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Are Enforceable Undertakings A "Cop Out" for the Australian Securities and Investments Commission?

Jingyi Yu[1,*]

[1]Faculty of Law, The University of New South Wales, Sydney NSW 2052, Australia

*Corresponding author email: yujingyiau@outlook.com

Abstract

Enforcement undertakings (EUs) have become a widely used regulatory enforcement tool in Australia, particularly by the Australian Securities and Investments Commission (ASIC).EUs were originally designed to provide an efficient and collaborative approach to compliance, offering regulators a flexible alternative to litigation. However, ASIC's increasing use of EUs has sparked debate as to whether they represent a pragmatic enforcement mechanism or a means for firms to avoid more severe penalties. This paper examines ASIC's reliance on EUs, compares its approach to that of the Australian Competition and Consumer Commission (ACCC), and assesses the effectiveness, deterrence and transparency of EUs as a regulatory tool. While the EU can lead to faster resolution of issues and improved compliance measures, concerns about its leniency, lack of punitive effect and opaque enforcement raise questions about its effectiveness. By analyzing the EU's strengths and limitations, this paper proposes measures to improve its regulatory effectiveness, including stronger rules, greater transparency, and a balanced integration of the EU and litigation to ensure greater public confidence and regulatory accountability.

Keywords

Enforceable Undertakings; ASIC; ACCC.

1. Introduction

Enforceable undertakings(EUs) represent a novel type of administrative sanction developed by Occupational Health and Safety (OHS) Australia in response to the issuance of a notice of infringement.[1] They are essentially a promise that is enforceable in court and relates to a contract in which the holder of the obligation alleged to be in breach undertakes to do something and, in the event of a failure to comply, can be enforced in court. The OHS obligor offers these undertakings, which function as an agreement between the obligor and the OHS regulator.[1] The obligor agrees to either perform or refrain from performing certain activities. This agreement effectively replaces or augments other methods of regulatory enforcement, such as civil, administrative, or even criminal proceedings.

In 1993, EUs was introduced as an enforcement method to the Australian Competition and Consumer Commission (ACCC). Prior to this, the ACCC generally accepted "administrative resolutions" or settlement agreements between parties in lieu of, or in addition to, prosecution. Since then, section 87B of the Trade Practices Act has formalised these agreements as "enforceable undertakings" and clarified their enforceability.[2] Enforceable undertakings are designed to ensure that regulatory breaches are remedied expeditiously and effectively without the necessity for court proceedings, and to provide non-adversarial and constructive solutions to regulatory compliance issues. They are formal settlement agreements between regulators and individuals and firms to address non-compliance with the laws administered by that regulator. The terms of EUs are negotiated between the regulator and the promisor. However,

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if the terms are not met, the regulator may apply to the court for an order to that effect, including an order requiring the promisor to comply. To comply with a term of the EUs, the promisor may either pay to the Commonwealth an amount not exceeding the amount of any financial benefit that is directly attributable to the breach or indemnify any other person who has suffered loss or damage as a result of the breach. While a violation of an EUs agreement is not considered a contempt of court, a violation of a court order is a contempt of court once the court orders the promisor to comply with the EUs agreement.[3]

In the present era, certain regulatory bodies, including the Australian Securities and Investments Commission (ASIC), are increasingly willing to utilize EUs as in conjunction with other enforcement measures. EUs have the potential to provide a "tailored, more certain outcome" for instances of corporate misconduct, with the possibility for the obligor to implement significant alterations to its internal risk management systems and, when appropriate, compensation. The EUs could theoretically provide a "tailored, more certain outcome" for corporate misconduct, with the possibility for the obligor to make significant changes to its internal risk management systems, corporate culture, and, where appropriate, compensation. This sanction allows ASIC and other regulators to rectify suspected misconduct more quickly than if sanctions higher up the pyramid were imposed.

While in some instances, EUs are employed by ASIC to achieve outcomes that may not be attainable through the utilization of enforcement instruments situated at a higher level within the enforcement hierarchy, ASIC's over reliance on the EUs as an enforcement instrument against large organizations has also been a subject of recent debate. It is evident that there are numerous instances where ASIC's preference for EUs over litigation can result in the avoidance of more rigorous regulatory enforcement measures, which can have significant implications.

The objective of this paper is to examine the rationale behind ASIC's selection of EUs as a regulatory tool for large organizations, the utilization of EUs by both the ACCC and ASIC, and the positive effects they have had. Additionally, this paper will analyze the evasive behaviors and specific evasive aspects that may be involved in ASIC's over-reliance on EUs. Finally, by comparing the feedback on the adoption of EUs by ASIC and the ACCC, the paper seeks to identify ways to improve the evasion problems that may exist when ASIC uses EUs.

2. ASIC's Reasons for Adopting EUs

2.1. The EUs is an Effective Instrument for the Enforcement of Regulations

Assessing the need to take a case to a higher level in the sanctions pyramid can slow down the case process compared to using an EUs as an administrative sanction. In 2010-11 and 2012-13, the Office of the Commonwealth Director of Public Prosecutions (CDPP) took 42.6 weeks to assess cases referred by ASIC that ultimately resulted in prosecution.[4] Such long delays can be attributed to a number of factors: the complexity of ASIC matters and the number of witnesses required; the existing caseload resulting in a backlog of court lists; the need to establish the availability of witnesses; and the adjournment of trial and hearing dates.The Chairman of ASIC has stated that the reason why something like an enforceable undertaking is often used is because it allows for timely results and actually deals with the problem.159 The CDPP has stated that it is important to have a clear understanding of the nature of the problem in order to be able to take action. The CDPP has also stated that it is not always possible for the CDPP to take the necessary steps to ensure that the matter is dealt with. Similarly, former ASIC officials have said that in ASIC's Kleenmaid case, the CDPP took a year and a half to lay charges, which is the same amount of time it took ASIC to investigate the matter. On April 1, 2014, ASIC announced that the former directors of Kleenmaid had been convicted; this conviction occurred several years (2007-2008) after the alleged misconduct.[5] The length of time between the allegations and the sentencing makes this punitive measure much less effective.

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In contrast, the EUs represents a highly effective and versatile regulatory tool that enables ASIC to address suspected misconduct in a more expeditious manner than would be possible through the imposition of sanctions at a higher level within the regulatory framework.[6] As stated in ASIC's report, the EUs will be employed where the sanctions "provide a more effective regulatory outcome than non-negotiated, administrative, or civil sanctions." This is because the EUs involves compensating affected consumers for losses and a compliance update program designed to change promisors' compliance practices. This is because it involves reimbursement of losses to affected consumers as well as a compliance update program designed to change the compliance practices of the promisor.[6] In particular, the EUs meets the conditions for ASIC to be "effective." These include promoting integrity and public confidence in financial markets and corporate governance; specifically deterring individuals and firms from committing the conduct that gave rise to the undertaking in the future; promoting general deterrence so that the business community understands the conduct and the consequences of engaging in it; and providing sustained benefits through an improved compliance program. Furthermore, ASIC may accept the EUs in conjunction with other enforcement actions. For instance, ASIC could pursue a civil penalty action against a party in addition to the EUs, which would result in a more comprehensive remedial outcome for a greater number of affected consumers than would have been possible had the EUs been mentioned in the court action.

2.2. The EUs Exerts a Deterrent Effect

Deterrence is a core objective of the EUs. There may be specific deterrents against misconduct by specific individuals or organizations. For organizations in particular, the EU's deterrent mechanism is designed to prevent them from engaging in insubordinate behavior. One interviewee described the EUs as "a big stick that I think most organizations try to avoid." The three primary motivations for organizations to accept EUs and implement positive changes are to avoid the perceived influence of penalties and external intervention within the organization, to avoid the associated costs, and to avoid reputational damage.[6]

The EUs also has a ripple effect on the behavior of peers. A pilot study by the University of New South Wales Faculty of Law on the deterrent effect of the EUs on peer financial services and credit providers found that the majority of "peer providers" interviewed perceived the deterrent effect of an EUs signed by a competitor.[6] For businesses, their organizations would also implement costly reforms if competitors joined the EUs. For instance, one peer provider observed that it was implementing reforms that had been initiated by competitors, despite the associated costs, in order to ensure compliance with regulations and to avoid any scrutiny from regulators.

The deterrent effect of the EUs is not limited to the imposition of high penalties; the EU's intrusion into business is also a significant concern for businesses. In addition to imposing the idea that the regulator may be challenged on an organization, the EUs frequently brings in outside parties such as independent experts with oversight powers and a perceived direction for the business. For a financial services provider, the prospect of an external party determining the direction of the business is one of the most intimidating possibilities.[6] Consequently, it is prudent for an organization to adopt a proactive stance and operate in a manner that adheres to all pertinent standards, regulations, and guidelines. This approach is the most effective means of ensuring continued growth and success.

3. The Utilization of EUs in ACCC

3.1. The ACCC has Made a "Deliberate" Decision to Utilise EUs

Chronologically, the ACCC's utilization of EUs precedes ASIC and represents the inaugural instance of their use as a formal administrative sanction. This pioneering approach also

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influenced ASIC's decision to employ EUs. As previously stated, prior to 1993, informal undertakings by parties, "administrative resolutions," and later deeds of settlement were commonly accepted in lieu of, or in addition to, prosecution. In light of this context, the Commission has determined that in certain instances, protracted litigation can be effectively avoided by accepting undertakings from businesses to cease particular conduct or to take action to mitigate the adverse effects of their conduct in other ways. The Commission has found that in some cases, protracted litigation can be effectively avoided by accepting undertakings from businesses to cease particular conduct or to take action to mitigate the adverse effects of their conduct in other ways.[7]

The ACCC employed this methodology in a number of appropriate cases over an extended period. Extensive data and reporting revealed that it could result in significant cost avoidance for both the Commission and the businesses concerned. However, it was also recognized that the outcome was clearly beneficial to affected third parties and consumers in general.[8] Consequently, the Commission acknowledged the value and desirability of employing EUs as a flexible approach to trade practice issues. Following the enactment of the 1993 Act, the Government proceeded to confer legal recognition upon the practice. By providing for the enforceability of undertakings, the Act eliminates the necessity to rely on external means to enforce the commitments made by individuals when necessary.

3.2. Circumstances in which the ACCC has Elected to Utilize the EUs

In previous instances, ACCC has indicated that it seeks the following types of remedies through the acceptance of EUs agreements: corrective advertisements in print and electronic media; refunds to affected consumers; community service remedies; and industry-wide educational programs funded by the company or business providing the undertaking.[9]

In contrast to ASIC, which hopes that the EUs will be a forward-looking means of penalizing and controlling businesses, the ACCC believes that the EUs should be the second choice of penalization, and that it should only be chosen as an administrative tool after assessing the impact of the case on third parties and society, as well as the public interest. The greater the impact, the less likely it is to accept EUs. In contrast to ASIC, the ACCC does not consider accepting the EUs to be a "soft option" and does not take it lightly. Furthermore, it states that it will only consider an EUs settlement if it believes that a contravention of the Competition and Consumer Act has occurred or is likely to occur and that an EUs settlement is the best solution from the perspective of "sustained compliance with the law and redress for aggrieved parties".[9]

In addition, there are special considerations regarding the potential for entering into an EUs with a specific business. In particular, there are important requirements regarding the complaint history of the undertaking. Because the ACCC does not closely monitor businesses, this task is usually delegated to an external independent monitor. The degree of cooperation between the undertaking and the ACCC will be key in determining whether the party is acting in "apparent good faith."

3.3. The positive effects of EUs on the ACCC

ACCC has observed that the authority to enter into EUs agreements enables it to pursue efficacious and innovative outcomes without resorting to litigation. Research conducted for the Australian Competition and Consumer Protection Authority in 2001 demonstrated that EUs are frequently employed in In lieu of court proceedings, EUs often include assurances from the promisor that a comprehensive compliance program will be implemented. ACCC has noted that the power to enter into EUs agreements allows it to seek efficient and innovative outcomes without litigation.[9] Furthermore, instances have been documented where "enforcement agreements" have been reached as part of a settlement of court proceedings.

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Another beneficial aspect of the EUs is a significant area of focus for the ACCC. It provides mechanisms for compensation, indemnification, or other appropriate forms of redress for parties adversely affected by misconduct. Furthermore, to ensure transparency and accountability, the ACCC's policy is to make the list of EUs publicly available, including by placing it on the public register of section 87B businesses on its website and by referring to the list of EUs in press and media statements.

4. The Use of EUs by ASIC Is A 'Cop-out'

4.1. EUs allow companies to escape higher penalties

As an administrative sanction, EUs should be somewhat punitive. However, just because peer providers may view the cost of EUs as punitive does not mean that EUs are punitive from a legal perspective. A relevant consideration in determining their punitive nature is whether EUs have criminal consequences. Although the law's focus on punishment is not limited to monetary extortion, an order for restitution is not a punishment. This is because the fundamental distinction between EUs and civil penalties or criminal fines is that EUs are voluntary agreements. When an organization enters into an EUs agreement with ASIC, for example, when a business is accepted as being allowed to be "onerous," no wrongdoing is discovered. Even in instances where the undertaker agrees to a voluntary injunction, EUs do not result in an involuntary loss of citizenship as a consequence of the loss of a position. Consequently, EUs are unlikely to be punitive in nature.

Enforceable undertakings have been utilized in criminal prosecutions when they were originally intended for compliance purposes. For instance, ASIC provided enforceable undertakings to BNP and UBS banks for influencing Australian swap index rates for a period of three years. ASIC imposed a fine of only $1 million, which was a relatively modest amount in comparison to the gravity of the offenses.[4] This is at odds with the ASIC's own guidelines, which stipulate that enforceable commitments should not be made in the event of serious misconduct in the market. Furthermore, CPA Australia maintains that EUs are an inappropriate sanction if a person has committed a serious breach of their statutory duties on a continuous basis and if their conduct is reckless, as opposed to unintentional.

In other instances, despite the enforcement of EUs provisions by the court, there have been instances where the court has questioned whether there would be any benefit to doing so. For instance, in ASIC v Empower Invest Pty Ltd, the judge enforced the EUs provisions, but noted that he was "concerned that an order directing a company to comply with its undertakings would be of little use."[8]

4.2. EUs usage to circumvent high-cost litigation proceedings

One of the most apparent challenges in pursuing enforcement action against large companies is the considerable variation in the resources that regulators can devote to cases. Regulators may be required to incur significant expenditure when taking complex legal action. For instance, the Storm Financial case cost ASIC $50 million. Nevertheless, ASIC was prompt to dispel concerns that it lacked the necessary financial resources. The Levitt Robinson Solicitors submission criticized various aspects of ASIC, noting that ASIC was second only to the Australian Taxation Office in terms of expenditure on legal fees, with ASIC spending A$300 million between 2008 and 2012.[4] The Australian Taxation Office has also been a significant contributor to ASIC's legal costs.

There are numerous pressures on ASIC to select undertakings over litigation. While it is understandable that resources must be prioritized so that enforceable undertakings are the more cost-effective and expedient option, there is a risk that cost considerations or cooperation

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with the regulator may influence the correctness of that decision, to the detriment of consumers, investors, and the public's confidence in the marketplace.[4]

ASIC may face challenging decisions regarding the imposition of specific sanctions or remedies. Nevertheless, the Committee believes that the public interest would be better served if ASIC were more willing to pursue legal proceedings in complex matters involving large entities. The prevailing trend appears to be either a reluctance to take court action or a greater preference within ASIC for negotiated settlements and enforceable undertakings. Nevertheless, the prevailing conclusion is that there is minimal evidence that large entities are concerned about the prospect of litigation by ASIC. While other remedies, such as enforceable undertakings, may be effective in correcting behavior within a particular organization, they do not carry the broader and more significant regulatory benefits associated with successful court action.

4.3. The EU's less transparent system allows enforcement to evade public regulation

The manner in which the various regulators in the EUs ensure and enhance transparency varies considerably. This reality has led to criticism of some of ASIC's past practices. For example, the Australian National Audit Office (ANAO) has recommended that ASIC formalize its process for obtaining EUs approval.[8] In addition, the ANAO has been critical of the fact that information on EUs is held in multiple systems, which means that no single system contains all the information on the EUs. This increases the risk that ASIC staff will not have access to the full picture when dealing with the EUs, especially in the absence of staff training related to the instrument. It is conceivable that if an agency is in doubt about how its EUs is being used, the problem will be most serious from the public's point of view as they will not be able to fully understand how the EUs is being relied upon and managed.

Furthermore, in a report, a former media advisor to the Australian Securities and Investments Commission made the following observations about the process of obtaining licenses for EUs: the undertakings were discussed and debated for months, conducted behind closed doors and in secrecy by a large number of lawyers, with very few details disclosed regarding how investors would be harmed, how many investors would be affected, or even whether the undertakings would be honored. In some instances, the companies in question undertook to write letters to the affected clients, inviting them to come and discuss their concerns. The extent to which these letters were sent, the manner in which they were worded, whether they were responded to, and the compensation offered remain undisclosed.[4] All appeared to be resolved after the Australian Securities and Investments Commission issued a brief but carefully crafted press release.

The public acceptance of an enforceable commitment as a remedy for misconduct, and its ability to deter misconduct within or by other regulated entities, may be undermined by a variety of perceived deficiencies in the commitment. These deficiencies include, in particular, a lack of transparency about the misconduct and the remedial action required; concerns about the independence of the experts appointed to oversee the firm's compliance with its obligations; and a lack of confidence that compliance with the undertaking will be effectively monitored and the terms enforced. Consequently, ASIC must implement alternative strategies to enhance transparency within the system, particularly from the perspective of the general public.

5. A Solution to the Issues That Arise in ASIC is to Utilize EUs

5.1. The EUs must implement stronger provisions to limit the activities of ASIC

An increase in the cap on fines imposed by the EUs may prove an effective means of persuading firms to focus on the punitive nature of EUs sanctions. In 2018, ASIC entered into 20 enforceable undertakings, including mandatory undertakings with the Commonwealth Bank and ANZ

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concerning its practice. The fines were imposed for a number of reasons, including the charging of customers for no service and the distribution of retail superannuation products. In addition, the Commonwealth Bank's (CBA's) involvement in the manipulation of bank bill swaps was a contributing factor. It should be noted that the fines are not enforceable by the government, but by the court system, which can be used to enforce fines for breaches of the law. The situation changed after the government passed legislation in 2019, which allowed ASIC to impose fines of up to $25 million per breach through the court system. In contrast, ASIC's register of enforceable undertakings shows that the regulator has only entered into one enforceable undertaking with Gold Coast accountant Jenan Thorne in 2019.

As enforceable undertakings can be utilized as an alternative to court proceedings, it is recommended that ASIC, when contemplating the acceptance of enforceable undertakings, formulate clauses that necessitate more rigorous requirements, particularly in relation to remedial action. [4]Additionally, it is imperative that ASIC be more explicit in its requirements for firms to identify wrongdoing in the undertakings they have taken on and to take steps to ensure that compliance with these clauses can be enforced in court.In addition, EUs documents are themselves legal instruments and therefore contain a range of legal jargon, which makes them less accessible to an unsophisticated audience.[8] A pilot study of the deterrent effect of ASIC's EUs demonstrated that some regulated entities found it challenging to understand the terms of EUs. Searching the EUs register is often challenging due to the manner in which EUs are scanned into the system, which makes analyzing and searching for keywords difficult. Although not formally regulated, ASIC may take positive initiatives such as issuing media releases or including a summary of EUs in its register. These practices allow EUs to be described in simple terms, which may assist consumers who may have been affected by the alleged breach in pursuing claims against the alleged offender.

5.2. Increased regulation and transparency in the use of EUs

It can be observed that there is a lack of clear regulatory rules within the EUs. This lack of clarity has led to the issue of EUs not being effectively monitored in ASIC. In order to circumvent the implementation inefficiencies associated with regulatory opacity, the ACCC has initiated the incorporation of some monitoring obligations into its EUs. These obligations are primarily geared towards organizations that advise the ACCC, with the objective of ensuring that EUs agreements can be complied with. However, over time, it became evident that this low level of monitoring was also insufficient due to organizational bias and potential conflicts of interest. Consequently, the ACCC has once again initiated the involvement of independent expert consultants to monitor compliance with the terms of the EUs. These independent experts are designed to provide a more impartial report on a company's performance and compliance with the terms of its commitments. Furthermore, the ACCC has determined that "independent reviews are more effective than reviews conducted by internal staff." This is because an unsatisfactory report identifies deficiencies in a company's performance and provides the regulator with an opportunity to address any breaches of commitments. To strengthen its oversight regime, the ACCC has also taken the initiative to create and develop detailed templates of how independent experts should deal with EUs. These templates provide additional guidance to the business community and independent experts on regulatory expectations in relation to surveillance, including surveillance best practices.

In response to the relevant critical recommendations, ASIC has implemented a policy whereby the regulator reports to the public on a committer's compliance with the EUs to which it is a party. These reports are available on ASIC's registry. By providing the public with the level of compliance of a committer, this initiative increases transparency. The move also sends a message to the regulatory community that ASIC is closely monitoring the compliance of its EUs, and that other regulators should take heed. However, even in ASIC's case, more could still be done to strengthen regulatory oversight. For example, ASIC could issue a media release at each stage, highlighting compliance with the terms of the commitment. Such a course of action would serve to alert the industry and the public to the unacceptable behavior that ASIC deems to be in question, while also holding the promisor accountable for their actions.

While the focus of monitoring described above is on organizations, it is important to note that individuals can also be considered "committers." However, it is rare for regulators to proactively monitor the compliance of individual committers, and monitoring of their compliance usually relies on self-reporting.[8] In some cases, ASIC also requires auditors to have their work audited by independent parties, but this is determined on a case-by-case basis.

5.3. EUs and litigation are used in a proportionate manner to better serve the public interest

In the Interim Report of the Hayne Royal Commission, Commissioner Hayne expressed criticism of ASIC's approach to enforcement, stating that the starting point for ASIC was erroneous. In determining how to respond to instances of misconduct, ASIC's initial approach appears to be to prioritize the resolution of such matters through negotiated agreements. This has led ASIC to prioritize the agreed resolution method as the first order of business when choosing the means of enforcement, placing the question of whether the public interest will be harmed by the agreed resolution as a second or even lower order of business. It is therefore evident that behavioral regulators should not use this as a starting point. Upon the discovery of a violation, the regulator must ascertain whether there exists a rationale for the infraction and, if so, determine whether the public interest would be served by the imposition of penalties. The imposition of penalties for non-compliance with the law is a consequence of societal expectations and demands for compliance with the law.

In order to ensure that the threat of litigation is credible, it is necessary to strengthen ASIC's Special Account for Enforcement. Currently, the ASIC Enforcement Special Account does not appear to be sufficient to support ASIC in funding large and complex cases. In order to provide a greater deterrent effect and to ensure that ASIC is not constrained in its ability to bring major litigation, it is necessary to significantly increase the size of the ASIC Enforcement Special Account. It is also necessary for the government to provide support for this initiative to ensure its effectiveness. In particular, the government should not use the funds or reduce the funds given to ASIC so that the ASIC Enforcement Special Account can have a healthy balance and support ASIC in bringing additional proceedings.

6. Conclusion

In conclusion, the use of EUs by ASIC presents both advantages and challenges in the context of enforcement measures. While EUs offer a timely and effective alternative to prolonged litigation, and can be efficient in resolving misconduct and facilitating effective rehabilitation of firms, there is still the issue of "evasion". It is evident that concerns remain about the lenient penalties it has imposed in recent years, the fact that it allows companies to avoid higher penalties, and the lack of transparency in the enforcement process. These concerns can be alleviated by examining the ACCC's approach to the utilization of EUs, which entails the enhancement of fines for EUs, the reinforcement of regulation and transparency, and the equilibrium of EUs and litigation. These initiatives are crucial for the maintenance of public trust, regulatory integrity, and the effective enforcement of financial and trade regulation.

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