Australian Academy of Law Online Event, 22.1.2021, 5.00 – 6.45pm
Regulatory Enforcement of Directors' Obligations

Reducing the overlap between proceedings for criminal offences and for civil penalties

Robert Bromwich

1. The emphasis in this topic is on the desirable level of reduction, not elimination, of overlapping between criminal and civil penalty proceeding enforcement options to reduce the scope for such arrangements to be legally or practically unnecessary, counterproductive or unfair, and how best to achieve it. Three possible key ways of seeking to achieve this are:

   - reducing the extent to which the same conduct can be the subject of either kind of proceeding, especially for less serious conduct;

   - the regulator improving clarity and transparency as to the bases for choosing between criminal or civil penalty proceedings; and

   - the regulator and/or prosecutor making and communicating the decision as to which type of proceeding (if any) is going to take place at as early a time as is possible.

2. I will focus on the first and third of these remedies – legislation and timely decision-making on which avenue to pursue – but also touching on the second remedy of clarity and transparency as to the likely basis for such decision-making.

Reducing the extent to which the same conduct can be the subject of either kind of proceeding

3. The legislative remedy in aid or reducing the overlap between proceedings for criminal offences and for civil penalties was an important aspect of the Australian Law Reform Commission (**ALRC**) Report 136 of April 2020 on Corporate Criminal Responsibility. The ALRC report was structured to identify and address a number of problems, the first of which was that corporations are not adequately held to account for serious corporate misconduct.[1] One of the identified sources of the accountability problem was a proliferation of criminal offences stemming from an incremental building block approach to corporate regulation, having the effect of creating an ad hoc array of criminal, civil penalty and administrative sanctions.

4. In the *Corporations Act 2001* (Cth) there are many more criminal offences than civil penalty provisions, whereas intuitively the opposite might have been expected given that criminal sanctions ought generally to be the last resort. There are solely criminal offences for relatively minor things.

[1] Chapter 5 of the final report, "*Principled Criminalisation*", especially from p.178.

5. Examples identified in the ALRC report include failure to notify ASIC of a change in registered office hours (s.145(3)), and failure to include an ACN on certain company documents (s.153), which would only ordinarily be expected in the absence of any viable alternative sanction options. By contrast, the serious matter of market manipulation can be dealt with as a civil penalty contravention, but can also be a criminal offence if the criminal fault elements are present.

6. The ARLC concluded that the overall picture for the regulation of corporate wrongdoing is one of considerable and unnecessary complexity. This not only makes compliance harder than it needs to be, but encourages a checklist approach rather than genuine risk identification and management.

7. The ALRC identified little by way of an overarching normative guideline to companies and those who run them, leaving priorities to be worked out in an ad hoc and largely subjective way. Effective enforcement by regulators is inevitably driven by resource allocation, which will only coincide with the biggest problems in corporate conduct by chance rather than design.

8. Often there is no material distinction between the conduct for a criminal offence and the conduct for a civil penalty provision, especially, I might add, for lower level conduct where state of mind – a key conceptual distinction between civil penalty and a criminal offence – has little part to play due to lower level offences being strict liability.

9. As a practical matter, corporations are rarely taken to court for committing any criminal offence, to which again may be added, directors and officers are rarely taken to court for criminal offences either.

10. The ALRC's approach in the context of the existing arrangements was that civil regulation should be the primary mechanism of corporate regulation. That premise led to the identification of three aspects of this problem, of which first two are presently relevant. The third aspect concerns penalty notices and can be passed over today.

11. The first aspect of the problem of insufficient accountability for serious corporate wrongdoing followed from a survey of the number and range of existing criminal offences. This produced the rationale for a legislative cull directed to reducing the nature and scope of criminal offences, including, collaterally, the actual and potential overlap with civil penalty provisions. The aim of this proposal was to confine the scope for overlap to the most serious conduct. The ALRC report accepts that this cannot be done overnight and would have to take place over time.

12. The second and related aspect of the problem of insufficient accountability for serious corporate wrongdoing concerns preventing the problem of an excess of existing lesser criminal offences from continuing to grow or re-emerge in the future – that is, arresting the growth in the existing problem and avoiding or at least reducing the need to cull again in the future.

13. Looking first to the first aspect, effectively advocating for a cull, the point made is that there is no principled limit on the type of corporate misconduct conduct that is treated as criminal. This leads to ALRC recommendation 2[2] that corporations should be subject to a criminal offence only when one or more of the following features are present:

    (a) denunciation and condemnation of the conduct is warranted;

    (b) the stigma of being a "*criminal*" would be appropriate;

    (c) the deterrence from a civil penalty would be insufficient;

    (d) the potential harm that may occur justifies a criminal offence; or

    (e) it is in the public interest.

14. Necessarily, this recommendation would leave conduct that does not meet any of these criteria to the primary sanction of civil penalty proceedings, although that is not exhaustive given parallel or alternative options such as disqualification from holding office as director. The implementation of this recommendation would not eliminate this more confined operation of the criminal law also being covered by civil penalty sanctions, especially when state of mind is difficult to establish. But it would substantially reduce the scope for an overlap outside more serious offences.

15. The ARLC identified the following benefits from such a change from the ALRC inquiry terms of reference and the final ALRC report perspective of corporate criminal responsibility:

    - First, breaches of the criminal law by corporations will more readily be recognised as serious, with "*criminal corporations*" experiencing significant reputational harm.

    - Secondly, corporations will be more likely to direct their attention and efforts to preventing criminal conduct, and less likely to take a tick-a-box approach to regulatory compliance.

16. It is not hard to come up with other benefits.

17. There may also be some disadvantages from the absence of criminal sanctions in some areas, largely due to reduced deterrence if a criminal sanction is not possible. However this may be addressed to some extent by ALRC recommendation 8,[3] which proposes that there should be new criminal laws that address systems of conduct or patterns of behaviour that result in multiple contraventions of civil penalty provisions, giving incentives to improve compliance systems and other collateral benefits.

[2] See again pg. 178 of the ALRC report.
[3] Page 270 of the ALRC report.

18. The same reasoning as to the stated and other benefits necessarily applies to directors, and indeed to officers, especially senior executives. When we speak of the thought processes of corporations we are necessarily referring to the human actors who reflect the mind of a company – its directors and its most senior executives.

19. Looking next to the second aspect of preventing the regrowth of the same problem of too many criminal offences for less serious conduct, and too much overlap between criminal offences and civil penalty provisions, recommendation 4[4] is that if a proposed law includes a new criminal offence provision for corporations, the government should be required to explain publicly why it is appropriate and necessary.

20. The rationale, not unrelated to the first aspect of a cull being needed, is that there are already too many criminal offences directed to companies, many of which prohibit low level conduct, and which are never enforced.

21. The benefits identified by the ALRC are as follows.

- First, that maintaining simpler, clearer laws will reduce this aspect of the regulatory compliance burden that falls on corporations, to which may be added the human burden, at least in terms of the responsibility that falls on directors and senior executives.

- Secondly, this will help to ensure new criminal offence provisions only apply to the most serious corporate misconduct, which enables investigators and prosecutors to apply their efforts and resources more appropriately.

- Thirdly, greater scrutiny of proposed new criminal offence provisions for corporations will help to prevent the spread of criminal law to lower level misconduct – that is, preventing the cull problem from re-emerging.

- And finally, over time there will be fewer offence provisions directed at corporations, reflecting only serious misconduct by corporations. All of this necessarily promotes better and more focused risk management by directors and senior executives, directed to the seriousness of a contravention, including the presence in a normative way of criminal sanctions.

22. As to the final resting place for both the cull and limits on new criminal offences, the ARLC's earlier consultation stage proposal suggested there be both an effective halt, and over time, elimination, of *any* overlap between criminal and civil penalty sanctions. This involved a wholesale repudiation of the notion of a universal or ubiquitous "*dual track*" regulation approach, involving the same conduct being prohibited by identical, or near-identical, civil and criminal prohibition. It is fair to say that this proposal as a global solution was strongly opposed by regulators as reducing regulatory flexibility.

[4] Page 211 of the ARLC report.

23. The revised approach that was contained in the final ARLC report proposed retaining an overlap for more serious conduct, but not for less serious conduct. Given that the dual track approach will almost certainly remain for the most serious conduct, retaining regulator flexibility where it is most needed, the substance of the concerns expressed by the regulators have been accommodated. Thus, the final ALRC proposal does not entail halting or eliminating dual-track regulation, but rather to make the continuation of criminal offences only occur upon a principled basis, of much more limited scope than presently exists. The dual track approach would remain for more serious conduct, with the main distinguishing feature generally being a criminal offence containing a fault element – that is, proof of state of mind. That limitation would only not apply when the risk of harm is great enough to warrant strict or absolute liability. A good example of this are serious environmental offences.

24. My personal view is that the trade-off for regulatory flexibility being retained for more serious conduct is that regulators should providing greater clarity and transparency in relation to the exercise of that flexibility, especially as to which track is likely to be taken and earlier decision-making as to that chosen track. This is the substance of the second and third remedies to which I now turn.

The regulator improving clarity and transparency as to the bases for choosing between criminal or civil penalty proceedings

25. The second remedy in aid or reducing the overlap between proceedings for criminal offences and for civil penalties of improving clarity and transparency cannot really be expanded upon in a session such as this to any great extent. There are already some publically available policies, such as the Prosecution Policy of the Commonwealth, in relation to deciding when to prosecute, with the primary considerations unsurprisingly being sufficiency of evidence and public interest. This remedy is therefore more directed to improvement, and a call for greater clarity and transparency as to the likely bases for decision-making.

26. An observation to be made is that improved public disclosure of this kind is likely to be cast at a relatively high level of generality to accommodate the complexity of the competing considerations that may arise in any given case, and the fact-specific aspects that are likely to be determinative. However a greater degree of clarity and transparency, even on broad criteria, is a desirable in this most important area of discretionary executive decision-making, especially given that it is generally not possible to obtain reasons for a decision that has been made, and practically impossible to have judicial review of such decisions.

The regulator and/or prosecutor making and communicating the decision as to which type of proceeding (if any) is going to take place at as early a time as is possible

27. This is probably the most immediate concern for directors and the legal advisors to them and their companies. It is also perhaps the most contentious from the regulators' perspective. This largely arises in the context of higher level conduct of the kind that is not necessarily confined to directors or even senior executives, such as breach of director's duties and like obligations under the Corporations Act 2001 (Cth), but also other areas that readily enough apply to them, including:

(a) conduct illegally affecting market integrity contrary to the *Corporations Act*, such as insider trading, market manipulation and the like;

(b) insolvent trading – there has only been a single prosecution in Queensland in recent years;

(c) anti-competitive conduct, most pointedly at present cartel conduct because of the dual criminal/civil penalty sanctions under the *Competition and Consumer Act 2010* (Cth).

28. One can readily enough predict that the two major regulators, ASIC and the ACCC, are going to be most reluctant to surrender their likely preferred position of not bringing the decision forward until it really suits them. Generally speaking, this is often a difficult and finely-balanced decision. It can include tipping point considerations to do with the nature and quality of the evidence and any continued attempts to improve upon that.

29. This in turn includes the ever-present possibility of a participant deciding to cooperate at some time during the investigation phase. This plays out most starkly in the interplay between ACCC markers and CDPP undertakings (that is, indemnities) for cartel conduct. Unlike indemnities for any other kind of criminal conduct, which generally confines their availability to persons who are significantly less culpable, cartel offences allow for an equal participant in the alleged conduct to be indemnified if they come forward first, provided they are not prime movers in the contravening conduct.

30. There may also be some complexity in determining whether a contravention has taken place at all, before deciding what sanction action is viable.

31. Although those reasons for the regulator and prosecutor wishing to retain a discretion for as long as possible, including the obtaining of advice from counsel, may be and be seen to be compelling, there does need to be some line in the sand. I would understand leading defence representatives to be asserting that the decision-making process is too prolonged and too uncertain. It can be an inhumane burden on a person not knowing what they are facing.

32. Ultimately, the earliest possible decision is in the interests of the regulator and the prosecutor, as well as the person being investigated. It preserves resources for addressing other conduct by bringing things to a head with a judgement call. And if compliance is to be most effective, the gap between the conduct occurring and any litigation needs to be kept as small as possible. In crude terms, it is better to do a 90% effort on 10% of the conduct, than a 10% effort on 90% of the conduct.