

**House of Representatives Standing Committee on Economics
Inquiry into the Corporations (Fees) Amendment Bill 2011**

Submission by the Treasury

Background

- The Government announced support for competition between markets for trading in listed shares on 31 March 2010, with a media release by the then Minister for Financial Services, Superannuation and Corporate Law, the Hon Chris Bowen MP.
 - This decision paved the way for the potential entry of new market operators in Australia in competition with ASX in relation to the trading of ASX-listed securities. Those operators would also be subject to market supervision by ASIC.
- The November 2009 Johnson Report (*Australia as a Financial Centre: Building on Our Strengths*), identified openness to new entrants in relation to exchange traded products as ‘an essential condition for competition, efficiency and innovation’. The Report recommended increased competition on exchange traded markets. It also encouraged ‘the early consideration of licences for new trading platforms and exchanges, with a view to introducing competition as soon as possible...’¹
- On 1 August 2010, pursuant to the *Corporations Amendment (Financial Market Supervision) Act 2010*, supervisory responsibility for Australia’s domestic financial markets was transferred from market operators, such as ASX Ltd (ASX), to the Australian Securities and Investments Commission (ASIC).
 - Transferring responsibility for market supervision from individual market operators to ASIC was an important first step in facilitating competition between Australia’s licensed equity markets.
- On 4 May 2011, the Government granted a licence to Chi-X Australia Pty Ltd (Chi-X), as the first market operator to offer an alternative venue for trading ASX-listed shares. Chi-X is expected to commence operations from 31 October 2011, subject to fulfilment of a number of regulatory preconditions and the operator’s readiness.
 - Following the commencement of Chi-X’s operations, we would expect a substantial number of major ASX market participants to become participants of the Chi-X market. Over the medium term, we would expect the majority of market participants to be connected to both the ASX and Chi-X markets.
- Treasury has released the consultation paper ‘Proposed financial market supervision cost recovery model’ (26 August 2011)² to seek industry feedback on a proposed post-competition cost recovery regime.

¹ *Australia as a Financial Centre Building on our Strengths* Report by the Australian Financial Centre Forum November 2009 at 4.4.

² Available at <http://www.treasury.gov.au/contentitem.asp?NavId=037&ContentID=2138>.

- The proposed cost recovery regime is intended to replace the current interim arrangements from 1 January 2012, and is aimed at allocating costs to both operators and participants on a fair and transparent basis.
 - The consultation paper outlines the Government’s proposed cost recovery regime, but also seeks feedback on several alternatives. A final cost recovery regime will not be settled until industry feedback has been taken into consideration.
 - The Government’s view is that the final cost recovery regime should be based on charging both operators and participants, in order to ensure transparency and fairness.

Purpose of the Corporations (Fees) Amendment Bill 2011 Bill

- Currently, only market operators may be charged fees for the performance by ASIC of its functions under Part 7.2A of the *Corporations Act 2001* (the Corporations Act) (i.e. its market supervision functions).
 - This was an interim arrangement that was put in place to facilitate the recovery of ASIC's market supervision costs prior to the commencement of competition. This interim arrangement was regarded as suitable in an environment where the markets operated by the ASX Group were the primary financial markets subject to ASIC’s supervision.
 - The interim arrangement was intended to be reviewed and updated in 2011 to reflect the move to a competitive multi-operator environment.
 - Once competition commences, it will be more appropriate for costs to be recovered from both operators and participants, in order to more closely align ASIC's costs to the entities that have created the need for the costs to be incurred.
- The Bill amends the *Corporations (Fees) Act 2001* to enable fees to be charged to market participants, as well as to market operators, so as to recover the funding provided to ASIC to undertake its new market supervision functions and for the development of a framework to support competition.
 - Specifically, the Bill adds to the definition of a **chargeable matter** under the Act to include ASIC’s performance of its functions in relation to a participant in a licensed market under Part 7.2A of the Corporations Act. The Bill also amends the list of entities that are liable for a fee for a chargeable matter to include the participant in a licensed market.
 - The term ‘participant’ is defined in Chapter 7 of the Corporations Act, and will have the same meaning under this amendment. A participant, in relation to a financial market, means a person who is allowed to directly participate in the market under the market’s operating rules. ASIC estimates that there are currently around 100 ASX market participants. Many of them can be expected to become participants in the market operated by Chi-X.
- Funding has been provided to ASIC to cover its costs for performing its new market supervision functions following the transfer of supervision (approved in Portfolio

Additional Estimates Statements 2009-10), as well as the costs associated with implementing the Government's policy to introduce market competition (approved in Budget 2011-12). This funding was provided on the basis of full cost recovery.

- The consultation paper provides a detailed breakdown of ASIC's costs and the proposed fee arrangements.
- Treasury considers the Bill will enable the implementation of a more flexible cost recovery regime that is in line with the Government's cost recovery guidelines. Failure to enact the Bill would potentially require the imposition of substantially higher charges on market operators in order to fully recover ASIC's costs. These could be expected to be passed on to the market participants in any event.
 - The Bill as proposed will not impact on the quantum of costs to be recovered for ASIC's new market supervision role and its costs of implementing competition in trading of ASX-listed securities.
 - Rather, the amendments will affect where the direct incidence of the fees occurs to enable cost recovery to take place.
 - The direct charging of participants alongside operators will allow the new cost recovery arrangements to adhere to the Government's cost recovery guidelines, and will result in a fairer and more transparent fees arrangement.
- Treasury's consultation paper 'Proposed financial market supervision cost recovery model' seeks industry feedback on a proposed post-competition cost recovery regime.
 - Treasury's view is that the final cost recovery regime should be based on charging both operators and participants, in order to ensure transparency and fairness.
 - Treasury intends to review the new cost recovery regime within 18 months of implementation to assess the impacts of the new regime on industry, and more broadly, Australia's financial markets. Where adjustments are required, these will be incorporated in the new cost recovery arrangements that will commence from 1 July 2013.

Reasons for charging participants alongside market operators

In Treasury's view, there are several key reasons for charging participants alongside market operators in respect of ASIC's market supervision functions, as set out below.

- **Fairness:** Imposing costs on participants and, indirectly, on investors, alongside market operators, is the fairest way to fund the increased supervision burden that comes with a multi-operator trading environment.
- **Benefits outweigh costs:** Introducing competition in trading is likely to lead to significant overall cost reductions for participants and investors, as well as greater choice of services. The overall benefits of introducing competition are expected to significantly outweigh the costs imposed under this cost recovery regime.

- **Expressed preference:** Participants have expressed a preference for direct costs, rather than having costs passed through via operators. Direct charging increases the transparency of the fees arrangement.
- **Fees will be passed on regardless:** While imposing fees directly on participants will result in a substantial change in the incidence of the fees, in effect these fees can be expected to be passed on by operators if participants are not directly charged.
- **Lower barriers to entry:** This approach lowers barriers to entry for new market operators by reducing the charges that they are directly subject to, and by not increasing their participant's contribution to ASIC's market supervision costs according to how many markets they are connected to.

Conclusion

- Opening Australia's financial markets to competition will reap significant overall benefits to market participants and investors. However it also brings the challenge of supervising multiple markets in an environment of increasing speed and complexity of trading.
- As an essential precondition of implementing competition in trading, there will be an increase to ASIC's costs so that it can continue to properly supervise the market in a multi-operator environment.
- Given that there will be costs associated with the transfer of supervision and implementation of competition, the fairest and most transparent approach available for recovering those costs should be used.
- These amendments are an important step in continuing to facilitate competition between Australia's licensed securities markets into the future.

*Department of the Treasury
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