



APX SUBMISSION
TO TREASURY ON
PROPOSED INDUSTRY FUNDING
MODEL FOR THE AUSTRALIAN
SECURITIES AND INVESTMENTS
COMMISSION

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Proposed Industry Funding Model for ASIC

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The views expressed in this submission are intended to reflect the collective view of APX. However, no representation or warranty is given that either the author or individual APX office holders, consultants or employees subscribe to each of the views herein described.

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1. Introduction

Thank you for the opportunity to comment on the above consultation paper (“**Consultation Paper**”).

Asia Pacific Stock Exchange Limited (“APX”) welcomes the opportunity to make a submission on the proposed industry funding model for ASIC (“the Model”).

2. Executive Summary

This submission is structured in three parts

- Structural issues which need to be addressed prior to finalizing levies and fees;
- Issues arising from the proposals; and
- Alternative solutions

APX believes that the proposals will have a major detrimental impact on competition for the provision of market services in Australia by significantly increasing the barriers to entry and ongoing operation for market operators. This will have the practical effect of reinforcing the ASX monopoly in this sector. The annual fees payable to ASIC are a material amount that represents a significant increase over currently budgeted ASIC costs and will be the second highest cost incurred by APX behind staffing costs. As the APX market grows, it has been made clear that the ASIC fees will also grow. Hence, we expect that in a short time, the ASIC fees will be the largest single cost incurred by APX to operate its market.

Proposals to recover ASIC costs should not be a simplistic exercise of adding up ASIC’s total costs, then allocating them to industry. Policy development of this scale needs to take account of the industry economics in each sector affected to ensure that any policy decision to introduce cost recovery does not have materially adverse effect on these downstream markets. An assessment needs to be made of the underlying profitability and competitiveness (both domestically and internationally) of each industry sector, the materiality of the fees to be charged and the ability of industry to absorb or pass on those costs. If the industry does not have the capacity to absorb or pass on the costs, there is a very real risk that cost recovery proposals of the scale being proposed will have major detrimental impact on Australia’s financial services sector and do untold damage to our global competitiveness and ability to ever establish Australia as a regional financial centre. The financial services industry is one of the largest employers and exporters in the country and any damage to it will have knock on effects to employment and the broader economy. In fact, it is not inconceivable in an industry already suffering margin compression and increased technology and regulatory costs that many investment banks, stockbrokers and even market operators could seek to retreat from the Australian market and trade here from regional offices based in Hong Kong or Singapore.

APX makes the following submissions in relation to the Consultation Paper

- The proposition to introduce substantially increased fees for market operators is premature whilst substantive structural issues remain unresolved;
- The proposed fees are business-model changing and could serve to entrench the existing ASX monopoly;
- There are structural distortions in the cost recovery model which makes the model both flawed and inequitable; and
- The proposed fees will re-inforce an uncompetitive Australian financial services sector in a globally competitive environment.

There is a very real problem with the Government seeking to recoup 100% of ASIC’s costs. Without the pressure of Government budget constraints, there is a very real risk that ASIC’s costs will inflate at a rapid rate simply because someone else is paying. In addition, market supervision and ensuring market integrity are fundamental roles of



ASIC that are very much in the public interest. While there is scope for some industry funding, it is essential that Government funding is also provided to reflect this overwhelming public interest in ensuring that our markets remain robust, competitive and above all else fair and efficient.

3. About APX

APX is an Australian licensed listing market operator having held a market licence since 2004. APX was given approval by ASIC to re-commence operating its equities market in November 2013. APX is wholly owned by the AIMS financial group¹ and is 100% Australian owned.

APX provides opportunities for Asian and Australian companies to raise the capital they need for expansion from a diversified range of domestic and international investors, especially from the Asia-Pacific region. APX is an exporter of Australian financial services IP.

We believe significant capital market development opportunities exist in relation to capital flows between Australia and China. Key market segments upon which APX is focused are:

- Chinese - based companies seeking capital, market opportunities, or a listing in Australia;
- Australian - based companies seeking capital or market opportunities in China; and
- Markets for Australian and international companies which are not presently well serviced in the Australian market.

Owing to its strong links with China, APX sees itself as the natural Australian stock exchange for RMB denominated trading in securities in line with Australia's move to create an international RMB hub. APX is planning to introduce dual trading and settlement capabilities in both AUD and RMB for its equities market.

APX provides new competition for the provision of listing and trading services. To develop as a vibrant capital market Australia needs competition for listing services, as it needs competition for clearing and settlement services.

APX has a rare chance to be innovative and to fundamentally redefine the interactions between, and understanding of, both Australian and Chinese financial markets. We are offering a competitive and innovative alternative to the likes of Australia's ASX and China's Shanghai and Shenzhen stock exchanges. But to promote innovation in markets, markets need government and ASIC support for innovation. As APX progresses its rethinking of how markets can work in the future, we need others to step out of the mindset of "how it has always been done", in order to embrace "how it can be done".

The APX market currently provides both listing and trading services. The market is currently settled by means of the Settlement Facilitation Service (the "SFS") provided by ASX Settlement Pty Limited ("ASX Settlement"). Settlement obligations are direct broker – broker counterparty obligations utilising the ASX Settlement DvP services.

As set out above, APX is wholly owned by the AIMS financial group. The AIMS Group, which is a diversified financial organisation built up over 25 years encompasses mortgage lending and securitisation, funds management, stock broking and corporate advisory, is wholly owned by Mr George Wang. APX is 100% Australian owned.

¹ www.aims.com.au



APX and its parent, AIMS Group, have developed extensive financial connections throughout China over the last 25 years. The AIMS Group believes Australia has significant potential to further develop its position as a financial hub in the region and should be a more dominant force than centres such as Singapore in the region. In line with Government policy AIMS has sought to expand and internationalise throughout Asia and promote Australia as a regional financial centre.

Since 2008 Mr Wang has personally funded the development of the APX market, investing several million dollars into the establishment and growth of an Australian market to provide a competitive and innovative listing and trading alternative to that of ASX domestically and, internationally, to develop a market leveraging Australia's quality and cost effective regulatory environment to promote capital flows between Australia and Asia, particularly China. Mr Wang has invested in the development of new market rules frameworks, robust technology (by way of the adoption of the Trayport trading platform and then the NASDAQ trading platform), employment and, more recently, innovation initiatives. AIMS Group and APX staff have focused upon the recruitment and development of quality human resources in both Australia and China to develop a financial market presence which the likes of ASX, NYSE and others have, to date, been unable to achieve.

However, growth and, in particular, international growth and the partnerships required to support that growth require certainty. Exporters of Australian financial services, such as APX, also require the support of Government, not endeavours which act to the significant detriment of those exporters.

The currently proposed level of fees is of such significance, that the estimated timeframe for APX to satisfy its inequitable financial licence conditions to be cashflow positive would be substantially extended. Whereas APX could have reasonably expected to have satisfied those conditions, thereby freeing up several million dollars of regulatory capital for investment back into APX and facilitating greater competition, APX will be placed at a considerably extended competitive disadvantage to other market operators. Further, the forecast timeframe for APX to generate operating profits is extended by a similar timeframe and the estimated timeframe to recover the substantial investment over 8 years to date is extended by an even greater timeframe.

4. Scope of the Consultation Paper

APX is cognizant of the objectives of the Consultation Paper and the proposal for an industry funding model.

However, as an observation, we have noted that there the paper does not consult on whether an industry funding model is an appropriate model for the Australian market given its scale and fight for regional relevance. There is an inherent assumption that industry funding is appropriate and the paper then presents a single model.

APX would have preferred to see an initial debate and consultation on appropriate funding methodologies for ASIC and, following that debate, discourse and consultation on a number of different models which may be considered to deliver on that methodology.

We submit that the presentation of a single model is not ideal and there needs to be greater consultation.

5. Structural issues need to be addressed first



APX submits that the proposals set out in the Consultation Paper are premature as a number of structural questions addressed in this section 5 need to be addressed before a determination on cost recovery is valid. In essence, consideration of substantially increased fees for market operators at this point in time is putting the cart before the horse.

5.1. 2012 Market operator licensing review

In November 2012 Treasury initiated a review of markets licensing.

As part of its ongoing work considering regulation of dark pools, the Government asked Treasury to conduct a review of Australia's financial market licensing regime. The review was to examine the licensing of dark pools, and whether the market licensing regime is generally fit for purpose. The consultation paper "Australia's financial market regime: Addressing market evolution"² (the "2012 review") considered the adequacy of current licensing arrangements, and raised possible options for reform. It also considered the regulation of non-market participant high frequency traders.

To date, the 2012 review has not been finalised.

The 2012 review Consultation Paper set out that "ASIC has not previously undertaken any licensing activity relating to dark pools, and any moves to licence these would create additional work. There are currently 15 dark pool operators in Australia, with recent rapid growth in numbers. Market innovation in dark pool product offerings is ongoing, which ASIC would need to keep abreast of."

More importantly, the Consultation Paper stated the current arrangements as follows:

"The regime was designed in 2001 with public exchanges in mind, and did not anticipate the extent of financial market evolution that has occurred since. As a result the system has not kept up with changing regulatory needs. In particular, the emergence of dark pools has exposed some of the limitations of current arrangements."

Over time, the legislative framework has been stretched to accommodate market developments. This has been necessary due to the lack of flexibility in the Act, with no scope to partially apply the licence obligations under Part 7.2. This has meant that a number of professional markets have received conditional licence exemptions, although the exemption power in the Act was not designed with the systematic regulation of alternative markets in mind. Dark pools are not formally licensed, with operators subject to the market integrity rules only through the fact that they are all market participants in public exchanges and hold an Australian Financial Services Licence (AFSL).

Differences in these arrangements mean that the regulatory landscape is inconsistent between markets that are effectively competitors, for example public exchanges and dark pools. Markets that are unlicensed face fewer compliance requirements, and are also not directly included in the cost recovery regime for market surveillance. This creates a competitive advantage for those outside of the market licensing regime, and also reduces the effectiveness of market supervision." [emphasis added]

² <http://treasury.gov.au/ConsultationsandReviews/Consultations/2012/Australias-financial-market-regime-Addressing-market-evolution>



APX submits that implementation of a fee regime as currently proposed in advance of addressing the “limitations of current arrangements” clearly identified in the 2012 review will serve to further entrench the “competitive advantage for those outside of the market licensing regime” and further entrench any resistance to licensing change.

ASX also understands that some of the proposals under consideration by Treasury arising from the 2012 review would have an impact upon the amount of work (and hence resources) required to be committed by ASIC, including a potential for differentiation between listing and trading exchanges or differentiated levels of compliance obligations for different types of market operators. This may require significant changes to the fee structure adopted by ASIC.

The failure to finalise the review has also contributed to the inequitable and anti-competitive licencing framework, and hence the implications under the levy proposals as referred to in section 5.2 below.

APX strongly submits that it is premature to consider the currently proposed fee structures until such time as the 2012 review has been finalized.

5.2. Inequity of current licensing framework

APX submits that the proposed fee framework will exacerbate the inequities which exist within the current market operator framework.

APX is subject to various financial conditions imposed in its market operator licence conditions which significantly adversely impact upon the competitiveness of APX. The proposed fees regime will exacerbate that issue as outlined in section 11 below.

APX’s licence conditions have been imposed on the basis of the possibility of APX failing and, in such circumstances, to ensure that APX has sufficient funding to wind down its market in an orderly manner. As a consequence, APX has a 300% cash outflow overhead obligation to which other market operators (other than FEX Global Pty Limited) are not subject.

APX submits that it is fallacious to assume that there is a probability that new market operators will experience failure or financial difficulties and yet the probability that existing market operators will experience failure or financial difficulties is zero. A consequence of that erroneous assumption is that new market operators are subjected to financial stability conditions in their licence whereas existing market operators are not.

This places new market operators at a significant competitive disadvantage to existing operators. As outlined in section 0 below, the combination of this inequity and the proposed new fee structure could be terminal for some market operators.

ASIC is aware of the fallacious nature of these assumptions and that the probability of an existing market operator experiencing failure or financial difficulties is not zero.

APX submits that unless there is equity amongst the licence conditions imposed upon both new and existing market operators to provide a level playing field, it is premature to consider the current fee structures in the knowledge of the potential consequences upon some market operators.



5.3. Service levels

APX submits that elements of ASIC's function include not just a market supervision element but also business development elements from a market operator's perspective. Business development is key to innovation and competition and time to market is a key requirement, whether to facilitate competition and innovation domestically or, increasingly, internationally. Yet experience to date is that the major barrier to timeliness to market is the service level (or absence of service level) provided by ASIC. Whilst we fundamentally disagree with the scale of the proposed cost recovery levies and fees, the charging of any fees would normally be associated with an expectation of service and that expectation should be measurable by way of defined service levels.

Operating Rules are the key product functional design specifications for a market operator. As such, in an environment in which competition between market operators is policy and encouraged, quality of design and speed to market are key elements of any change to the Operating Rules.

APX does not dispute that, in the interests of market integrity, ASIC has a role to play in ensuring the quality of the rules. However, ASIC also has a role to play in promoting competition and innovation and, hence, speed to market. Experience to date suggests that ASIC does not have the capability or the service level obligations to facilitate speed to market.

APX does not dispute that the current fees for amendments to Operating Rules are low.

However, if fee increases of the magnitude proposed (34,666%) are to be adopted, given that rule amendments are key to market innovation and market innovation is a key element of competition, the adoption of significant fee increases must be accompanied by the adoption of service levels and/or substantial changes to the existing process of rule amendments.

The existing process, as set out in s793D of the Act requires that the proposed amendments be lodged with ASIC and, from that point in time, the Minister has 28 days to disallow the amendments as set out in s793E.

Conceivably, formal lodgment of rule amendments with ASIC for the first time could be commencement of the timeframes under s793D and E. In reality, formal lodgment with ASIC is the end of the process. Considerable negotiation has generally been undertaken on an informal basis to reach the point at which, when formal lodgment occurs, the rule amendments have already been agreed and Ministerial non-disallowance is a formality. However, as experienced by APX and other market operators, ASIC has no guaranteed service levels to progress rule amendments prior to formal lodgment and can be a significant barrier to innovation in that regard. For example, it has taken over 2 years to obtain informal ASIC approval of the proposed APX Listing Rules relating to the Mining and Oil & Gas (MOG) sector. Once formally lodged, the formal process will take no longer than 28 days.

ASIC has advised that the \$52,000 proposed fee for amendments of the operating rules is a reflection of the average estimated ASIC cost of processing amendments over recent years. Of course, there is no way of publicly verifying that figure. However, if the average estimated ASIC cost includes costs associated with the above 2 year process, then it is reasonable to assume that the estimate includes the cost of significant ASIC inefficiency.

With the above example of time and cost in mind APX can envisage scenarios in which the proposed fee increase will result in unintended consequences. For example, an exchange may adopt the perspective that given the fees applicable and the absence of service levels, it is a commercially rational process to formally lodge an amendment with ASIC rather than to go through the informal process. This immediately initiates the 28 day time limit, thereby introducing a statutory service level upon ASIC and forcing the Minister to either approve or disapprove



amendments, thereby creating tension between the Minister and ASIC, the Minister and the market operator and the ASIC and the market operator. Responding to formal lodgments in such a scenario on a repeated basis would significantly adversely impact upon both the Minister and ASIC. The system would shortly become dysfunctional.

Alternatively, the market operator may increasingly rely upon waiver powers to bring about innovation. This again would create tension between the market operator and ASIC. It would also create an uncertain environment in which the Rules, as published, would not provide an accurate representation of the standards and quality of supervision of the market. Again, the system would shortly become dysfunctional.

APX is aware of views within ASIC that one resolution to these structural issues would be to delegate the rule approval power from the Minister to ASIC. APX would strongly oppose such a move on the basis that:

- The Ministerial disallowance process is not the key component of time or cost;
- The Ministerial disallowance process provides an avenue for consideration of views which may differ to those of ASIC;
- Delegating to ASIC would place ASIC in the equivalent position of both judge and jury.

APX submits that, any proposals to introduce significant price increases or taxes on innovation should only be implemented after completion of the ASIC competency review, structural reform of the Operating Rule amendment process and the introduction of statutory service levels upon ASIC.

In the absence of such reform, consideration of the proposed fee increases is premature.

5.4. Inequity in cost recovery from C&S facilities

Page 58 of the Consultation Paper sets out the proposed annual levies for market Infrastructure Providers (“MIPs”) as follows:

Type of MIP	Proposed Annual Levy – Range
Australian Market License Holder – Domestic	\$116,000 - \$4,000,000
Australian Market License Holder – Foreign	\$12,000
Clearing and Settlement License Holder	\$34,000 - \$420,000
Trade Repository License Holders	\$93,000 - \$161,000
Exempt Markets	\$45,000

It is noticeable that the proposed annual levies are heavily skewed to the detriment of domestic market license holders and to the benefit of both foreign market license holders and C&S facilities (whether C&S license holders are trade repositories).

It is APX’s understanding that the bias in favour of the C&S facilities is a consequence of such facilities being jointly regulated by both ASIC and the RBA. As a consequence of the current proposals relating solely to ASIC cost recovery and the RBA not having a policy of cost recovery, the C&S facilities are only partially levied.

We submit that this presents a structural distortion in the cost recovery model which makes the model both flawed and inequitable.



From a systemic risk perspective, it has been recognised that the C&S facilities play a significant role in the stability of the financial system. The importance of this sector and the issues associated with its complexity are, to some extent, reflected in the current considerations in relation to competition in the provision of clearing services.

It is inequitable that, whilst systemically important financial services regulated by APRA are levied on a full cost recovery basis and financial market operators are to be levied on a full cost recovery basis, C&S facilities which present a higher risk to systemic financial stability are levied on a partial cost recovery basis solely on the grounds that they are regulated by a different regulator with a different funding model.

The Consultation Paper sets out on page that “Industry funding would drive economic efficiencies in the way that resources are allocated. Industry funding for ASIC’s regulatory activities would establish clear price signals that would influence the behaviour of regulated entities that create the need for government oversight.” Further, the ASIC Annual Report for 2013-14 states “We will continue to push the case for a user pays funding model for ASIC. Such a model is not about increasing ASIC’s budget but about providing the economic incentives to drive the Government’s desired regulatory outcomes for the financial system”³ [emphasis added]

The pricing model proposed for C&S facilities is clearly inconsistent with the objectives set out in the Consultation Paper. It is inconceivable from a financial services sector perspective that whilst “ASIC’s regulatory costs are driven by its assessment of the risk that each MIP presents to the operation of Australia’s financial markets”⁴, C&S facilities represent a risk and a cost approximately 90% less than that of market operators. If a cost recovery model were to truly be representative of the perspective that regulatory costs (on a broader regulatory cost basis than just ASIC) are driven by an assessment of the risk that each MIP presents to the operation of Australia’s financial markets then the fees paid by C&S facilities should be substantially higher than those paid by market operators.

In effect, relative to other systemically important sectors of the financial services sector, ASX (as the dominant C&S Facility and trade repository in Australia) is effectively to be given a “free ride”. This is not consistent with the objective of establishing “clear price signals” and being reflective of risk.

5.5. Competition in clearing

In addition to the inequity and price distortion referred to in section 5.4, APX submits that it is premature to consider fee structures for MIPs until the issue of competition in clearing has been resolved and implemented.

The introduction of competition in clearing (if agreed by Government) will raise new issues and challenges for ASIC and RBA. It will require the commitment of new resources (or redistribution of existing resources) which has the capacity to significantly change the resourcing model within ASIC and hence the cost allocation and the price signalling.

If, as it seems, there is no new entrant ready to provide alternative clearing services in the cash equities market, it will be necessary for Government to regulate ASX Clear on an interim basis in respect of pricing and access arrangements.

It is essential that the regulatory framework also address access to essential infrastructure, such as the ASX settlement facility and impose obligations on ASX as the current monopoly provider of clearing services to ensure that ASX Clear has positive obligations to connect with new entrants into the clearing market; independent

³ ASIC Annual Report 2013-14 page 4

⁴ Consultation Paper page 57.



processes to review applications from such entities, how they will connect, how interoperability will work (including how the clearing houses will margin positions across the clearing houses). Absent this rule framework (referred to as “**Clearing Integrity Rules**” for convenience), ASX will have scope to delay and frustrate any potential new entrant into the market for clearing services. Having Clearing Integrity Rules in place provides industry certainty and certainty for any new entrant that is interested in the Australian market.

The alternative unsatisfactory outcome is for Government to wait until a new entrant makes enquiries. This would no doubt result in further delay and analysis, which would reflect poorly on Australia and such uncertainty more than likely fail to elicit any new entrants. The Government and regulators have had firsthand experience implementing a competitive framework for trading. While that took longer than Chi-X and the industry anticipated, that experience should now see Government and regulators well placed to proactively facilitate a competitive framework for clearing that leads the world. The timing for this framework should recognize that the process of reviewing competition in this industry sector already dates back to 2012.

These outcomes, if resultant from the review of clearing competition, will have an impact on the cost modelling adopted by ASIC, but the extent of that impact will not be known until the recommendations of the Council of Financial Regulators is published and the Government’s response to that review is made public.

APX has had recent experience with seeking to access the ASX clearing facilities and the extent to which the current moratorium arrangements are less than ideal. APX has no doubt that, as a monopoly provider, ASX will seek to pass on some of the ASIC charges to competing market operators which use the ASX clearing facility. The extent to which it can do so may be different in a competitive environment.

Any decision to not introduce competition for clearing and without adjustment of the pricing model will reinforce the price distortion referred to in section 5.4.

However, as the outcome of the competition in clearing review has not as yet been finalised, APX submits that considering a cost recovery structure is premature.

5.6. Regulatory framework still not catering to competition

APX submits that, whilst competition between market operators for both listing and trading services has existed for several years, the regulatory framework has still not caught up to accommodate that competition. The resultant inequity and resource impost upon both market operators and ASIC to deal with a dysfunctional regulatory system distorts the historical resource allocations upon which the ASIC cost recovery model is based. If market operators are to be charged a substantial, business-model changing annual fee, then market operators are entitled to demand the regulatory environment and regulatory services be “fit for purpose” and provide a level playing field.

For example:

- A large number of ASIC Class Orders and Regulatory Guides remain drafted in ASX-centric terms. This provides both ASX with a natural competitive advantage but also means that ASIC resources have had to be diverted to dealing with requests to address the inequity.
- The investor compensation regime remains fragmented. ASX investors are covered by the National Guarantee Fund (NGF) which is administered by the Securities Exchanges Guarantee Fund (SEGC) under Part 7.5 Division 4 of the Act. Other market operators are required to develop and administer their own compensation arrangements under Part 7.5 Division 3 of the Act. As a consequence, investors in the ASX, Chi-X, NSX and APX market may be covered by 4 different compensation arrangements. Other market operators could become members of the SEGC in order to gain access to coverage by the NGF. However,



the SEGC has not developed a transparent framework for how it would manage multiple members. As a consequence, the multiple compensation arrangements results in less than optimal environment for members, increased cost for market operators and increased cost for ASIC having to supervise multiple arrangements. Further, as the compensation arrangements for markets other than ASX are included in Operating Rules, if a market operator were to become a member of SEGC, the cost may be prohibitive as there would be SEGC risk assessment charges, ASIC rule amendment charges of \$52,000 and an unknown quantum of “contribution” to the SEGC required.

5.7. Cost control and governance

APX has significant concerns regarding cost control and governance under the proposed new regime. APX submits that the ASIC governance framework and Commission composition are not structured to optimally manage cost control and fee structures as proposed.

APX submits that the introduction of fees as proposed should be accompanied by structural reform of ASIC to optimize its efficiency and to introduce new non-executive, independent members as Commissioners.

APX acknowledges that ASIC utilizes industry panels for feedback and commentary on proposals. However, such panels have no formal standing and are advisory only.

APX also acknowledges that ASIC is subject to Ministerial and Senate Estimates Committee oversight. However, we submit that this is not at a sufficiently detailed level to oversight internal governance, efficiency and management recommendation.

We submit that, if new fees which have the potential to significantly impact upon industry are to be introduced, increased oversight by an independent Commission would be highly desirable. At the very least, the Chair of ASIC should be independent of executive management.

5.8. ASIC capability review

APX submits that it is less than ideal to introduce a cost recovery structure based upon historical estimates of cost and entrenched methodologies prior to the finalisation of the current review of ASIC capability.

APX submits that it would be more rational to conduct the review to examine what capability ASIC requires going forward, what capability ASIC currently has, what are the gaps and what structural and prioritization reform is required to allow ASIC to deliver an optimal outcome and demonstrate value for the funding being committed by industry.

Based upon that foundation, a more realistic estimate can be made of future ASIC funding requirements.



6. Financial impact of the model upon APX arising from licence conditions

APX submits that the impact of the combination of the inequitable standard ASIC licence conditions for new market operators and the proposed fee increases will result in a reduction in the provision of market services and may prove terminal for some existing market operators. APX submits that the proposed fee structure has the potential to re-inforce and thereby endorse the existing ASX monopoly on the provision of market services.

6.1. The APX financial resources licence conditions

APX, as new market operator, is subject to anti-competitive licence conditions to which existing market operators are not subject.

The APX market licence is subject to a number of conditions. In particular, section 14 of the APX market licence reads as follows:

Financial resources

- 1) From the date that APX commences to operate the market until APX's monthly cash flow, or the aggregated monthly cash flows of APX and any Service Provider in respect of the administration of APX's affairs and finances, is cash flow positive for each of the six consecutive months, APX:
 - a) must not transfer any funds to a related body corporate (other than to its Service Provider under any agreement for the provision of services for the administration of APX's affairs and finances or as part of trading fee rebates that may be due through trading on the market);
 - b) must give ASIC for each quarter, and no later than 28 days after the end of each quarter, a report which contains:
 - i) a statement of cash flows of:
 - A. APX;
 - B. any Service Provider
 - C. any Service Provider, to the extent that the cash flows are in respect of the administration of APX's affairs and finances.
 - ii) a statement of financial position of:
 - A. APX; and
 - B. any Service Provider
 - iii) a projection of cash flows for the next 12 months of:
 - A. APX; and



- B. any Service Provider, to the extent that cash flows of the Service Provider constitute payments in respect of the administration of APX's affairs and finances for each month within the period, based on APX and its Service Provider's reasonable estimate of what is likely to happen over that period; and
- iv) a statement of the Directors regarding whether APX continues to satisfy the requirements of paragraph 14 (1)(c);
- c) must have at all time:
 - a) base on the most recent projected cash flows provided to ASIC under paragraph 14(1)(b)(iii), an amount of cash no less than the total of the next six monthly projected cash outflows under:
 - A. paragraphs 14(1)(b)(iii)(A) excluding cash outflows payable to any Service Provider in respect of the administration of APX's affairs and finances; and
 - B. paragraph 14(1)(b)(iii)(B);
 - ii) net tangible assets of an amount that is no less than the projected total cash outflows under paragraph 14(1)(c)(i);
 - iii) an enforceable and unqualified commitment given to APX by an eligible financial provider to pay on demand from time to time to:
 - A. APX, an amount of cash that is sufficient to cover the total projected cash outflows of APX and its Service Providers as calculated under paragraph 14(1)(c)(i); or
 - B. Creditors or to a trustee for creditors of:
 - i) APX; and
 - ii) any Service Provider

an amount for which APX or its Service Provider, to the extent that the cash flows of the Service Provider constitute payments in respect of the administration of APX's affairs and finances, is liable to those creditors at the time of the demand, not exceeding the amount referred to in paragraph 14(1)(c)(i);
- d) as soon as practicable, must give written notice to ASIC if APX or its Service Provider:
 - i) Considers its financial resources are insufficient to meet the requirements of paragraph 14(1)(c); or
 - ii) Fund are called upon to the commitment described in section 13(4) or paragraph 14(1)(c)(iii),



including a description of the circumstances that led to APX or its Service Provider having to give notice to ASIC under this paragraph and the measures, if any, that APX or its Service Provider is taking to obtain the financial resources necessary to meet the requirements of paragraph 14(1)(c); and

- e) must advise ASIC in writing within 10 business days of the commencement or cessation as a Service Provider of APX of:
- i) the Service Provider's name and Australian Company number; and
 - ii) the date of appointment or cessation as the Service Provider; and
 - iii) provide a copy of any agreement between APX and the Service Provider

Relevant to the consideration of the Model, section 4(c) of the APX market licence requires APX to:

- hold an amount of cash no less than the total of the next six monthly projected cash outflows;
- have net tangible assets of an amount that is no less than the total of the next six monthly projected cash outflows; and
- an enforceable and unqualified commitment given to APX by an eligible financial provider to pay on demand from time to time an amount that is no less than the total of the next six monthly projected cash outflows.

The model has significant implications upon the financial circumstances and ongoing viability of APX in the context of the licence conditions.

The first impact of the levy is that APX would be required to have sufficient cash reserves to pay the levy without breaching licence conditions. This would require a cash injection.

The second impact of the levy is that the AIMS Group, as owners of APX, would be required to inject an, at least equivalent, amount of equity capital as cash in accordance with section 14(c)(i).

The third impact of the levy is that the AIMS Group, as owners of APX, would be required to inject an, at least equivalent amount of cash, towards an increased bank guarantee in accordance with section 14(c)(iii) of the licence.

Hence, the direct cost to APX of the proposed levy would be represented by the cash payment of the levy, the equity injection and the bank guarantee.

In addition, the Model proposes the introduction of fees of \$52,000 per change to the operating rules (listing rules and business rules) lodged in accordance with section 793D. APX anticipates that at least two changes per set of rules per year (i.e. four changes per year) would be made. If it is assumed that two changes will occur to each set of rules within any six month period at a cost of \$208,000, there is a combined licencing impact upon APX pursuant to section 14 of the licence of \$624,000.

In combination, the proposed annual levy and the rule amendment fees would have a direct cash impact upon APX.

This is in addition to the existing bank guarantee and cash reserves currently invested to satisfy the licence conditions.



Further, as the cash injection and the cash supporting the bank guarantee cannot be utilized for working capital purposes, the total regulatory reserves represent idle capital which would otherwise be invested in the development of the APX market and the provision of greater competition for market services. That is, capital which other market operators and competitors of APX (other than FEX Group Pty Limited) are not required to commit.

Based upon the fee structure proposed in the Model and applicable to APX, the following table sets out the direct financial impact of the proposal upon APX:

Fee Description	Increase
Annual fee	1,685%
Rule amendments fees⁵	34,666%
TOTAL IMPACT	2,242%
Existing regulatory capital	
TOTAL REGULATORY CAPITAL	220%

As set out above, this will have a significant impact upon the economics of the continued operation of the APX market.

The annual fees payable to ASIC will be the second highest cost incurred by APX behind staffing costs. As the APX market grows, it has been made clear that the ASIC fees will also grow. Hence, we expect that in a short time, the ASIC fees will be the largest single cost incurred by APX to operate its market.

Further, the currently proposed level of fees is of such significance, that the estimated timeframe for APX to satisfy its financial licence conditions, that is, “until APX’s monthly cash flow, or the aggregated monthly cash flows of APX and any Service Provider in respect of the administration of APX’s affairs and finances, is cash flow positive for each of the six consecutive months” has now been substantially extended. Whereas APX could have reasonably expected to have satisfied those conditions, thereby freeing up several million dollars of regulatory capital for investment back into APX and facilitating greater competition, APX will be placed at a considerably extended competitive disadvantage to other market operators. Further, the forecast timeframe for APX to generate operating profits is extended by a similar timeframe and the estimated timeframe to recover the substantial investment over 8 years to date is extended by an even greater timeframe. The impact of the significant increase in unbudgeted expenses and profitability are clearly represented in Figure 1 below⁶.

⁵ Assumes 2 amendments to each of a set of Listing Rules and Operating Rules per annum at \$52,000 per amendment.

⁶ Values have been removed from the vertical axis for commercial confidentiality.

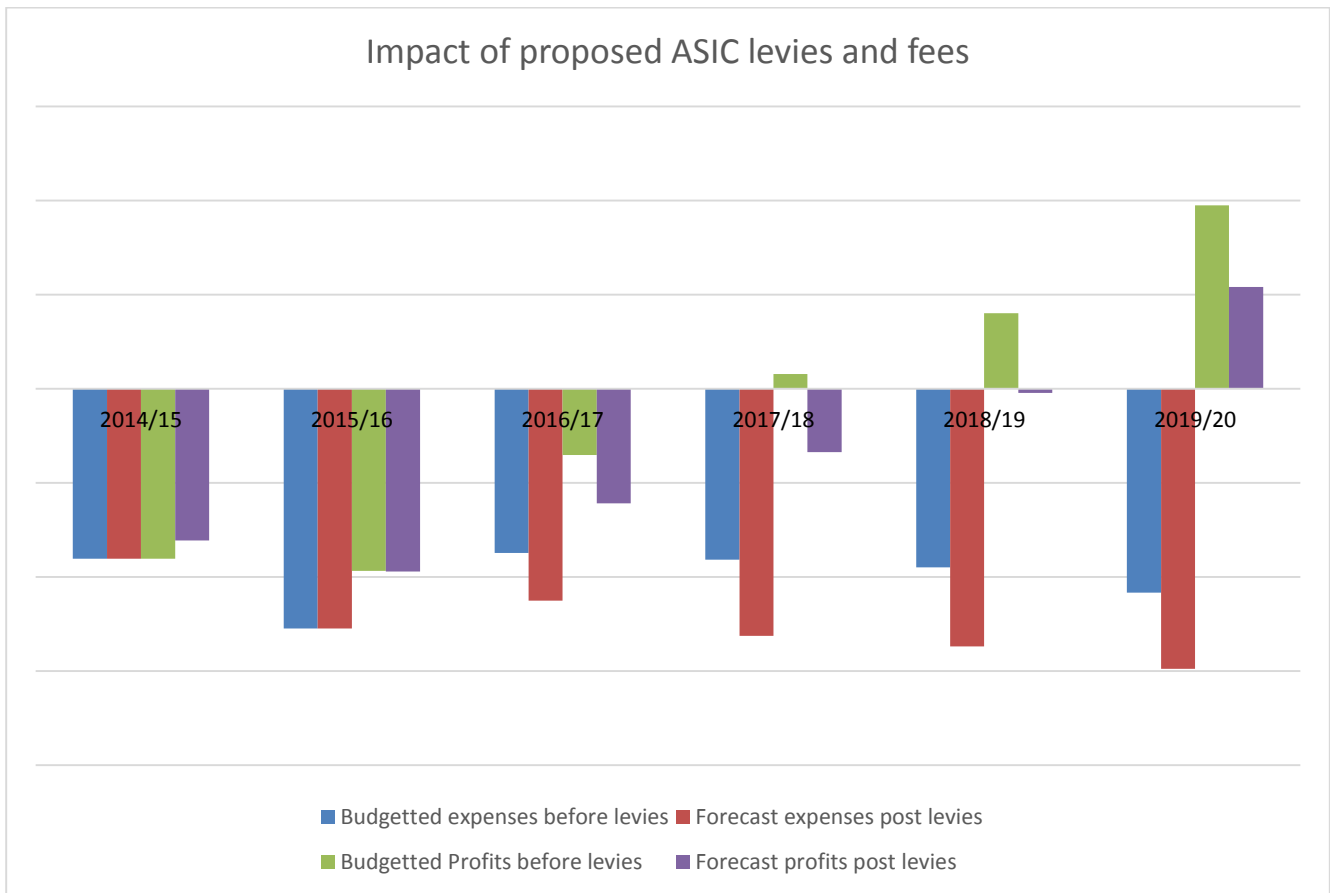


Figure 1 - Impact of proposed ASIC levies and fees

The immediate total cash impact of the proposed fees upon APX would be 50% of the cash impact of the proposed fees upon the largest market operator, notwithstanding that APX has less than 1% market share. From a total regulatory cost perspective, the total cash impact of the proposed fees upon APX in the context of the licencing regime would be 91% of the cash impact of the proposed fees upon the largest market operator, notwithstanding that APX has less than 1% market share.

We strongly submit that it is unrealistic to expect any business, especially during start-up phase against an entrenched monopoly, to incur an increase of over 2,000% in its unbudgeted regulatory cost burden without that cost alone being transformative or terminal.

6.2. Financial impact of the model upon APX operating costs

The APX market commenced operations in March 2014 and is operating on a low cost base. The major costs incurred by APX are staffing and trading system costs.

The Model proposes that the average ASIC related costs to APX would be significant and would represent the second highest cost to APX behind staffing costs and would be higher than technology costs.

As the APX market grows, it has been made clear that the ASIC fees will also grow. Hence, we expect that in a short time, the ASIC fees will be the largest single cost incurred by APX to operate its market.



As a start-up market, APX will not be in a position to pass on the costs. Hence, the ASIC fees will need to be absorbed by APX. This will have major implications for the ongoing financial viability of APX.

6.3. Entrenching the ASX monopoly

APX submits that ASX, as the dominant market operator in Australia, could not have asked for a more favourable proposal than that set out in the Consultation Paper. The proposed fee structure for market operators will have the unintended consequence of entrenching an ASX monopoly on listing and trading services.

In normal commercial operations it would be open to a market operator to pass on the proposed fee impost to its clients. Large markets may well do this. However, as a start-up market, APX will not be in a position to pass on the disproportionate costs to its small customer base of brokers and listed companies. Hence, the ASIC fees will need to be absorbed by APX.

However, given the scale of ASX operations and the ASX balance sheet relative to the scale of operations and balance sheets of its competitors, it would be rational for ASX to not pass on the cost of the ASIC fees to its clients, but to absorb them as a cost of doing business. The impact would be less than 1% of the ASX 2015 reported earnings before interest, tax, depreciation & amortisation (EBITDA). It would also be rational for ASX to not pass on the ASIC costs as a method of putting further cost pressures on any competing market operator which seeks to pass on the costs. This would force competing market operators to absorb the ASIC costs at a time when they are not making profits thereby assisting ASX to force competitors out of the market.

APX notes that Prime Minister Malcolm Turnbull has set out a policy direction “committed to freedom, the individual and the market. It will be focused on ensuring that in the years ahead, as the world becomes more and more competitive, and greater opportunities arise, we are able to take advantage of that. The Australia of the future has to be a nation that is agile, that is innovative, that is creative.”

APX submits that the proposed fees will serve to entrench the ASX monopoly and is anathema to the Prime Minister’s stated policy objective focussed on market behaviours, agility, innovation and creativity.



6.4. Barrier to entry

Based upon the minimal fee structure proposed in the Model and the multiplier effect of the existing anti-competitive ASIC licence conditions, the following table sets out the direct financial impact of the proposal upon a new market entrant:

Fee Description	Minimum scheduled fee amount	Minimum financial impact	Current financial impact	Increase
Year 1				
Licence application fee ^{7,8}	\$210,000	\$210,000	\$1,484	14,150%
Annual fee	\$116,000	\$348,000	\$105,000	330%
Rule amendments fees ⁹	\$52,000	\$624,000	\$1,800	34,666%
TOTAL	\$378,000	\$1,182,000	\$108,284	1,092%
Years 2 onwards				
Annual fee	\$116,000	\$348,000	\$105,000	330%
Rule amendments fees ¹⁰	\$52,000	\$624,000	\$1,800	34,666%
TOTAL	\$168,000	\$972,000	\$106,800	910%

In addition to the leveraged impact of the regulatory fees, there will be the leveraged impact of normal operating costs under the licence conditions.

If it is assumed that the circumstances of APX would apply equally to any new entrant to the sector the impact of the Model would be that any new entrant would be required to assume regulatory cash reserves and resources of at least \$4 to \$5 million in addition to the resources required for working capital. We submit this presents a significant barrier to entry for new competitors and reduces innovation and competition in the Australian market.

⁷ Assumes rule approval is included in the application fee. If not, and extra \$104,000 should be added.

⁸ Assumes the application fee is no subject to the multiplier effect.

⁹ Assumes 2 amendments to each of a set of Listing Rules and Operating Rules per annum at \$52,000 per amendment.

¹⁰ Assumes 2 amendments to each of a set of Listing Rules and Operating Rules per annum at \$52,000 per amendment.



7. Transparency of methodology

The Consultation Paper indicates that the cost of regulating industry in 2016-17 will be \$196 million.

7.1. Apparent inconsistency of estimates

The fees proposals for set out in the Consultation Paper propose to raise fees as follows in the 2016-17 year.

Sector	Fees (\$ million)
Companies	\$53
Credit Licensees	\$24
AFS Licensees	\$91
Registered Liquidators	\$9
Auditors	\$6
Market Infrastructure Providers	\$13
TOTAL	\$196

However, the implementation schedule does not fully recover fees until the 2018-19 year. Owing to the absence of transparency of the modelling contained in the Consultation Paper it is not possible to accurately ascertain what proportion of the full cost recovery is represented by the \$196 million. Further, it would appear from the Consultation Paper¹¹ that fees for Companies, Registered Liquidators and Auditors would not commence until the 2017-18 year. This suggests that the recovery for the 2016-17 year will not be \$196 million. The Consultation Paper indicates¹² that the amount raised in 2016-17 (\$196 million) would be 40% of the cost of regulation and that once fully implemented by 2018-19, the amount raised by ASIC from industry will be 85% of the contribution. This suggests that once fully implemented the amount raised by ASIC from industry will be in the vicinity of \$416 million.

This is despite the Consultation Paper indicating that the cost of regulating industry in 2016-17 will be \$196 million.

It would appear that the methodology in the Consultation Paper is not consistent.

7.2. Transparency and granularity

Notwithstanding this, there is very little transparency or granularity about the methodology adopted for calculating the relevant annual fees and fees for service. We find this very unsatisfactory given the transformative nature the proposals will have upon APX and industry.

From a detailed perspective, we have been informed that the costs attributed to a market operator are based on historical headcount allocations from the Market Infrastructure, Market Surveillance, Participant Supervision, Capital Markets and Enforcement units of ASIC.

APX submits that inclusion of an allocation from Enforcement is not appropriate. This is on the basis that enforcement action is against the Participant or a Listee in relation to a breach of the Market Integrity Rules or the

¹¹ Page 27

¹² Page 28



Act. How or whether a Participant or a Listee breaches the Market Integrity Rules or the Act is outside the control of the market operator. Further, whether ASIC decides to take action and what form of action it decides to take, is totally outside the control of the market operator. In many instances, the market operator has already committed resources (time and cost) to the supervision of that Participant or Listee as first-line supervisor.

To seek to charge the market operator (as the provider of the market infrastructure) for enforcement activity is analogous to seeking to charge a toll road operator for the cost of prosecuting speeding motorists. Like the toll road operator, the market operator does not have control over the behaviour of its users.

Enforcement is a natural element of being a market regulatory agency. It is a public good which provides the stakeholders with confidence in the market. It should not be included in cost recovery.

There is no clarity as to how the costs of the Participant Supervision unit are allocated between market operators when most of those market participants are participants in multiple markets.

For example, BBY Limited was a participant in the ASX, APX and Chi-X markets. The apparent reason for the failure of BBY was as a consequence of activities in the ASX options market. Would the cost of any BBY related ASIC supervisory action be 100% allocated to ASX? Or would it be equally allocated between ASX, APX and Chi-X? Or would it be allocated between ASX, APX and Chi-X on the basis of the percentage of trading executed on each market?

Without greater transparency and granularity of the cost allocation process, industry will be skeptical of the proposed model and resultant charges.

7.3. Sensitivity analysis

It is surprising that the Consultation Paper contains no sensitivity analysis of the potential impact of the new fees.

It is assumed that the new charges will not have an impact on the number of listed companies or on the number of AFSL holders.

As set out below, given the increased cost of listing, APX would expect that the fees will have an adverse impact on the number of listed companies. The impact would be most significant at the smaller capitalisation end of the market. There is no estimate of the extent of the declined revenue upon the revenue estimates.

A similar issue is evident in relation to AFSL holders. It is reasonable to assume that the increased costs will result in a number of AFSL holders relinquishing endorsements on their AFSL or relinquishing their AFSL. There is no estimate of the extent of the declined revenue upon the revenue estimates.

Whilst more difficult to model, for the reasons set out below, the proposed charges are sufficiently transformative that they may actually directly influence a decline in the financial services sector. As a consequence, the revenue stream to ASIC may be drawn from a smaller pool in future years. If this results in the marginal to cost to each remaining participant in the financial service sector increasing as a consequence, the Model may well result in a downward spiral in financial services activity, to the detriment of the national interest. No analysis of the impact has been presented.



8. Barrier to market operator innovation

8.1. Rule amendment fees - quantum

The Consultation Paper proposes a flat fee of \$52,000 for rule amendments lodged pursuant to s793D of the Act.

APX, as a listing and trading market, has established Listing Rule and Business Rules. It is reasonable to assume that each set of Operating Rules will require at least 2 amendments per year. The impact will be \$208,000.

APX appreciates that the current flat fee of \$150 undervalues the work required by ASIC to process the majority of rule amendments and a moderate increase may be desirable. However, the proposal represents an increase of **34,666%**. As the Consultation Paper refers to market operators as “taxpayers”¹³, this can be characterised as a tax increase of 34,666%.

APX was informed that the \$52,000 is based upon the average cost incurred by ASIC in processing rule amendments.

However, the proposed flat fee does not take account of the nature, complexity or drivers of proposed rule amendments.

APX appreciates that some rule amendments driven by business development initiatives (such as the introduction of rules for a new ETF market or for a new derivatives market) will require substantial work by both the market operator and ASIC. However, other changes are less substantive or have different drivers. For example:

- Some rule changes are necessary consequences of other environmental changes:
 - o APX is a trading market utilising the clearing and settlement services of ASX. ASX is proposing to adopt a T+2 settlement regime from March 2016. As a consequence of being an upstream user of ASX services, APX is required to amend both its Listing Rules and Operating Rules. Under the proposed model, each time APX is impacted by a downstream change by ASX it will cost APX \$52,000 or \$104,000;
 - o ASIC has previously approved certain content to be included in the APX Listing Rule Procedures which form part of the APX Listing Rules. Procedures do not require lodgment with ASIC or Ministerial review. ASIC has subsequently reversed its view and demanded that the content now be relocated from the Procedures into the Listing Rules. If the changes were to be introduced under the proposed new pricing regime, the cost to APX would be \$52,000 for changes with which APX does not agree and which have been forced upon it by ASIC.
- Some rules do not involve substantial work. If the T+2 changes referred to above were to be introduced under the proposed new pricing regime the APX Listing Rules amendments, at their simplest, would require a change to 2 words in each set of Rules at a cost of \$26,000 per word.

APX submits that any change to the fee structure should take into account the nature, complexity and drivers of proposed rule amendments.

APX also submits that, as Operating Rules are quasi-legislative in nature (being enforceable under the Act) it is appropriate that they be subject to ASIC scrutiny. However, as Operating Rules are quasi-legislative in nature

¹³ Page 58.



there is a substantial “public good” in them to the extent that they define and protect the integrity of public financial markets. Hence amendments to the Operating Rules should not be subject to substantial fees.

APX submits that, if there is to be a change to the fee structures, Operating Rule amendments should be subject to a tiered fee structure based upon the complexity of the changes. Further work would be required to develop this so there was clear definition of the tiers (frameworks in other jurisdictions may provide guidance).

8.2. Rule amendment fees – innovation barrier

The proposed Operating Rule amendment fees represent a significant barrier to innovation.

APX submits that the proposed charges of \$52,000 will significantly reduce innovation in financial services and regulatory quality.

The Operating Rules of an exchange are not just a regulatory tool. They represent the product or service design specifications of the exchange offerings. They are the mechanism through which exchange and market innovation is delivered.

APX submits that the fees will slow either (or both) the nature of innovation and/or the timing of innovation.

APX acknowledges that rule amendments, being costly for both the market operator and ASIC, should not be progressed without a good business case. However, experience has shown that only a small proportion of innovative new products or services introduced by market operators actually progress to being successful and it is often the case that the products initially considered marginal are those which prove most successful. The magnitude of the fees will further marginalize innovative business cases and thereby further marginalise market development.

APX submits there is a strong argument that, as rule amendments support innovation, they should not be subject to substantial fees.

Alternatively, or in addition, the magnitude of the fees will change market operator behavior and result in unintended consequences. For example, rule amendments which may be distributed throughout a year will be bundled to comprise only one substantial amendment rather than multiple smaller amendments. This will result in change occurring only once per annum and, as multiple initiatives will be bundled into a single package thereby making each initiative contingent on each other initiative, place greater pressure on ASIC resources to address the amendment package in a timely manner.



9. Impact on listed companies

9.1. Listed vs unlisted public company fees

The Consultation Paper proposes the following fees for listed, disclosing public companies:

Table A1: Proposed Levy Arrangements — Public Companies (Listed, Disclosing)

	Number of entities	Minimum Levy (market capitalisation less than or equal to \$20 million)	Levy for each additional \$1 in market capitalisation between \$20 million and \$15 billion	Maximum Levy (market capitalisation more than or equal to \$15 billion)
Public company (listed, disclosing)	2,000	\$6,000	0.000023	\$320,000

By contrast, the Consultation Paper proposes the following fees for unlisted, disclosing public companies:

Table A2: Proposed Levy Arrangements – all other company sub-sectors

	Population	Annual Levy
Public company (non-listed, disclosing)	3,000	\$920

At a roundtable meeting to discuss the Consultation Paper, it was suggested that the fee differential reflects the different levels of risk and work involved in administering listed, disclosing public companies versus unlisted, disclosing public companies.

APX questions this assumption and methodology.

The number of unlisted, disclosing public companies is not dissimilar to the number of listed, disclosing public companies.

There are 2 levels of oversight in relation to listed, disclosing public companies – by the market operator in the first instance and by ASIC in the second instance. Listed public companies are also subject to significant market oversight by investors, media and analysts. In addition, listed public companies are subject of higher levels of disclosure and governance standards. APX therefore submits that the unlisted, disclosing public companies, being subject to lower standards of disclosure and governance but still having similar access to public investment and funding, actually pose the higher risk. As referred to above, if ASIC’s focus is upon industry funding for ASIC’s regulatory activities to establish clear price signals that would influence the behaviour of regulated entities that create the need for government oversight, then the rationale for differential pricing between listed, disclosing public companies and unlisted, disclosing public companies is not consistent.



9.2. Cost of listing

The Consultation Paper proposes the following fees for listed, disclosing public companies:

Table A1: Proposed Levy Arrangements — Public Companies (Listed, Disclosing)

	Number of entities	Minimum Levy (market capitalisation less than or equal to \$20 million)	Levy for each additional \$1 in market capitalisation between \$20 million and \$15 billion	Maximum Levy (market capitalisation more than or equal to \$15 billion)
Public company (listed, disclosing)	2,000	\$6,000	0.000023	\$320,000

The annual fees for listed, disclosing public companies listed on APX are

Value of securities	Annual Listing Fee
\$0 - \$3,000,000	\$10,000
\$3,000,001 - \$10,000,000	\$10,000 + 0.15% over \$3,000,001
\$10,000,001 - \$100,000,000	\$20,500 + 0.017% over \$10,000,001
\$100,000,001 - \$1,000,000,000	\$35,800 + 0.0030% over \$100,000,001
\$1,000,000,001 - \$10,000,000,000	\$62,800 + 0.0010% over \$1,000,000,001
Over \$10,000,000,001	\$152,800 + 0.0003% over \$10,000,000,001 capped at \$300,000

The table below sets out the impact of the proposed fees upon APX listed companies:

Market Capitalisation	APX Fees	ASIC Fees	Increased annual cost of listing in Australia
\$3,000,000	\$10,000	\$6,000	60%
\$10,000,000	\$20,500	\$6,000	29%
\$20,000,000	\$22,200	\$6,000	27%
\$50,000,000	\$27,300	\$6,690	25%
\$100,000,000	\$35,800	\$7,840	22%
\$250,000,000	\$40,300	\$11,290	28%
\$500,000,000	\$47,800	\$17,040	36%
\$1,000,000,000	\$62,800	\$28,540	45%
\$5,000,000,000	\$102,800	\$120,540	117%
\$10,000,000,000	\$152,800	\$235,540	154%

The impact is not dissimilar for other Australian market operators.

In addition, market operators may pass on to listed companies a proportion of the ASIC fees they incur, thereby further increasing the percentage increase in cost experienced by companies listed on the Australian markets.

APX offers the following comments upon the proposed ASIC fee methodology:

- The ASIC fees appear based upon equity capital only. They do not appear to take into consideration other securities such as options, preference shares, convertible notes, etc.
- The ASIC fees do not disclose how dual listed foreign companies would be charged



- The ASIC fees do not disclose how dual listed exempt foreign companies would be charged
- The ASIC fees do not disclose how the fees will be determined for companies suspended from trading on 30 June each year
- Are issuers such as warrant issuers to be included in the fee structure? If so, how? If not, why not?

The consultation paper does not acknowledge the substantial role that listing market operators, such as APX, ASX and NSX play in front line supervision of listed companies. The listing market operators perform the majority of supervision of the continuous disclosure obligations of listed companies. They invest in surveillance systems, qualified staff and resources to support their statutory obligations.

We acknowledge that ASIC enforces the continuous disclosure regime, however, it is hard to see how the cost of enforcement (as represented by the proposed fee scale) is higher than the cost of front line supervision. We therefore question the methodology and assumptions which have been adopted to develop the proposed fee model. The Consultation Paper does not include sufficient detail or transparency to make a meaningful assessment in this regard.

The Consultation Paper states that larger companies pose a higher risk to the Australian economy yet there is no indication as to how this risk is measured and what methodology is adopted. There is no indication or analysis as to how it is determined that the risk posed by listed, disclosing public companies differs to the risk posed by unlisted, disclosing public companies which could equally have a high number of investors and pose a risk to the economy. Practical experience suggests that it is the smaller listed companies which take up more resources to supervise.

The Consultation Paper states that larger companies pose a higher risk and that the fee structure represents ASIC's supervisory intensity, yet the smaller end of the market bears a proportionally high percentage increase in total cost of listing.

10. Competitiveness

10.1. Impact on domestic listings

As outlined above, the proposed fees will result in a 29% to 60% increased cost of listing in the small cap sector (less than \$10 million market capitalisation).

The Consultation Paper includes no impact analysis on how this may impact upon the small cap sector, especially upon cashflow sensitive sectors such as the mining exploration sector. APX expects that increased listing costs will discourage smaller companies from listing. This is at a time when government policy is seeking to promote innovation, small cap investment and ease of access to capital.

It would appear that the potential impact is not consistent with other Government endeavours.



10.2. Impact on international listings

Capital market are increasingly regional and global. Competition for listings is also increasingly regional and global. A decision regarding on which market to list is increasingly a discretionary decision. Companies do not have to list in Australia. They could equally list in Hong Kong, Singapore or any other quality regional market.

The APX business model is very much focused upon capital flows between Australia and Asia. A key element of the business is focused upon attracting Asian listings into Australian markets.

APX submits that the significant increases in the cost of listing in Australia and the resultant decline in international competitiveness, in addition to the proposed market operator fees (which will also have to be passed on to APX listees), will have a significantly detrimental impact upon the business and may result in a rethinking of the role of APX in the Australian market.

10.3. Impact on trading

Whilst listing is an increasingly competitive business internationally, trading is an even more competitive business and trading in Australia is increasingly discretionary.

APX is very concerned that the proposed fee structures, whether the direct fees on AFSL holders or the indirect fees arising from market operators passing the fees to customers, will force large, low margin international brokers to rethink their presence in Australia and potentially relocate their Australian operations to more cost effective jurisdictions such as Hong Kong or Singapore.

The potential offshore relocation will not only reduce trading activity in the Australian market, but will reduce access to capital and reduce the skill-base of the Australian market.

10.4. The “cascade effect”

A notable element of the design of the funding model is the cascade effect of the fees.

ASIC is proposing to levy substantial fees upon market operators and C&S facilities. Each market operator and each C&S facility will pass those fees on to its clients – market participants, clearing participants and settlement participants. But those participants, are largely common participants across all markets. For example, if Participant X is a market participant of ASX, Chi-X and APX and is a clearing participant of ASX Clear and is a settlement participant of ASX Settlement, they are going the cost to the participant will be:

Cost to Participant A = %ASX + % Chi-X + %APX +%ASXClear + %ASXSettlement

Participant A is itself going to be levied by ASIC. Participant X will pass those costs on to its clients.



If Client is a client of, say, 3 brokers (Participants A, B and C), the cost to that client will be:

$$\begin{aligned} \text{Cost to Client X} = & \% \text{Participant A} + \% (\% \text{ASX} + \% \text{Chi-X} + \% \text{APX} + \% \text{ASXClear} + \% \text{ASXSettlement}) \\ & + \% \text{Participant B} + \% (\% \text{ASX} + \% \text{Chi-X} + \% \text{APX} + \% \text{ASXClear} + \% \text{ASXSettlement}) \\ & + \% \text{Participant C} + \% (\% \text{ASX} + \% \text{Chi-X} + \% \text{APX} + \% \text{ASXClear} + \% \text{ASXSettlement}) \end{aligned}$$

The net effect upon clients will be a compounded cost to the end client arising from “taxes” at multiples levels throughout the trade value chain (the “cascade effect”). This is going to significantly increase the cost of financial services in Australia.

In addition, listed companies will not only be levied directly by ASIC but Exchanges may also, to the extent they can, seek to pass on some or all of the ASIC levies imposed upon the Exchange. This will result in increased listing fees resulting in further increased cost to the listed companies and exacerbating the diminished Australian international competitiveness.

10.5. Impact on international competitiveness

As outlined above, markets are increasingly cost conscious and margin conscious. The competition for financial services is increasing within the region. APX is concerned that the proposed fee structures will serve to make Australia uncompetitive in the region.

APX is also concerned that the imposition of the proposed fees sends a message that Australia is not open for business and is comfortable to reinforce the ASX monopoly in the market.

10.6. Impact on competition for listing and trading services

As outlined above, APX believes that the proposals will have a major detrimental impact on competition for the provision of market services in Australia and will reinforce the ASX monopoly in that regard. The proposed fees are business-model changing and could be terminal for some market operators and will serve to entrench the existing ASX monopoly.

APX submits that, for this reason, it is imperative that the Australian Competition and Consumer Commission (ACCC) is consulted on the potential impact of the proposed cost recovery model.

APX has provided a copy of this submission to the ACCC.



11. Alternate models

11.1. Registry operations revenue for funding ASIC

In 2013–14, ASIC received \$347 million in appropriation revenue, incurred operating expenses of \$405 million and raised \$763 million for the Commonwealth in fees and charges¹⁴.

APX is aware of the proposals to sell the ASIC registry business. The registry business is already a user pays based model generating sufficient revenue to fund ASIC to the extent proposed in the Consultation Paper. Based upon the ASIC Annual Report, the registry business would provide ASIC with a self-sustaining source of funding without the introduction of additional fees and charges as proposed.

11.2. Triennial funding stability for ASIC

APX is of the view that one of the major deficiencies in the current ASIC funding model is that appropriation funding is determined on an annual basis, thereby providing no certainty of ongoing appropriation funding.

APX submits that many of the current challenges experienced by ASIC could be overcome by the adoption of a rolling three year appropriation funding model, thereby providing ASIC with three year forward certainty of appropriation funding.

APX submits that to the extent any future funding model relies upon Commonwealth appropriation funding of ASIC, that funding model guarantee three year forward appropriation funding.

11.3. Contract note based funding model

As outlined elsewhere in this submission, the proposed funding model could have terminal impact upon some market operators and potentially upon other segments of the financial services industry. APX acknowledges that some form of industry funding for ASIC is desirable from ASIC's perspective. Hence an alternate model is required.

To the extent that a new funding model is adopted, APX submits that a preferable model is the adoption of an "ASIC levy", introduced in a manner similar to that of the GST. That is, relevant bodies subject to the ASIC levy act as agents for ASIC for the collection of the levy. A levy set at an appropriate basis points level on the value of each trade in the cash equities and the derivatives markets could provide an alternate mechanism for raising the majority of funds sought by ASIC from the markets and stockbroking sectors.

Such a model may be structured such that market operators must levy market participants on a basis points structure for each trade entered into, or reported to, the market. The market participants must then levy clients on the same basis points structure for each contract note issued, with the amount of the levy clearly identified on the

¹⁴ ASIC Annual Report page 24



contract note. The market participant may then claim the amount of the levy paid to the market operator. To the extent that any trade is by the market participant as principle, the market participant would bear the cost of the levy.

A model of this nature makes absolutely transparent to industry and consumers the impact of the ASIC cost recovery model. The reality of the situation is that any fees and charges imposed by ASIC will be passed on to the end consumers. For this reason, it would be preferable that there be transparency of the charges and the impact of the charges.



12. Consultation questions

Chapter 2: ASIC's Activities

1. Do you agree that the exclusion of these activities from cost recovery is appropriate? If not, why not?

APX agrees with the exclusions

2. Are there any other specific regulatory activities undertaken by ASIC, such as those that support innovation, that should not be cost recovered from industry? If so, please provide examples.

As outlined in section 8 above, the proposed fees represent a significant barrier to innovation. The Operating Rules of an exchange are not just a regulatory tool. They represent the product or service design specifications of the exchange offerings. They are the mechanism through which exchange and market innovation is delivered.

APX submits that the fees will slow either (or both) the nature of innovation and/or the timing of innovation.

APX acknowledges that rule amendments, being costly for both the market operator and ASIC, should not be progressed without a good business case. However, experience has shown that only a small proportion of innovative new products or services introduced by market operators actually progress to being successful and it is often the case that the products initially considered marginal are those which prove most successful. The magnitude of the fees will further marginalize innovative business cases and thereby further marginalise market development.

APX submits there is a strong argument that, as rule amendments support innovation, they should not be subject to substantial fees.

Alternatively, or in addition, the magnitude of the fees will change market operator behaviour and result in unintended consequences. For example, rule amendments which may be distributed throughout a year will be bundled to comprise only one substantial amendment rather than multiple smaller amendments. This will result in change occurring only once per annum and, as multiple initiatives will be bundled into a single package thereby making each initiative contingent on each other initiative, place greater pressure on ASIC resources to address the amendment package in a timely manner.

APX also submits that the cost of change to the AMRF should be considered to be a cost of innovation and should not be cost recovered. Refer to Q56 below.

3. Do you support cost recovery arrangements for ASIC's regulatory activities being consolidated within a single ASIC industry funding model? If not, why not?

As set out in section 4, we have noted that the paper does not consult on whether an industry funding model is an appropriate model for the Australian market given its scale and fight for regional relevance. There is an inherent assumption that industry funding is appropriate and the paper then presents a single model.



APX would have preferred to see an initial debate and consultation on appropriate funding methodologies for ASIC and, following that debate, discourse and consultation on a number of different models which may be considered to deliver on that methodology.

We submit that the presentation of a single model is not ideal and there needs to be greater consultation.

- 4 Are there any activities cost recovered by other agencies on ASIC's behalf that should continue to be recovered by the current responsible agency? If so, please give reasons why.

No comment

- 5 The Government currently recovers most of the costs of operating the MoneySmart website through APRA's supervisory levies. Should these costs no longer be recovered from industry? Why or why not?

No comment

- 6 Do you support the SCT continuing to be funded through APRA's levies on APRA-regulated superannuation funds? Why or why not?

No comment

- 7 If the Government decided to introduce an industry funding model for ASIC, would you support not proceeding with the planned review of ASIC's market supervision and competition cost recovery arrangements? Why or why not?

The planned review of market supervision and competition cost recovery should be discontinued if the proposed levies and fees proposed in this broader industry funding model are implemented. To do otherwise would amount to double dipping.

Chapter 3: International funding models

- 8 Are there any approaches to industry funding adopted by other regulators that you believe should be applied to an industry funding model for ASIC? If so, please describe and provide reasons why.

APX submits that analysis should be undertaken and published in relation to the funding models adopted in Singapore and Hong Kong, being the 2 major regional competitors for financial services.

Chapter 4: The proposed industry funding model

- 9 Is the proposed methodology for determining the levy mechanisms appropriate? If not, why not?

As set out above, APX submits that there is insufficient transparency regarding the methodology to make a meaningful assessment as to whether or not it is appropriate.

As set out in sections 0 and 8 above, the methodology of the fees is not appropriate for the reasons set out. Further, it is clear that in developing the methodology, no account had been taken of the multiplier impact of the current inequitable market operator licence obligations referred to in section 0.



- 10 Are there any activities proposed to be recovered through fees that you believe should be collected through annual levies? If so, which activity or activities and why?

No comment

- 11 Is the proposed approach for calculating fees-for-service appropriate? If not, why not?

As set out above, APX submits that there is insufficient transparency regarding the methodology to make a meaningful assessment as to whether or not it is appropriate.

As set out in sections 0 and 8 above, the methodology of the fees is not appropriate for the reasons set out. Further, it is clear that in developing the methodology, no account had been taken of the multiplier impact of the current inequitable market operator licence obligations referred to in section 0.

- 12 Do you have any suggestions for how the proposed methodology for calculating fees-for-service could be modified? If so, please provide details.

Refer section 0 above.

Chapter 5: Determining ASIC's annual funding and levies

- 13 Do you support the proposed process for determining funding for ASIC's regulatory activities under an industry funding model for ASIC? If not, why not?

As referred to above, there is a fundamental governance control absent from the proposal, being independent non-executive Commissioners, especially the Chair of ASIC. Industry does not have insight into the inner workings of ASIC in order to ascertain whether ASIC is "efficiently" implementing its mandate. Industry does not set the ASIC priorities, which in turn drive the funding need.

In addition, any industry funding model should be subject to review by an independent industry panel to scrutinise ASIC budgets and cost drivers to provide transparency and endeavour to avoid or reduce inefficiency arising from otherwise untested or ambit claims for expenditure growth by ASIC.

- 14 Do you think this process will provide industry with certainty as to the fees and levies to be charged? If not, why not?

APX does not believe the proposed model will provide certainty for a number of reasons:

- the absence of three year forward appropriate funding for ASIC;
- fees which are market activity or market capitalisation base will vary from year to year depending on market circumstances. In a worst case scenario, if market activity declines but ASIC determines it requires the same level of funding as the prior year, then the cost per fee-payer will increase at a time when industry may least be able to sustain an increase owing to the market decline.

- 15 Are the proposed consultation arrangements on the levy mechanisms and funding appropriate?

No comment



- 16 Do you support ASIC's fees-for-service being revised every three years? Alternatively, would you prefer that ASIC's fees for service be revised more regularly?

As set out above, APX has a strong objection to the proposed fees for service.

- 17 Do you have any further suggestions for enhancements to be made to ASIC's accountability structure or industry funding model? If so, please provide details.

As referred to above, there is a fundamental governance control absent from the proposal, being independent non-executive Commissioners, especially the Chair of ASIC. Industry does not have insight into the inner workings of ASIC in order to ascertain whether ASIC is "efficiently" implementing its mandate. Industry does not set the ASIC priorities, which in turn drive the funding need.

- 18 How should the Cost Recovery Stakeholder Panel operate? How should the membership be determined?

The Cost Recovery Stakeholder Panel should have a mandate to oversee ASIC and how it justifies its budget demands. Ideally, Cost Recovery Stakeholder Panel would be chaired by a non-executive ASIC Commissioner. Given the potential impact of the proposed levies and fees, the industry panel should have an opportunity to scrutinise what is proposed by the ASIC executive and provide for governance structures around the whole budgeting process. As referred to above, Without the pressure of Government budget constraints, there is a very real risk that ASIC's costs will inflate at a rapid rate simply because someone else is paying. It will also help to provide transparency and endeavour to avoid or reduce inefficiency arising from otherwise untested or ambit claims for expenditure growth by ASIC

Chapter 6: Phase-in arrangements and levy administration

- 19 Are the proposed arrangements for phasing in cost recovery levies appropriate? If not, what alternative approach would you suggest and why?

As outlined above APX believes that the proposals will have a major detrimental impact on competition for the provision of market services in Australia and will reinforce the ASX monopoly in that regard.

The proposition to introduce substantially increased fees for market operators is premature whilst substantive structural issues remain unresolved.

The proposed fees are business-model changing and could be terminal for some market operators and will serve to entrench the existing ASX monopoly.

Notwithstanding the above submissions, if it is determined to proceed with the fees as proposed, in acknowledgement of the potential implications the fees should be phased in over a 5 year period.

- 20 Is it appropriate to set fees to recover ASIC's costs from 1 July 2016? Why or why not?

Refer to question 19

- 21 Are the proposed administration arrangements suitable? If not, why not?

No comment



- 22 Is it appropriate not to levy entities entering the market part way through the year? If not, how do you propose that these entities be treated?
- No comment
- 23 Is it appropriate for the Government handle the over or under collection of levies through a reduction or increase in the levies payable for the next year? If not, why not?
- No comment
- 24 Are additional arrangements necessary to ensure appropriate administration by ASIC of its industry funding model? If so, please provide details.
- No comment

Attachment A – Funding Model for Companies

- 25 Are the proposed arrangements for company levies appropriate? Why or why not?
- Refer to section 10 above.
- 26 Will the proposed levy arrangements for companies be competitively neutral? If not, why not?
- The proposed levies will have a significant impact upon Australia’s ability to attract international business and hence Australia’s competitiveness. Further, it will discourage lower capitalisation companies from listing given the significant (and unwarranted) levy disparity between listed and unlisted public companies as referred to section 10 above.
- 27 Will the proposed levy arrangements for companies support innovation? If not, why not?
- 28 Will the proposed levy arrangements for companies support small business?
If not, why not?
- Refer to section 8 above.
- APX submits that the fee structures will be a significant barrier to innovation in equity markets.
- 29 Do you have any concerns with 31 March being used as the assessment date for determining market capitalisation? If so, why and what date would you prefer?
- No comment

Attachment B – Funding Model for Australian Credit Licensees

- 30 Do you support the proposed arrangements for Australian Credit Licensees’ levies? Why or why not?
- No comment
- 31 Will the proposed levy arrangements for Credit Licensees be competitively neutral? If not, why not?
- No comment
- 32 Will the proposed tiering arrangements support the growth of Credit Licensees? Why or why not?
- No comment



33 Will the proposed levy arrangements for Credit Licensees support innovation? If not, why not?

No comment

34 Will the proposed levy arrangements for Credit Licensees support small business? If not, why not?

No comment

35 Do you believe that a graduated approach to determining the levy payable by credit licensees would be preferable to the proposed levy arrangements? Why or why not?

No comment

Attachment C – Funding Model for AFS Licensees

36 Do you support the proposed arrangements for AFS Licensees' levies? Why or why not?

No comment

37 Will the proposed levy arrangements for AFS licensees be competitively neutral? If not, why not?

No comment

38 Will the proposed tiering arrangements support the growth of AFS Licensees? Why or why not?

No comment

39 Will the proposed levy arrangements for AFS Licensees support innovation? If not, why not?

No comment

40 Will the proposed levy arrangements for AFS Licensees support small business? If not, why not?

No comment

41 Will the proposed levy arrangements for AFS Licensees support access to financial services in regional Australia? If not, why not?

No comment

42 Do you believe that a graduated approach to determining the levy payable by AFS licensees, such as responsible entities and superannuation trustees, would be preferable to the proposed levy arrangements? Why or why not?

No comment

Attachment D – Funding Model for Registered Liquidators

43 Which of the potential levy arrangements for liquidators do you support? Why?

No comment

44 Would any of the proposed levy arrangements for registered liquidators not be competitively neutral? If so, why?

No comment



- 45 Would any of the proposed levy arrangements for registered liquidators have detrimental impacts on small business? If so, why?

No comment

- 46 Would any of the proposed levy arrangements for registered liquidators have detrimental impacts on access to liquidators in regional Australia? If not, why not?

No comment

Attachment E – Funding Model for Auditors

- 47 Are the proposed levy arrangements for auditors appropriate? Why or why not?

No comment

- 48 Is audit fee revenue an appropriate metric for determining the levy payable by entities that audit publicly listed companies? Why or why not? What alternative metric would you support?

No comment

- 49 Will the proposed levy arrangements for auditors be competitively neutral?
If not, why not?

No comment

- 50 Will the proposed levy arrangements for auditors support small business?
If not, why not?

No comment

- 51 Will the proposed levy arrangements for AFS Licensees support access to auditors in regional Australia? If not, why not?

No comment

Attachment F – Funding Model for Market Infrastructure Providers

- 52 Are the proposed levy arrangements for MIPs appropriate? Why or why not?

Refer sections 5 to 0 above

- 53 Will the proposed levy arrangements for MIPs be competitively neutral? If not, why not?

Refer sections 5 to 0 above.

APX submits that ASX, as the dominant market operator in Australia, could not have asked for a more favourable proposal than that set out in the Consultation Paper. The proposed fee structure for market operators will have the unintended consequence of entrenching an ASX monopoly on listing and trading services.

Further, the model cannot be competitively neutral given the inequitable impact of the current licencing framework adopted by ASIC.

APX submits that, for this reason, it is imperative that the Australian Competition and Consumer Commission (ACCC) is consulted on the potential impact of the proposed cost recovery model.



- 54 Will the proposed levy arrangements for MIPs support innovation? If not, why not?

APX submits that, as outlined in section 8, the proposed levy arrangements will have the opposite effect. The arrangements will significantly reduce both innovation and competition.

- 55 Do you prefer an alternative proxy for supervisory intensity on which to determine the levy payable by MIPs? If so, why is this metric more suitable?

The Consultation Paper is not at all transparent in relation to the derivation of “supervisory intensity”. As a “metric”, there is no defined or transparent method of measurement of “supervisory intensity” hence it cannot be considered a metric. Hence it is not possible to make meaningful comment in response to the question.

- 56 Should the costs of maintaining the AMRF be collected from the entity responsible for making the change or from all MIPs through the annual levies? Please give reasons.

APX appreciates the “first mover” challenge referred to in the Consultation Paper. However, as a market averaging a very small number of trades per day relative to that of ASX and Chi-X, APX does not use the AMRF. APX provides data to ASIC by way of spreadsheet on a daily basis. Further, APX has been granted relief by ASIC from having to use AMRF until further notice. On this basis, APX submits it should be exempt from any AMRF charges.

We therefore strongly object to the proposition that APX contributes to the funding of changes proposed by ASX and/or Chi-X from which APX derives no benefit and has no reason or resources to subsidise.

APX is also cognizant that, at the time of the transfer of supervision from ASX to ASIC, ASX received public funding from the National Guarantee Fund for its connection to AMRF.

APX believes that changes to AMRF should be considered to be a cost of innovation and hence should not be cost recovered.

- 57 Should operating rule changes be funded by MIPs through annual levies or on a fee for service basis? Why or why not?

As outlined in section 8 above, the proposed fees represent a significant barrier to innovation. The Operating Rules of an exchange are not just a regulatory tool. They represent the product or service design specifications of the exchange offerings. They are the mechanism through which exchange and market innovation is delivered.

APX submits that the fees will slow either (or both) the nature of innovation and/or the timing of innovation.

APX acknowledges that rule amendments, being costly for both the market operator and ASIC, should not be progressed without a good business case. However, experience has shown that only a small proportion of innovative new products or services introduced by market operators actually progress to being successful and it is often the case that the products initially considered marginal are those which prove most successful. The magnitude of the fees will further marginalize innovative business cases and thereby further marginalise market development.

APX submits there is a strong argument that, as rule amendments support innovation, they should not be subject to substantial fees.



Alternatively, or in addition, the magnitude of the fees will change market operator behaviour and result in unintended consequences. For example, rule amendments which may be distributed throughout a year will be bundled to comprise only one substantial amendment rather than multiple smaller amendments. This will result in change occurring only once per annum and, as multiple initiatives will be bundled into a single package thereby making each initiative contingent on each other initiative, place greater pressure on ASIC resources to address the amendment package in a timely manner.

Refer Question 2 above.

Attachment G – Proposed Fee Schedule

- 58 Are the proposed fee amounts for professional registration, licensing and document compliance review forms appropriate? If not, why not?

No comment

- 59 Do you think that the proposed fee amounts may act as a disincentive for some entities from submitting a professional registration or licence application, or a document for compliance review, with ASIC? If so, why?

No comment

- 60 Do you support the fee payable for applications for relief being tiered based on the complexity of the application? If so, why?

No comment

- 61 Are the proposed fee amounts for applications for relief appropriate? If not, why not?

No comment

- 62 Do you think that the proposed fee amounts may act as a disincentive for some entities from submitting applications for relief with ASIC? If so, why?

No comment

- 63 Would you support the Government only imposing partial cost recovery for applications for limited AFS licences? (See Form P-FS01A and P-FS01B).

No comment

Attachment I – Definitions of industry sectors and subsectors

- 64 Do you agree with the proposed definitions for industry sectors and sub-sectors? If not, why not?

No comment