits such orders to be made in very narrow circumstances.

7.3 Facilitating compensation for victims

The ALRC poses the question whether court powers need to be reformed to better facilitate the compensation of victims of criminal conduct and civil penalty proceeding provision contraventions by corporations.

Such species of order exists under section 239 of the *Australian Consumer Law* (***ACL***). Section 12GM(2)(c) of the *Australian Securities and Investments Commission Act 2001* (Cth) (***ASIC Act***) also permits a court, on the application of a person (or ASIC) who has suffered, or is likely to suffer, loss or damage by contravention of the ASIC Act to compensate 'the person or any of the persons on whose behalf the application was made'.

The ALRC suggests that one option for reform would be to amend section 21B of the *Crimes Act 1914* (Cth) to provide for compensation orders in respect of a 'class of persons', as currently provided for by section 239 of the ACL. Section 21B(1)(d) allows a court to order that a person who has been convicted of a federal offence 'make reparation to any person, by way of money payment or otherwise, in respect of any loss suffered, or any expense incurred, by the person by reason of the offence'.

Another option proposed by the ALRC is the introduction of a general power to make 'redress facilitation orders' as part of the sentencing process.

We generally support the further exploration of whether and how law reform could better provide for compensation for victims of corporate crime, however in our view any proposed reforms require careful consideration, particularly because they would apply to a very broad range of offences and therefore need to be workable in a range of scenarios. Particular attention will need to be paid to the challenges that can arise in relation to identifying the class of persons to whom compensation should be paid, including the overlap with any other civil claims, and establishing causation.

We would also welcome further consideration of the kinds of remedial orders that could be made pursuant to any such reform and relevant factors to consider in the decision-making process, including consideration of the type of statutory guidance that should be introduced in relation to the making of such orders.

Schedule 1: Issues to be considered by proposed review of corporate criminal enforcement

In this Schedule we summarise some of the key issues that we submit should be considered by a review of corporate criminal enforcement as referred to in section 2.1 of this submission:

- the appropriateness of jury trials for complex corporate matters;
- the structure of having distinct investigative and prosecutorial agencies in the context of complex corporate criminal matters and the alternative approach in relevant foreign jurisdictions including the UK and New Zealand, which have adopted a model of having a single investigating and prosecuting agency for complex corporate matters and the USA, in which prosecutors actively work with investigators;
- the principles for appropriate interactions between investigating and prosecutorial agencies and corporations in circumstances where the nature and status of criminal investigations can have serious consequences for corporations, including potentially triggering disclosure obligations to markets, counterparties and regulators and other obligations. This should include the approach to giving notice of an intention to prosecute and allowing representations to be made by the potential subject of the prosecution prior to criminal charges being laid given the significant implications that such a decision (let alone a conviction) can have for a corporation;
- the circumstances and means by which corporate criminal liability can be resolved without a conviction given that not all criminal matters in respect of all companies are best resolved through a prosecution. The experience in other jurisdictions has shown that DPAs and other methods of resolution may be more appropriate where a company has voluntarily disclosed the relevant conduct, undertaken significant remediation of the issues and has actively cooperated with regulators in their investigation; and
- the desirability of introducing formal incentives for companies to self-report potential misconduct and cooperate with investigations, including considering models based on the immunity programs in respect of cartel conduct, the Foreign Corrupt Practices Act Corporate Enforcement Program in Chapter 9.47.120 of the Department of Justice *Justice Manual* and the Australian Federal Police and Commonwealth Director of Public Prosecutions *Best Practice Guidelines for Self-reporting of foreign bribery and related offending by corporations.*