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Corporations and Schemes Unit
Financial System and Services Division
The Treasury
100 Market Street
Sydney NSW 2000

To Whom it May Concern

Submissions in response to the Consultation Paper regarding the Proposed Industry Funding Model for the Australian Securities and Investments Commission

We set out below our submissions in response to the questions in the Consultation Paper dated 28 August 2015 (**Consultation Paper**) on the Proposed Industry Funding Model for the Australian Securities and Investments Commission (**ASIC**). In preparing these submissions, we have sought to provide our views with respect to:

1. the appropriateness of the proposed industry funding model;
2. the costs and benefits of introducing an industry funding model for ASIC;
3. the impact of the proposed model on competition and innovation; and
4. the regulatory burden associated with the introduction of an industry funding model.

Questions and responses

Chapter 2: ASIC's Activities

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

We agree that the exclusion of the services set out on page 6 of the Consultation Paper is appropriate. We consider that services that are not referable to a particular recipient but which are required for the operation of ASIC or for the promotion of innovation and growth generally are for the good of the nation as a whole, and should not be cost recovered from industry.

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.**

We consider that there are additional regulatory activities undertaken by ASIC that should not be cost recovered from industry.

The list of services set out on page 6 of the Consultation Paper which are identified as being those which will not be cost recovered, consists of narrowly defined services. It does not appear to us to be a comprehensive list of all services that are inappropriate for cost recovery.

services. It does not appear to us to be a comprehensive list of all services that are inappropriate for cost recovery.

On page 6 of the Consultation Paper, the view is expressed that it is “usually not appropriate to cost recover some government activities, such as general policy development and ministerial support”. The Consultation Paper does not explain why it is not appropriate to cost recover those government activities, but the examples provided suggest that it is due to those activities being important for the promotion of innovation and growth, which are for the good of the nation as a whole.

Given the nature of the policy that appears to underpin the list on page 6 of the Consultation Paper, we would expect that list to be more comprehensive.

On page 15 of the Consultation Paper there is a list of matters in respect of which it is proposed that a levy will be used to recover ASIC’s costs. That list is as follows:

- (a) undertaking surveillance (which includes front-line supervision);
- (b) enforcing the law;
- (c) providing guidance;
- (d) developing advice for the Government;
- (e) engaging with stakeholders; and
- (f) certain activities in relation to educating consumers and investors.

These matters are important for innovation and growth, and are not referable to a particular entity. For those reasons, we consider that they are not appropriate targets for cost recovery. They should be either paid for by the Commonwealth Government out of consolidated revenue, or they should be recovered by using fines for non-compliance.

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?

We support the cost recovery arrangements for ASIC’s regulatory activities being consolidated within a single ASIC industry funding model, provided that the model that is adopted increases efficiencies, and fairly and reasonably allocates cost recovery so as to promote competition, innovation and growth.

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.

It is not possible to give a definitive answer to this question with the information provided in the Consultation Paper, as it does not set out sufficient detail with respect to the costs currently recovered by the relevant responsible agencies.

However, we consider that the most efficient model should be adopted. If a new model were adopted whereby ASIC were to recover costs that are currently recovered by other agencies and that would increase efficiencies and decrease waste, we would give our in-principle support to that model.

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?**

No comment.

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.**

No comment.

Chapter 4: The proposed industry funding model

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

The proposed methodology for determining the levy mechanisms appears to be appropriate, although we note that no alternative methods are explained.

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?**

There are no activities proposed to be recovered through fees that we believe should be collected through annual levies.

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

We agree that a fee-for-service approach is generally appropriate and that it should be strictly applied in some circumstances.

However, in other circumstances, we consider that some fees should be subsidised by ASIC, even where the fee is for a specific service on the request of a specific organisation. Subsidising particular fees will assist with the following:

- (a) promotion of innovation;
- (b) growth of small companies with no material revenue into productive companies;
- (c) somewhat counterintuitively, reduced costs for ASIC.

Specifically, we note the proposed fees for applications for relief are excessive. Many applications for relief are made by companies seeking to reduce their regulatory

burden. To increase the costs for making an application for relief creates a deterrent for those companies to seek relief, and increases their regulatory burden.

We would suggest that if applications for relief are regularly being made in a particular area, that there is some need for wider policy review. If applications for relief are not made, then ASIC will not be aware of the need for policy review.

This problem becomes more acute with respect to applications for novel relief, which are proposed to be costed at the prohibitively high fee of \$21,000 each. If this fee were imposed, only companies with large balance sheets would be able to afford to apply for relief. Smaller companies would suffer as regulation that applies to them would not be reviewed as frequently by ASIC, and larger companies would have even more competitive advantage.

More generally, we note that small companies without material revenue are often particularly cost-sensitive. Any increase to ASIC's fees represent an increase to fixed costs that must result in reduced expenditure elsewhere. Other than to reduce research costs, development costs or exploration costs, other variable costs that may be reduced include legal expenditure. With less expenditure on legal costs, we expect that companies will do more of their own document preparation, leading to documents of poorer quality. Furthermore, it is likely that lawyers will not be able to afford to spend the time required to produce quality documents.

It is in ASIC's interests to promote the high quality of disclosure and other documents at the drafting stage, as detailed review and amendment or replacement add to ASIC's costs, and to the costs of industry.

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

Yes, we consider that the proposed methodology for calculating fees for services should be reviewed to:

- (a) subsidise the fees for services that promote innovation and productivity; and
- (b) decrease fees for services that represent part of the "fixed costs" of all companies.

For the reasons more fully set out in our response to question 11 above, we consider the fees for relief applications to be excessive and that at the proposed levels they will increase the regulatory burden, particularly on small companies, and that they will decrease the perceived need for policy review over time.

Some of the services for which there is a proposed fixed fee are services that are required by all companies, such as approval for related party benefits (increased from \$37 to \$1,000), supplementary disclosure documents (increased from nil to \$1,600), and replacement prospectuses (increased from nil to \$1,600). For a small company, these amounts can represent a large proportion of operating expenses.

Consider a small listed company whose business is in exploration for minerals (**Exploration Co**). Exploration Co has no material revenue, but has exploration expenditure of \$2,000,000 per year and typically reports a net loss of \$2,500,000 per year.

To fund its operations, Exploration Co has one rights issue per year (**Rights Issue**). Currently, that rights issue to raise \$2,500,000 costs Exploration Co approximately \$200,000, comprising the following:

- (a) underwriting costs – \$100,000 (4% of underwritten amount);

- (b) lead manager costs – \$50,000 (2% of underwritten amount);
- (c) legal costs – \$12,500;
- (d) ASIC prospectus lodgement fee – \$2,320;
- (e) ASIC fee for relief under section 655A of the Corporations Act – \$1,154;
- (f) ASIC fee for approval of foreign nominee – \$625;
- (g) ASX listing fees – \$9,045;
- (h) foreign nominee for ineligible shareholders – \$4,000; and
- (i) postage and printing costs – \$20,000.

The Rights Issue comprises approximately 8% of Exploration Co's annual expenditure, not including the effect on the share price of Exploration Co, which would be likely to make the following year's Rights Issue more dilutive.

Further increases to ASIC's costs, such as to the application for relief (increased from \$1,154 to \$6,500), to the lodgement costs (which could be \$1,600 or more depending on whether or not supplementary or replacement documents are required), and the imposition of an annual levy of at least \$6,000, would increase the amount spent by Exploration Co on fixed costs by approximately \$10,000-\$12,000 per year.

The increased cost recovery by ASIC from Exploration Co will be dealt with by Exploration Co by reducing expenditure on:

- (a) research, development and exploration, which will reduce economic growth; and
- (b) services such as legal, accounting and auditing costs, which will reduce document quality and disclosure standards, and will ultimately add to ASIC's regulatory burden.

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?**

No comment.

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

No comment.

- 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?**

No comment.

- 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.**

We have a further suggestion for enhancement for ASIC's proposed industry funding model.

In addition to our concerns set out above with respect to the fees-for-service aspect of the proposed model, we have a concern with respect to the size of the proposed annual levy for small listed companies.

Many small listed companies without any material revenue, such mineral exploration companies, are exposed to the proposed significant increase in the annual levy. Those companies have no revenue to absorb the increase and no capacity to pass the cost onto any customer. Generally speaking, many other companies such as industrials and financial service providers do have some capacity to pass the cost onto customers.

The service which ASIC provides is for the general benefit of the economy and the community generally, not just the companies themselves. It seems inequitable that small listed companies, which is a group that includes many mineral exploration companies, appears to be being hit with a very large increase relative to their size, in circumstances where that sector must simply absorb that cost, whereas other "users" can to some extent share the cost .

If the mandatory annual levy is to be even partially "user pays" there should be proper justification that the actual users are paying only for a fair share in an equitable manner.

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

No comment.

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?**

No comment.

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

No comment.

- 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?

No, we do not consider that the proposed levy arrangement for companies to be appropriate.

We have a concern with respect to the size of the proposed annual levy for small listed companies.

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The service which ASIC provides is for the general benefit of the economy and the community generally, not just the companies themselves. It seems inequitable that small listed companies, which is a group that includes many mineral exploration companies, appears to be being hit with a very large increase relative to their size, in circumstances where that sector must simply absorb that cost, whereas other “users” can to some extent share the cost.

It is not apparent to us that the annual fee of \$6,000 payable by a small listed company with a market capitalisation of under \$20 million is able to be justified on a “user pays” basis. This fee compares to:

- (a) the current annual fee of \$1,161;
- (b) the proposed annual fee for a public listed company with a market cap of say \$100 million – \$7,840;
- (c) the proposed annual fee for an unlisted public company which is a disclosing entity (ie. not listed on ASX but still has to give continuous disclosure because it has raised money from the public) – \$920; and
- (d) the proposed annual fee for a large unlisted public company, including ones generating revenue in the many millions – \$350.

All of the above companies must lodge audited annual and half-yearly financial statements and reports with ASIC and it would seem unfair that a small junior listed company generating no revenue should automatically be required to pay a substantially higher fee than a large proprietary company or a large unlisted public company.

If a higher annual fee is justified for disclosing entities then that justification is not explained and is inconsistent with the proposal that unlisted companies with are disclosing entities are to pay an annual fee of only \$920.

If the mandatory annual levy is be even partially “user pays” there should be proper justification that the actual users are paying only for a fair share in an equitable manner.

26. Will the proposed levy arrangements for companies be competitively neutral? If not, why not?

No, the proposed levies will not be competitively neutral. This is because the levies are based on market capitalisation, and not revenue, and so do not only have the potential to make up a large proportion of smaller companies' revenue than of larger companies, but in addition, smaller companies without material revenue have no way of passing on the costs to consumers. Those smaller companies will be at a competitive disadvantage compared with their larger peers.

27. Will the proposed levy arrangements for companies support innovation? If not, why not?

No, the proposed levy arrangements will not support innovation. For many companies, the levies will represent an increase in their fixed costs, which will be recovered through decreased expenditure on other goods and services, including those that would support innovation. We note that many of the fees that will be abolished with the introduction of the annual levy (as set out in Attachment H to the Consultation Paper) are small and not applicable to the majority of companies. To abolish fees that a company was not previously paying and then impose an annual levy in their place will decrease that company's funds available for expenditure on innovation.

28. Will the proposed levy arrangements for companies support small business? If not, why not?

The proposed levy arrangements may or may not support small business, depending on the kind of small business that is being considered. For small proprietary limited companies that would pay an annual levy of only \$5, there will likely be very little difference to their competitiveness. However, for a small listed mining company with little revenue, there may be a significant decrease in competitiveness.

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. Whilst we agree with the distinction drawn between credit providers and intermediaries, we question the underlying assumption to the proposed arrangements in that in this sector risk is a function of the amount of the credit advanced or the number of clients of the credit business. In our view, the risk profile of a small amount (eg. formerly payday) lender servicing a typically vulnerable client base who cannot obtain credit from financial institutions may differ markedly from a larger credit provider with established and well resourced internal compliance frameworks. In many respects, the smaller lender is more likely to require ASIC resources to be expended.

31. Will the proposed levy arrangements for Credit Licensees be competitively neutral? If not, why not?

No, for the reasons set out in our answer to question 30.

32. Will the proposed tiering arrangements support the growth of Credit Licensees? Why or why not?

Without expressing a view on this, we question why the growth of Credit Licensees (and by logical implication, the growth of Australian household debt) is considered to be a desirable policy outcome.

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

There would not appear to be any reason to suggest that the proposed levy arrangements for Credit Licensees support innovation.

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. Once again, we question the underlying assumption to the proposed arrangements in that in this sector risk is a function of the amount of the credit advanced. From a regulatory perspective the small and medium amount loan contracts and the lending to clients with a poor credit history preventing them from borrowing large amount so of credit are highly likely to require ASIC resources to be expended.

Attachment C – Funding Model for AFS Licensees

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

We question the underlying assumption to the proposed arrangements in that in this sector risk is a function of the number of authorisations held. Whilst it is not apparent from the Consultation Paper what is meant by "number" in this regard, we have inferred from the examples provided that each class of product listed against a financial service authorisation (such as "dealing" or "advice" for example) is being classed as a single authorisation.

We are generally supportive of a model to the extent that it recognises the inherent differences between the risk profile associated with the broad classifications of licence authorisations relating to financial services, with advice having a higher regulatory risk profile than dealing (for example), personal advice having a far higher regulatory risk than general advice. Operating a registered scheme would be another example of a broad category of financial service having high regulatory risk. Overlaying this, there would be a different regulatory risk profile associated with different financial products in relation to which such financial services are provided. Complex products such as derivatives and managed investment products would have a high regulatory risk profile, more generally understood products such as general insurance and basic deposit products would have a much lower regulatory risk profile.

The model as set out in the Table C1 figure (Overview of Tiering Methodology), whilst headed according to "Authorisation" appears to be more industry based rather than reflecting the actual underlying licence authorisations of the participants in each industry. In some cases the risk profile of the participants within the same industry will vary greatly depending on the particular class of product authorisations held – for

example a financial planner who advises on derivatives has a much higher profile than one who advises on less complex investment products.

We fail to understand in particular why the Consultation Paper does not appear to distinguish between general insurance products and life insurance products, which from an advice perspective have completely different regulatory risk profiles.

We also make the observation that in the course of our practice, we have seen some examples of what we would regard as high risk licensees who do not hold the correct authorisations to perform the financial services that they are providing and are apparently not aware of this fact. Under the proposed system as depicted in figure C1, they would pay a lower levy than a compliant licensee yet be far more likely to require regulatory attention from ASIC.

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

No comment.

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

No comment.

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

No comment.

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

No comment.

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

No comment.

41. 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?

There is insufficient detail on this proposed model in the Consultation Paper for us to form a view in this regard. Given the diversity of the managed investment sector however, query whether a model that groups all responsible entities together without recognising the different risk profiles of the different managed investment sectors (listed share trusts for example, compared to agribusiness schemes, for example) is the appropriate approach in the circumstances.

Attachment D – Funding Model for Registered Liquidators

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

No comment.

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

No comment.

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

No comment.

- 45. 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

- 46. Are the proposed levy arrangements for auditors appropriate? Why or why not?**

No comment.

- 47. 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.

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

No comment.

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

No comment.

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

Attachment F – Funding Model for Market Infrastructure Providers

- 51. Are the proposed levy arrangements for MIPs appropriate? Why or why not?**

No comment.

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

No comment.

- 53. Will the proposed levy arrangements for MIPs support innovation? If not, why not?**

No comment.

- 54. 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?**

No comment.

- 55. 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.**

No comment.

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

No comment.

Attachment G – Proposed Fee Schedule

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

We consider that the proposed fee amounts to be generally appropriate, but make the following observations which have largely been explained in our responses to other questions:

- (a) Some fees will directly increase regulatory burden and decrease efficiencies and policy innovation. For example, the proposed increases for applications for relief.
- (b) Some fees represent the fixed costs of the smallest listed companies and have been increased significantly. These costs include the costs for supplementary and replacement prospectuses, relief applications and approvals for related party transactions.
- (c) Some fees are proposed to be increased to levels that are very high and may represent a barrier to entry to some industries, which will decrease competitiveness, innovation, and ultimately efficiency. For example, we note the proposed fee for an Australian trade repository licence (\$210,000), registration as a liquidator (to increase from \$366 to \$8,800), for an Australian markets licence application (to increase from \$1,484 to \$210,000), and an Australian clearing and settlement facility licence application (to increase from \$1,484 to \$210,000).

- 58. 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?**

Yes, we consider that the proposed fees for some items will constitute a disincentive for the acquisition of those services. For example, often a relief application will be made to reduce regulatory burden and it is a matter of small degree that that the application is made. An increase in the cost of making an application will result in fewer relief applications being made.

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

No, we consider that sometimes complex applications highlight the need for more in-depth regulatory change. With increased application costs, applications for complex relief will become more rare, and as a result the need for policy change will be unknown.

60. Are the proposed fee amounts for applications for relief appropriate? If not, why not?

No, the proposed fee amounts for applications for relief are far too high. Applications for relief are a service that we consider should be subsidised as they are at the coal face of reducing regulatory burden; an end which they achieve on a micro-scale (being with respect to the particular application and particular company) and also on a macro-scale, as they can be the means of highlighting a need for reform that would otherwise go unnoticed.

61. 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?

Yes, we consider that the proposed fee amounts may constitute a disincentive for some companies submitting applications for relief with ASIC. Many relief applications are made to reduce the regulatory burden of a company. They may not save that company a large amount of money on a one-off basis, and so even a small increase in their cost may deter companies from applying. A decrease in the number of relief applications would, over the long term, decrease the perceived need for regulatory review. This would allow inefficiencies to become engrained.

62. 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

63. Do you agree with the proposed definitions for industry sectors and subsectors? If not, why not?

No comment.

Yours faithfully



Jackson McDonald