

26 October 2018

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The Treasury
Langton Crescent
PARKES ACT 2600

via email to Regmod@treasury.gov.au

Dear Matthew

Consultation on the draft legislation for Modernising Business Registers and Director Identification Numbers

Thank you for the opportunity to provide a submission responding to draft legislation and accompanying materials proposed by the Australian government to modernise business registers and introduce Director Identification Numbers (**DINs**).

The Australian Institute of Company Directors (**AICD**) has a membership of more than 43,000 including directors and senior leaders from business, government and the not-for-profit sectors. The mission of the AICD is to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society.

The AICD supports the development of a new flexible and technology-neutral modern business registry regime. We note that the aim is a whole-of-government platform to support businesses and companies to be established and regulated. We recognise that DINs are being developed as part of this process and to support the government's aim to deter illegal phoenix activity.

The AICD strongly supports efforts to deter and disrupt illegal phoenixing activity. In addition to the damage caused to immediate creditors, employees and stakeholders impacted by specific instances of phoenixing, this illegal activity damages confidence in the corporate model, to the detriment of the clear majority of responsible businesses and directors. Effective laws, vigorously enforced, and attracting impactful and proportionate sanctions, are essential to combat these destructive illegal activities. Timely gathering and sharing of information between regulators and other government agencies is also critical to addressing illegal phoenixing, where the introduction of DINs can make a positive contribution.

If effectively implemented, the AICD considers that DINs will help enforcement agencies verify and track relationships between directors and the entities with which they are associated. However, it is vital that the new regime addresses concerns about disclosure of personal information in the current system.

While the draft legislation contains the framework for the modernisation of the business registry system, the AICD's comments relate specifically to the DIN framework.

1. Executive summary

The AICD is broadly supportive of the proposed framework for the implementation of DINs. We consider this legislation an important step in improving the accountability of directors to assist with the detection of fraudulent phoenix activity.

We have identified a number of opportunities for improvement, discussed below.

We note that the draft legislation provides a high-level framework, with the vital detail of security and personal information required to be provided, held and disclosed to be moved from the *Corporations Act 2001* and dealt with through disallowable instruments.

The AICD has concerns about this approach, given the importance of ensuring data integrity and addressing the privacy of personal information displayed on current registers. It is vital that there is effective consultation on these arrangements with all impacted parties, such as directors and other officers.

The AICD does not support the proposal for the defendant to carry the evidential burden of proving the defences that exist in relation to the obligation for a director to apply for a DIN within 28 days of being appointed and the obligation not to apply for additional DINs. We consider that the Registrar is in a far better position, with greater powers, to investigate such matters relating to DIN applications.

Further, while we support the ability for a prospective director to apply for a DIN, we question the rationale for the automatic cancellation of the DIN after a 12-month period of not being appointed as a director. At a minimum, a longer period may be more appropriate.

On the broader issue of DIN implementation, not dealt with specifically in the draft legislation, we note the following important considerations:

- Confidentiality and security of information held internally on the Registrar systems is critical to provide directors with confidence in supplying identity information.
- The introduction of DINs and identity verification processes must be accompanied by the removal of certain personal information from the Australian Companies Register (**ACR**) due to concerns related to issues of privacy, cyber-security, and personal safety. These concerns include the real risk of identity theft because of criminals being able to publicly access the register for little cost.
- We consider it important that the DIN information is complete and accurate and includes registered charities as such information is not currently updated on the ACR.

2. Obligations on directors and relevant penalties

The AICD supports the four obligations included in the draft legislation in respect of DINs, being:

- Directors must apply for a DIN within 28 days of being appointed as a director;
- Directors must apply for a DIN within 28 days of being directed to by the Registrar;
- A person must not knowingly apply for multiple DINs; and
- A person must not misrepresent a DIN to a government or registered body.

We also support the applicable penalties, which allow for different tiers of penalty depending upon the severity of the breach. In principle, we support extending the civil penalty regime to the new obligations.

We note that the Explanatory Memorandum states that the fact that a contravention of each obligation is both a civil penalty provision and an offence 'allows the regulator or prosecutor to take a proportional approach to the enforcement of the new regime' and concur.

While the AICD has expressed concern about the expansion of the infringement notice regime in other proposals¹, given the nature of the first two obligations, we consider that it is appropriate for the regulator to have discretion to issue an infringement notice for a breach. We consider this consistent with the Attorney-General's Department *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* which states that:

'An infringement notice scheme may be employed for relatively minor offences, where a high volume of contraventions is expected, and where a penalty must be imposed immediately to be effective.'

To support compliance with the obligations during the early phases of its implementation and noting the significant change in obligations regarding director registration proposed, the AICD strongly recommends that the government and Registrar commit to a comprehensive director and community communication and education program. Given the estimated 2.7 million company directors on the ASIC register, we anticipate that communication efforts will involve an extensive media campaign as well as targeted efforts with relevant member bodies (including the AICD and Governance Institute of Australia, and more broadly industry bodies with wide reach in different sectors of the economy, including small business) and intermediaries. It may be necessary to write repeatedly to directors given, for many individuals, being a director may not be their primary occupation.

In relation to the proposed offences, however, the AICD does not support the defendant carrying an evidential burden in relation to:

- the defences that exist in relation to the obligation for the director to apply for a DIN within 28 days of being appointed (i.e., that the director has not applied for a DIN within the relevant timeframe or that the director was appointed without their knowledge); and
- the defence that exists in relation to the obligation not to apply for additional DINs (i.e., that the Registrar directed the person to make the application).

The Explanatory Memorandum states that the evidential burden is reversed because the 'subject of the defences is peculiarly within the knowledge of the defendant and is significantly more difficult and costly for the prosecution to disprove than for the defence to establish' (in accordance with the *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers*).

The AICD does not agree that this principle applies in relation to these defences.

¹ AICD submission on Reforms to strengthen penalties for corporate and financial sector misconduct dated 23 October 2018
<https://aicd.companydirectors.com.au/advocacy/policy/reforms-to-strengthen-penalties-for-corporate-and-financial-sector-misconduct>

In circumstances where the director makes representations to ASIC that they applied for a DIN within the relevant timeframe, or that the Registrar directed them to make an application for a DIN, it will be a straightforward matter for the regulator to address these matters with the Registrar. This is a more appropriate approach than imposing an evidential burden on the director which he or she would then be required to establish in court.

In circumstances where a person alleges that they were appointed without their knowledge, ASIC is in a far better position than that person (who may have no knowledge whatsoever of the relevant circumstances) to investigate those circumstances through its compulsory information gathering powers under the ASIC Act, including the power to require the production of documents or to require disclosure of information.

We accept that a person may falsely allege that they were appointed without their knowledge, but in the context of criminal proceedings and given the risk of unfair punishment, it is more appropriate that the prosecution be put to proof, rather than an innocent person being obliged to discharge an evidential burden when they may not be in a position to effectively do so – particularly noting that the question of whether the evidential burden has been discharged is a question of law for the trial judge.

The AICD's strong view is that the legislature should not lightly depart from the fundamental tenet of criminal law that the prosecution bears the onus of proving all elements of an alleged offence, particularly where proof is neither difficult nor onerous.

3. Transition period

The AICD is supportive in principle of a transition period of 15 months for existing directors to apply for a DIN, provided the implementation process is supported by a comprehensive and funded education and communication program. It will be critical that companies and directors are supported with simple and easy to use processes and effective education and communication on obligations, linked to annual company review procedures.

4. Who must obtain a DIN

The AICD supports the mandatory application of a DIN to directors and alternate directors. Further, we support the ability of prospective directors to apply for a DIN within a designated period.

However, we are concerned that the proposal for automatic cancellation of prospective DINs for individuals who do not become directors within a 12-month period is too short, risking unnecessary administrative and other costs for individuals and government.

We also suggest that the process for prospective directors should differ from existing directors who step down from boards for a period and may subsequently take up new directorships after a period of time (where, we assume, DINs will remain in place while inactive for relevant individuals).

5. Applicability to registered charities

We note the applicability of the DIN to registered charities that are registered companies. We fully support this approach as it will ensure the record of directorships for each DIN holder is current, complete and able to be in one place.

Currently, the ASIC register has a flag for those registered charities that are incorporated as limited by guarantee companies indicating that the information on display may not be current and that the user should refer to the ACNC website. This position is not sustainable under a new business register approach and could undermine the objectives of the DIN including to allow more effective tracking of directors and their corporate history and improve data integrity and security.

We do not consider the legislative changes made to date will support this approach since the registered charities retain their existing obligation to only notify the ACNC of the details of each responsible entity (which are considered the directors). Further, for administrative simplicity, we would not want to see legislation that required the notification of responsible entity information to more than one regulator.

We understand that Treasury does not intend, at this stage, to incorporate the ACNC register into the Modernising Business Registers roll-out. Given this, we encourage the Government to develop of a technology solution to transfer responsible entity data from the ACNC register to the Registrar to ensure the information with the Registrar is complete and accurate.

6. Structure of the reform

The draft legislation provides a framework for the introduction of the DIN, with the detail behind the DIN incorporated into data standards and a disclosure framework that will be determined by the Registrar once the Registrar is appointed. The data standards and a disclosure framework will be disallowable instruments.

We have concerns about this approach, the Registrar having the ability to determine critical features of the DIN – such as what information is required to obtain a DIN and the type of information about an individual director that is disclosed publicly. The latter issue is of significant concern to the AICD and directors and is discussed further in point 8 below.

As outlined in the *Legislative Instruments Act 2003*, as disallowable instruments, the Minister must be satisfied as to 'appropriate' consultation. The AICD considers that it is critically important that the data standards and the disclosure framework in relation to DINs are subject to comprehensive consultation, with those most impacted, including having due regard to the Privacy Act 1988 and what private information needs to be made publicly available.

7. Identity verification processes

Whilst outside the current draft of the legislation, the AICD supports stronger identity verification processes for directors as part of the DIN application process.

This would provide a valuable (although not comprehensive) safeguard against individuals being registered as directors by third parties without their knowledge or consent, fictitious individuals being registered as directors, as well as fraudulent registrations.

As with any electronic identification system, information confidentiality and security issues will be of paramount importance in implementing the DIN regime. The extent of identity information held internally on the Registrar systems should be strictly limited to that required for regulatory purposes. The security of such identity information is paramount to provide confidence to directors that their information will not be subject to cyber exploitation, a malicious activity to covertly collect information from IT systems.

We recommend that any communication with directors on DINs include robust information on the security (including safeguards and procedures) around identity verification processes and the storage of any data retained by the Registrar. This is crucial given that ASIC estimates that there are currently 2.7 million company directors registered.

8. Privacy considerations

Privacy considerations appear to be outside the scope of the current draft of the legislation, as we understand it is the government's intention that this will be dealt with in both the data standards and the disclosure framework.

To facilitate the structure of the reform in this way, the current requirements for personal details of directors and alternate directors contained in section 205B(3) of the *Corporations Act 2001* requiring name, former name, date and place of birth and address have been removed in the draft legislation. In its place is a reference to the (not yet drafted) data standards

The DIN, a robust form of individual identity verification, will reduce the need for other publicly accessible verification mechanisms (such as the residential address and date of birth which are available on the current register). Our previous submission² highlights that Australia is out of step with comparable jurisdictions (such as the United Kingdom and New Zealand) regarding the extent of publicly accessible information on directors and presents further arguments in support of reform to address these concerns.

In our view, it is critical that these issues are addressed in the overall implementation and regulatory environment for DINs and we look forward to further consultation as a priority.

² AICD submission on Consultation on Modernising Business Registers (including Director Identification Numbers) dated 17 August 2018 <https://aicd.companydirectors.com.au/advocacy/policy/consultation-on-modernising-business-registers>

9. Next steps

The implementation of DINs is a significant undertaking by the Government which needs appropriate resourcing and careful consultation with those impacted.

Given the impact on our membership will be significant, we have been pleased to have participated in consultations to date and welcome the opportunity to provide further input as more detailed plans for user testing are developed.

We hope our comments will be of assistance. If you would like to discuss any aspect of this submission, please contact Ms Kerry Hicks GAICD, Senior Policy Adviser, on (02) 8248 6635 or khicks@aicd.com.au.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Louise Petschler', with a long horizontal flourish extending to the right.

LOUISE PETSCHLER
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