



SUBMISSION PAPER:

ASIC Consultation Paper 260

Further measures to facilitate innovation in financial services

JULY 2016

This Submission Paper was prepared by FinTech Australia working with and on behalf of its Members and with a wider group of fintech stakeholders and startups across Australia.



About this Submission

FinTech Australia is the peak industry body for the Australian FinTech Industry, representing over 90 FinTech Startups, Hubs, Accelerators and Venture Capital Funds. Its vision is to make Australia one of the world's leading markets for FinTech innovation and investment.

In July 2016, FinTech Australia held several consultative engagements with its members as well as with a wider group of fintech startups in hubs such as Stone & Chalk and Tyro. This submission summarises FinTech Australia's findings and recommendations as a result of these discussions. It also identifies economic and competitive impacts, supported by inputs and examples from FinTech Australia's network of international peers in leading FinTech jurisdictions - Europe and the United Kingdom.

The following people have contributed to the development of this submission:

- Jack Quigley – Crowdfundup
- Toby Heap – H2 Ventures
- Alexander Walrut – CheckVault
- Alice Chauvel – Airwallex
- Sasson Grigorian and Gilbert Verdian – Remitt
- Claire Wivell Plater – the Fold Legal
- Daniel Knight – K&L Gates
- Alex Scandurra – Stone & Chalk

Fintech Australia's detailed recommendations are outlined in proceeding sections in response to ASICs Consultation Paper 260.



A - BACKGROUND TO THE PROPOSALS

We are considering the options set out in paragraph 31. Our preferred option is Option 4 (i.e. a combination of Options 1–3). In this proposal, we are seeking your general feedback on our approach to further facilitating innovation in financial services. We are consulting in more detail on particular aspects of our proposals in Sections B and C.

<p>A1Q1</p>	<p><i>Do you agree that we should put in place additional measures to facilitate innovation, or maintain the status quo? Please provide reasons.</i></p> <p>Fintech Australia supports Option 4, being a combination of Options 1, 2 and 3, subject to our more detailed submissions below.</p> <p>Options 1 and 2 will assist businesses to successfully apply for AFSL whose responsible managers do not have traditional financial services qualifications or experience, in circumstances where that experience is not as important due to the use of technology to deliver the financial services. Option 3 will allow new businesses to test the market for innovative financial services before being required to hold an AFSL, without exposing consumers to excessive risks.</p> <p>Fintech Australia also welcomes additional guidance in Consultation Paper 260 regarding existing flexibility in the financial services framework to accept responsible managers under Option 5 of ASIC Regulatory Guide 105 Licensing: Organisational competence.</p> <p>Some guidance is already contained in ASIC’s recent Licensing Activity Report and in Consultation Paper 260, however it would provide greater certainty if the principles underpinning the examples were articulated and incorporated into Regulatory Guide 36 Licensing: Financial Product Advice and Dealing, and Regulatory Guide 105 Licensing: Organisational competence.</p>
<p>A1Q2</p>	<p><i>What benefits do you consider will result from our proposed approach?</i></p> <p>Fintech Australia considers that the following benefits could result from increased certainty regarding the regulatory requirements for innovative businesses and that ASIC’s guidance should be directed towards achieving these:</p> <ul style="list-style-type: none"> • In respect of the proposed changes regarding organisational competence: <ul style="list-style-type: none"> ○ Reduced cost for both business and ASIC. By ensuring that businesses understand the regulatory requirements that apply to them and how their organisational competence will be assessed, business will be better equipped to prepare and provide relevant material to ASIC at the outset. ASIC will avoid the need to consider material which is not relevant to its assessment; ○ Increased speed to market by reducing the time required to assess licence applications; ○ Increased access to the AFS licensing regime for new and innovative businesses, thereby reducing risk for consumers;



	<ul style="list-style-type: none"> • In respect of the proposed regulatory sandbox: <ul style="list-style-type: none"> ○ Reduced regulatory barriers for innovative fintech companies; ○ Greater diversity of ideas in the financial services sector, leading to more tailored solutions for consumers; and ○ Enabling Australia to be a leading fintech hub.
A1Q3	<p><i>What disadvantages do you consider will result from our proposed approach?</i></p> <p>Our detailed submissions below outline areas where we consider the proposed approach could be improved.</p>
A1Q4	<p><i>Are there any other options we should consider to meet our regulatory objective of further facilitating innovation, while ensuring that appropriate protections apply to all financial consumers?</i></p> <p>Our detailed submissions below outline our recommendations for additional measures ASIC could take to facilitate innovation and continue protecting consumers.</p> <p>In addition, the Consultation Paper highlights the ability of businesses who do not qualify for the sandbox to apply for an individual exemption from holding an AFSL. To enable more start-ups take advantage of the availability of individual relief, Fintech Australia considers it would be useful for ASIC to provide additional guidance about the types of relief ASIC has granted for fintech businesses and the relief ASIC is willing to consider.</p>



B1 - Additional guidance on assessing knowledge and skills under Option 5 of RG 105

We propose to provide additional guidance on how we assess submissions about a responsible manager’s knowledge and skills under Option 5 of RG 105. This will include:

- (a) more detail about what we expect a prospective AFS licensee to include in its submission; and**
- (b) examples of situations where we generally would (or would not) consider that a responsible manager has the appropriate knowledge and skills (see Example 1 to Example 4 below).**

Note: We are not proposing to change how we assess submissions under Option 5 of RG 105 in this proposal.

B1Q1	<p><i>Do you agree with this proposal? Please give reasons for your answer.</i></p> <p>Fintech Australia agrees with this proposal. Additional guidance regarding how ASIC assesses submissions under Option 5 would assist businesses to ensure that the material provided, and the people nominated to assume the role of responsible manager, meet ASIC’s requirements and expectations.</p>
B1Q2	<p><i>Do you think the examples provided below are helpful? If not, why not?</i></p> <p>While the examples are helpful, they are unnecessarily limited in scope and applicability. Fintech Australia submits that a structured approach would be most helpful; whereby ASIC systematically describes the manner in which it assesses Option 5 submissions.</p> <p>This would assist innovative businesses to rely on Option 5, rather than expending scarce financial resources on hiring special purpose external responsible managers. Our brief survey of members indicates that this costs approximately \$4000 per month and may in fact be used by fintech start-ups more frequently than an Option 5 submission.</p>
B1Q3	<p><i>Subject to the other proposals in this paper, is there anything else you think we should cover in our updated guidance on Option 5 of RG 105?</i></p> <p>No.</p>



B2 - Nominating responsible managers

We propose to amend RG 105 so that a small-scale, heavily automated business would be able to meet its organisational competence obligation by nominating responsible managers in the following two categories:

- (a) responsible managers (as currently defined in RG 105) that have knowledge and skills that are relevant to some, but not all, aspects of the financial services the business will provide; and**
- (b) an appropriately regulated and experienced professional third party that will provide sign-off for the remaining aspects of the business’s financial services.**

To rely on B2, we propose that businesses will also need to meet the terms set out in proposals B3 and B4.

B2Q1	<p><i>Do you agree with this proposal? Please give reasons for your answer.</i></p> <p>Fintech Australia agrees with the proposal to permit an appropriately regulated and experienced professional third party to provide signoff for aspects of the business’s financial services for which the responsible manager does not have sufficient expertise. We believe that this will provide considerable additional flexibility for new businesses whose existing employees and directors do not meet all of the knowledge and skill requirements.</p> <p>As set out above, a considerable number of our members have hired external professionals to perform the role of responsible managers. This proposal would encourage transfer of learning from these external responsible managers, to internal staff as it would only be a fraction of the third party’s relationship with the AFSL holder (i.e. a lawyer or accountant provides other services to the AFSL holder). Further, instead of working within the business, the external professional could review and sign off processes developed by internal staff which would better equip individuals within the business who are closer to the financial services being provided, to gain the knowledge and skills required to become responsible managers and no longer rely on third party sign-off.</p>
B2Q2	<p><i>What sort of professionals should ASIC accept as responsible managers that provide sign-off?</i></p> <p>The professional should have sufficient understanding of the nature of the services and method of operation of the business being assessed, as well as the financial services or credit regulatory requirements to be able to confidently review and sign off on its compliance arrangements. This should be assessed by reference to the individual or firm, rather than their profession as not all members of the professions nominated in the consultation paper would have the requisite knowledge and experience.</p>
B2Q3	<p><i>Are there any other situations where this type of flexibility should be available?</i></p> <p>Fintech Australia submits that there is no reason in principle why this should be limited to a small-scale, heavily automated business. Indeed, external financial auditing is an integral part of corporate governance in listed and unlisted businesses of all sizes.</p>



	<p>Fintech Australia is of the opinion that all fintech businesses should be able to rely on third party responsible manager sign-off as sufficient proof of meeting their required organisational competence obligations under an AFSL.</p>
B2Q4	<p><i>Are there any risks associated with this proposal? If so, what are they?</i></p> <p>While much would depend on the suitability of the knowledge and experience of the external professional for the business being reviewed, some risks suggested by members include the following:</p> <ul style="list-style-type: none"> • A third-party compliance consultant may only have a superficial view of the regulations which would not be adequate; or • The third party consultant may not have an adequate understanding of the business and its real risks.
B2Q5	<p><i>Please estimate any cost savings that a new business would expect to realise from this proposal.</i></p> <p>Members' views were divided regarding the costs savings to be gained from this proposal. Some believed that annual external signoff would be cheaper than hiring an external responsible manager. Another estimated the cost saving to be \$50,000 per year, despite recognising that the third party signoff should be extensive.</p>

B3 - Requirements for third-party sign-off

We propose that a professional third-party responsible manager providing sign-off under proposal B2 would be required to examine all the relevant material and certify that the AFS licensee is materially compliant with ASIC-administered legislation.

We propose that:

- (a) sign-off would be required every 12 months, or on significant changes to the AFS licensee's operations; and**
- (b) the AFS licensee would need to lodge a copy of the sign-off with ASIC. Responsible managers who provide a sign-off that contains false or misleading statements may commit an offence under s1308 of the Corporations Act.**

B3Q1	<p><i>What sort of sign-off should a third-party responsible manager be required to provide?</i></p> <p>Fintech Australia considers that the third party responsible manager should be required to consider all the operating and compliance procedures and randomly chosen work samples in the areas in which the existing responsible managers lack the requisite skills and knowledge. They should confirm that the procedures are adequate and they are being followed by the business.</p>
------	-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------



B3Q2	<p><i>Is an annual sign-off appropriate?</i></p> <p>Fintech Australia considers that a minimum of annual signoff would be required, depending upon the rate of growth and change occurring in the business. Businesses who are changing and growing rapidly, may need more frequent signoff. Annual signoff (and perhaps even less frequent) would be adequate for businesses who are not experiencing significant change or growth.</p>
------	------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------

B4 - Conditions of eligibility for third-party sign-off

<p>We propose that proposal B2 will only apply to AFS licensees that:</p> <p>(a) provide financial services to no more than 1,000 retail clients; and</p> <p>(b) only give advice on, or arrange for another person to deal in, liquid financial products, non-cash payment facilities, and products issued by a prudentially regulated business.</p>	
B4Q1	<p><i>Do you agree with our proposed restrictions on the types of business eligible for this flexibility? For example, is a limit of 1,000 clients appropriate?</i></p> <p>Consistent with our submission in part C below, Fintech Australia considers there is no reason to limit the flexibility offered by this proposal by reference to the number of retail clients or the nature of the financial services or nature of the financial products provided by the business.</p> <p>Indeed, Fintech Australia considers that, provided the third party has the appropriate qualifications and experience, the level of assurance offered by its third-party signoff will be sufficient and no further restrictions are necessary.</p>
B4Q2	<p><i>Are other restrictions—such as an exposure limit on investment products—also warranted?</i></p> <p>Fintech Australia does not feel that any additional limitations are necessary.</p>



C1 - Six months of unlicensed financial service testing with retail clients

We propose to give conditional, industry-wide relief to allow new Australian businesses to test certain financial services for one period of six months without needing to obtain an AFS licence. We refer to this as the ‘regulatory sandbox exemption’.

We propose to place the restrictions and conditions outlined in proposals C2–C9 on the licensing exemption to ensure that:

- (a) the risk of poor consumer outcomes is minimised; and**
- (b) activities carried out under the exemption are limited to early-stage testing (i.e. concept validation).**

We will continue to consider requests for an individual exemption by businesses that do not meet the terms of the industry-wide relief.

C1Q1 *Do you agree with this proposal? Please give reasons for your answer.*

Fintech Australia wholeheartedly supports ASIC’s proposal to give conditional industry-wide relief to allow new Australian businesses to provide a limited range of financial services for a short period without needing to obtain an AFS licence (**‘AFSL’**). This relief would enable new businesses to test the market for their services before making the time and monetary commitments necessary to apply for an AFSL.

However, Fintech Australia is concerned that some of the restrictions currently proposed by ASIC will limit the usefulness of the ‘regulatory sandbox’ to the point where it will be available to only a small handful of businesses. We address these concerns in our submission below.

Fintech Australia’s first concern is that ASIC’s proposal only allows fintech companies to rely on the ‘regulatory sandbox’ class order exemption (**‘exemption’**) for a period of 6 months. In our view, this does not provide a business sufficient time to validate their concept and, if successful, apply for and obtain an AFSL.

The experience of our members is that it can take in the order of 3 months to prepare application materials and 12 to 18 months for an innovative fintech business to obtain an AFSL. This period is inevitably longer when a company is located overseas or when responsible managers reside overseas as foreign documentation needs to be sourced.

Fintech Australia accepts, however, that the exemption must be a temporary measure which allows start-ups to test fintech ideas before obtaining a full AFSL. The aim for successful sandbox participants should always be to apply for and obtain an AFSL. For this reason, we propose the following:

1. Initial 12-month class order exemption.

We propose that the regulatory sandbox be available for a period of 12 months, rather than 6 months. During this time a start-up must test their idea and comply with the limitations set out below to protect consumers.



We note that a 12-month exemption would make it easier and more cost effective to obtain insurance coverage as most insurance contracts last for 12 months. Further detail regarding insurance is set out in C5Q1.

2. **Extension while AFSL application is pending.**

If a start-up has lodged its AFSL application while relying on the exemption, we propose that it be allowed to continue to rely on the exemption until ASIC either grants or denies the application to obtain an AFSL. Without this extension, sandbox participants wishing to transition smoothly from testing to ongoing operation may need to apply for an AFSL before completing substantial testing. This would limit the usefulness of the sandbox, as it could require many start-ups to commit to the licensing process before their concept had been adequately validated.

It is already ASIC's practice to require applicants to submit documents and respond to queries within specified timeframes. This practice would ensure that a start-up cannot extend the exemption indefinitely by lodging an AFSL application.

3. **2 x subsequent 6 month extensions.**

If a start-up has been unable to lodge its AFSL application or requires further time to test an idea, we propose that it be permitted to apply to ASIC to be allowed to continue to rely on the exemption for a further 6 months. We propose that a start-up could extend its reliance on the exemption twice for up to a further 6 months each time.

Granting the extension would be at ASIC's discretion, however we submit it should be granted where the start-up has abided by the sandbox requirements and the spirit of Chapter 7 of the Corporations Act, and the start-up can show that it is making progress towards obtaining an AFSL.

We envisage that this will be of use where a proposed responsible manager has not yet received documents required to lodge an AFSL by virtue of factors out of its control. Other circumstances may include a situation where a start-up has had to pivot away from the original project it was testing, and instead requires the extra time to program and test a different idea.

In either case, once the application for an extension has been lodged, the start-up can continue to rely on the exemption unless and until ASIC provides notice that the application for an extension has been denied.

These proposals would ensure continuity of business whilst a start-up is in the processing of applying for and awaiting the grant of an AFSL. This would mean that they are able to continue to provide services whilst they are waiting for an AFSL. Even a temporary pause of a few months at this early stage of a business could be fatal.

Our submissions below highlight other areas which Fintech Australia considers could unnecessarily restrict sandbox eligibility.



C1Q2 *Do you agree the exemption should only apply to new Australian businesses? If not, who else should be eligible, why and on what conditions?*

Fintech Australia agrees with ASIC's suggestion that the exemption should apply to new Australian businesses. It is also of the opinion that the exemption should apply to foreign start-ups looking to enter the Australian market, provided the business meets a set of criteria that are similar to those which apply to an Australian company. Opening the sandbox to locally registered foreign companies will position Australia as a fintech hub for the region.

ASIC's proposal has 2 limbs, first that it should be a new business, second that it should be an Australian business.

New business

Given that the exemption is designed to allow businesses to test ideas when they are in their infancy, business that can no longer be classified as start-ups should not be able to rely on the exemption. We propose that any business that meets all of the following criteria will be a 'start-up' and will be eligible to rely on the exemption:

1. Neither the business nor any of its related bodies corporate hold, or have held an AFSL, or have acted as an authorised representative of an AFSL holder, where the AFSL authorised the business to provide the financial products or services that it proposes to test in the sandbox;
2. The business is a small proprietary company as set out in section 45A of the Corporations Act; and
3. The business has not been incorporated for more than 3 years.

In our view, an entity should not be excluded from the sandbox if they have an AFSL with authorisations which are different from those required to test the service they wish to test if they otherwise comply with the sandbox requirements (e.g. a business which has an AFSL to provide a financial service to wholesale clients only can rely on the sandbox to test the market to provide that service to retail clients).

These limitations will prevent a company which is otherwise able to obtain an AFSL from relying on the exemption.

Fintech companies

Fintech Australia also proposes that the exemption is only open to 'fintech' business. Of course any company which would otherwise require an AFSL falls within the 'fin' part of the definition, however 'tech' must also be defined for it to truly be an industry wide exemption. We propose that a 'fintech' business uses technology to provide a solution that would require an AFSL. Although this may appear broad, it restricts it to genuinely innovative companies in this space. For instance, arranging for a deposit product to be issued is not innovative, however arranging for that same product to be issued via a robo-advice platform is innovative and should be able to rely on this exemption.



C1Q3 *Please estimate any cost savings that a new business would expect to realise from this change.*

Whilst the sandbox allows a deferral of capital outlay needed to apply for and obtain an AFSL, the real cost saving is in accelerated time to market and in the likely reduction in legal fees. In many instances this opportunity cost may prove too high a barrier to entry, and dissuade fintech companies from ever being established.

Currently, until an AFSL is granted, a business is unable to provide financial services. This means that a business needs to undertake the process of applying for and obtaining a license before it can even test whether the product offering is viable.

The current general estimate of the cost of applying for an AFSL is set out in the table below.

Lawyers fees	\$50,000
ASIC lodgement fee	\$1,609
Insurance	\$1,000 (Depends greatly on nature of AFSL)
External dispute resolution	\$500
	\$53,609

Apart from External dispute resolution, participating in the sandbox would defer these initial capital outlays until the business has ascertained whether there is a minimum viable product and determined what type of AFSL is required.

Deferring these costs also ensures that the business has revenue which can be used to fund the AFSL application. Fintech Australia has received anecdotal evidence that some members have waited up to 18 months to be granted an AFSL. During this time, the business operated without revenue. This strategy is prohibitive for many businesses and acts as a significant hand brake to fintech innovation. The sandbox exemption will eliminate this opportunity cost as the businesses will be able to trade (within limits) whilst the application for an AFSL is pending.

C1Q4 *Please estimate any additional costs or savings that consumers might be expected to incur as a result of this change.*

As set out above the sandbox would enable a deferral of initial costs associated with applying for, obtaining and complying with an AFSL. Without this relief, start-ups will incur these costs at the earliest stage which at best would be passed to their clients and at worst would be a barrier to entry into the market.



C2 - Service restrictions

We propose that the industry-wide AFS licensing exemption should only apply to:
(a) giving financial advice in relation to listed or quoted Australian securities, simple managed investment schemes and deposit products; or
(b) arranging for other persons to deal in the products in C2(a).
We will continue to consider requests for an individual exemption by businesses using a different business model.

C2Q1 *Our industry-wide proposal only covers giving financial advice and arranging for other persons to deal in a financial product. Do you believe there are other financial services that should be covered by the licensing exemption? If so, what risks would a wider exemption create and how could these risks be mitigated?*

Financial product advice and arranging

In the initial stages, Fintech Australia is comfortable that the sandbox will only be available to businesses that are providing financial product advice and arranging for others to deal in the financial products noted below (subject to our comments in relation to non-cash payment facilities). For clarity, a start-up should only be exempt from the requirement to hold an AFSL to deal in financial products if it is dealing by:

1. Arranging for a person to issue, vary or dispose of a financial product; and
2. Applying for the issue, variation or disposal of a financial product.

Issuing non-cash payment facilities

Fintech Australia is concerned that issuers of non-cash payment facilities (such as digital wallet providers) will not be able to take advantage of the sandbox exemption. Dealing in a financial product by issuing, varying or disposing of the product is not included in the sandbox and non-cash payment facilities are not included in the list of eligible products.

Fintech Australia acknowledges the existing exemption from holding an AFSL for low value non-cash payment facilities set out in ASIC Corporations (Non-cash Payment Facilities) Instrument 2016/211. However the relevant thresholds of \$10m in aggregate and \$1,000 per person have not been altered since the exemption was introduced in 2005 and are too low to accommodate many digital wallets and digital payments solutions. As a result, a considerable number of early stage fintech businesses do not fall within this exemption. We understand that ASIC will review the scope of this low value exemption within the next 3 years and look forward to reviewing these thresholds.

Accordingly, Fintech Australia requests that ASIC raise the thresholds for the low value exemption to align with the aggregate and per person thresholds adopted for the sandbox. In the alternate, and as an interim measure, we ask that ASIC permit start-ups which otherwise qualify for the regulatory sandbox to deal by issuing, varying or disposing of non-cash payment facilities. Under this exemption, the maximum amount held by a person in a facility would be \$5,000 and the maximum aggregate value of the facility would be \$25,000,000.



Credit services

The current proposal only seeks to provide an exemption from holding an AFSL. It does not provide relief from the need to hold an Australian Credit Licence. Consumer finance is an active area of fintech innovation, representing approximately 15% of current Fintech Australia members. Given the importance of consumer credit in the fintech landscape, we propose that the sandbox be expanded to include a similar exemption from holding an ACL. Fintech Australia submits that the provision of credit assistance or acting as an intermediary should have the benefit of the exemption, but not acting as a credit provider. In our view, the risk profile associated with these services is equivalent to (and has a similar risk profile to) the provision of financial product advice and arranging services.

We have included comments throughout our submission about how the sandbox could be applied to ACL issues. For example, it is submitted that requiring credit assistance providers to comply with the responsible lending and other obligations which apply to them under the *National Consumer Credit Protection Act 2009* (Cth) and the *National Credit Code* will provide adequate protection for consumers.

ASIC may wish to consider expanding the range of services in the future (for example, to include issuing certain financial products), however Fintech Australia does not see this as a current priority.

- C2Q2 *Our industry-wide proposal only covers services that relate to listed or quoted Australian securities, simple managed investment schemes and deposit products:*
- *Are there any other products that should be covered by the proposal, such as non-Australian listed or quoted securities or general insurance contracts? If so, why and on what basis?*
 - *Should the exemption cover services in relation to a wider range of products where the testing business only deals with wholesale clients? If so, what product classes should be included?*
 - *If you believe the exemption should be extended to less liquid or more long-term arrangements, how could any additional risk to consumers be mitigated?*

Fintech Australia considers that the current scope of the exemption is not truly 'industry-wide' as it would only apply to a limited list of financial products. Any business concerning life and general insurance, superannuation, unlisted securities or complex managed investment schemes would be ineligible to rely on the exemption.

We are concerned that that the proposed limitations are so restrictive that the vast majority of fintech start-ups are unlikely to be able to rely on the exemption. For example, under the eligibility criteria proposed in Consultation Paper 260, it is estimated that less than 5 of Stone & Chalk's 75 full time start-ups would be eligible to participate in the Sandbox. If the scope of products is expanded, then 60-70% of all start-ups resident in Stone & Chalk would be eligible to rely on the exemption.

In consultation with the insurance industry, Fintech Australia has been informed that the costs of insurance will be reduced if there is a wider diversity of financial products are allowed in the sandbox. Industry has told us that being able to increase the number of companies using the sandbox and increasing the range of financial products lowers the



insurance risk and subsequently the cost of providing the requested insurance coverage. Please refer to further details in section C5.

Fintech Australia acknowledges that additional risks may arise for businesses dealing with complex products such as derivatives. However, it considers that the risks of allowing start-ups to rely on the exemption to provide financial services for the financial products described above are low. By restricting the financial services to providing advice and the dealing authorisations listed above, the potential liability to clients of sandbox participants is already restricted.

In respect of dealing in a financial product, where a start-up is only able deal in the manner described above, it will not be responsible to clients for the ongoing delivery and performance of the product. This is the responsibility of the issuer.

In relation to providing financial product advice, Fintech Australia considers that the risk of loss to clients when providing these financial services is limited as sandbox participants will be required to comply with a range of ongoing obligations, detailed in C4 – C6 below. As these obligations mirror the requirements set out in the *Corporations Act 2001* (Cth) they will sufficiently protect clients. Furthermore, businesses relying on the sandbox exemption will be required to have compensation arrangements which will provide a remedy for aggrieved clients.

In light of these robust compliance obligations, we submit there is scope to increase the products to which the sandbox can apply. We request that ASIC increase the scope to include the following financial products:

- Unlisted securities and managed investment schemes other than simple managed investment schemes;
- International securities;
- General and life insurance;
- Superannuation and retirement savings accounts; and
- Foreign exchange accounts.

The reasons for including each financial product are set out below.

Unlisted securities and managed investment schemes other than simple managed investment schemes

Consultation Paper 260 proposes to exclude unlisted securities. It also limits the exemption to simple managed investment schemes, being schemes with 80% highly liquid assets (i.e. assets deposited with a bank or realisable within 10 days). These limitations are based on a concern that investment in illiquid products or arrangements cannot easily be unwound and so expose particularly retail clients to increased risk. In our view, the liquidity of the underlying financial products being recommended is not a material risk factor for clients of sandbox participants.



The risks posed by entities providing advice and arranging to deal in financial products are no different when the underlying products are liquid or illiquid. Imposing such a restriction is equivalent to imposing a restriction on a start-up investing in another start-up because it is 'illiquid'. The requirements to comply with certain provisions of Chapter 7 and to have appropriate dispute resolution and compensation arrangements ensure the client is not without a remedy, even if the underlying product cannot be easily unwound. external dispute resolution

International securities

The restriction on Australian securities will restrict the advice that sandbox participants can provide. It is not clear why the risk profile of foreign securities would be higher than Australian securities. For example, it would exclude investments such as international indices or 'blue chip' stocks which are appropriate for some clients. Furthermore, this may make it difficult for sandbox participants to fulfil the 'best interests' duty, as this imposes an automatic constraint on the types of products the start-up can recommend.

General and Life Insurance

Financial product advice for insurance products is an attractive field for digital advice, as it is commonly sought and relatively simple to tailor to a requested need.

The risks associated with financial product advice and dealing in insurance products (other than by issuing) are limited for three reasons:

- Insurance products can be cancelled by consumers and a pro rata refund obtained at any time;
- The mandatory cooling off period, which applies to all retail insurance products, allows consumers time to reconsider their purchase; and
- The *Insurance Contracts Act 1984* (Cth) requires retail general insurance contracts to offer minimum coverage which provides additional protection for consumers.

Superannuation and retirement savings accounts

Superannuation is similarly a field which lends itself to digital advice. Superannuation appears to have been excluded from the sandbox on the basis that it is a long term product. However, as a result of the statutory choice of fund provisions, superannuation is inherently portable. A client who wishes to change fund can do so at any time. This allows a sandbox client to switch to a different fund if they are unhappy with the fund which has been recommended to them. external dispute resolution



Foreign exchange contracts

Fintech Australia considers that the provision of financial product advice and dealing services (other than by issuing) in respect of foreign exchange contracts (which are not derivatives) carries an equivalent risk profile to the provision of advice about the other products proposed to be eligible for the sandbox.

In our view, excluding foreign exchange is unnecessarily restrictive and the compliance obligations of the sandbox, together with volume and dollar restrictions, provide sufficient means of managing the risk of these transactions occurring in an unlicensed environment.

C3 - Existing AFS licensees

We do not propose to provide industry-wide relief to existing AFS licensees. We will continue to consider requests for relief by existing licensees on a case-by-case basis.

C3Q1 *Do you agree with this proposal? Please provide reasons for your answer.*

Fintech Australia does not see a need for a company which has an AFSL with authorisations covering the services it wishes to test to participate in the sandbox.

However, we submit that if an entity would otherwise qualify for the sandbox as set out in C1Q2, but it has an AFSL which is restricted to certain financial services or clients, it should not be excluded from relying on the sandbox exemption to test other services, or providing existing services to other classes of clients. For example, we consider that an entity which holds an AFSL to provide a financial service to wholesale clients should be permitted to participate in the sandbox to test whether there is a market to provide those services to retail clients.

Our comments in response to C1Q2 are also relevant to this issue.

C3Q2 *Are there issues related to innovative services from existing licensees that could be dealt with on an industry-wide basis? If so, what are they?*

Fintech Australia does not have any comments on this issue.



C4 - Client and exposure limits

We propose that the AFS licensing exemption in proposal C1 should only apply where the testing business:

- (a) provides services to no more than 100 retail clients, each with a maximum exposure limit of \$10,000; and
- (b) ensures the total exposure of all clients (wholesale and retail) is less than \$5 million.

C4Q1 *Are the retail client exposure limits we have identified appropriate?*

Fintech Australia supports the inclusion of both an overall exposure limit and an individual exposure limit for retail, but not wholesale, clients. However, we consider the proposed limits are too restrictive and would unnecessarily prevent sandbox participants from adequately testing the market for the proposed business.

Individual retail client exposure limits

Fintech Australia considers that an exposure limit of \$25,000 would be a more appropriate individual retail client exposure limit. This amount represents a typical investment amount and would align the sandbox with market practice. This limit should apply in respect of all assets under advice or management, excluding superannuation and insurance. We set out these limits in the table below.

	Retail limit per investment	Wholesale limit per investment
All financial products other than insurance	\$25,000	No limit
Insurance	\$5,000 total annual premium	No limit
Credit services	\$20,000 unsecured loans \$500,000 secured loans	

We consider the above limits are appropriate for the initial 12 month period of the sandbox. If, as a result of a pending AFSL application or an extension, the sandbox exemption runs beyond the initial period, we consider that the exposure limits should be increased proportionately.

Aggregate exposure limits

For the initial 12 month period of the sandbox, Fintech Australia considers that an appropriate exposure limit would be \$10 million, excluding insurance and credit products.

A \$10 million limit is consistent with the existing threshold below which licensing is not required for non-cash payment facility issuers. The risks are lower in the regulatory sandbox than for unlicensed non-cash payment facility issuers, as sandbox participants



are required to participate in external dispute resolution and have compensation arrangements in place.

We set out these limits in the table below.

	Limit for first 12 months
All financial products other than insurance	\$10 million
Insurance	\$5 million total premiums
Credit services	\$1 million unsecured loans \$10 million secured loans

Number of retail client limits

By imposing exposure limits per investor and in aggregate, the sandbox limits the risk to individual consumers and prevents systemic risk. Accordingly, we do not consider that it is necessary to also impose a limit on the number of retail clients to whom services can be provided.

- C4Q2 *An alternative approach would be for the exposure limit of retail clients to vary depending on each client's total net assets:*
- (a) *How easy would it be to comply with a more graduated exposure limit?*
 - (b) *Would any benefits with this approach outweigh the resulting complexity for the testing business?*
 - (c) *Are there any risks with a graduated approach?*

Fintech Australia considers that it would be more complex for start-ups to comply with a graduated exposure limit based on the net assets of a retail client.

It is worth noting that these per investor limits do not apply to wholesale clients as they are sufficiently capable to assess the risks involved with such a business. Imposing a limit on wholesale clients would be contrary to the rest of the Corporations Act.

- C4Q3 *Are there other ways that we could facilitate innovation while limiting the risk of loss to any one individual?*

As discussed above, Fintech Australia proposes that the monetary thresholds for the low value facilities exemption be increased.

Fintech Australia does not have any further comments on this issue.



C5 - Client and exposure limits

We propose that the AFS licensing exemption in proposal C1 should only apply if the testing business maintains adequate compensation arrangements.

<p>C5Q1</p>	<p><i>Do you believe that testing businesses will be able to obtain professional indemnity insurance to compensate retail client losses?</i></p> <p>The insurance industry was particularly supportive of the proposal to extend the exemption to 12 months and to broaden the pool of financial products that can be tested in the sandbox. An exemption period of 12 months would align the sandbox timeframe with most insurance policies, making it easier to insure. Also, providing insurance for 6 months is 60-70% of the cost of providing the same policy for 12. Including different types of financial products will disperse the risk across a greater number and type of financial services which is likely to reduce insurance premiums.</p> <p>Further, we have been informed that the aggregate exposure limits and the small nature of these businesses mean that the minimum public indemnity insurance limit requirement could be reduced to \$1million. This would assist in keeping the insurance costs down</p> <p>To limit the risk further, insurers have noted that ASIC must maintain a regulatory oversight role and that participants should substantially comply with Chapter 7 of the <i>Corporations act 2001 (Cth)</i>. These are in line with the current sandbox proposal.</p>
<p>C5Q2</p>	<p><i>What other compensation arrangements could be used by testing businesses (e.g. group cover or mutual fund schemes)? What practical issues exist with other compensation arrangements?</i></p> <p>Model of insurance</p> <p>Insurance can either be in the form of an individual company by company policy, or a master policy.</p> <p>Whilst an individual policy would be tailored to the businesses needs and can be used once the participant obtains an AFSL, due to the difficulty of assessing risks and underwriting such a policy the premium may be prohibitive in this early stage of a business lifecycle.</p> <p>A master policy could cover all participants as they apply for an exemption. This would have an overall claims limit and an individual participant claim limit (i.e. aggregate claims of \$10million, individual participant limit of \$1million). By bundling the policies, the cost will reduce. It will also enable companies to be added and removed as the enter and exit the sandbox, without locking them in for the contract term.</p> <p>One insurer suggested that accessing the master insurance policy could be built into the exemption notification process. If ASIC wishes, this insurer has offered to speak with ASIC to discuss the minimum insurance requirements and details on how the master policy might operate.</p>



C6 - Other consumer protections

We propose that the AFS licensing exemption in proposal C1 will apply only if the testing business:

- (a) is a member of an ASIC-approved external dispute resolution scheme;**
- (b) complies with the modified disclosure requirements; and**
- (c) complies with the best interests duty and conflicted remuneration provisions as if the business were an AFS licensee.**

C6Q1	<p><i>Are the compliance conditions we have identified—in relation to dispute resolution procedures, disclosure and conduct (i.e. best interests duty and conflicted remuneration)—appropriate? If not, please provide reasons.</i></p> <p>Fintech Australia agrees that it is appropriate for sandbox participants to be a member of an external dispute resolution scheme.</p> <p>Fintech Australia also accepts that sandbox businesses should, when providing services to retail clients, be subject to a modified disclosure regime which mirrors certain provisions of Chapter 7 of the Corporations Act (such as providing statements of advice and financial services guides to retail clients). We note that where requirements such as the 'best interests' duty and conflicted remuneration arrangements are only imposed on retail clients, sandbox participants should only be required to comply with these in respect of retail clients as they should not be subject to more onerous the same ongoing compliance obligations than licensed entities.</p>
C6Q2	<p><i>Are there any other consumer protections that should apply to clients of testing businesses? If so, what are they?</i></p> <p>If, as proposed above, the sandbox is expanded to include credit services, it would be necessary to consider which aspects of the consumer credit legislation should apply to sandbox entities. We anticipate that this could include a modified disclosure regime and, in respect of credit assistance, responsible lending obligations.</p>



C7 - Sandbox sponsorship

We propose that the AFS licensing exemption in proposal C1 will apply only if the testing business is ‘sponsored’ by an organisation (‘sandbox sponsor’) recognised by ASIC. We propose that sandbox sponsors will be not-for-profit industry associations or other Government-recognised entities. The ASIC-approved sponsors would be named in the licensing exemption (and could be updated from time to time). We expect sandbox sponsors to only sponsor testing businesses if:

- (a) that business is operated by fit and proper persons; and**
- (b) they have conducted a preliminary assessment that the testing business’s proposed business model is reasonably sound and does not present significant risks of consumer detriment.**

C7Q1	<p><i>Do you support the requirement for a testing business to be ‘sponsored’ by an industry organisation? Please give reasons for your answer.</i></p> <p>Subject to our comments below, Fintech Australia supports the requirement for sandbox participants to be sponsored. The sponsorship requirement will provide a first line review of the entities in the sandbox.</p> <p>Our comments in relation to the role of a sandbox sponsor are in C7Q4 below.</p> <p>If ASIC is concerned that there may not be sufficient entities with the requisite experience which are willing to act as sponsors, ASIC may wish to implement an alternative application process for sandbox participants who are not sponsored. Such businesses could be required to submit relevant material to ASIC directly to enable ASIC to perform the gatekeeper role which would otherwise be performed by a sponsor.</p>
C7Q2	<p>What types of entities should ASIC approve as sandbox sponsors?</p> <p>We consider ASIC should be given a broad power to nominate entities to act as sponsors. A sponsor should be an entity which ASIC is satisfied has sufficient experience with technology and the provision of financial services to enable it to assess potential sandbox participants and perform the role of a sandbox sponsor.</p> <p>Fintech Australia suggests that a sponsor should demonstrate sufficient experience with financial services by either holding an AFSL, or by having persons within the organisation who have successfully completed a short course, such as a Regulatory Guide 146 Licensing: Training of financial product advisers (RG 146) compliant diploma. Holding this diploma, or equivalent, provides evidence that individuals who operate the sponsor appreciate the nature of their financial services obligations of the sandbox participants, equipping sponsors to adequately assess and monitor the participants.</p> <p>This training will ensure that individuals operating as sandbox sponsors are aware of, and appreciate the nature of the financial services being provided by the sandbox participant and the participants obligations to clients. Any individual who has received this training, will be obliged to complete a minimum of 20 hours per year of continuing professional development training to ensure that they continue to have appropriate skills and knowledge to effectively monitor sandbox participants.</p>



	<p>We do not consider there should be restrictions on the legal form of a sponsor (e.g. ESVCLP, not for profit, corporation or other entity type).</p>
C7Q3	<p><i>How should ASIC ensure that a sandbox sponsor is only sponsoring appropriate testing businesses?</i></p> <p>As noted above, we consider that ASIC should have discretionary power to designate entities to act as sponsors. If ASIC ceases to be satisfied that a sponsor is appropriate, ASIC could revoke that authority.</p>
C7Q4	<p><i>What circumstances should a sandbox sponsor take into account when sponsoring a testing business so that the business can rely on the licensing exemption?</i></p> <p>The role of a sponsor will need to be clearly defined. The more substantial the responsibilities and risks taken on by sponsors, the more significant the costs for performing this role are likely to be. We consider it necessary to confine the role of the sponsor to avoid imposing liability on the sponsor for the conduct of the sponsored businesses.</p> <p>The AFSL regime does not require ASIC to make a commercial assessment of an applicant's business model or the substance of the advice or services they will be providing. Accordingly, we consider it would be inappropriate to require sponsors to perform an assessment of that kind before sponsoring a business.</p> <p>Rather, we propose that the role of a sponsor would be to confirm that the start-up is eligible to rely on the exemption by undertaking the following:</p> <ul style="list-style-type: none"> • Review criminal history and bankruptcy checks; • Review external dispute resolution membership and professional indemnity insurance certificates; • Review the nature of financial services the business proposes to provide (e.g. which financial services? which financial products?); • Confirm, on the basis of the above, that the business is eligible to participate in the sandbox.; and • Any other matter that the sandbox sponsor feels should be taken into account.
C7Q5	<p><i>What costs, if any, would testing businesses incur in obtaining sponsorship?</i></p> <p>We consider that a sandbox sponsor should be permitted to charge a fee for sponsoring a business.</p>



C8 - Notifying ASIC

We propose that a testing business will need to:

- (a) notify ASIC that it intends to rely on the AFS licensing exemption in proposal C1 from a specified date;**
- (b) provide evidence of sponsorship from a sandbox sponsor (see proposal C7); and**
- (c) declare that it has reasonable grounds to expect that it can operate its business for a period of six months from the specified date.**
- (d) We also propose to require that testing businesses give us a short report about their test following completion of the testing period.**

C8Q1 Do you agree with this proposal? Please give reasons for your answer.

Fintech Australia supports the requirement for businesses to notify ASIC that they wish to rely on the exemption from a specified date. The notification should allow the business to specify that it intends to rely on the exemption either from the date the notification is lodged with ASIC or from some other date in the future.

We do not have any objection to the provision of evidence of sponsorship, a declaration that the business expects to be able to operate throughout the sandbox period (which we believe should be extended to 12 months), and a report after the sandbox period.

Indeed, to facilitate this, we suggest that notification of reliance on the exemption should be via the following automated process:

1. The sandbox participant lodges the exemption form, and all additional documents (such as a bankruptcy check) electronically via the ASIC portal. As part of the eform, the applicant must identify the relevant sandbox sponsor.
2. Once lodged, the sponsor should automatically receive an email notifying them that the sandbox participant has claimed to be endorsed by the sponsor. The sponsor will use the online portal to verify the participant's sponsorship.
3. Once verified, the sandbox participant and sponsor will receive an email noting the start date of the exemption, being either the day that the sponsor endorses the participant, or such other time as elected by the participant.

This suggested process aligns with ASIC's shift towards e-lodgement. Fintech Australia is willing to work with ASIC to develop an electronic platform that fully integrates lodgement of forms, and verification of sponsorship.

We also propose that ASIC maintain a register of sandbox participants. This will include the date that the participant began to rely on the exemption, whether there has been an extension and for what period, and if an AFSL application has been lodged. This will assist clients to confirm which businesses are relying on the exemption and the status of their authorisation.



C9 - Withdrawal of relief

We propose that ASIC will have the power to withdraw the AFS licensing exemption in proposal C1.

C9Q1 *When should we exercise our power to withdraw the licensing exemption?*

Fintech Australia considers that ASIC should have the power to withdraw the AFS licensing exemption if it has reasonable grounds to believe that the business is not compliant with the terms on which the exemption applies. ASIC should also have power to impose conditions on a sandbox participant, rather than just withdraw the exemption.

However, Fintech Australia does not believe that compliance with Regulatory Guide 234 Advertising financial products and advice services including credit: Good practice guidance (**RG 234**), should be mandated as part of the exemption. Whilst regulatory guides are important in informing how a company should behave, they are not law. Forcing sandbox participants to comply with RG 234 goes beyond the requirements placed on AFSL holders. Given the sandbox is a step on the road towards an AFSL, the requirements for sandbox participants should not exceed those of AFSL holders and this should not be mandated.

ASIC should notify the business of its concerns and provide the opportunity to rectify those concerns within 20 business days or to provide evidence to ASIC that the concerns are unfounded. If the business is unable or unwilling to do so, ASIC should have the right to withdraw the licensing exemption.

ASIC noted that a 'person' should only be able to rely on the exemption once. Fintech Australia interprets this to mean that a business should only be able to rely on it once. Whether a business is 'new' should only be determined based on the business's activities and not the previous activities of any founders or investors. If an investor or founder has previously been part of a business that relied on the sandbox exemption, that should not prevent a new business involving that individual from relying on the sandbox to test another business.