AFMA

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Australian Securities and Investments Commission
100 Market Street
Sydney NSW 2000

By email: policy.submissions@asic.gov.au

Dear ASIC Team

Cost Recovery Implementation Statement: ASIC industry funding model (2021–22)

The Australian Financial Markets Association (AFMA) welcomes the opportunity to comment to ASIC on the Cost Recovery Implementation Statement (CRIS) that outlines the ASIC industry funding model for 2021-22. With our membership of over 120 financial services firms, AFMA represents a wide spectrum of financial market participants operating in Australia that are subject to ASIC's cost recovery fees and levies. These include banks, stockbrokers, dealers, market makers, market infrastructure providers and treasury corporations.

The starting point in commentary on the CRIS is that the ASIC Cost Recovery model is flawed. While it is a matter for Government policy beyond the scope of this consultation, AFMA restates here for the record our fundamental disagreement with this process. Moral hazard is a significant problem in the design of cost recovery arrangements. The structures for these arrangements present little incentive for government to keep costs low or efficient, as these costs are passed onto the invoiced entities. Moreover, governments have paid little attention to the cumulative burden of ad hoc increases in cost recovery levies and also have failed to recognise that the primary beneficiary of regulation is the public, whose interests can in effect only be reflected in a government contribution to regulator funding.

Cost recovery arrangements should recognise the mix of private and public benefits flowing from regulation. This should be reflected in a mix of cost recovery and public funding through the budget. Cost recovery has justification where the benefits are exclusively or predominately private benefits. While recovering costs from users reduces the financial burden on the broader community, it is crucial that those who actually receive the benefit are targeted and intermediaries and other incidental actors are not targeted merely because they provide convenient revenue collection points from a government administration perspective. While there may be challenges in quantifying the mix of private versus public benefits, this should not be seen as precluding a mix of cost recovery and public funding given that full cost recovery also often involves subjective judgements about a regulator's efficient costs and the risks and effort associated with the regulated activity. Partial cost recovery coupled with government funding can strike a better balance where there are significant public benefits from regulation, even if these may be difficult to quantify.

Another long-standing issue we continue to point out is that cost recovery for ASIC's Enforcement Special Account (ESA) is unfair, as it charges the cost of an enforcement action against a particular person to all of the regulated entities in the relevant segment of the industry. Moreover, industry should not be charged for the recovery of enforcement costs where ASIC is unsuccessful in an action, or where ASIC already receives monies from entities involved in an enforcement action to cover the cost of its related investigation and action.

More generally, the mapping of regulator costs to the regulated community is imperfect and creates distortions and inequity, particularly where the cost burden is poorly calibrated to regulatory risk. Significant variances in the estimated and actual costs over time continue to arise. The market intermediary charges were put in place to enable market competition, yet the charges for messages came close to preventing the establishment of competition. These charges have also been a factor in the withdrawal of some significant participants from certain local markets, and subsequent reductions in liquidity. Through their volatility and increases over time they continue to create significant business challenges that should be addressed through a redesign of the charging system.

Volatile costs for the Intermediaries sector

ASIC's cost recovery arrangements continue to produce volatile cost fluctuations for investors and intermediaries each year. We note this time around that large OTC Traders are seeing their levy per FTE staff engaged in OTC trading activity jump from $4,362 in last year's assessment to $7,396 in the current CRIS. This close to doubling is unexpected and enormous by any measure.

Such unpredictability creates significant challenges for intermediaries providing services in the sector and ultimately increases costs further for investors. The current claw back cost model based on actual costs incurred by ASIC causes uncertainty and a lack of timeliness for market participants. Levies for different market activity varies from year to year and there is always a variance from the indicative look forward levy and the actual levy.

For intermediary firms that bill investors on an accrual basis these fluctuations can cause investors to receive large and unexpected bills for transactions well beyond the financial year in which they were incurred. For intermediaries bearing the charges, these are large unbudgeted expenses. The potential for large unbudgeted expenses creates pricing pressures that are not in the interest of investors. The invoicing of market intermediaries in March for the previous financial year ending on 30 June is fundamentally problematic from a commercial perspective as by then, the financial expenses for previous financial year would have been offset from revenue. Getting the invoice so late results in participants having to accrue expenses which is not keeping with good business practice. This fundamentally demonstrates that the levy system is designed around the needs of government bureaucracy and not the needs of the financial market community for which it exists and is meant to serve.

We note also in passing that the CRIS provides little visibility into the use of funds or investment raised from the industry for enforcement activities. These enforcement activities are a major reason for the large variances between estimated and actual costs. The explanations provided by ASIC in relation to them do not provide significant insight into where these costs are incurred.

OTC trader count methodology

A key priority for the industry is to resolve the uncertainties around the OTC trader metric used in calculating cost recovery allocations. For a fair distribution of substantial costs for the industry it is important that there is a widespread common understanding of the application of the OTC trader count methodology. This area of concern has been raised by us with ASIC over a number of years. In this regard, AFMA notes the separate recent communication between ASIC and us about the need to take this issue forward.

There currently is a lack of certainty around the intended application of the definition, particularly in relation to staff that might work for two or more entities, and staff that may execute occasional bookings to an entity where this activity is not ordinarily carried out by them.

AFMA understands that the OTC Trader metric currently could potentially be read on a technical basis to include overseas staff working on foreign listed markets, such as US Cash Equities and Futures as only Australian listed markets have been excluded from the OTC Trader metric. The industry is of the understanding that this is not the intent of the metric. For clarity we would request that both domestic and international listed markets be explicitly excluded from this headcount metric. This clarity would be appreciated and aid consistency on approach across our members.

Please contact David Love either on 02 9776 7995 or by email at dlove@afma.com.au in regard to this letter.

Yours sincerely

David Love

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