Chapter 25

ASIC's responsibilities and funding: problems with the current framework and suggested changes

25.1 This chapter considers two issues fundamental to ASIC's performance as a regulator: its functions and responsibilities and the resources available for it to perform these tasks. Successive governments have given additional responsibilities to ASIC at various times since it was established. In recent years there has been a marked increase in the functions ASIC has acquired.[1] This chapter considers the implications of this and, in light of the issues raised in previous chapters, the extent to which ASIC's growing list of functions and responsibilities has affected the agency's performance.

25.2 When considering the responsibilities given to ASIC, it is helpful, indeed necessary, to examine the resources given to ASIC to perform these tasks. Accordingly, this chapter also considers the amount of funding ASIC receives and whether the mechanism in place for funding ASIC should be changed.

Is ASIC overburdened and underfunded?

25.3 There is clearly a correlation between the list of responsibilities ASIC has, the funding it receives and the outcomes it can achieve. ASIC's submission contained the following statement on this relationship:

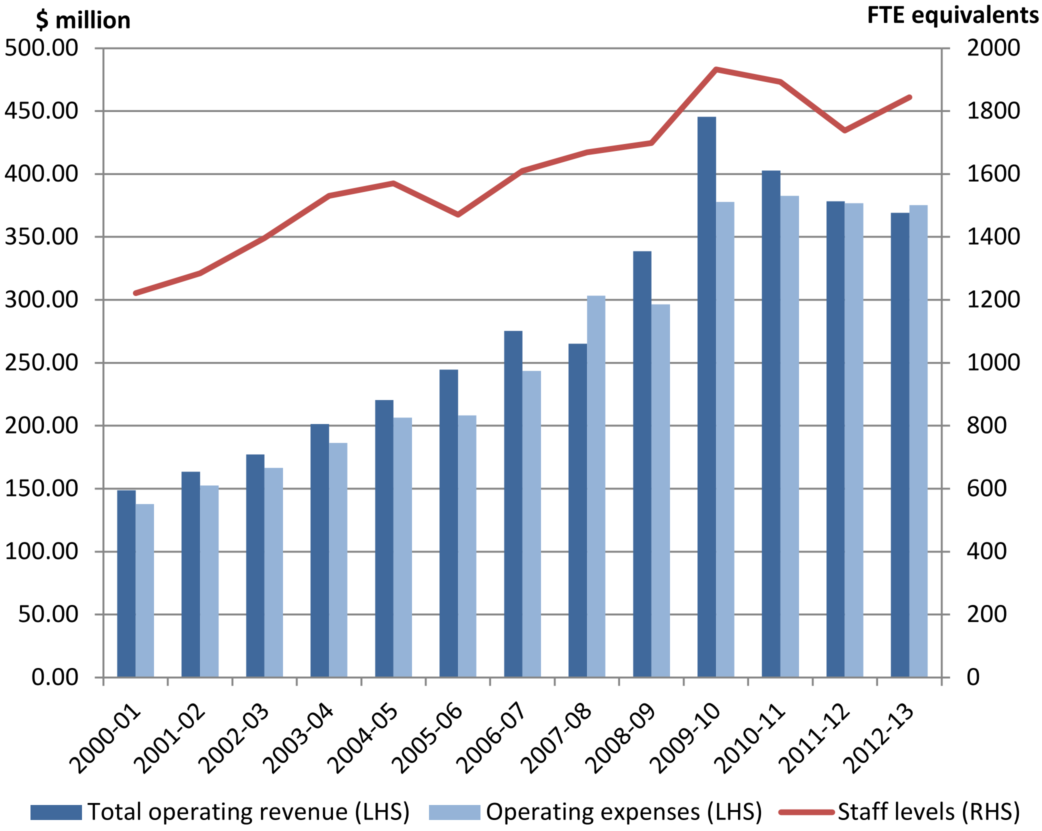
> What we are able to achieve also depends on our level of funding. Ensuring ASIC has adequate resources affects the strength and integrity of the financial system and the confidence of investors.
>
> ASIC can only achieve what it is resourced to do. Funding levels should be set by reference to Government and community expectations of what ASIC should deliver and, as a result, what level of resilience they want in the financial system.[2]

25.4 Figure 25.1 outlines ASIC's operating revenue, expenses and staff numbers since the 2000–01 financial year. Between 2000–01 and 2012–13, ASIC produced an operating surplus for eleven of the 13 financial years, averaging a $16.7 million surplus each year.

1 See Appendix 4 for a timeline of changes to ASIC's responsibilities.

2 ASIC, *Submission 45.2*, p. 11.

Figure 25.1: ASIC's operating revenue, expenses and staff levels, 2000–01 to 2012–13



Source: Figures for operating revenue and expenses taken from research prepared by the Parliamentary Library, based on cash flow statements contained in ASIC's annual reports, various years. Figures for staff levels are taken from ASIC's annual reports, various years.

Note: Total operating revenue includes appropriation revenue and other cash received.

25.5 A 2012 report prepared by staff of the International Monetary Fund (IMF) argued that ASIC 'has rightfully earned its reputation as an effective and credible enforcer of market regulation, but would benefit from increased resources and budgetary flexibility'. The IMF staff argued that:

> …ASIC is hampered in its ability to fully carry out proactive supervision because of the lack of budgetary resources. A significant amount of ASIC's funding is non-core funding earmarked for specific projects, and the share of non-core funding has been increasing in the last few years. To supervise a large number of financial services licensees, ASIC uses desk-top, rather than on-site, reviews for initial risk-based assessments, reflecting in part its resource constraints. In determining the target and intensity of its supervisory actions, ASIC relies heavily on its initial risk-based assessments, self-reporting of breaches of regulatory requirements and third

> party notifications. It is important that ASIC be given more resources and flexibility over its operational budget.[3]

25.6 Many individuals and organisations agreed that ASIC is currently underfunded. A view also frequently expressed was that ASIC's expanded regulatory remit had negatively affected ASIC's performance. This was either as a logical consequence of ASIC having a longer and more diverse list of responsibilities, or because the additional funding provided to supplement specific new responsibilities has been insufficient. The following extracts from the evidence taken by the committee illustrate some of the concerns:

> In recent years, two trends regarding ASIC have emerged. Firstly, ASIC has been given increasing responsibility for important areas of corporate and financial regulation, including stock market regulation, financial services licensing, consumer protection in financial services, business names registration and credit regulation. These matters add to ASIC's already full regulatory brief covering general corporate regulation and administrative matters (document lodgments, searches and maintenance of registers). During this time while ASIC's funding has increased, much of the funding has been tied to particular projects (such as key investigations into HIH and other high profile matters), and the numbers of staff working at ASIC has only increased from 1221 in 2000 to 1738 in 2012 (according to ASIC's Annual Reports). The increases in funding and staffing are wholly inadequate to account for exponential increase in ASIC's responsibilities.[4]

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> …the increase in ASIC's mandate over the last decade has not been matched by financial appropriations and has stretched its personnel.[5]

* * *

> …the constant accrual of functions and services by ASIC has played some part in reducing the ability of ASIC to devote resources to its legislative, surveillance and investigative responsibilities.[6]

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> Our sense is that the problem ASIC has is complexity of legislation, huge areas of responsibility and resources that are too limited. It is not a lack of powers, it is a lack of resources, really, and the practical ability to make things happen.[7]

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3 International Monetary Fund, *Australia: Financial System Stability Assessment*, IMF Country Report, no. 12/308, November 2012, pp. 25–26.

4 Mr Jason Harris, *Submission 116*, p. 1.

5 Professor Dimity Kingsford Smith, *Submission 153*, p. 5.

6 Governance Institute of Australia, *Submission 137*, p. 6.

7 Mr Bruce Dyer, Member, Corporations Committee, Business Law Section, Law Council of Australia, *Proof Committee Hansard*, 20 February 2014, p. 6.

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> In our view, any deficiencies in ASIC's performance and effectiveness are more likely to be caused by a lack of adequate funding and resources to allow ASIC to fulfil its role as a corporate regulator. Being well-funded and resourced is essential for a regulator to be able to effectively use its powers and discharge its duties. Relevantly, being adequately resourced allows a regulator to be more pro-active and therefore maximise the chances of ASIC being able to properly enforce existing legislation. Company Directors has long called for and supported moves to provide appropriate funding to ASIC and other regulators to meet the increasing demands that they face, and we continue to believe that this is the best way to increase ASIC's performance as a regulator.
>
> This lack of funding is likely, at least in part, to be due to the fact that ASIC's role as a regulator has been increased significantly over time and its resources have been stretched as a result. In addition to increasing the existing funding and resources of ASIC, going forward ASIC's roles should only be added to or extended where there is also a commensurate increase in ASIC's funding and resources.[8]

* * *

> The finance world is increasingly complicated with emerging risks and challenges. It is essential that ASIC is adequately funded and resourced to carry out its duties. We would not support any proposals to cut ASIC's funding.[9]

25.7 Members of the public that had dealt with ASIC also called for ASIC to receive more funding:

> ASIC needs more funding to go after criminals and credit providers. ASIC should have enough funding that it can anticipate rorts and take steps to protect people…There is a perception in the community that ASIC is reluctant to take a stand possibly because of lack of funding.[10]

25.8 Others were less sure. Levitt Robinson Solicitors argued that 'ASIC's failures cannot be blamed on budgetary constraints, given ASIC's apparent profligacy in the deployment of public money spent on, or in outsourcing legal services'.[11] CPA Australia noted that ASIC is possibly overworked, but it considered other problems with ASIC's approach were more significant:

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8 Australian Institute of Company Directors, *Submission 119*, p. 2.

9 Industry Super Australia, *Submission 201*, p. 12.

10 Name withheld, *Submission 135*, p. 1.

11 Levitt Robinson Solicitors, which criticised various aspects of ASIC, noted that ASIC was second only to the ATO in expenditure on legal fees, with $300 million spent by ASIC between 2008 and 2012. The figures are based on the Attorney-General's Department's *Legal Services Expenditure Report 2011–2012*. Levitt Robinson Solicitors, *Submission 276*, p. 11.

> I think there has been a lot of commentary by ASIC to say that they are very stretched with their resources and there is more to do. There may be an element of truth in that argument. I think the bigger issue is that their sense of priority needs to be revisited.[12]

25.9 The Institute of Chartered Accountants Australia (ICAA) noted that all organisations face financial pressure and need to ensure they use the resources they have as efficiently as possible. The ICAA argued that ASIC is currently undertaking work which 'generally has very little effect but consumes quite a lot of resources'.[13] On this issue, the Community and Public Sector Union (CPSU) acknowledged that every organisation needs to focus on and review whether it is undertaking activities in the most efficient way. However, the CPSU argued:

> …if you are not actually reinvesting in the work that is needed to be done, and having that investment being made then you are likely to see the services slip. And I think we sometimes confuse at the moment conversations about productivity and effectiveness with cuts.[14]

25.10 It is evident that funding issues are not just relevant to ASIC; rather they are something that all regulators encounter. The former chairman of the Trade Practices Commission, the predecessor to the ACCC, argued that there 'is a fundamental flaw in the way in which our regulators are funded':

> Having acted as chairman of the Trade Practices Commission (TPC)…I can say with complete confidence that the level and nature of funding provided to the TPC at the time to conduct its various activities was well below what was needed to properly and adequately undertake its tasks. This was certainly the case in the context of community and media (and some politicians') expectations of the role of the regulator. The apparent unwillingness of the TPC to undertake certain investigations or to pursue certain court actions was often misunderstood, because the critics did not appreciate the problems that the regulator faced due to its inadequate and restricted use of its funding.[15]

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12 Mr Alex Malley, Chief Executive Officer, CPA Australia, *Proof Committee Hansard*, 19 February 2014, p. 46.

13 Mr Lee White, Chief Executive Officer, Institute of Chartered Accountants Australia, *Proof Committee Hansard*, 19 February 2014, p. 46. In its submission, the ICAA argued that 'there are many examples where ASIC initiates a specific regulatory program that targets particular areas of focus in the marketplace, but then continues to allocate resources to the same program even when many would argue that the impact (or relevance) in the marketplace of the work that continues to be done has significantly diminished'. The ICAA used ASIC's accounts surveillance program as an example; in the ICAA's view that program 'was initially very effective in lifting the standard of financial reporting in Australia. However, many stakeholders in the capital markets would question whether ASIC's work continues to have a major impact on the quality of financial information in the marketplace, given that many of ASIC's initial objectives have now been met'. *Submission 203*, p. 3.

14 Mr Alistair Waters, CPSU, *Proof Committee Hansard*, 19 February 2014, pp. 63–64.

15 Professor Bob Baxt AO, *Submission 189*, pp. 6–7.

25.11 Professor Baxt added that regulators also have 'inadequate' resources to bring cases that challenge well-resourced defendants that 'usually enjoy deep pockets and are not burdened by significant restrictions in the way in which they operate in defending the relevant matter'.[16]

25.12 Whether ASIC has sufficient resources to adequately supervise the entities it regulates can also be considered by reviewing the number of staff ASIC allocates to each group of the regulated population. As noted in Chapter 4, ASIC publishes figures on the number of staff members allocated to each of its stakeholder teams, the number of regulated entities they oversee and the number of years it would theoretically take to conduct surveillance on every regulated entity. These figures highlight the challenges ASIC faces in fulfilling its regulatory responsibilities with its current resources. For example, ASIC has 29 staff members that oversee 3,394 AFS licensees authorised to provide personal advice as well as 1,395 AFS licensees authorised to provide general advice. Approximately 65 staff members oversee: 173 authorised deposit-taking institutions; 141 insurers; 641 licensed non-cash payment facility providers; 13 trustee companies; and 5,688 non-ADI credit licensees with 28,201 credit representatives. These figures were outlined in full in Chapter 4 (refer to Table 4.1).

25.13 However, striking figures on supervision coverage and an imbalance between the regulator's financial resources and those of the large firms it regulates are not unique to ASIC. For example, in recent fiscal year budget requests to the United States Congress, the Securities and Exchange Commission (SEC) has given the following bleak assessments of its resources and capacities:

> …during the past decade, trading volume in the equity markets has more than doubled, as have assets under management by investment advisers, with these trends likely to continue for the foreseeable future. A number of financial firms spend many times more each year on their technology budgets alone than the SEC spends annually on all its operations. Similarly, SEC enforcement teams bring cases against firms that spend more on lawyers' fees than the agency's annual operating budget.[17]
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> * * *
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> Currently, the average transaction volume cleared and settled by the seven active registered clearing agencies is approximately $6.6 trillion a day. Yet the SEC only has approximately sixteen examiners devoted to them, with limited on-site presence in only three of the seven.[18]
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> * * *
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> Seven years ago, the SEC's funding was sufficient to provide nineteen examiners for each trillion dollars in investment adviser assets under

16 Professor Bob Baxt AO, *Submission 189*, pp. 6–7.

17 US Securities and Exchange Commission, *FY 2014 Congressional Budget Justification*, www.sec.gov/about/reports/secfy14congbudgjust.pdf, p. 4 (accessed 19 September 2013).

18 US Securities and Exchange Commission, *FY 2014 Congressional Budget Justification*, p. 6.

management. Today, that figure stands at ten examiners per trillion dollars.[19]

How do ASIC's responsibilities compare with foreign regulators?

25.14 The breadth of responsibilities entrusted to ASIC compared to regulators in other jurisdictions was noted by witnesses and used to argue that a review of ASIC's responsibilities was warranted:

> At the moment ASIC has an incredibly broad remit in comparison to most securities regulators globally. If there was that reduction in supervisory capacity or its responsibilities perhaps it would allow it to focus more specifically on some of the issues which concern so many of the people who made submissions to the inquiry and the members of this committee.[20]

25.15 Even a cursory comparison of Australia's framework of regulators and those of other key jurisdictions indicates that the breadth of ASIC's responsibilities is significantly greater than those of its foreign counterparts. In the UK, for example, ASIC's securities and markets regulation functions are undertaken by the Financial Conduct Authority (FCA). The FCA also has responsibility for market supervision and governance (through the UK Listing Authority, a division of the FCA). The FCA also is tasked with financial products and services regulation and credit and financial services licensing. However, the FCA does not have responsibility for matters relating to the corporations law generally, such enforcing directors' duties or regulating auditors and insolvency practitioners. Company registration is performed by Companies House, an executive agency of the Department for Business, Innovation and Skills.

25.16 In the US, ASIC's securities and markets regulatory counterpart is the SEC, with some functions also performed by the Federal Commodity Futures Trading Commission (CFTC) and state authorities. However, the Consumer Financial Protection Bureau (CFPB) is tasked with financial products and services regulation, and credit and financial services licensing is undertaken by state authorities. The regulation of auditors is carried out by the Public Company Accounting Oversight Board (PCAOB), although this is overseen by the SEC. Reflecting the chapter 11 bankruptcy and reorganisation system in place in the US, corporate insolvency is dealt with by specialist bankruptcy courts with an office in the Department of Justice (the US Trustee Program) responsible for overseeing the administration of bankruptcy cases.

25.17 In Canada, provincial and territorial regulators are responsible for securities and markets regulation and market supervision. The Financial Consumer Agency of Canada (FCAC) supervises financial institutions' compliance with consumer

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19 US Securities and Exchange Commission, *In Brief: FY 2013 Congressional Justification*, www.sec.gov/about/secfy13congbudgjust.pdf, p. 2 (accessed 19 September 2013).

20 Dr George Gilligan, *Proof Committee Hansard*, 19 February 2014, p. 52.

protection obligations and promotes increased financial literacy. Financial advice is regulated by provincial and territorial agencies. The federal registration of companies is administered by Corporations Canada with provincial agencies registering other companies. The Canadian Public Accountability Board deals with auditors.

Should ASIC lose some of its functions?

25.18 Following on from the previous discussion, this section examines the evidence received by the committee that questioned the wisdom of one agency being given numerous important regulatory and law enforcement functions as well as other administrative responsibilities. During the course of the inquiry, various possible changes that could be considered were suggested or noted by stakeholders. These options, which are discussed in the following paragraphs, include:

- transferring ASIC's corporate and business name registry functions to another government agency, or privatising these functions;
- splitting ASIC into smaller regulators along the lines of its broad business areas; and
- transferring responsibility for consumer protection to the ACCC or creating a new consumer protection agency.

Corporate registration and other administrative functions

25.19 Since ASIC was established it has been responsible for the administration of corporate registration. However, in 2012 ASIC also gained responsibility for the registration of business names after this function was transferred from the states and territories to the Commonwealth. ASIC also maintains a register of SMSF auditors. Stakeholders questioned whether it was necessary for these functions to be performed by a regulator such as ASIC.

25.20 The devolution of ASIC's registry function to another body was noted by the Governance Institute of Australia as a possible change that could allow ASIC to devote resources to its other legislative, surveillance and investigative responsibilities. To facilitate this, an equivalent of the UK's Companies House could be established in Australia.[21]

25.21 The committee is not aware of an example of an advanced economy where the company registration function is undertaken by the securities and markets regulator. In a newspaper article published in 2010, former ASIC chairman Alan Cameron was reported as identifying Pakistan as the only other country where these roles are combined.[22] When asked about ASIC's registry responsibilities, the current ASIC chairman described them as a 'technology business' and 'not really a regulatory business'. Mr Medcraft also considered there were a number of opportunities

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21 Governance Institute of Australia, *Submission 137*, p. 6.

22 Stuart Washington, 'ASICs powers put to the test', *The Age*, 5 June 2010, p. 4.

to leverage economies of scale and to create a better user experience by transforming ASIC's registry function. As an example, he referred to merging ASIC's corporate register with other government registries:

> The Siebel system we have has, currently, six million names on it. Verizon use the Siebel system in the States for telephones. They have 70 million customers on it. So I think there are huge benefits in actually separating out that registry business and merging it with other government registries to leverage the economies of scale from the Siebel management system. Basically, it has enormous capacity.
>
> What that also means from a consumer perspective is that you end up with a one-stop shop for financial services and even other registry things you go to. If you want to update, you want to go to one place et cetera. And you have to think about the massive opportunity for extracting revenue from the metadata that actually comes from that.[23]

25.22 Mr Medcraft explained that although ASIC has its newest registers[24] operating on the more advanced system, ASIC does not have the resources to invest in the corporate register. Mr Medcraft opined that there 'is cash there for somebody':[25]

> …at the moment we have only two registers on the Siebel management system. We have the business names and we have the self-managed super funds. We have not got the capital to invest to bring the corporate register onto that. If I were in the private sector, I would finance it as a banker because that $70 million, by moving those registers onto Siebel, would allow things like person search so every Australian could log on and check everything a person has to do with ASIC—whether they are deregistered or whatever. It also allows for online company registration. That $70 million, if you were in private enterprise, you would invest because the cash flow you would get out of it would pay back. It is 10-year payback in simple, straight cash. It removes all the duplication across the registers.
>
> There are economies of scale. Potentially, an investment in that could eventually yield $350 million of benefits to small businesses outside of that. So I think the registry is one that probably would be better moved out, aggregated with other registries to provide a one-stop shop for Australians.[26]

25.23 A small business owner similarly observed that ASIC's corporate and business names registers do not appear to have a regulatory role 'beyond maintaining up-to-date information and not registering conflicting names'. After expressing criticism about the fees levied on small businesses to fulfil their obligations to provide information, the fees imposed to access information, and ASIC's performance at managing

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23 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, pp. 33–34.

24 The registers for business names and SMSF auditors.

25 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, p. 38.

26 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, pp. 33–34.

the register, the small business owner concluded that a commercial enterprise could undertake ASIC's registry functions for less than 'one tenth of the fee ASIC charges'.[27] Other submissions also noted the cost of accessing information on ASIC's register, such as $18 to obtain each current and historical extract of a company.[28]

25.24 The Governance Institute of Australia observed that ASIC's registry and other administrative functions, including its call centre, do not utilise senior or experienced ASIC staff; in fact it indicated that 'call centre staff appear to be trained only to the extent of referring callers to the ASIC website in situations where there is uncertainty about the interpretation of specific provisions'. The Institute argued that:

> …there may be service efficiencies to be gained by ASIC outsourcing its administrative function in a bid to broaden its educative function. That is, it might be cost-effective for ASIC to use a commercial operator to run its administrative function rather than maintaining these responsibilities inhouse.[29]

25.25 The CPSU was asked about the possibility of certain functions being separated from ASIC and privatised. The CPSU argued that, as the registries raise 'a reasonably significant source of income and would appear to be a monopoly service', it would be in the public interest for an Australian government body to be tasked with the function, rather than the function being privatised.[30]

25.26 Academics also commented on how privatising ASIC's registry function could affect the provision of information for research purposes. Mr Jason Harris, in consultation with other academics, recommended that if ASIC's registry was privatised, that this only occur with a requirement that information continue to be provided for research and accountability purposes.[31]

25.27 In May 2014, as part of the 2014–15 Budget, the government announced that a scoping study would be undertaken into future ownership options for ASIC's registry function.[32]

Split along clusters or tasks

25.28 Stakeholder organisations and academics also identified other possible changes to Australia's framework of regulatory institutions. One of the options for consideration identified by the Governance Institute of Australia was dividing ASIC into smaller agencies with specific tasks:

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27 Name withheld, *Submission 263*, pp. 3, 8.

28 See Mr Jeffrey Knapp, *Submission 274*, pp. 3, 6, 8 and 9.

29 Governance Institute of Australia, *Submission 137*, p. 6.

30 Mr Alistair Waters, CPSU, *Proof Committee Hansard*, 19 February 2014, p. 64.

31 Mr Jason Harris, answer to question on notice, no. 8 (received 17 April 2014), p. 4.

32 Australian Government, *2014–15 Budget—Budget Paper No. 2*, May 2014, p. 117.

> [A] number of smaller regulators could be established to manage the wide range of regulatory functions currently allocated to ASIC, leaving ASIC focused solely on its original regulatory functions or more limited regulatory functions than it is currently tasked to manage.[33]

25.29 CPA Australia suggested that thought could be given to restructuring ASIC and setting clear priorities:

> I think it is worth a conversation and some questions perhaps around splitting ASIC into some segments that can focus on particular things. When you have a regulator on Monday chasing a corporate, on Tuesday charging a small business and on Wednesday giving marriage cost advice, that says that perhaps we need to pause for a moment, set the agenda for the year, tell the public what they can expect and let's see how accountable you are, because that is what you keep telling others they have to be.[34]

25.30 Associate Professor David Brown noted the committee's 2010 report that recommended that ASIC's insolvency functions be transferred to the Insolvency & Trustee Service Australia (ITSA), since renamed the Australian Financial Security Authority. Professor O'Brien added that:

> …a lot of the rules for that body would come from the best practice of ITSA, which had shown itself to be a more effective regulator in that area, because 'insolvency' was in its title as opposed to it being one of the many functions of ASIC…[35]

Consumer protection responsibilities

25.31 Some witnesses suggested that the division of consumer protection responsibilities between ASIC, which has responsibility for consumer protection in financial products and services, and the ACCC, which has responsibility for consumer protection in the remaining sectors of the economy, should be reviewed.[36] Other submissions outlined different proposals. For example, many individuals dissatisfied with their treatment by ASIC and external dispute resolution schemes called for the creation of an agency dedicated to consumer protection in financial services.[37] A former ASIC employee argued that ASIC has too much work and that this detracts from ASIC's ability to protect retail investors:

> These are the working Australians—the millions of people who are putting the money into the superannuation system and are least empowered to protect themselves. They are the ones who need the most protection. I think they are the ones who have been let down the most by ASIC, and I think the

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33 Governance Institute of Australia, *Submission 137*, p. 6.

34 Mr Alex Malley, CPA Australia, *Proof Committee Hansard*, 19 February 2014, p. 51.

35 *Proof Committee Hansard*, 19 February 2014, p. 55.

36 Professor Justin O'Brien, *Proof Committee Hansard*, 19 February 2014, pp. 55–56.

37 For example, see *Submissions 51.1*, p. 1; *199*, p. 1; *254*, p. 1; *351*, p. [3].

> only way that you can really get them protected is with an agency that is dedicated to nothing but protecting retail investors.[38]

25.32 In reaching its recommendation that responsibility for consumer protection in financial services should be transferred from the ACCC to the agency that ultimately became ASIC, the Wallis Inquiry considered alternative approaches. In particular, the Wallis Inquiry noted concerns put to it that without a dedicated consumer protection agency for financial services 'consumer protection would otherwise become subservient to other objectives'. However, the report concluded that:

> …this risk is more likely to arise where consumer protection is combined with the functionally different task of prudential regulation. The tasks of consumer protection, market integrity and corporations regulation are more complementary than conflicting.[39]

25.33 The approach taken following the Wallis Inquiry was queried at the time[40] and more recently. In 2008, the Productivity Commission found that the financial services carve out from the general consumer law occasionally leads to uncertainty about whether the ACCC or ASIC had jurisdiction. The Productivity Commission recommended that the economy-wide jurisdiction of the ACCC for consumer protection be restored but with ASIC continuing to be the primary regulator for financial services.[41] Around the time of the Productivity Commission inquiry, a former ACCC chairman and a former editor of the *Australian Financial Review* wrote in various newspaper opinion articles that '[t]he natural home of financial consumer protection is the ACCC, not the carve-out to ASIC created by Wallis';[42] ASIC had a 'noted lack of consumer zeal to date'; and the government should consider making the ACCC the sole consumer regulator, including for financial services as '[c]arving out these powers for ASIC has not worked'.[43] Concerns about the current framework remain; for example, in late 2013 a Monash University forum on the government's upcoming review of competition policy suggested that the review

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38 Mr James Wheeldon, *Proof Committee Hansard*, 2 April 2014, p. 23.

39 Financial System Inquiry, *Final Report*, March 1997, p. 244.

40 A research paper produced soon after the Wallis Inquiry report was released surveyed the arguments opposing some of the key conclusions and recommendations. See Phil Hanratty, 'The Wallis Report on the Australian Financial System: Summary and Critique', *Parliamentary Library Research Paper*, no. 16 1996–97, www.aph.gov.au/About_Parliament/Parliamentary_Departments/Parliamentary_Library/pubs/rp/RP9697/97rp16 (accessed 20 August 2013) (footnotes omitted).

41 Productivity Commission, *Review of Australia's Consumer Policy Framework*, vol. 1, report no. 45 (30 April 2008), p. 24.

42 Allan Fels and Fred Benchley, 'Consumer watchdog tipped to get more bite as Rudd revolution gains pace', *The Age*, 5 April 2008, p. 2.

43 Fels and Benchley, 'Consumer watchdog tipped to get more bite as Rudd revolution gains pace', p. 2; 'Rudd's consumer activism over the top', *Sydney Morning Herald*, 21 March 2009, p. 4.

should consider whether the ACCC's and ASIC's consumer law functions 'should be jointly administered by a single separate body'.[44]

25.34 It is noteworthy, however, that recent reforms undertaken in other countries have not resulted in responsibility for financial services consumer protection being taken from the securities regulator and given to the general consumer protection agency. For example, in the United Kingdom the opposite has occurred.[45]

Proposal for a user-pays funding model

25.35 In addition to suggestions that some of ASIC's responsibilities be transferred to other bodies, the committee explored how ASIC is funded and whether the current funding model encourages better regulatory outcomes.

25.36 Although ASIC collects fees, charges and fines on behalf of the Commonwealth, this substantial revenue ($717 million in 2012–13) is returned by ASIC to consolidated revenue.[46] With the exception of some cost-recovery arrangements,[47] the majority of ASIC's funding has no relationship with the revenue collected by ASIC.[48] Nevertheless, the fact that ASIC collects significantly more revenue than its operating expenses was noted in submissions.[49] Further, although the growth in revenue from Corporations Act fees appears steady, Treasury's submission, received in October 2013, noted that ASIC's funding was projected to decline.[50] In May 2014, the government announced that it would achieve savings of $120.1 million over five years by reducing funding given to ASIC, with ASIC's funding reduced in the first year by $26 million. The impact of the savings announced by the government and the termination of various measures are outlined in Table 25.1.

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44 Monash Business Policy Forum, *Agenda for National Competition Policy Inquiry (2013)*, November 2013, www.buseco.monash.edu.au/mbpf/agenda.pdf (accessed 21 November 2013), p. 18.

45 On 1 April 2014, responsibility for the regulation of consumer credit was transferred from the Office of Fair Trading, the UK's general consumer protection regulator, to the Financial Conduct Authority. Further, in the US, the creation of the CFPB consolidated the administration of federal consumer financial protection laws, a responsibility previously shared by various agencies such as the Federal Trade Commission.

46 As required by section 81 of the Constitution.

47 Operators of domestic licensed financial markets regulated by ASIC and some market participants are subject to an annual levy. Levies collected by the APRA and the ATO also cover some of the costs of ASIC. See APRA, *Annual Report 2013*, p. 81; Treasury, *Submission 154*, p. 4.

48 Treasury, *Submission 154*, p. 4.

49 For example, see Industry Super Australia, *Submission 201*, p. 11.

50 Treasury, *Submission 154*, p. 4.

Table 25.1: Projected funding for ASIC, 2013–14 to 2017–18 ($ million)

($ million)	2013–14	2014–15	2015–16	2016–17	2017–18
Changes announced in 2014–15 Budget	3.0	–26.0	–32.5	–32.1	–32.4
Total annual department expenses*	366.28	321.25	306.04	303.40	306.29

* This funding relates to ASIC's annual departmental expenses under for its main functions (in the Budget papers, this is Programme 1.1 under Outcome 1). That is, ASIC's expenses for the administration of unclaimed money from banking and deposit taking institutions and life insurance institutions are not included.

Source: Australian Government, *2014–15 Budget: Budget Related Paper No. 1.16*, Treasury Portfolio Budget Statements, May 2014, p. 159.

25.37 The committee reviewed the funding arrangements in place for foreign regulators. As with ASIC, the US SEC collects fees and has funding linked to government appropriations. However, the arrangement is different in that there is more of a direct link between revenue raised and funding.[51] Another US agency, the CFPB, primarily receives its funding from the Federal Reserve. Subject to statutory rules and limits, the CFPB determines the amount of funding necessary to fund its operations. The funding is not subject to review by Congress.[52] While these arrangements attract some controversy,[53] it does provide the CFPB with a relatively stable source of funding.

25.38 An alternative model of funding a regulator already utilised in Australia and prevalent internationally is based on cost-recovery levies. In Australia, industry levies are used to fund APRA and, as noted earlier, a small proportion of ASIC's functions. ASIC's chairman noted that, internationally, levies are the predominant means by which regulators are funded.[54] Examples of foreign regulators that receive funding

51 The fees collected by the US SEC offset the appropriation it receives, and in recent years total fees have been a similar amount to the funding the SEC receives through appropriations resulting in most appropriated funds being returned. US SEC, *Fiscal Year 2012 Agency Financial Report*, November 2012, www.sec.gov/about/secpar/secafr2012.pdf (accessed 18 September 2013), p. 36.

52 The CFPB can also request from Congress discretionary appropriations if the amount received from the Federal Reserve is insufficient, however, it has not yet needed to make such a request. See US CFPB, *Fiscal Year 2013: CFPB budget in brief*, http://files.consumerfinance.gov/f/2012/02/budget-in-brief.pdf (accessed 19 September 2013), p. 1.

53 These funding arrangements have been criticised by some members of Congress: see US House of Representatives Committee on Financial Services, 'CFPB Lacks Oversight and Accountability', *Media Release*, 18 June 2013, http://financialservices.house.gov/news/documentsingle.aspx?DocumentID=339512 (accessed 19 September 2013).

54 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, p. 29.

from industry levies include the UK FCA[55] and the New Zealand Financial Markets Authority. ASIC also identified that regulators in Canada, France, Hong Kong and Malaysia are funded through various forms of levy arrangements.[56] Other foreign professional bodies such as the US Public Company Accounting Oversight Board, which oversees audit standards and quality, are similarly funded through levies imposed on main accountancy firms based on their market size.[57]

25.39 While not necessarily advocating that ASIC should be funded by industry-based levies, Industry Super Australia outlined some of the benefits and disadvantages it considered such arrangements would have:

> It would ensure that the cost of the regulatory framework is borne by those who give rise to the greatest regulatory burden, so that the funding is not just borne out of general revenue. That is obviously a clear advantage. ASIC raises a reasonable amount of revenue in its activities, particularly in markets. In terms of the disadvantages I suppose it changes the nature of the relationship that ASIC has with industry. If there are parts of industry that are providing a greater level of funding, it might alter the perception of the independence of the regulator from those parts of the industry.[58]

25.40 ASIC was questioned about its funding patterns and alternative funding models such as a levy-based arrangement. Mr Medcraft outlined how, in his view, ASIC's expanding responsibilities had created a 'problem' with ASIC's funding model. He explained that when ASIC was established as a corporate regulator, the fees collected and costs incurred were 'reasonably correlated'; that is, in the early 1990s it cost ASIC around $127 million a year (in nominal terms) to regulate corporations but it collected around $189 million in revenue on behalf of the Commonwealth. However, over time this connection has become weaker. ASIC's costs for regulating corporations have fallen in real terms to about $142 million, largely as a result of technological advancements. The revenue from company regulation and business names registration is now around $680 million, 80 per cent of which comes from small businesses.

25.41 Reflecting the expansion in ASIC's responsibilities since it was established, ASIC now allocates the majority of its financial resources to its non-registry

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55 The estimated amount required to fund the FCA's budgeted costs for the year ending 31 March 2014 is £432.1m which is the figure used when determining the fees that will be charged. FCA, *Business Plan 2013/14*, www.fca.org.uk/static/documents/business-plan/bp-2013-14.pdf, pp. 53, 55 (accessed 17 September 2013). The New Zealand Financial Markets Authority is funded by a mixture of cost recovery fees and direct government funding. NZ Financial Markets Authority, 'How we are funded', www.fma.govt.nz/about-us/who-we-are/how-we-are-funded (accessed 24 March 2014).

56 See *Proof Committee Hansard*, 19 February 2014, p. 33 and ASIC, *Submission 45.7*, p. 8.

57 Professor Justin O'Brien, *Proof Committee Hansard*, 19 February 2014, p. 53.

58 Ms Robbie Campo, Deputy Chief Executive, Industry Super Australia, *Proof Committee Hansard*, 20 February 2014, p. 32.

functions. ASIC's overall costs are currently around $350 million. The approximately $260 million in costs that do not relate to corporate regulation are attributable to three areas of responsibility ASIC has gained over time: financial services; consumer credit; and markets. Mr Medcraft explained that of these three growth areas, ASIC has only received additional revenue associated with the markets function (about $30 million), and even then only ASIC's frontline costs are recovered.[59] Therefore, despite the significant financial services and markets functions ASIC now performs, it could be considered that the revenue streams from Corporations Act fees effectively results in the burden of funding ASIC disproportionally falls on small business.

25.42 To further bolster its argument that the current framework may not be fairly allocating the burden associated with funding ASIC's regulatory functions, ASIC's chairman advised that:

- auditors cost ASIC about $6 million a year to regulate but only pay $425,000 in fees (also, regardless of any difference in the allocation of resources necessary to regulate large audit firms compared to small firms, both large and small firms pay $146);[60] and
- AFS licensees cost ASIC $108 million a year to regulate but only pay $3.7 million in fees.[61]

25.43 The following diagrams summarise ASIC's evidence about how the revenue it collects on behalf of the government and the cost of performing particular regulatory activities have changed over ASIC's history.

59 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, pp. 29, 30.

60 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, pp. 31–32.

61 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, p. 33.

Figure 25.2: Revenue and costs—companies, business names and searches 1991–2013 (nominal terms)

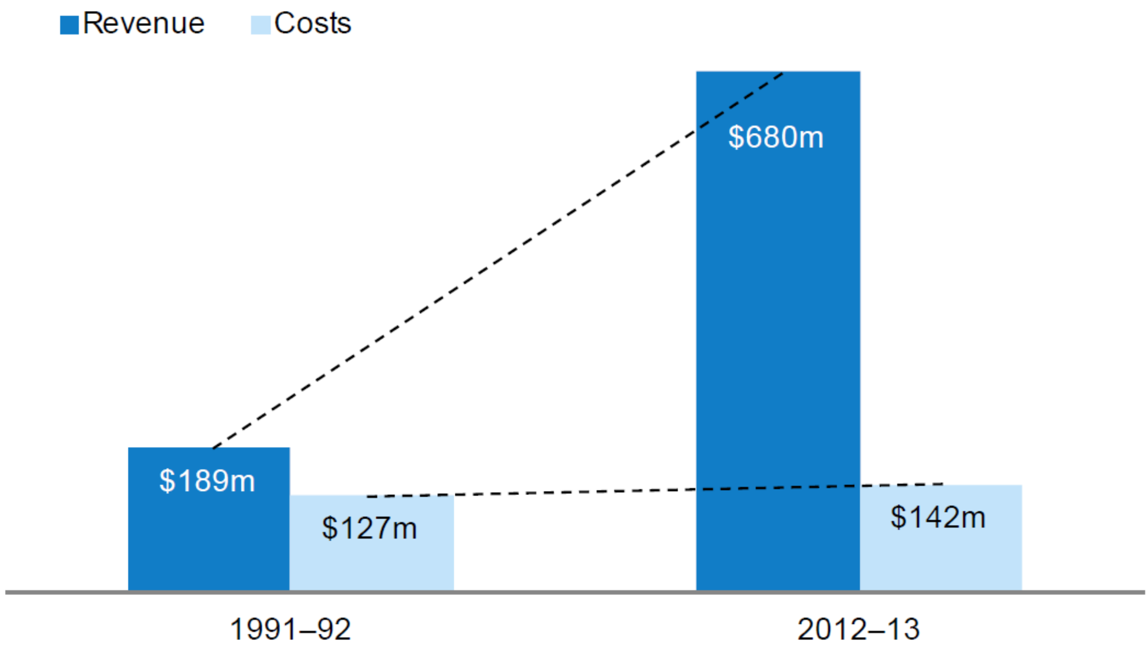
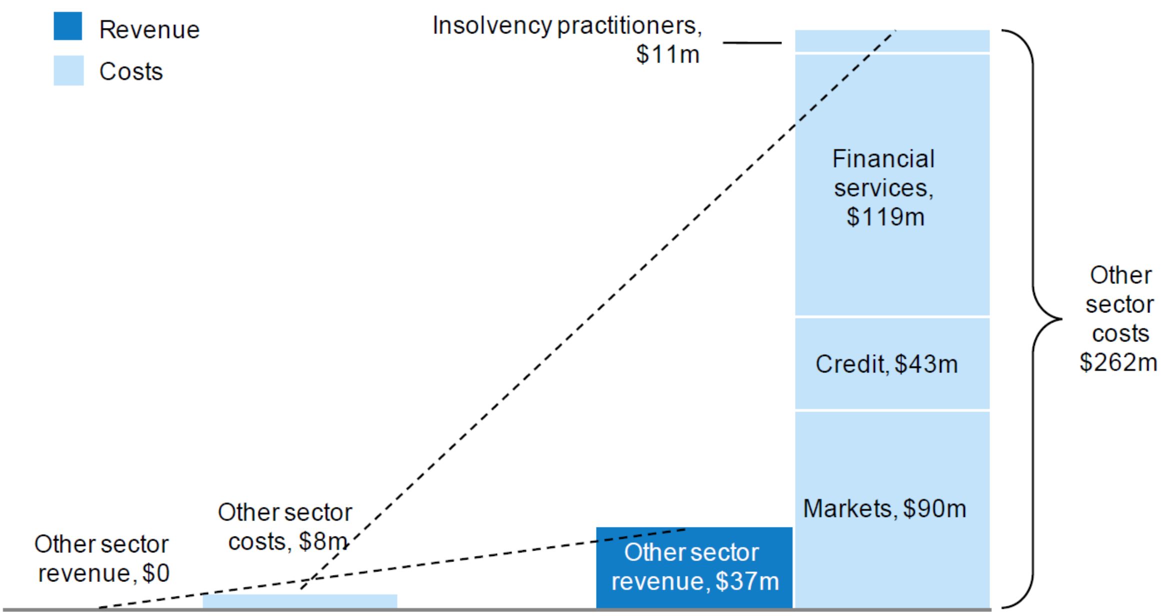


Figure 25.3: Revenue and costs—all other sectors 1991–2013 (nominal terms)



Note: Figures are estimates only, and are not adjusted for inflation. Costs include depreciation. In Figure 25.2, revenue is from companies, business names and searches; costs are from regulating companies, including administering business names and searches. In Figure 25.3, 'Other sectors' includes insolvency practitioners, AFS licensees, credit providers, exchange market operators, market participants and consumers. 'Financial services' includes financial advisers, insurers, responsible entities, superannuation fund trustees, deposit takers, investment banks, consumers and custodians.

Source: ASIC, *Submission 45.7*, pp. 2–3.

25.44 Mr Medcraft stated that he is 'a very big believer in user-pays'. After reflecting on his evidence about how ASIC's costs and its responsibilities have changed over time, Mr Medcraft observed that 'those that generate the need for regulation should pay for that regulation', and that user-pays systems are 'far more transparent'.[62] In addition to arguments based on fairness and accountability, ASIC's chairman also argued that a user-pays levy model could lead to better outcomes for the financial system. According to Mr Medcraft, a well-designed levy system could encourage better self-regulation and lead to more efficient regulatory outcomes:

> The fundamental concept here—from my days in banking—is that frankly if you provide somebody with the free option, they will take as much of it as they can get. That is why I think we have to put an incentive into the system to discourage the use of our resources and that drives an efficient outcome.[63]

25.45 ASIC subsequently expounded on the argument that a sector-based user-pays system designed to discourage the use of ASIC's resources could lead to better outcomes:

> At present, there are also no economic incentives (price signals) in the market for the use of ASIC's resources. Stakeholders acting rationally will seek to efficiently allocate their own resources and may choose low-cost or no-cost ASIC services over other, more costly, alternatives available in the market (e.g. private legal advice).
>
> Price signals associated with the use of ASIC's resources would allow business to identify the cost of regulation required to achieve the desired regulatory outcome. If industry can deliver the Government's desired policy outcomes more efficiently and effectively through co-regulation or self-regulation, and therefore require less use of ASIC's resources and cost less to regulate, they would have an incentive to allocate resources to undertake part or all of the regulation themselves. This would ensure that the desired policy outcomes are delivered in the most economically efficient way. However, these price signals are not currently in place.[64]

25.46 Mr Medcraft observed that the financial incentive such a framework creates also 'incentivises industry groups':

> …I know from running an industry group that one of the biggest challenges you have is demonstrating your value as an industry group to your members. If an industry group can actually say to its members, 'Look, if you sign onto our industry standards and you do a good job and we enforce the industry standards, we should end up with a lower cost from ASIC because actually we are achieving the outcomes that government desires.'[65]

62 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, p. 29.

63 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, pp. 31–32.

64 ASIC, *Submission 45.7*, p. 4.

65 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, p. 32.

25.47 The committee explored how a levy-based system would operate. Mr Medcraft outlined a model of levies that would be sector-based and adjusted periodically. Any adjustment would be based on the costs incurred by ASIC in regulating that sector to achieve an outcome determined by the government. Mr Medcraft provided the following reasoning:

> If you want to have a system that works you really want to have it such that it is at a sufficiently granular level that, if the industry does a good job, it should be adjusted both downwards and upwards. Let's take the audit sector, for example. The government might say, 'We want to make sure that at least no more than five per cent of audits are poor quality. If the sector is not achieving that then it needs more effort from ASIC, therefore more resources.[66]

25.48 ASIC put forward a proposal where $286.55 million (based on its 2012–13 costs) would be recovered from industry through a combination of:

- fees for service of $37.84 million, where charges are directly linked to the cost of ASIC delivering a particular service, such as takeover approvals; and
- sector-based levies of $248.71 million, where sector participants pay an annual fee based on 'volume-related metrics'.[67]

25.49 The equity argument put forward by ASIC found some support. Dr Suzanne Le Mire remarked that ASIC's point on equity 'is well made' and that a levy system 'has some appeal'. Dr Le Mire noted that the development of levies for ASIC could be informed by the WorkCover model:

> …where you could increase levies for those who step out of line. Using a model whereby levies are higher for those who break the rules and lower for those who are consistently compliant would have some appeal and perhaps give ASIC some purchase that it does not currently have without pursuing more serious options.[68]

25.50 Dr George Gilligan was relatively supportive of the concept of introducing a levy-based funding system, although he indicated that the mechanism for determining the levies would require careful consideration:

> I think from the perspective of equity that it was a fairly powerful argument when it stated the proportion of the fees that were generated by lower-scale firms and the amount of regulatory activity or attention that those firms actually require or receive from the regulator. So there is the sense that

66 Mr Greg Medcraft, Chairman, ASIC, *Proof Committee Hansard*, 19 February 2014, p. 31.

67 For example, ASIC envisaged that for financial advisers, the cost of regulatory activities would be recovered 'as part of an AFS licence sector levy based on the size of financial adviser groups as determined by the number of authorised and employee representatives. Tiered models would be used to distribute the industry levy between industry participants'. ASIC, *Submission 45.7*, pp. 6–7.

68 Dr Suzanne Le Mire, *Proof Committee Hansard*, 19 February 2014, p. 53.

> there should be greater proportionality, one would have thought, in terms of the user pays model. Philosophically, it would be hard to argue against that. The mechanics may be a little more problematic but, certainly, one would have thought that there could be different scales of registration or licensing fees, for example, for the different actors who participate within the industry, depending on the size scale and, of course, the profits that they generate from the privilege of having the licence to operate in the industry.[69]

25.51 Professor Dimity Kingsford Smith also recognised that a user-pays levy would support a regulatory regime that was self-executing. However, Professor Kingsford Smith cautioned that it was necessary to ensure the public interest was reflected in any changes:

> If you have the entire regulatory revenue coming from levies, particularly in a concentrated market such as Australia where a lot of the levy income might come from a very few players, you have to watch out for undue influence coming from those who pay.
>
> I also would encourage us to do a little bit more research into the notion that big players always cost more in regulatory resources. I have had some experience in the UK as well, and there, with their user pays system, particularly at the compensation-fund end, the big players are always complaining that it is the smaller players who are having the compensation payouts from the fund and that because they are big players they pay the levies but the moneys go out to the clients of the smaller players, who are a bit harder to keep in line compliance-wise.
>
> So it is not an open and shut case by any means. But having some of ASIC's income derived from levies could be something very seriously to consider.[70]

Committee view

25.52 This report has highlighted specific instances where ASIC could have performed better and considered ways that ASIC could undertake its tasks more effectively in the future. Some of the problems identified were linked to ASIC's approach to enforcement, failures to utilise evidence to establish links and problems with complaints management and stakeholder communication. The committee considers these are matters that ASIC can largely address on its own initiative. However, ASIC's long list of regulatory tasks and the resources available to ASIC to perform these tasks clearly act as constraints on its ability to meet expectations the public and stakeholders may have. Neither of these matters are in ASIC's control; they are matters determined by the government and the Parliament. To the extent that a problem with ASIC relates to its funding, it would be unfair to criticise ASIC.

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69 Dr George Gilligan, *Proof Committee Hansard*, 19 February 2014, p. 52.

70 Professor Dimity Kingsford Smith, *Proof Committee Hansard*, 19 February 2014, p. 53.

25.53 Evidence before the committee strongly indicates that ASIC is unfocused and over-stretched with an evident weakness in consumer/investor protection. ASIC has always had a significant role in the Australian corporate world, however, over many years successive governments have entrusted ASIC with additional important functions. ASIC is now firmly established as one of Australia's key financial regulators. However, one outcome of this is that it is increasingly difficult to identify, articulate and prioritise what ASIC's key regulatory functions and priorities should be. ASIC would have a clearer mandate if it was relieved of some of its functions.

25.54 The committee noted earlier that in the 2014–15 Budget, the government announced that it would fund a scoping study to consider options and provide recommendations on the optimal ownership arrangements for ASIC's registry function. The scoping study is intended to inform the government on key strategic policy and implementation issues for consideration before commencing a sale, licensing or external management process.

25.55 The committee has independently considered suggestions of re-positioning the function elsewhere. Although these ideas were developed in parallel (one through a public inquiry process and the other through confidential budget processes), they both point towards a common point that the operation of a sophisticated IT database is a mere enabling function for ASIC and not core to its regulatory role.

25.56 The committee does not consider that it would be appropriate to make a final decision on where those IT functions should go before the findings of the scoping study are known. The purpose of scoping studies on government assets is generally to identify the most efficient and effective ways of delivering a service to the public, without a predisposition for any particular model. The committee fully endorses the work of the scoping study that is examining future ownership options for ASIC's registry function as an important first step toward relieving ASIC of its registry function.

Recommendation 49

25.57 The committee recommends that the scoping study examining future ownership options for ASIC's registry function take account of the evidence that has been presented to the committee.

25.58 The amount of funding allocated to ASIC through the annual appropriations process was considered by the committee. For the health of the financial system it is clearly necessary that ASIC receives an amount of funding that enables proactive regulation and meaningful law enforcement. However, governments have competing priorities and the committee recognises the difficulties associated with increasing ASIC's funding due to the present fiscal circumstances. In any case, the issue is not limited to the quantum of funding; it is also apparent that the current model for funding ASIC is outdated and does not promote efficient outcomes. ASIC regulates many different sectors of the financial system but its funding does not account for differences in the cost of regulating each sector. It does not provide an incentive through a price signal for sectors to take action to limit the amount of resources ASIC allocates to regulating them.

25.59 The committee considers that ASIC should be funded on a user-pays principle like many of its international counterparts. To implement this, a framework of sector-based levies should be introduced to provide the majority of ASIC's funding. By making regulated entities more accountable for the cost of regulating their sector, a clear incentive would be provided for these entities to minimise the number of problems that the regulator has to deal with. This feature of a well-designed levy system could, over time, promote more efficient regulatory outcomes through better self-regulation, resulting in more resources being available, within existing financial constraints, for the regulator to investigate misconduct reports and deliberate non-compliance. The levies would be reviewed periodically to ensure they are set at appropriate levels and to provide greater transparency of how ASIC manages its resources. ASIC would need to justify why it requires the amount of funding it proposes and industry would have the opportunity to respond to ASIC's assessment. However, as ASIC would no longer be funded through the Budget process, the levies should ensure that ASIC's core funding is more stable on a year-by-year basis and that ASIC has sufficient resources to undertake proactive regulatory activities.

25.60 A further advantage of a levy model for funding ASIC is that it could provide a revenue-neutral means for the government to reduce the fees charged for lodging and inspecting information and documents. The committee considers that the fees currently charged to the public for accessing information held by a government body are too high. These fees effectively act as a barrier to accessing information and potentially counteract efforts to inform the marketplace and promote the confident and informed participation of investors and consumers in the financial system. The public interest would be better served if the size of these fees were significantly reduced. Increased efficiencies resulting from the committee's recommendation regarding the transfer of ASIC's registry responsibilities to another agency could also allow the fees to be reduced further.

Recommendation 50

25.61 The committee recommends that the current arrangements for funding ASIC be replaced by a 'user-pays' model. Under the new framework, different levies should be imposed on the various regulated populations ASIC oversees, with the size of each levy related to the amount of ASIC's resources allocated to regulating each population. The levies should be reviewed on a periodic basis through a public consultation process.

25.62 The government should commence a consultation process on the design of the new funding model as soon as possible.

Recommendation 51

25.63 Following the removal of ASIC's registry responsibilities and the introduction of a user-pays model for funding ASIC outlined in Recommendations 49 and 50, the committee recommends that the government reduce the fees prescribed for chargeable matters under the *Corporations (Fees) Act 2001* with a view to bringing the fees charged in Australia in line with the fees charged in other jurisdictions.