

26 April 2019

Australian Securities & Investment Commission
GPO Box 9827
Brisbane QLD 4001

By email: policy.submission@asic.gov.au

Dear Sir/Madam

**Feedback on draft Cost Recovery Implementation Statement:
ASIC industry funding model (2018-19) (CRIS)**

We refer to the draft CRIS for 2018-19 released by the Australian Investments & Securities Commission (ASIC) for feedback in late March 2019.

ARITA - Australian Restructuring Insolvency and Turnaround Association - makes this submission on the draft CRIS for 2018-19 and also reiterates our fundamental concerns on the operation of the industry funding model (IFM) as it applies to the registered liquidator subsector. More information about ARITA is provided at the end of this submission.

General feedback

ARITA has been heavily involved in providing ASIC and The Treasury with feedback and commentary (both through formal consultation processes and separately) expressing our concerns over the implementation and impact of the IFM on registered liquidators.

A summary of the previous submissions and correspondence provided by ARITA is included in the Annexure to this submission.¹

Consistently throughout our feedback and submissions we have raised the following fundamental concerns in relation to the operation of ASIC's IFM for registered liquidators:

- There are significant negative market consequences of the IFM for registered liquidators which has diminished the proper, competitive operation of the market. There have been ongoing contractions in the number of registered liquidators and we

¹ We have not reproduced the body of each of these submissions (as they have been previously provided on more than one occasion) but we can provide them again to ASIC or The Treasury upon request.

continue to estimate that some 200 of the 705 registered liquidators registered and capable of taking appointments as at 1 July 2017² will cease their registration by the end of 2019. In 2017-2018, 55 registered liquidators exited their registration, with only 7 new registrations. Noting that 11 registered liquidators are unable to take new appointments, this leaves 652 active registered liquidators as at 30 June 2018. The reduction in registered liquidator numbers places the proper operation of the economy at risk, especially in any future recession as these skills will be lost to the market.

- Noting the above actual figures reported by ASIC (Report 610), ARITA is concerned regarding the discrepancy for the number of levied entities reporting in the 2018-19 CRIS. This report (at page 48) indicates that there are 718 registered liquidators subject to the IFM as at 1 July 2018 and calculated the indicative levy of \$81 per metric based on this number. This figure appears to be based on the actual number of registered liquidators levied in 2017-18, however, this is inconsistent with the number of registered liquidators reported as at 30 June 2018 of 663. While we acknowledge that the CRIS notes that the indicative levies for 2018-19 are based on “estimates of population” for each subsector³, this statement was published in March 2019, after the reporting of the actual figures by ASIC, resulting in the calculation of the indicative levy being based on knowingly inappropriate information.
- The IFM levy is considerably unjust given the very high cost per liquidator compared to other similar regulated populations and international comparatives; it also disregards for the work done by liquidators in support of ASIC and the limited benefits from the current ASIC supervision.
- The ex-post nature of the levy has resulted, and will continue to result, in creditors being disadvantaged due to the distinct and finite nature of insolvency appointments. Registered liquidators were only advised of their 2017-18 applicable metric cost (\$77 per metric) in December 2018, having already based approved costs in external administrations on ASIC’s initial estimated metric (\$125 per metric). Given the discrepancy between the estimated and actual metric for 2017-18, there is a lack of confidence within the subsector as the accuracy of the 2018-19 estimate of \$81 per metric event, particularly noting the above comment regarding its calculation based on the knowingly inappropriate number of registered liquidators.
- Further, the ex-post nature of the levy also means that insolvency practitioners cannot budget for the significant costs they face. Despite being assured of the stability of this charge, practitioners previously saw a 30% variation in the fee from forecast. For the current year there appears to be a further proposed 5% change

² ASIC Report 610 ASIC regulation of registered liquidators: January 2017 to June 2018.

³ Cost Recovery Implementation Statement: ASIC Industry Funding Model 2018-19 paragraph 90.

from the previous year's graduated levy charge, with this estimate being released nine months after the commencement of the year.

- Liquidators are already obliged to carry out significant, often unpaid work on behalf of ASIC and the government. Liquidators are required by law to undertake investigation and reporting work for the benefit of ASIC and are required to finalise a liquidation even if they are unable to recover their fees. This unique situation means liquidators are being double taxed by the IFM when they are already subsidising ASIC. ARITA's research indicates the population of less than 700 liquidators has to write-off some \$100 million in unrecoverable fees each year.
- We also note that the ex-post structure of the IFM is deeply problematic for registered liquidators in that, unlike other regulated populations, liquidators must have their remuneration approved by creditors or Courts who may take no consideration of the cost impact of the IFM. This places an unreasonable burden on liquidators, especially those dealing in the SME space where remuneration is often unrecoverable

Now that the IFM levy has been in place for a year, we confirm that each of these concerns remain valid and, in many cases, issues previously raised by ARITA in our feedback and commentary have eventuated but have not yet been resolved or, in most cases, responded to.

Some specific feedback on the draft CRIS for 2018-19 is set out below.

Part 1 – Industry funding levies

The CRIS asserts (at [64]) that, for ASIC, the IFM:

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

However, the IFM, in its application to the registered liquidator subsector, fails to achieve any of the objectives stated above.

Disproportionate application and lack of transparency

The application of the IFM to registered liquidators is disproportionate particularly when:

- (a) consideration is given to the significant amount of work carried out in terms of unfunded investigations, much of which is done for the benefit of ASIC; and
- (b) comparison is made with other regulated communities, for example, registered company auditors who have been assigned a flat levy.

There is a lack of transparency in the manner of allocation of costs across subsectors and exactly what are included in direct and indirect costs. Given the high levels of disclosure which are required of insolvency practitioners when seeking approval of their remuneration from creditors or the Court it is highly unfortunate that ASIC is not able to provide more detailed information, on a specific subsector basis, of the manner in which its costs are allocated and charged.

This lack of transparency in accounting is particularly galling for insolvency practitioners who are regularly publicly lectured by ASIC about disclosure of practitioner remuneration. That ASIC are unable to display more than a few budget line items for some \$10 million of charges levied to the insolvency profession is hypocritical, and fails to follow the same standard it demands of the regulated population.

Further, again, when liquidators are required by ASIC to seek approval for future remuneration from Courts or creditors, the lack of reliable forward budgets for ASIC shows a lack of planning and accountability by ASIC which also harms the ability of liquidators to plan for the costs of the IFM with even a modicum of certainty.

By way of example, in “Table 13: Budgeted costs to regulate registered liquidators” (on page 44), there is an allocation of “\$0.903m” in budgeted costs which is attributable to “IT support”.

Based on the limited description of what is included in ASIC’s indirect costs charged as part of the IFM, IT costs or support are described (at [79]) as being “allocated based on storage capacity, length of processes and activity volumes, while other costs to build, support and maintain [ASIC’s] support systems are attributed...based on.. the number of ...staff who use [them].”

Insolvency practitioners are required by the *Corporations Act 2001* (Cth) (Act), and by ASIC, to lodge a large number of detailed and often lengthy forms and documents which then, it is understood, are stored on ASIC’s IT systems, resulting in high “activity volumes” and use of “storage capacity”.

It is also noted that when discussing the ASIC technology platforms (as they apply to the business register systems) before the Senate Economics Legislation Committee recently,⁴ Commissioner Price stated that:

“The current technology utilised by ASIC...is ageing and is not adequate to meet growing future demand.

...

I’d strongly encourage people not to build new functionality into ASIC’s existing legacy systems, particularly the companies’ database. It is at the end of its usable life.”

An analysis of this particular indirect cost, and the manner in which it is applied to registered liquidators under the IFM, illustrates the entirely circular impact of the regulatory requirements imposed by the Act and ASIC. Registered liquidators are required to make lodgements and file a large number of documents, which then increase activity volumes and take up storage capacity, which then, seemingly, increase the proportion of IT costs allocated to the registered liquidator subsector under the IFM. Those payments are then used by ASIC to prop up its ageing and inadequate IT infrastructure.

Combined with the fact that many of the lodgements required of registered liquidators will also attract a specific metric charge for calculation of the graduated levy, this simple example is one of many which illustrates how registered liquidators are disproportionately impacted by the IFM.

Further, at [119], ASIC sets out the manner in which it will carry out its regulatory activities for registered liquidators, and these activities underlie ASIC’s costs for the subsector.

Included in the activities for which ASIC seeks to recover the costs of its regulatory activities is:

“(f) provide input into legislative reform like reforms addressing illegal phoenix activity and monitor the effectiveness of changes under the *Insolvency Law Reform Act 2016* and the insolvency safe harbour and *ipso facto* clause law reforms;”

Given that ASIC has within its functions and powers under s 11 of the *Australian Securities and Investment Commission Act 2001* (Cth) (ASIC Act) an ability to make recommendations on matters including law reform, and in certain instances there are in-built statutory obligations for review of the efficiency and efficacy of law reforms as implemented, it is both

⁴ Senate Economics Legislation Committee hearing into the Commonwealth Registers Bill 2019 and related bills held in Melbourne on 13 March 2019.

surprising and seemingly unnecessary for this type of activity to be included in the list of matters for which ASIC effectively charges registered liquidators.

Increased compliance burden and lack of guidance as to practical implications

The application of the IFM to registered liquidators is also placing a significant regulatory and compliance burden on what is a small and highly specialised subsector.

These challenges are highlighted by the inability of registered liquidators to budget for the imposition of the IFM when the estimated amount for calculation of the graduated levy is not publicised until nine months into the financial year for which it is being charged (although we note that there is no requirement in the law for ASIC to meet these reporting guidelines, meaning that liquidators have no certainty as to when they will find out the cost impact of the IFM).

Further, a specific issue with the practical implementation of the IFM, which was flagged by ARITA in our submission dated 25 May 2017, is the recovery of IFM levies from leviable entities that enter into external administration.

Since the commencement of the IFM in July 2018, ARITA has received a large number of queries which relate to this issue and specific queries have been raised of the relevant ASIC team.

However, to date only limited guidance has been provided in response to these queries.

Part 2 – Fees for service

The second aspect of CRIS covers the operation of the “fees for service” model under the IFM.

In respect of this aspect and its impact on insolvency practitioners, ARITA separately wrote to ASIC on 10 December 2018 raising a number of concerns regarding specific fees for services.

In particular, the concerns raised by our members related to the disproportionate increase in fees charged for applications for reporting relief, particularly in how these are applied to corporate groups, and the changes to fees charged by ASIC for its review of documents under scheme of arrangement provisions. In both of these instances the fees have increased in the range of 1000%.

ASIC has recently responded to this letter and acknowledged that the operation of the fixed cost fees for service framework “may have unintended consequences for corporate groups”.

ARITA will respond separately to ASIC on the specific issues arising from the correspondence, however, we note that the concerns previously expressed remain.

Part 3 – Stakeholder engagement

This section of the CRIS summarises the steps taken in terms of stakeholder engagement on the IFM.

As noted and evidenced in the annexure, ARITA has been an active participant in the consultation program concerning the implementation of the IFM and has consistently raised concerns over the impact of the model on registered liquidators, and the economy more generally.

However, there has been little specific engagement in response from ASIC or The Treasury on these issues.

Given the impacts of the IFM on the registered liquidator subsector ARITA will continue to review and press for reform of the approach taken by ASIC, particularly as we remain fundamentally concerned that the impact of the IFM, alongside a protracted downturn in the insolvency profession, continues to drive liquidators from the market.


Noting that 10% have already chosen not to renew their registration and a further 10% still likely to follow, this hollowing out of the insolvency profession, that has only begun since the IFM was introduced, will leave the Australian economy significantly under-serviced when the next major downturn occurs. Given the high barriers to entry applicable to the liquidator registration process, we believe it will take many years to rebuild liquidator numbers. This scarcity will drive dramatically up the cost of liquidations in the next major downturn, hurting an already impacted economy.

It is also disappointing that the neither the draft CRIS, nor any of the supporting documentation issued by ASIC, appear to contain any commentary or detailed analysis as to whether the overall system is meeting the objectives set out for the IFM approach.

Noting the matters discussed above for the registered liquidator subsector, ARITA's submission is that the implementation of the IFM has wholly failed to meet those objectives and is instead having a significantly negative effect.

Should you have any queries concerning this submission please contact us.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'John Winter', with a long horizontal flourish extending to the right.

John Winter
Chief Executive Officer

Annexure

Summary of ARITA submissions and feedback on IFM

Date	Summary of feedback
9 October 2015	<ul style="list-style-type: none"> - First round of consultation on implementation of industry funding model (IFM). - Letter to Treasury expressing concerns over IFM, including detailing the risks of significant negative market consequences.
14 December 2016	<ul style="list-style-type: none"> - Letter to (then) Minister for Revenue and Financial Services, the Hon Kelly O'Dwyer MP expressing concerns over proposed IFM and its implications for the insolvency profession
16 December 2016	<ul style="list-style-type: none"> - Second round of consultation on implementation of IFM. - Letter to Treasury reiterating concerns over IFM and providing responses to consultation queries.
10 March 2017	<ul style="list-style-type: none"> - Letter to Treasury providing feedback on exposure drafts of ASIC Supervisory Cost Recovery Levy Bill 2017 and related bills.
25 May 2017	<ul style="list-style-type: none"> - Letter to Treasury providing feedback on the ASIC Supervisory Cost Recovery Levy Regulations 2017.⁵
10 July 2017	<ul style="list-style-type: none"> - Letter to ASIC and Treasury expressing concerns over IFM and Public Notices Website (PNW) charges.
10 December 2018	<ul style="list-style-type: none"> - Letter to ASIC regarding changes to the ASIC fees and impact of calculation approach to ASIC fees for service. (Response received from ASIC on 13 March 2019. Further queries to be raised by ARITA.)
7 February 2019	<ul style="list-style-type: none"> - Letter to Treasury, submission on ASIC IFM and Registry Search Fees.

⁵ As discussed above, specific examples were raised in this correspondence have eventuated and passed onto ASIC, but practitioners still have not guidance.



About ARITA

The Australian Restructuring Insolvency and Turnaround Association (ARITA) represents professionals who specialise in the fields of restructuring, insolvency and turnaround.

We have more than 2,400 members and subscribers including accountants, lawyers and other professionals with an interest in insolvency and restructuring.

Around 84 percent of registered liquidators and 87 percent of registered trustees are ARITA members. We represent firms of all sizes, from small practice through to multi-national firms, with the majority of our membership being drawn from those in small-medium practice.

ARITA's ambition is to lead and support appropriate and efficient means to expertly manage financial recovery.

We deliver this through the provision of innovative training and education, upholding world class ethical and professional standards, partnering with government and promoting the ideals of the profession to the public at large. In 2017, ARITA delivered close to 300 professional development sessions to around 5,000 attendees.

The Association promotes best practice and provides a forum for debate on key issues facing the profession. We also engage in thought leadership and public policy advocacy underpinned by our members' needs, knowledge and experience. We represented the profession at 23 inquiries, hearings and public policy consultations during 2017.