



**PROPOSED INDUSTRY FUNDING MODEL FOR THE AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION**

**SUBMISSION**

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**The Association of Superannuation Funds of Australia**

## Introduction

ASFA considers that ASIC has a crucial role as a conduct and disclosure regulator in maintaining confidence in superannuation and the financial system more broadly.

In principle, ASFA supports the adequate and appropriate funding of ASIC. Further, ASFA considers that all regulated entities should contribute to that funding. This outcome is, in ASFA's view, far more equitable and appropriate than funding ASIC solely from consolidated revenue.

The introduction of an industry funding model for ASIC has the potential to change significantly the character of ASIC's dealings with its regulated entities. Importantly, it also represents an opportunity to provide industry with greater insight into ASIC's activities and to provide genuine transparency and accountability regarding the manner in which ASIC's funding is utilised. Both are necessary in order for industry to have confidence that ASIC is functioning well as a regulator.

ASFA has, however, a number of concerns with the industry funding model put forward in the Australian Treasury's proposal paper: *Proposed Industry Funding Model for the Australian Securities and Investments Commission* (the Proposals Paper). Many of these concerns are similar to those that ASFA raised in its response to Treasury's initial consultation paper on the industry funding model (the *2015 Consultation Paper*), which Treasury released in August 2015. ASFA's main concerns are:

- The proposed industry funding model would impose a high cost burden on the APRA-regulated superannuation industry.
- Some of ASIC's regulatory activities that are to be cost-recovered from industry cannot be directly attributed to identifiable industry recipients. These activities should be funded from consolidated revenue rather than from industry.
- ASIC needs to improve its transparency and accountability – these are critical features of any industry funding model. Although there are a number of mechanisms in place (or in train) that should improve ASIC's accountability and transparency, some of these need to be strengthened.
- ASIC needs to improve its transparency and accountability regarding enforcement, particularly given ASIC's relatively heavy reliance on enforcement as a regulatory tool. ASIC should have to demonstrate that its mix of regulatory tools is appropriate.
- ASIC needs to improve the efficiency of its regulatory effort – by cooperation with other regulators to exploit regulatory synergies and minimising the impact of regulation on the regulated population.

This submission addresses ASFA's general concerns with the proposed the industry funding model, and responds to the specific questions in the Proposals Paper (at Appendix 1). ASFA's comments largely relate to superannuation trustees, which is a sub-sector of ASIC's sector category: *Investment management, superannuation and related services*. However, many of these issues are relevant to ASIC's broader regulated population.

## Main concerns with the revised industry funding model

### 1. High cost burden on the APRA-regulated superannuation industry

The APRA-regulated superannuation industry makes a substantial contribution to the cost of its regulation. For the 2016-17 fiscal year, the Government expects that levies paid by the superannuation industry will include \$30.5 million to fund APRA's regulatory activities and a further \$24.5 million to fund ASIC's activities (currently collected by APRA, then allocated to ASIC).<sup>1</sup>

With respect to current industry funding for ASIC's activities, expected levies for 2016-17 (\$24.5 million) are almost 250% higher than for 2015-16 (\$10.2 million).<sup>2</sup> Some of this increase reflects cost-recovery of non-ongoing programmes, so does not represent an increase in baseline levies (which is what matters for comparing the levies under the proposed industry funding model).<sup>3</sup> However, it is not possible to determine exactly the 2016-17 baseline levies from the APRA-regulated superannuation industry from the *Financial Industry Levies* publication (lack of data transparency is a broader issue, which is addressed in detail later in this submission).

That said, the available data suggests that the proposed industry funding model would lead to a significant increase in baseline levies from the APRA-regulated superannuation industry. For the 2015-16 fiscal year, ASFA has calculated that baseline levies for ASIC from the superannuation industry were \$3.6 million.<sup>4</sup> Under the proposed industry funding model, annual levies from the superannuation industry would be around \$8.5 million (based on the cost allocation for 2016-17 in the Proposals Paper). This is an increase of around 135 per cent.<sup>5</sup>

In addition to levies, superannuation trustees would be subject to fees for user-initiated services – though the Proposals Paper notes that the Government will delay implementation of a new fee-for-service framework. In principle, ASFA supports fees for ASIC's demand-driven services, such as processing a licence, provided that fees reflect the efficient allocation of effort to provide services. As ASFA noted in its response to the *2015 Consultation Paper*, that Paper did not provide sufficient detail to enable industry to assess properly the proposed fee-for-service framework or to provide suggestions for modifications or improvements to the methodology. Other stakeholders expressed similar concerns. ASIC should produce a revised fee-for-service framework only after it has accumulated the required data to generate informed estimates of the costs of services.

### 2. Scope of the industry funding model has increased

ASFA notes that the scope of the proposed industry funding model has widened compared with that proposed in the *2015 Consultation Paper*. In the revised model, ASIC levies its regulated population to recover the cost of all of its regulatory activities, except for the costs of ASIC's registry business

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<sup>1</sup> Australian Government 2016, *Financial Industry: Levies for 2016-17*, page 10.

<sup>2</sup> The Treasury and the Australian Prudential Regulation Authority 2015, *Financial Industry: Levies for 2015-16*, page 10.

<sup>3</sup> The increase for 2016-17 reflects, in part, Government decisions to increase funding for the Superannuation Complaints Tribunal (SCT) and to modernise ASIC's data management, surveillance and enforcement capabilities. Improving ASIC's capabilities is a four-year programme, which is scheduled to end in 2019-20.

<sup>4</sup> This excludes levies to fund the Superannuation Complaints Tribunal (The Treasury and the Australian Prudential Regulation Authority 2015, *Financial Industry: Levies for 2015-16*, page 7).

<sup>5</sup> This assumes that the baseline funding for 2016-17 is \$3.6 million.

and litigation costs for criminal matters that ASIC refers to the Commonwealth Director of Public Prosecutions.

It is ASFA's view that, as a general principle, where the cost of activities undertaken by ASIC cannot be directly attributed to identifiable industry recipients, those costs should be funded from consolidated revenue. ASFA does not consider it appropriate that ASIC's regulated entities should bear the cost of activities that substantially benefit non-regulated entities. This approach is consistent with the Government's framework for cost-recovery.<sup>6</sup>

ASFA notes that the *2015 Consultation Paper* excluded a number of ASIC's activities from the industry funding model on this basis. The Consultation Paper stated that such activities should be funded from consolidated revenue. Although ASFA suggested that administration of ASIC's Unclaimed Money programme should be funded via industry levies (to be consistent with the funding arrangements for the ATO's equivalent programme),<sup>7</sup> ASFA agreed that the other listed activities should be excluded. In addition, ASFA considers that there are other ASIC activities that should not be cost-recovered from industry. This is addressed in more detail in Appendix 1 (Question 1).

### ***3. Transparency and accountability still a concern***

Transparency and accountability are, in ASFA's view, critical features of any industry funding model. A robust accountability and transparency framework will be required in order to give ASIC's regulated population confidence that levies are being set and spent appropriately. ASFA has long-held concerns regarding the lack of transparency and accountability around the process by which supervisory levies are determined, allocated among regulatory agencies and utilised by those agencies.

#### *Need for mechanisms to improve ASIC's transparency and accountability*

There are a number of mechanisms in place (or in train) that should lead to greater accountability and transparency, and should lead to more efficient regulation and a more equitable distribution of the cost of regulation among ASIC's regulated population. However, ASFA considers that some of these mechanisms need to be strengthened.

The recent Capability Review of ASIC noted that ASIC's transparency and accountability needed to improve. As such, the Review made a number of recommendations that, if implemented, would be expected to enhance ASIC's transparency and accountability (the Review includes recommendations for ASIC and for Government). The key recommendations in the context of the industry funding model include improvements to ASIC's strategy-setting process (which helps ASIC to determine where it should focus its regulatory effort), better communication of ASIC's strategy to ASIC's

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<sup>6</sup> Australian Government 2015, *Australian Government Charging Framework*.

<sup>7</sup> A separate programme for administration of unclaimed superannuation money is administered by the Australian Taxation Office (ATO), and has historically been partially cost recovered from the APRA-regulated superannuation sector via an allocation to the ATO from the APRA supervisory levy. In the May 2015 Commonwealth Budget, the Government moved toward adopting full cost recovery of the ATO's administration of the unclaimed superannuation regime, and this is reflected in the APRA supervisory levy for 2015-16. As a result, APRA-regulated superannuation funds now fully fund regulatory activities in relation to the unclaimed superannuation programme.

regulated population and more transparent reporting of ASIC's regulatory performance. ASFA acknowledges that ASIC has developed a plan for implementing the Review's recommendations.<sup>8</sup>

The extent to which ASIC successfully implements the Review's recommendations is likely to have a significant bearing on whether the industry funding model produces equitable outcomes for ASIC's regulated population. As such, ASFA considers that Government should review, after an appropriate period, whether ASIC has implemented the Review's recommendations and the degree to which the changes have improved ASIC's transparency and accountability.

Established Government processes provide another check on ASIC's transparency and accountability. ASFA notes that Government oversight mechanisms for Commonwealth entities have been improved, and that this will be source of increased scrutiny of ASIC's performance. This includes the Government's Budget process, but also the broader accountability mechanisms in the performance framework for Commonwealth entities (overseen by the Department of Finance).<sup>9</sup> With respect to the Budget, ASFA notes that it is intended that ASIC's regulatory activities would continue to be funded through direct appropriation from the Commonwealth Budget, with the appropriation to be offset by levies and fees charged to industry.

ASIC also has set self-assessment indicators, as required by the Government's Regulator Performance Framework. ASFA supports the objective of the framework – to encourage regulators to undertake their functions in a way that minimises the impact on regulated entities. ASFA considers, however, that ASIC's performance metrics need refinement, and has provided feedback to ASIC in this regard. This issue is addressed in more detail Section 4.

#### *Need to justify enforcement focus*

ASFA considers that it is crucial that ASIC improve its transparency and accountability regarding enforcement, particularly given ASIC's relatively heavy reliance on enforcement as a regulatory tool.

The ASIC Capability Review did not make any specific recommendations about ASIC's enforcement focus, but did note that ASIC's resource allocation to enforcement far exceeds that of peer regulators, and stated that a better-balanced approach emphasising the full scope and use of ASIC's regulatory toolkit would be more appropriate.<sup>10</sup> Consistent with the Capability Review, the Proposals Paper shows that ASIC has a relatively heavy reliance on enforcement. According to the Proposals Paper, enforcement is expected to account for around 50% of costs in 2016-17.

ASIC's strong enforcement focus magnifies the problems of cross-subsidisation of enforcement activities. ASIC's enforcement activities involve ASIC ensuring compliance with the law in specific instances – that is, ensuring that regulated entities undertake prescribed conduct and/or cease prohibited conduct. However, under the proposed industry funding model all regulated entities would bear the cost of enforcement activities.

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<sup>8</sup> ASIC 2016, *ASIC Capability Review – ASIC's Implementation Plan*.

<sup>9</sup> The framework incorporates enhanced reporting requirements for entities against performance criteria, and assessment of regulatory efficiency (i.e. achievement of regulatory objectives at least cost).

<sup>10</sup> Australian Government 2015, *Fit for Future: A Capability Review of the Australian Securities and Investments Commission*, December, page 11.

Indeed, because of this cross-subsidisation, it would be more equitable to fund enforcement activities (and discretionary surveillance activities) from consolidated revenue rather than from industry levies. That said, ASFA does acknowledge that ASIC's enforcement activities may have broader benefits. In particular, it may lead to important behavioural change at an entity-specific level and across sectors/sub-sectors.

If enforcement is to be cost-recovered, ASFA considers that it is crucial that ASIC improve its transparency and accountability regarding enforcement. Given the Capability Review's findings about ASIC's strong enforcement focus, ASIC should have to demonstrate that its mix of regulatory tools is appropriate and is achieving ASIC's regulatory objectives at least cost. This could form part of ASIC's broader performance reporting requirements via the Commonwealth's revised performance framework.

ASIC also needs to be more transparent and accountable regarding its cooperation with other regulators on enforcement. As is discussed in Section 4, regulators should look to exploit regulatory synergies. This would help reduce duplication of regulatory effort among regulators. In this regard, ASFA members have indicated that they are observing an increasing overlap between ASIC and APRA on enforcement activity. It is unclear what steps, if any, regulators have taken to reduce any potential duplication. Again, ASIC could demonstrate its enforcement cooperation as part of the broader performance reporting requirements.

ASFA understands that, under the proposed model, the proceeds of ASIC's enforcement activities would be paid into consolidated revenue (and thus not provide ASIC with a direct revenue source). ASFA considers that this is an important safeguard to ensure that the regulatory model does not provide incentives for an excessively prosecutorial culture to develop.

#### *Need for more complete public data on regulatory effort*

In order to instil confidence in an industry funding model, all industry participants must have evidence that the funding burden is shared in a manner that appropriately reflects the level of regulatory intensity applicable to different types of participants or activities.

For ASIC's regulated population, determining whether the industry funding model allocates regulatory effort (and the associated costs) appropriately depends on the type and quality of the data that ASIC publishes. Although the data in the revised industry funding model is more detailed than in the previous version of the model (in the *2015 Consultation Paper*), the data is still not sufficient for industry to make an informed judgement about whether the allocation of regulatory effort and costs is appropriate.

ASIC provided a cost breakdown at the sector level in the Proposals Paper (which was lacking in the *2015 Consultation Paper*), but has not provided the same breakdown for the sub-sectors (including for superannuation trustees in the *Investment management, superannuation and related services* sector). Therefore, it is still difficult to make a judgement whether the relative allocation of regulatory effort among sub-sectors is appropriate (and whether the relative allocation of levies is appropriate).

It is also not clear whether ASIC has the relevant sub-sector level data. Measurement of actual regulatory effort undertaken with respect to sub-sectors requires detailed data on workflows for

those sub-sectors. By its own admission, ASIC's workflow data needs improvement. To rectify this, ASIC recently commenced a three-year programme to improve data on the regulatory effort it applies to various sub-sectors (and the types of expenses related to those efforts).

ASIC's data quality has broader implications for transparency. As noted above, ASIC's strategy-setting process involves decisions about major strategic regulatory priorities, which informs ASIC's allocation of regulatory effort to sectors/sub-sectors and its allocation of resources.

Without detailed sub-sector data, however, this process can lead to a sub-optimal allocation of regulatory effort (and resources). Without detailed sub-sector data, it would be difficult for ASIC to determine if its required resource allocation is consistent with its actual allocation, and thus whether its actual allocation of regulatory effort is consistent with its required allocation of regulatory effort – as reflected in ASIC's strategic regulatory priorities.

More complete sub-sector data on the allocation of regulatory effort and resources would provide the regulated population with greater confidence that the allocation of costs among ASIC's regulated population is appropriate.

#### ***4. Efficiency of regulation needs to improve***

In a cost-recovery model of regulation, the regulated population reasonably expects that the regulator is functioning in the most efficient manner – that is, the regulator is achieving its regulatory objectives at least cost.

##### *Need to build expertise on superannuation*

ASFA has some concerns about ASIC's lack of experience with respect to superannuation and the implications for the efficiency of ASIC's regulatory effort. The superannuation industry has a myriad of complex structures and products – a one-size regulatory approach is not appropriate – and ASIC has few staff on the ground with extensive superannuation knowledge and experience. This may limit the effectiveness of consultation, supervision and enforcement. Indeed, there have been instances in the past five years where a lack of detailed knowledge of the superannuation and funds management industries have had an impact on ASIC's ability to develop effective and cost-efficient guidance.

##### *Need to acknowledge synergies in regulation*

Within the proposed industry funding model, it is not clear whether allocations of regulatory cost take into account the extent to which some sectors or sub-sectors are already subject to primary regulation by another regulator, and the resultant regulatory synergies. A regulator's supervisory efforts would be expected to change an entities' behaviour beyond the direct area of supervision – which would reduce the required regulatory effort by other regulators.

The 'superannuation trustee' sub-sector of the *Investment management, superannuation and related services* sector is already subject to full prudential supervision by APRA, for which it incurs substantial levies (excluding cost recoveries for ASIC and other agencies, APRA is budgeted to collect levies of \$30.5 million from the pooled superannuation sector in 2016-17).

APRA's supervision of superannuation trustees includes enforcement of prudential standards that govern trustees' conduct across a wide range of areas. In contrast, ASIC's direct regulatory and supervisory responsibilities in respect of the APRA-regulated superannuation sector is effectively limited to matters and conduct related to the 'issue' of interests in superannuation funds and to disclosure.<sup>11</sup>

Compliance with APRA's prudential standards has required superannuation trustees to implement robust compliance and risk frameworks. It also has led to a general improvement in standards of behaviour and professionalism which extends across trustees' entire business operations, including into areas which fall within ASIC's supervision.

Although ASIC applies a conduct-focussed lens, as opposed to APRA's prudential approach, it cannot be denied that synergies exist and that regulatory efficiencies arise due to the prudential supervision applied to superannuation trustees. In this regard, the ASIC Capability Review noted that ASIC should consider whether regulatory outcomes could be achieved by using existing regulation administered by another regulator, or other collaborative arrangements in order to ensure an integrated regulatory framework and reduce costs for regulated entities.<sup>12</sup>

Ultimately, greater recognition of synergies would allow Australian regulators to allocate their resources to where they are most needed, and would lead to a more efficient regulatory environment.

#### *Need to better account for impact of regulation*

In a cost-recovery model of regulation, the regulated population reasonably expects that the regulator is functioning in a way that minimises the impact on the regulated population. This is the main objective of the Government's Regulator Performance Framework – which requires regulators to develop outcomes-based key performance indicators and to implement a process for annual externally-validated self-assessment. As noted in Section 3, ASIC also has set its indicators.

ASFA supports the objective of this process, but considers that ASIC's proposed performance metrics need refinement to provide a more useful gauge of regulatory impact.<sup>13</sup>

In ASFA's view, any assessment of ASIC's performance needs to better capture how well ASIC balances the intended benefits of new regulatory measures against the costs to industry. This is crucial given that despite the Government's emphasis on minimising or reducing red tape, ASFA members report that their compliance burden continues to rise.

Further, indicators should better account for the time needed for industry to implement new regulatory requirements, and the need for all stakeholders to have sufficient clarity around the interpretation and operation of those requirements before commencing implementation. With respect to ASIC's recent regulatory initiatives, ASFA members specifically raised the example of changes to fee and cost disclosure.

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<sup>11</sup> To the extent that superannuation trustees provide advice under an AFS licence, they will be levied separately under the proposed arrangements as 'financial advice providers'.

<sup>12</sup> Australian Government 2015, *Fit for Future: A Capability Review of the Australian Securities and Investments Commission*, December, page 160.

<sup>13</sup> ASFA 2016, *Regulator Performance Framework – external validation of self-assessment*.

## Appendix 1: Responses to specific consultation questions

**Q1 Do you agree with the proposal that all of ASIC’s regulatory costs should be included in the industry funding model, excluding ASIC’s registry costs and criminal prosecutions incurred by the DPP? If not, please describe your preferred approach and reasons for it.**

**ASFA response:**

ASFA considers that a range of ASIC’s regulatory activities do not relate to industry activity. ASFA considers that the cost of these activities should not be funded by industry, and instead should be funded from consolidated revenue. These include:

- Financial literacy activities.
- Activities relating to ASIC’s strategic role such as its international engagement, including through participation in the International Organization of Securities Commissions.
- ‘Overhead’ expenditures, including those relating to the capabilities, training and development of ASIC staff.

In principle, cost-recovery from industry should be limited to regulatory activities where identifiable industry recipients have created demand for those activities. This is consistent with the Australian Government’s Charging Framework. In particular, the Framework’s equity principle states that *where specific demand for a government activity is created by identifiable individuals or groups they should be charged for it.*<sup>14</sup>

Under the proposed industry funding model, industry would fund the cost of nearly all of ASIC’s regulatory activities (the only exceptions would be the costs of ASIC’s registry business and litigation costs for criminal matters that ASIC refers to the Commonwealth Director of Public Prosecutions). As the Proposal Paper acknowledges, this would include activities for which industry funding would be inconsistent with the Government’s Charging Framework. Indeed, because of this, and as ASIC notes, the costs associated with such activities would need to be funded via a statutory levy on industry (rather than a cost-recovery levy as per the Charging Framework).

In ASFA’s view, regulatory activities for which industry cost recovery is inconsistent with the Charging Framework should be excluded from the industry funding model, and instead should be funded from consolidated revenue. This approach is broadly consistent with the *2015 Consultation Paper*, which included a list of activities that would not be funded by industry because doing so would be inconsistent with the Charging Framework.

In its response to the *2015 Consultation Paper*, ASFA supported the exclusion of all of the listed activities from the industry funding model, apart from the administration of ASIC’s Unclaimed Money programme. ASFA suggested that administration of this programme should be funded via industry levies (to be consistent with the funding arrangements for the ATO’s equivalent

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<sup>14</sup> Australian Government 2015, *Australian Government Charging Framework*.

programme).<sup>15</sup> With regard to the other listed activities, the most relevant for superannuation trustees is financial literacy initiatives (see below for details).

ASFA also identified other ASIC activities in its response to the *2015 Consultation Paper* that cannot be directly attributed to identifiable industry recipients, and so should not be cost-recovered from industry. These include:

- Activities relating to ASIC's strategic role such as its international engagement, including through participation in the International Organization of Securities Commissions.
- 'Overhead' expenditures, including those relating to the capabilities, training and development of ASIC staff.

Another example relates to self-managed superannuation funds (SMSFs). In line with ASIC's mandate, ASIC undertakes regulatory activities in relation to the 'gatekeepers' for SMSFs (auditors), whereas regulation of SMSFs is the responsibility of the ATO. The industry funding model incorporates SMSF auditors (as a sub-sector of the *Investment management, superannuation and related services* sector), and SMSF auditors would pay a levy. To the extent that ASIC undertakes regulatory activities in relation to SMSFs that extend beyond SMSF auditors, superannuation trustees should not bear the cost of such activities. This approach would be consistent with the principles of the Government's Charging Framework.

#### *Financial literacy initiatives*

ASIC's financial literacy initiatives include the National Financial Literacy Strategy and the MoneySmart website. The Proposals Paper proposes that these be funded via statutory levy.

ASFA strongly supports the continuation of these initiatives. They are a source of valuable education material regarding a diverse range of financial services, products and structures, including extensive resources relating to SMSFs.

There is no doubt that these initiatives benefit the broader financial system – better-informed consumers and investors make better financial decisions. Fundamentally, however, demand for such programmes originates from the broader Australian community rather than ASIC's regulated population.

As noted above, the Government's cost-recovery principles state that cost-recovery for regulatory activities should apply to the sources of demand for those activities. As such, it would be more equitable to fund ASIC's financial literacy activities from consolidated revenue.

At present, the MoneySmart website is funded largely by an allocation to ASIC from the supervisory levies paid by APRA-regulated entities (including superannuation funds). ASFA does not support the continued funding of MoneySmart from these levies.

#### *Enforcement*

ASFA considers that it would be more equitable to fund enforcement activities (and discretionary surveillance activities) from consolidated revenue rather than from industry levies. There is

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<sup>15</sup> See footnote 7.

significant cross-subsidisation in enforcement activity, and ASIC's strong enforcement focus magnifies this problem.

ASIC's enforcement activities involve ASIC ensuring compliance with the law in specific instances – that is, ensuring that regulated entities undertake prescribed conduct and/or cease prohibited conduct. However, under the proposed industry funding model all regulated entities would bear the cost of enforcement activities. That said, ASFA does acknowledge that ASIC's enforcement activities may have broader benefits. In particular, it may lead to important behavioural change at an entity-specific level and across sectors or sub-sectors.

If enforcement is to be cost-recovered, ASFA considers that it is crucial that ASIC improve its transparency and accountability regarding enforcement (this is discussed in detail in the front part of the submission).

**Q2 Will the proposed model design objectives ensure consistency of approach to setting levies and fees across ASIC's regulated population? Are there other objectives that should be considered? If so, why?**

**ASFA response:**

ASFA considers that the model design objectives are broadly appropriate. However, ASFA has concerns about the practical application of those objectives. These issues are addressed in ASFA's response to Question 3.

**Q3 Do you agree with the proposed model for calculating levies? Is there an alternate approach you would prefer? If so, please explain why.**

**ASFA response:**

On balance, ASFA considers that the FUM-based levy calculation for superannuation trustees is appropriate. However, ASIC should look to refine the methodology after the industry funding model has been implemented.

ASFA has concerns about the lack of transparency regarding how regulatory costs have been allocated between sub-sectors (in the *Investment management, superannuation and related services* sector). There is insufficient detail in the industry funding model to determine whether the relative allocation of regulatory effort (and costs) between sub-sectors is appropriate.

ASFA has concerns about the potential for double-counting of required regulatory effort where levies are calculated on the basis of FUM. To help alleviate this issue, ASIC could introduce a mechanism that allows entities to query assessments where they consider double-counting may have occurred.

*Levy methodology for superannuation trustees*

On balance, ASFA considers that the FUM-based levy calculation for superannuation trustees is appropriate. However, ASIC should look to refine the methodology after the industry funding model has been implemented. A revised methodology could incorporate a risk-based element that would reduce the degree of cross-subsidisation among entities and lead to a more equitable allocation of

regulatory costs. ASFA would be willing to assist ASIC to develop a risk-based metric for superannuation trustees.

With respect to levy methodology, ASFA acknowledges that it is difficult to strike an appropriate balance between the competing requirements of simplicity, transparency and the equitable allocation of the costs of regulatory effort (among the regulated population). This applies to the levy methodology for superannuation trustees, but also to the levy methodologies for other sub-sectors in the industry funding model.

The proposed FUM-based calculation is relatively simple and transparent, but it is an imperfect proxy for the risk that entities pose to the broader market (and thus an imperfect proxy for required regulatory effort). In particular, it does not account for differences in the sources of risk – such as trustee conduct. For entities with the same FUM, the proposed methodology effectively means that entities that are relatively ‘low-risk’ would subsidise ASIC’s regulatory effort regarding relatively ‘high-risk’ entities.

#### *Details of levy calculation for superannuation trustees*

Regarding the levy calculation as presented in the Proposals Paper, ASFA acknowledges that the revised levy calculation for superannuation trustees eliminates the problems of the tier-based calculation in the *2015 Consultation Paper*, where a marginal increase in FUM resulted in a very large increase in levies (which would not be warranted by the change in required regulatory effort).

ASFA has some concerns, however, with the calculation of the minimum levy payable. Although ASIC notes that this reflects the fixed cost of regulating a superannuation entity, there is little information on how this is derived. Therefore, it is difficult to make a judgement as to whether the minimum levy is appropriate.

This relates to the broader issue of the lack of ASIC data for the sub-sector level. Although ASIC has provided a cost breakdown for the *Investment management, superannuation and related services* sector, ASIC has not provided the same breakdown for the sub-sectors (including superannuation trustees). Therefore, it is difficult to make a judgement whether the relative allocation of regulatory effort between sub-sectors is appropriate (and whether the relative allocation of costs is appropriate).

#### *Double-counting of FUM*

A shortcoming of the FUM-based approach is the potential for double-counting FUM when determining the regulatory effort related to discrete entities. Although ASFA’s comments relate to the proposed methodology for the *Investment management, superannuation and related services* sector, they have relevance to other sectors in the industry funding model.

To apportion the costs of regulatory effort, the FUM-based methodology calculates levies for different functions. With respect to the *Investment management, superannuation and related services* sector, this includes AFS licensees with authorisations to:

- Operate as superannuation trustees and responsible entities
- Issue interests in managed investment schemes

- Operate investor directed portfolio services

Double-counting of regulatory effort could occur where different authorisations apply to the same pool of assets. For example, for entities that have authorisations to operate as a superannuation trustee and as an operator of investor directed portfolio services (IDPS), assets of the trustee also may be assets of the IDPS. A guiding principle for calculating an entities' levy should be that the calculated levy with respect to each function should reflect the marginal regulatory effort required with respect to those functions. To help alleviate this issue, ASIC could introduce a mechanism that allows entities to query an assessment where they consider double-counting may have occurred.

**Q4 Do you agree with the proposed definitions for industry subsectors and levy metrics at Schedule 1? Is there an alternative approach you would prefer? If so, please explain why.**

**ASFA response:**

ASFA considers that with respect to superannuation trustees, the proposed definition for the industry subsector at Schedule 1 is broadly appropriate.

For the proposed levy calculation for superannuation trustees, the use of gross assets is broadly appropriate. Other issues with respect to the levy calculation are addressed in ASFA's response to Question 3.

**Q5 Do you agree with the proposed timeline for the annual reporting? Are there any reasons as to why the suggested timelines may not work for your organisation's business cycle?**

**ASFA response:**

ASFA considers that the proposed timetable for annual reporting is broadly appropriate. However, certain entities may have particular concerns with elements of the timetable.

**Q6 Do you agree with the proposed engagement and accountability measures? Are there additional measures you would prefer? If so, please explain why.**

**ASFA response:**

The recent Capability Review of ASIC made recommendations that would improve ASIC's transparency and accountability. ASFA considers that the Government should review, after an appropriate period, whether ASIC has implemented the Review's recommendations and the degree to which the changes have improved ASIC's transparency and accountability.

ASFA considers that ASIC should have to demonstrate that its mix of regulatory tools is achieving its regulatory objectives at least cost – particularly with respect to enforcement.

Lack of data on ASIC's regulatory effort at the sub-sector level means that it is difficult to make a judgement whether the allocation of regulatory effort between sub-sectors is appropriate.

The accountability measures in the Proposals Paper relate to established (though recently improved) Government oversight mechanisms for Commonwealth entities and specific processes associated with the proposed industry funding model.

### *Commonwealth Government oversight*

ASFA notes that Government oversight mechanisms for Commonwealth entities have been recently improved, and that this will be source of increased scrutiny of ASIC's performance. This includes the Budget process, but also the broader accountability mechanisms in the Commonwealth's performance framework for Commonwealth entities (overseen by the Department of Finance). Oversight includes assessment of regulatory outcomes against performance criteria.

ASFA considers, however, that the Government should consider a further accountability mechanism for ASIC that relates to the recommendations of the Capability Review of ASIC. The Review concluded that ASIC's transparency and accountability needed to improve, and it made a number of recommendations that, if implemented, would be expected to enhance ASIC's transparency and accountability (the Review includes recommendations for ASIC and for Government). As such, the Government should review, after an appropriate period, whether ASIC has implemented the Review's recommendations and the degree to which the changes have improved ASIC's transparency and accountability.

### *Commonwealth Government oversight – ASIC's enforcement focus*

ASFA considers that it is crucial that ASIC improve its transparency and accountability regarding enforcement, particularly given ASIC's relatively heavy reliance on enforcement as a regulatory tool.

The ASIC Capability Review did not make any specific recommendations about ASIC's enforcement focus, but did note that ASIC's resource allocation to enforcement far exceeds that of peer regulators, and stated that a better-balanced approach emphasising the full scope and use of ASIC's regulatory toolkit would be more appropriate.<sup>16</sup>

Given the Capability Review's findings about ASIC's strong enforcement focus, ASIC should have to demonstrate that its mix of regulatory tools is appropriate and is achieving ASIC's regulatory objectives at least cost. This could form part of ASIC's broader performance reporting requirements via the Commonwealth's revised performance framework.

ASIC also needs to be more transparent and accountable regarding its cooperation with other regulators on enforcement. As is discussed in the front part of this submission, regulators should look to exploit regulatory synergies. This would help reduce duplication of regulatory effort among regulators. Again, ASIC could demonstrate its enforcement cooperation as part of the broader performance reporting requirements.

ASFA understands that, under the proposed model, the proceeds of ASIC's enforcement activities would be paid into consolidated revenue (and thus not provide ASIC with a direct revenue source). ASFA considers that this is an important safeguard to ensure that the regulatory model does not provide incentives for an excessively prosecutorial culture to develop.

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<sup>16</sup> Australian Government 2015, *Fit for Future: A Capability Review of the Australian Securities and Investments Commission*, December, page 11.

### *Industry funding model processes*

ASFA broadly supports the proposed mechanisms, as set out in the Proposals Paper, by which industry can assess ASIC's breakdown of its regulatory effort and the allocation of levies.

ASFA remains concerned, however, about the lack of data regarding ASIC's allocation of regulatory effort at the sub-sector level. With respect to superannuation trustees, although ASIC has provided a cost breakdown for the *Investment management, superannuation and related services* sector, ASIC has not provided the same breakdown for the sub-sectors (including superannuation trustees). Therefore, it is difficult to make a judgement whether the relative allocation of regulatory effort between sub-sectors is appropriate (and whether the relative allocation of costs and levies is appropriate). This issue applies to other sectors/sub-sectors in the industry funding model.

This has implications for the accurate disclosure of the allocation of regulatory effort, but also whether the actual allocation is consistent with the regulator's high-level strategic regulatory priorities.

Measurement of actual regulatory effort undertaken within ASIC requires detailed data on workflows. By its own admission, ASIC's data on its workflows needs improvement. Without detailed sub-sector data, it would be difficult for ASIC to determine if ASIC's required resource allocation is consistent with actual allocation, and thus whether the actual allocation of regulatory effort is consistent with the required allocation of regulatory effort – as reflected in ASIC's strategic regulatory priorities.

More complete sub-sector data on the allocation of regulatory effort and resources would provide the regulated population with greater confidence that the allocation of costs among ASIC's regulated population is appropriate. The Proposal Paper notes that ASIC recently commenced a three-year programme to improve data on the regulatory effort it applies to various sub-sectors (and the types of expenses related to those efforts). However, it is not clear when this process will produce data that is of sufficient quality.

#### **Q7 Do you have any preliminary comments on the legislative arrangements?**

##### **ASFA response:**

ASFA broadly supports the proposed approach for the Superannuation Complaints Tribunal, user-initiated service costs, and for the proposed legislative arrangements – including the over/under-collection of levies.

### *Superannuation Complaints Tribunal*

ASFA welcomes the proposed approach for funding the Superannuation Complaints Tribunal (SCT). ASFA agrees that the SCT should continue to be funded from the Financial Institutions Supervisory Levies (FISL, levied by APRA), at least until the final outcomes of the Review of the financial system external dispute resolution and complaints framework (the Ramsay Review) are known. The interim report from that Review has recommended moving to a new external dispute resolution (EDR) framework for superannuation that would be both industry-based and directly-funded (by industry).

We note that in the event that a new funding model for superannuation EDR arrangements is recommended by the Ramsay Review and adopted by the Government, it would be critical to ensure that the SCT receives adequate funding from the FISL during any transition period. The level of funding provided to the SCT on an ongoing basis has not been adequate to ensure that it can deal effectively with the volume of complaints received within an appropriate timeframe. This shortfall in ongoing funding has had the tendency to cause a 'backlog' of unresolved complaints, which must then be addressed via additional funding allocations as part of the Budget process (most recently in the 2016-17 Commonwealth Budget).

ASFA also considers it important that, notwithstanding any eventual outcomes from the Ramsay Review, industry's concerns regarding deficiencies in the transparency and accountability of the SCT's funding are addressed. In particular, it is not clear how much of the FISL is currently collected on behalf of ASIC for disbursement to cover costs of operating the SCT, nor how much ASIC disburses for that purpose (this data is not disclosed in the most recent *Industry Levies Proposal* or the most recent *Cost Recovery Implementation Statement*).

#### *User-initiated service costs*

ASFA agrees that ASIC should delay implementation of the proposed fee-for-service framework. ASFA agrees with broader industry concerns that there was insufficient information in the *2015 Consultation Paper* to enable industry to assess properly the proposed fee-for-service framework or to provide suggestions for modifications or improvements to the methodology. ASIC should produce a revised fee-for-service framework only after it has accumulated the required data to make informed estimates of the costs of services.

As noted in ASFA's response to the *2015 Consultation Paper*, ASFA considers that where ASIC provides general relief from regulatory requirements via a class order after it has provided relief from those requirements to licensees in response to specific applications for relief, the fees paid by those licensees for lodgement and processing of their relief applications should be refunded.

#### *Over/under-collection of levies*

In principle, ASFA supports ASIC dealing with over/under-collection of levies via an adjustment to the following year's levy. However, it would be necessary to ensure that any under/over collections are accurately and transparently identified and attributed back to the relevant industry sector or sub-sector, and that ASIC's proposed treatment of under/over collections is highlighted as part of the annual levy consultation.

**Q8 Do you have any comments on the proposed implementation timetable? Please provide details of any concerns**

**ASFA response:**

ASFA has no specific concerns about the proposed timetable.

ASFA would like, however, to emphasise that any required changes to entities' IT and data systems will impose costs on entities. As such, ASIC should consult and communicate with industry on portal design and data reporting formats, and provide industry with adequate lead times to make required changes to IT and data systems.

*Required changes to IT systems*

The Proposals Paper states that entities would be expected to report their activity data to ASIC via an online portal. The Proposals Paper does not include additional information on the proposed portal, except that ASIC expects that it will be open to receive data towards the end of 2017.

ASIC's reporting requirements with respect to the industry funding model will require entities to make changes to their internal data reporting systems and to their IT systems. This will impose costs on those entities.

ASIC should seek to minimise these costs. ASIC should consult and communicate with industry on portal design and data reporting formats, and provide industry with adequate lead times to make required changes to IT and data systems. In general, industry requires a lead-time of around 12 months to implement required changes in the most cost-effective manner.

Entities' IT systems will need to be changed so that they can interact with the ASIC portal. For any change to IT systems, business requirement documents, and functional and technical specifications, must be agreed upon and signed off. The complexity of IT system design frequently necessitates complex testing to mitigate the risk of unintended consequences, which can take longer to perform than the initial coding of the changes to the system.

When it comes to implementing system changes, often there are capacity constraints – especially access to skilled/knowledgeable resources. Rushing to meet unrealistic regulatory deadlines increases the risks to a project and can increase costs materially, which are ultimately born by the consumers. Accordingly, any delays in finalising changes to regulatory obligations significantly affects the ability of providers to implement the required changes in an orderly and appropriately risk-managed fashion.

**Q9 What do you estimate the regulatory cost of complying with the new requirements in the model to be?**

**ASFA response:**

Regulated entities may provide estimates of compliance costs.

**Q10** Do you agree with the proposed business activity metrics and subsector groupings for calculating levies? If not, please outline you preferred approach and reasons for this preference.

**ASFA response:**

See Question 3.

**Q11** Which levy metrics are available within your business? And which are you currently reporting?

**ASFA response:**

Not applicable.