

7 November 2022

Senior Adviser
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: ASICIFMReview@treasury.gov.au

Dear Ms Bhan,

ASIC Industry Funding Model Review discussion paper

CPA Australia represents the diverse interests of more than 170,000 members, working in over 100 countries and regions around the world. We make this submission on behalf of our members and in the broader public interest.

The stated objectives for the ASIC Industry Funding Model (IFM) are that it will:

- (a) ensure that the costs of the regulatory activities undertaken by ASIC are borne by those creating the need for regulation, rather than Australian taxpayers;
- (b) establish price signals in the way resources are allocated within ASIC;
- (c) provide economic incentives to drive the Government's desired regulatory outcomes for the financial system;
- (d) provide greater stability and certainty in ASIC's funding and ensures that ASIC is adequately resourced to carry out our regulatory mandate; and
- (e) improve ASIC's cost transparency and accountability to industry.

However, we question if the ASIC IFM, in its current form, meets these objectives. In particular:

- The retrospective nature of the IFM results in the current participants, in a given sector, being levied for past regulatory and enforcement activities that covered participants who may or have been unlicensed, unregulated or may no longer be part of the sector. That is, the IFM does not reflect the current composition of the sector and its participants who make financial contributions to it.

This is particularly acute in the financial advice sector. The majority of the large institutional Australian Financial Services (AFS) Licensees have ceased to provide retail financial advice yet continue to be subject to historical enforcement activities. The costs of these historical enforcement activities are borne by the remaining AFS licensees who are predominantly small to medium sized businesses.

- The cost of enforcement activity against unlicensed operators appears to be borne by those who are appropriately licenced, which is arguably inconsistent with Section 10(4) of the ASIC Supervisory Cost Recovery Levy Act 2017.
- There has been a significant increase in regulatory and enforcement costs across some sectors, such as the financial advice sector, whilst at the same time there has been a considerable reduction in the number of participants paying the ASIC levy. This means that fewer numbers of participants are each paying higher levies to cover the overall increasing total cost of enforcement, regulation and oversight.

- Ongoing regulatory reform in many sectors is expected to increase ASIC's costs further, which under the current IFM will add further upward pressure on the levies borne by these sectors.
- Indirect costs make up a disproportionate amount of the total operating expenditure of regulatory costs, averaging up to 40 per cent each year. The lack of transparency with respect to these costs means that industry participants may be covering some general and administrative costs that are unrelated to ASIC's regulatory and oversight functions. This is particularly evident with the financial advice sector's indirect costs increasing significantly at the same time that enforcement costs have also risen significantly.
- Enforcement penalties and fines are not recoverable by the sectors paying for the cost of the action and cost recoveries that do go back into the pool rarely offset the cost of enforcement activity borne by ASIC in those sectors.
- The significant delays between ASIC levy estimates being provided and the final levies being announced each year, coupled with the significant variations between the estimated levies and the final levies charged, makes it extremely difficult for participants to accurately budget for their ASIC levies and to set adequate fees for their clients to recoup these costs.
- There are no clear indicators or metrics published on ASIC's effectiveness. In a system where ASIC is able to fully recover its regulatory costs there is no clear incentive for ASIC to reduce regulatory costs, drive efficiencies and improve regulatory outcomes.

To address the concerns raised above and to increase the likelihood the ASIC IFM will meet its objectives, CPA Australia makes the following recommendations.

- Enforcement costs be separated from ASIC's day to day or 'business as usual' (BAU) regulatory costs and instead be attributed to and, where possible, recovered from the entities to which the enforcement activity directly relates
- All proceeds from enforcement action, including fines, civil and criminal penalties, should be allocated to the ASIC Enforcement Special Account and attributed to the relevant sector to offset enforcement costs
- The cost of regulating unlicensed or unregulated activities or activities relating to entities that are no longer regulated entities should be recovered from them, where possible, and not from regulated sub-sectors
- Transition to a forward-looking forecast annual levy, based on expected budget, with any adjustments made in the following year based on actuals
- ASIC's capital expenditure costs should be borne by the Government
- A single Cost Recovery Implementation Statement (CRIS) be issued before the commencement of the financial year, to assist sector participants in their budgeting purposes, and that any material variances are carried over to the next financial year
- The Government commissions a review by the Australian National Audit Office (ANAO) of how ASIC allocates costs between sectors and sub-sectors, the steps ASIC takes to ensure its regulatory activities are efficient and cost-effective, and how ASIC is held to account to ensure its regulatory activities are efficient and cost-effective
- There are no changes to the current design, structure or legislative framework for fees-for-service until after the above-mentioned review is completed.

Our responses to the discussion paper questions are included in the **Attachment**.

If you have any queries regarding CPA Australia's ongoing engagement on these matters, please contact Michael Davison, Senior Manager, Advocacy and Retirement Policy on 0422 939 957 or michael.davison@cpaaustralia.com.au.

Yours sincerely,

Dr Gary Pflugrath
Executive General Manager
Policy and Advocacy

Attachment

Following are our responses to the questions raised in the discussion paper.

Key features of levies

1. Appendix D provides a catalogue of sub-sector definitions, metrics and formulas. If the status quo remains (that is, there are no substantial changes to the IFM framework), are any changes required to ensure the existing industry sub-sectors, levy formulas and entity metrics remain fit for purpose in the longer-term and/or can respond to changes within industry sub-sectors?

Note: Changes to sub-sector definitions, formulas and metrics would change the way levies are calculated and distributed amongst entities in a sub-sector and would impact the levy amounts for individual entities but would not change the total amount recovered from the relevant sub-sector.

2. Do stakeholders understand ASIC's methodology for allocating costs of activities that impact multiple sub-sectors? Is the current level of transparency relating to this approach appropriate?

The retrospective nature of the IFM results in the current participants in a sector being levied for past regulatory and enforcement activities against participants who may be unlicensed (or have been), unregulated or may no longer be part of the sector and thus do not contribute towards ASIC funding.

This is particularly acute in the financial advice sector. The majority of the large institutional AFS Licensees have ceased to provide retail financial advice yet continue to be subject to historical enforcement activities. The costs of these historical enforcement activities are borne by the remaining AFS licensees who are predominantly small to medium sized businesses.

We do not believe this is fair, equitable or fit for purpose. It is inconsistent with the policy intent of the IFM and the overarching principle of the Government Charging Framework that those entities that cause the need for regulation should generally pay for it.

Principles for levies

3. Is it more important to have a simpler model that can be more readily understood by entities and administered by ASIC which may result in increased cross-subsidisation, or a more equitable model (similar to the status quo) that closely links the recovery of costs to the groups of entities causing the need for those costs?
4. Is cross-subsidising costs for entities within a sub-sector or sector more appropriate than cross-subsidising costs across all of ASIC's regulated population? If so, why?
5. Are there other opportunities to simplify the design, structure and legislative framework for levies? If so, what opportunities and what benefits would they provide?

We do not believe there should be a trade-off between simplicity and equity. The different entities in the regulated populations and the structural differences between sectors mean ASIC's remit is inherently complex. Given the retrospective nature of the IFM, we do not believe it is possible to simplify cost recovery in a way that would be equitable or fair to all participants when current participants bear the cost for past regulatory activity. The IFM should provide certainty, transparency and accountability.

As further elaborated in our response to question 8 below, a significant component of the year-on-year variance in the levies is enforcement costs. Separating enforcement costs from ASIC's day to day or BAU regulatory activity, and ensuring enforcement costs are recovered from the entities responsible, would result in much more stable and predictable annual regulatory costs. More predictable annual costs could then facilitate a shift to a forward-looking forecast annual levy based on an expected budget with any adjustments made in the following year based on actuals.

6. Does the design, structure and legislative framework of the levy component of the IFM have sufficient flexibility to respond to changes in markets, sectors and products ASIC has oversight of? If not, what aspects require more flexibility and what changes could be made?

No. The IFM does not have the flexibility to respond to significant structural change within a sector. As mentioned previously, the retrospective nature of the IFM results in new and current sector participants paying for the regulatory activities directed at past participants who are no longer regulated.

Key issues related to levies

7. How can costs associated with enforcement activity be recovered most equitably? What changes could be made to the current approach, and what benefits would they provide?
8. Are there opportunities to improve the transparency and reporting of enforcement costs? If so, what changes could be made and what benefits would they provide?

Enforcement costs should be attributed to and, where possible, recovered from the entities to which the enforcement activity directly relates.

As an example, there have been a number of enforcement actions taken against large institutional entities within the financial adviser sector as a result of historical contraventions of the law identified by the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. However, there has been significant structural change within the sector with the majority of the large institutional AFS Licensees having ceased to provide retail financial advice and having exited the sector. The sector has transformed from being dominated by five large financial institutions to being made up of predominately small to medium sized business. Approximately 70 per cent of AFS Licensees have four or less authorised representatives.

We recommend that enforcement costs be separated from ASIC's day to day or BAU regulatory costs and instead be attributed to and levied on those participants responsible for the enforcement activity. This could be done by directly recovering costs from them and applying the funds to the ASIC Enforcement Special Account (ESA).

An alternative, which would be particularly relevant to the financial adviser sector, would be to levy a larger share of enforcement costs on the largest participants in a sector, say the largest ten or twenty, to ease the burden on the small participants.

Importantly, all proceeds from enforcement action, including fines, civil and criminal penalties, should be allocated to the ESA and attributed to the relevant sector to offset enforcement costs.

Separating enforcement costs from BAU regulatory activity would also result in a much more stable year on year regulatory cost and provide greater certainty to sector participants as to what their annual levies will be.

9. Is the approach of attributing costs of illegal unlicensed conduct to the most 'relevant' sub sector the most appropriate recovery method? Alternatively, how should these costs be recovered, and why?

Apportioning costs of unlicensed or unregulated activities, or activities relating to entities that are no longer participating in a regulated sector, to a particular sector or sub-sector is inappropriate and inequitable. It is inconsistent with the policy intent of the IFM and the overarching principle of the Government Charging Framework that those entities that cause the need for regulation should generally pay for it.

Further, the cost of enforcement activity against unlicensed operators being charged to those who are appropriately licenced is arguably inconsistent with Section 10(4) of the ASIC Supervisory Cost Recovery Levy Act 2017.

The entities responsible for the regulatory or enforcement activity should be held accountable and, where possible, costs should be recovered from them.

The impact of the current approach has been particularly acute in the financial advice sector, which has undergone significant structural change over the last few years. The majority of the large AFS Licensees have ceased to provide retail financial advice yet continue to be subject to historical enforcement activities. The costs of these historical enforcement activities are being borne by the remaining AFS licensees who are predominantly small to medium sized businesses.

Additionally, liquidators are tasked with paying the bill for untrustworthy advisers (i.e., pre-insolvency advisers) when ASIC could take other regulatory action to recover costs against these individuals/organisations for providing unlicensed advice under the Credit Act, Tax Acts, SMSF Act and Corporations Act. This does not occur, and it appears more expeditious to instead take action against its regulated population. For example, as part of the investigation process of the liquidator, he/she could advise ASIC whether there was "advice" provided by an unregistered or unregulated party that was to the detriment of the company. ASIC should then be able to issue civil fines or penalties under the Corporations Act as a result of the advice.

10. Are there alternative ways to recover the costs of ASIC's activity relating to emerging sectors and legal unlicensed conduct from current industry sub-sectors, and why?

Consistent with the Charging Framework principles, those entities that cause the need for regulation should generally pay for it.

The Government has a responsibility to maintain trust and integrity in the financial system and promote consumer protection. Where unlicensed activity occurs and as new sectors emerge, it is up to the Government to ensure the community is protected by operators who fall outside current regulatory frameworks. As such, these costs should be borne by government until such time that it is suitable to license or register participants in these sectors.

11. How can costs associated with capital expenditure be recovered most equitably and transparently? What changes could be made to the current approach, and what benefits would they provide?

Capital expenditure is a cost of doing business. It should not fall on regulated sectors to pay for ASIC's capital expenditure costs. Expenditure on capital improvements, such as software upgrades, to enable ASIC to run more efficiently and maintain current standards are costs of government, as it would be for private organisations.

12. How can costs associated with education and policy advice be recovered most equitably and transparently? What changes could be made to the current approach, and what benefits would they provide?

13. What changes could be made to the reporting of indirect costs to improve stakeholder understanding of these costs?

Unfortunately, there is no transparency as to how the cost of other regulatory activities – industry engagement, education, guidance and policy advice – are allocated to particular sub-sectors, what they entail, and how they benefit the sub-sector or consumers.

Clear performance indicators or metrics are required to understand ASIC's effectiveness in undertaking these activities. As an example, it is not uncommon for ASIC officers to outnumber industry representatives in industry engagement meetings. However, only a small number of them may make a direct contribution to the meeting. It is assumed that the time cost for all of these attendees are attributed to the relevant sub-sector(s) via the IFM.

Indirect costs make up a disproportionate amount of the total operating expenditure of regulatory costs, averaging up to 40 per cent each year. Again, the lack of transparency with respect to these costs means that industry participants may be covering some general and administrative costs that are unrelated to ASIC's regulatory and oversight functions. This is particularly evident with the financial advice sector's indirect costs increasing significantly at the same time that enforcement costs have also risen significantly.

More broadly, there are no clear indicators or metrics published on ASIC's effectiveness. In a system where ASIC is able to recover fully its regulatory costs there is no clear incentive for ASIC to reduce regulatory costs, drive efficiencies and improve regulatory outcomes.

We recommend the Government commissions a review by the ANAO of how ASIC allocates costs between sectors and sub-sectors, the steps ASIC takes to ensure its regulatory activities are efficient and cost-effective, and how ASIC is held to account to ensure its regulatory activities are efficient and cost-effective

14. Do regulated entities find estimated levies useful, and how is this information used by entities?

14.1. Noting the trade-off between timing and accuracy, when is it most beneficial for entities to receive estimated levy amounts?

14.2. Would alternative information, such as a range for estimated levies, be more useful?

No. The significant delays between ASIC levy estimates being provided and the final levies being announced each year, coupled with the significant variations between the estimated levies and the final levies charged, makes it extremely difficult for participants to accurately budget for their ASIC levies and to set adequate fees for their clients, in order to recoup these costs.

Releasing a draft CRIS for comment so close to or after the commencement of the financial year and a finalised version later in the year, often with significant variances, provides no benefit to sector participants. We recommend a single CRIS be issued before the commencement of the financial year for budgeting purposes and that any material variances are carried over to the next financial year.

If enforcement costs were separated from BAU regulatory costs, as recommended in our response to question 8, there would be a lot more certainty as to the year-on-year regulatory costs.

15. Is it more important to have less volatile/more stable levy amounts year-on-year, or more granular and equitable apportionment of costs each year?

16. Are there other ways to manage or reduce volatility in levy amounts year-on-year, including other approaches to spreading costs? If so, why, and what benefits would it provide?

For the reasons mentioned previously, it is more important to have a more granular and equitable apportionment each year.

As per our response to questions 13 and 14, separating enforcement costs from BAU regulatory costs would provide a more stable levy each year, particularly when any variations in regulatory cost are carried over to the next financial year.

Fees-for-service

17. In relation to the design, structure and legislative framework for fees-for-service:

17.1. Are any changes required to ensure it remains fit for purpose in the longer-term and/or can respond to changes in industry?

17.2. Are there opportunities to simplify the design, structure, and legislative framework for fees-for-service?

18. Are there any costs currently recovered through fees-for-service that would be more appropriate to recover through industry levies? If so, why?

We do not support any change to the current design, structure and legislative framework for fees for service until there are clear indicators or metrics published on ASIC's effectiveness and accountability is demonstrated for the actions taken by ASIC to reduce regulatory costs, drive efficiencies and improve regulatory outcomes.

As mentioned previously, we recommend the Government commissions a review by the ANAO of how ASIC allocates costs between sectors and sub-sectors, the steps ASIC takes to ensure its regulatory activities are efficient and cost-effective, and how ASIC is held to account to ensure its regulatory activities are efficient and cost-effective.

19. If fee amounts are to be changed, should this be amended via a one-off increase or staged to spread the impact over multiple years?

Subject to the above comments, if fees were to be increased, we would support a graduated change.

20. Is it appropriate for ASIC to have the power to determine which of its regulatory activities/services it can charge a fee for?

21. Is it appropriate for ASIC to have the power to set fee amounts, or should this power remain with the Government?

21.1. If ASIC were provided the power to set fee amounts, should there be any limitations on what fees it can adjust, or by how much? For example, setting caps on specific fees in primary law or regulations, or setting principles to guide ASIC's setting of fee amounts?

22. What transparency and accountability mechanisms would be appropriate if ASIC were setting fee amounts?

Yes, if there are clear indicators or metrics published on ASIC's effectiveness and accountability is demonstrated for the actions taken by ASIC to reduce regulatory costs, drive efficiencies and improve regulatory outcomes.

As mentioned previously, we recommend the Government commission a review by the ANAO of how ASIC allocates costs between sectors and sub-sectors, the steps ASIC takes to ensure its regulatory activities are efficient and cost-effective, and how ASIC is held to account to ensure its regulatory activities are efficient and cost-effective.

23. Do fees for licence and registration cancellations provide a disincentive to cancel licenses and registrations? If so, would a lower fee or no fee remove this disincentive?

24. Would it be more appropriate for the costs associated with licence and registration cancellations to be recovered through industry levies (noting that there are wider benefits to ensuring entities and individuals that are no longer undertaking a particular licensed activity do not continue to hold a licence for that activity)?

Anecdotal feedback from our members strongly suggests that recovering fees for voluntary registration cancellations acts as a direct disincentive for participants to exit the regulated population when they have ceased practicing. Given

this process is undertaken via the online portal the processing costs should be minimal. To ensure the integrity of the industry and to maintain consumer confidence we believe it is the Government's responsibility to bear this cost.

25. Is it appropriate for ASIC's work on individual relief applications to be recovered via fees, with the costs associated with ASIC's work on relief provided to a class of entities to be recovered through industry levies?

Specific applications of relief should be borne by the party making the application and not the industry.

Reporting, transparency and consultation

26. How do regulated entities and other stakeholders engage with ASIC's transparency and consultation mechanisms relating to the IFM? What aspects are most useful?
- 26.1. What do stakeholders seek from mechanisms to engage with the IFM? Is it more important for these mechanisms to provide transparency, or to allow for stakeholder consultation and feedback?
27. Are the existing transparency and consultation mechanisms in relation to the IFM appropriate?
- 27.1. Would changes to existing mechanisms or alternative mechanisms be beneficial? If so, what changes could be adopted and what benefits would they provide?
28. How is the CRIS used by regulated entities and other stakeholders, and do stakeholders find the information in the CRIS useful?
- 28.1. Could improvements be made to the CRIS, including the form/format and nature of information provided? If so, what improvements and what benefits would they provide?
- 28.2. At what time is it most beneficial for the CRIS to be published?
29. Noting that changes to the IFM are for the most part decisions for the Government, is annual consultation by ASIC via the CRIS useful? Would less frequent but more substantive consultation be preferable?
30. Are changes required to the criteria determining material variance? If so, what should be changed – the percentage and/or dollar value amount, or be based on the number of entities impacted?
- 30.1. When should information regarding material variations be published?
31. What other information would be useful to regulated entities or other stakeholders to understand how ASIC sets its regulatory priorities and/or to understand the relationship between ASIC's costs and the amounts recovered from industry? What benefits would additional information provide?

As mentioned previously, there is little benefit to regulated entities from the current CRIS process where a draft is released for comment and a final version is released later in the year.

The significant delays between ASIC levy estimates being provided and the final levies being announced each year, coupled with the significant variations between the estimated levies and the final levies charged makes it extremely difficult for participants to accurately budget for their ASIC levies and to set adequate fees for their clients, in order to recoup these costs.

Releasing a draft CRIS for comment so close to or after the commencement of the financial year and a finalised version later in the year, often with significant variances, provides no benefit to sector participants. We recommend a single CRIS be issued before the commencement of the financial year for budgeting purposes and that any material variances are carried over to the next financial year.

If enforcement costs were separated from BAU regulatory costs, as recommended in our response to questions 5 and 8, there would be greater certainty as to the year-on-year regulatory costs. More predictable annual costs could then facilitate a shift to a forward-looking forecast annual levy based on an expected budget with any adjustments made in the following year based on actuals. A budget-based model, that is adjusted for actuals each year, would allow for a variance analysis with any large variations having to be justified.

Unfortunately, there are no clear indicators or metrics published on ASIC's effectiveness. In a system where ASIC is able to recover fully its regulatory costs there is no clear incentive for ASIC to reduce regulatory costs, drive efficiencies and improve regulatory outcomes.

We recommend the Government commissions a review by the ANAO of how ASIC allocates costs between sectors and sub-sectors, the steps ASIC takes to ensure its regulatory activities are efficient and cost-effective, and how ASIC is held to account to ensure its regulatory activities are efficient and cost-effective.