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By Email

Dear Alan

Submission – ASIC Consultation Paper 301: Foreign financial services providers

This submission is made in response to ASIC Consultation Paper 301 *Foreign financial services providers* (**CP 301**), which outlines relief relied on by foreign financial services providers (**FFSPs**) who would otherwise require an Australian financial services licence (**AFSL**) under the *Corporations Act 2001* (Cth) (**Corporations Act**) to carry on a financial services business in Australia (**AFSL Requirement**).

CP 301 requests feedback on ASIC's proposal to:

(a) repeal *ASIC Corporations (Repeal and Transitional) Instrument 2016/396* (**Instrument 2016/396**) which enables FFSPs that are regulated in another jurisdiction to a degree that ASIC has considered to be 'sufficiently equivalent', to 'passport' that overseas regulation in order to be exempted from the AFSL Requirement (**Passporting Exemptions**);

(b) repeal *ASIC Corporations (Foreign Financial Services Providers - Limited Connection) Instrument 2017/182* (**Instrument 2017/182**) which enables FFSPs physically located outside Australia and providing financial services from outside Australia, only to wholesale clients in Australia, to also be exempted from the AFSL Requirement (**Limited Connection Exemption**) (together with the Passporting Exemption, the **FFSP Relief**); and

(c) implement a modified licensing regime, a 'foreign AFSL', for certain FFSPs providing financial services to wholesale clients in Australia.

We provide our comments in respect of ASIC's proposals in this submission.

2 Regulatory settings

As a general observation, at a time when Australian financial services regulation is recognising and facilitating the globalisation of the financial services sector, for example by the introduction of the Asia Region Funds Passport, we would like to invite ASIC to revisit whether its regulatory concerns in relation to the FFSP Relief are capable of being addressed by the imposition of additional obligations under, or the addition of new conditions to, the Passporting Exemption and the Limited Connection Exemption.

We have spoken with a number of FFSPs in the US, Asia and Europe who share this view and have asked us to raise this point in our submission but who do not wish to make a submission to this effect themselves because they don't want to make a public statement which may be taken to be resisting regulatory change or criticising ASIC.

We would like to invite ASIC to consider whether:

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(a) in relation to the Passporting Exemption, its regulatory concerns could be addressed by imposing additional conditions on the Passporting Exemption or obligations under the deed of undertaking entered into by FFSPs, for example obligations on the FFSP to:

(1) comply with directions from ASIC;

(2) adopt enhanced breach reporting requirements, similar to section 912D Corporations Act; or

(3) provide reasonable assistance to ASIC during surveillance checks.

(b) in relation to the Limited Connection Exemption, its regulatory concerns could be addressed by limiting the scope of the persons entitled to use this exemption, for example to persons who have:

(1) given notice to ASIC in relation to their commencement of (and cessation of) reliance on the exemption. Such a notice would give ASIC visibility on the FFSPs using this exemption and their overseas regulation; and/or

(2) who are regulated overseas to a degree that ASIC considers to be sufficiently equivalent to holding an AFSL. Such an eligibility requirement would give ASIC comfort in relation to the regulation of FFSPs using this exemption; or

(3) made an application to ASIC for approval to use this exemption, and have provided a deed of undertaking to ASIC (similar to that provided under the Passporting Exemption).

If ASIC's primary regulatory concerns could be addressed through these additional obligations or conditions, rather than a foreign AFSL regime, the compliance cost and regulatory costs to FFSPs wishing to continue to provide financial services in Australia would be more manageable and would be less of a barrier to entry.

We, and a number of FFSPs that we have been talking to about CP 301, are concerned that:

(c) a significant amount of compliance work (and cost) will need to be incurred by FFSPs in order for them to fully understand and manage on an ongoing basis, all of the legal and regulatory consequences of becoming an AFSL holder, as noted below. For a FFSP regulated in a number of jurisdictions, the duplication of compliance arrangements and related costs in multiple jurisdictions can lead to significant inefficiencies and inevitably will force the FFSP to undertake a cost/benefit analysis in relation to its global footprint; and

(d) given this, the foreign AFSL regime, if imposed, is likely to:

(1) reduce the pool of FFSPs willing to continue to provide services in Australia to Australian institutions or deter FFSPs from extending their businesses to enter the Australian wholesale market; and

(2) reduce the diversification of investment managers and investment products available to Australian institutions which will ultimately reduce the diversification of managers and products available to retail investors investing through Australian institutions,

and that these consequences may in turn reduce the fee pressure and competition in the Australian market, and lead to higher management costs for retail investors.

3 Eligibility for foreign AFSL

We understand from CP 301 that FFSPs which currently rely on the Passporting Exemption would be automatically eligible to apply for a foreign AFSL on the basis that the FFSP's overseas licence or permission is sufficiently equivalent to an AFSL (**Eligible FFSP**).

However, we note that it is often important, for good governance, compliance and conflict and risk management purposes, for a FFSP's corporate group to segregate its business activities in the different jurisdictions in which the FFSP provides financial services.

We request that an Australian company which is a wholly owned subsidiary (under section 46 Corporations Act) of an Eligible FFSP is also eligible to apply for a foreign AFSL, in reliance on the Eligible FFSP's foreign licence or permission.

Confirming that a subsidiary of an Eligible FFSP is eligible to apply for a foreign AFSL (ie that the eligibility is not limited to the Eligible FFSP itself) would facilitate:

(a) international FFSPs growing and managing their global financial services businesses in Australia;

(b) more efficient management of FFSP's tax and financial reporting and general compliance obligations in relation to their Australian business; and

(c) FFSPs who are not required to make their financial reports publically available in their home jurisdiction applying for a foreign AFSL through an application by their wholly owned subsidiary. We understand that some Eligible FFSPs are not required to lodge accounts with their home regulator (or are able to lodge accounts on a commercial in confidence basis, where they are not available to the public) and that those Eligible FFSPs would prefer to hold the foreign AFSL at an Australian subsidiary level and to prepare and lodge accounts for their wholly owned Australian subsidiary.

4 Sufficiently equivalent

In CP 301.63-67, ASIC discusses the approach of other regulators to cross-border regulation of financial services and notes at 301.64 that:

> *Our inquiries suggest that our approach to AFS licensing relief for FFSPs may be broader than those of our peers in other major jurisdictions, including the United Kingdom, the United States, Germany, Hong Kong, Singapore, New Zealand and Japan, particularly looking at the range of services that our relief applies to.*

We request that this position is retested and reconsidered because it is an important point and an important rationale for the change in policy proposed in CP 301.

(a) We understand that there is an exclusion in the United Kingdom for an FFSP to be authorised by the Financial Conduct Authority (**FCA**) in the United Kingdom (**UK**) where that FFSP satisfies the requirements of an 'overseas persons'. This exemption and the relevant definition is set out in Article 72 of the *Financial Services and Markets Act 2000 (Regulated Activities) Order 2001*. If our understanding is correct, then ASIC's proposed approach to AFS licensing relief under CP 301 is narrower than that of its peers in the UK and could potentially lead to a change in respect of the eligibility of Australian FFSPs as 'overseas persons' in the UK.

(b) Further, we submit that ASIC's licensing relief regime for FFSPs, particularly in relation to the Limited Connection Exemption, may appear broader than ASIC's peers because the provision giving rise to the need for it, namely the 'inducing' provision in section 911D of the Corporations Act is not, to our knowledge, present in other jurisdictions.

(1) Section 911D is extensive and far-reaching. It deems activity outside Australia to be activity in Australia for the purposes of the AFSL Requirement.

(2) Under section 911D, a FFSP is deemed to be 'carrying on a financial services business in Australia' if the FFSP's conduct offshore:

(A) is intended to induce people in Australia to use the FFSP's services; or

(B) is likely to have that effect.

(c) Given ASIC's wide interpretation of the meaning of 'inducing' (see for example ASIC Regulatory Guide 121.52) FFSPs who have no physical presence or permanent establishment in Australia have found the Limited Connection Exemption to be particularly valuable in helping them make services available to Australian institutions from offshore, without incurring the cost and regulatory burden of holding an AFSL.

(d) It is for this reason that we request that ASIC considers maintaining the Limited Connection Exemption (potentially with additional obligations or regulations) or limiting the effect of section 911D, to help FFSPs address the extensive and far-reaching scope of section 911D, as discussed further in part 6 of this submission, below.

5 Passporting Exemption

5.1 Parliamentary intention

We also note for completeness that the Passporting Exemption is made available to FFSPs as an exemption to the AFSL Requirement under section 911A(2)(h) of the Corporations Act (**Legislative Exemption**) which provides that a person is not required to hold an AFSL where all of the following apply:

(i) the person is regulated by an overseas regulatory authority;

(ii) the provision of the service by the person is covered by an exemption specified by ASIC in writing under this subparagraph and published in the Gazette; and

(iii) the service is provided only to wholesale clients;

The codification of the Legislative Exemption in the Corporations Act demonstrates Parliament's intent at the time of the enactment of the Corporations Act in 2001 that an AFSL would not be required for FFSPs who are regulated by an overseas regulatory authority and only provide financial services to wholesale clients.

We ask ASIC to reconsider whether the repeal of the Passporting Exemption regime is in accordance with the intention of Chapter 7 of the Corporations Act and Parliament's intention to offer an exemption to overseas-regulated FFSPs who only provide financial services to wholesale clients.

5.2 Additional regulations and obligations

As noted in part 2 above, we would like to invite ASIC to revisit whether its regulatory concerns in relation to the Passporting Exemption are capable of being addressed by the imposition of additional obligations under, or the addition of new conditions to, the Passporting Exemption or under the deed of undertaking entered into by FFSPs, for example obligations on the FFSP to:

(a) comply with directions from ASIC;

(b) adopt enhanced breach reporting requirements, similar to section 912D Corporations Act; or

(c) provide reasonable assistance to ASIC during surveillance checks.

If additional conditions or obligations could give ASIC comfort that it has the tools that it needs to adequately supervise and carry out its enforcement function in relation to FFSPs, that would reduce the risks:

(d) that the pool of FFSPs willing to continue to provide services in Australia to Australian institutions reduces;

(e) that FFSPs are deterred from entering the Australian wholesale market; and

(f) of a reduction in the diversification of investment managers and investment products available to Australian institutions (and their retail investors) and in fee pressure and competition in the Australian market, potentially leading to higher management costs for retail investors.

5.3 Compliance with overseas laws and regulations

Under the Passporting Exemptions, FFSPs are currently subject to a condition (**Overseas Law Compliance Condition**) to the following effect:

> The [FFSP] must provide each of the financial services in [Australia] in a manner which would comply, so far as is possible, with the [home jurisdiction] regulatory requirements if the financial service were provided in [the home jurisdiction] in like circumstances.

CP 301 provides information in relation to which regulatory requirements are proposed to apply to foreign AFSL holders and which are not.

(a) Relevantly it proposes that certain Passporting Exemption conditions will be imposed on foreign AFSL holders though licence conditions (through pro forma 209).

(b) We note however that CP 301 does not propose that the Overseas Law Compliance Condition is a foreign AFSL licence condition through pro forma 209.

(c) We also note that CP 301 states that the eligibility of FFSPs for a foreign AFSL is based on ASIC's determination that the laws of the home jurisdiction are 'sufficiently adequate" and provides:

> *We propose to exempt foreign AFS licensees from requirements in the Corporations Act and the Corporations Regulations where the relevant overseas regulator will monitor or enforce the sufficient equivalence FFSP's compliance with the overseas regulatory regime as they apply to the FFSP's business activities in Australia and the regulatory regime in the sufficient equivalence FFSP's home jurisdiction produces similar regulatory outcomes to the Australian regime….*
>
> *Many of the obligations that we are proposing not to apply to the sufficient equivalence FFSP are equivalent to requirements that exist in the sufficient equivalence FFSP's home jurisdiction and we are satisfied that compliance by FFSPs in their home jurisdiction would translate to the activities of the FFSP in Australia.*

(d) Please confirm whether it is proposed that a foreign AFSL holder will be required to provide each of the financial services in Australia in a manner which would comply, so far as is possible, with its home jurisdiction regulatory requirements if the financial service were provided in the home jurisdiction in like circumstances. If it is so proposed, please also confirm how that is proposed to be effected.

6 Limited Connection Exemption

As noted above, the Limited Connection Exemption has been particularly valuable in helping FFSPs make services available to Australian institutions from offshore, without incurring the cost and regulatory burden of holding an AFSL, given the far reaching scope of the deeming provision in section 911D of the Corporations Act.

If the Limited Connection Exemption were to be repealed, as proposed, the ability of FFSPs to use alternative exemptions to the AFSL Requirement to manage the impact of section 911D is limited.

For example, Regulation 7.6.02AG of the *Corporations Regulations 2001* (Cth) (**Corporations Regulations**) provides limited exemptions which in our experience are rarely capable of use by FFSPs because:

(a) the scope of one exemption[1] is limited to:

  (1) professional investors, not wholesale clients more generally; and

  (2) a narrow range of financial products (limited to derivatives, foreign exchange contracts, carbon units, Australian carbon credits and eligible international emission units); and

(b) the scope of another exemption[2] applies a requirement to not 'actively solicit' persons in Australia to make an inquiry for the provision of financial service from a FFSP. The explanatory memorandum to this regulation provides some limited guidance in relation to what constitutes active solicitation, including that if a FFSP:

  (1) advertises its financial services or products in newspapers or other periodicals which are published and primarily circulate in Australia; or

  (2) directly contacts people in Australia (by whatever means – including telephone, e-mail or mail),

  that conduct will be considered to constitute active solicitation. This guidance indicates that the regulatory approach to active solicitation is to apply a broad definition, which of course reduces the availability of the exemption.

As noted above, we invite ASIC to consider whether in relation to the Limited Connection Exemption, its regulatory concerns could be addressed by changes to the exemption, rather than its revocation.

We appreciate that the conditions attaching to the Limited Connection Exemption are currently limited and do not presently require, for example:

(c) eligibility being restricted to FFSPs which are regulated in home jurisdictions that ASIC considers to be sufficiently adequate;

(d) an application for approval from ASIC;

(e) the provision of a deed of undertaking (as is the case under the Passporting Exemption); or

(f) a formal notification to ASIC in relation to a FFSP's commencement of (and cessation of) reliance on the exemption, similar to an 'in-use' or 'out of use' notice in respect of a product disclosure statement.

We would like to invite ASIC to explore the extent to which these or other modifications to the Limited Connection Exemption could give ASIC sufficient comfort in relation to visibility on the FFSPs using this exemption and their overseas regulation and ASIC's

[1] Under the modified section 911A(2E) under that regulation.

[2] Under the modified section 911A(2D)(d) under that regulation.

ability to adequately supervise the FFSPs and carry out its enforcement function in relation to FFSPs.

We submit that a modification, rather than a repeal, of the Limited Connection Exemption would also reduce the risks noted above in relation to the reduction in the diversification of investment managers and investment products available to Australian institutions and a reduction in fee pressure and competition in the Australian market.

Additionally, we invite ASIC to consider:

(g) amending section 911D, to reduce the extent of its far reaching impact and to make it more manageable, particularly having regard to equivalent regulations in other jurisdictions;

(h) updating ASIC's published policy in Regulatory Guide 121 in relation to the meaning of 'inducing';

(i) extending other exemptions to the AFSL Requirement, such as Regulation 7.6.02AG to widen the scope and useability of those exemptions; and

(j) providing new guidance in relation to the meaning of 'active solicitation', to facilitate more FFSP activity in Australia.

7 Unintended consequences

The concept of a 'financial services licensee' or 'holder of an Australian financial services licence' (**AFSL holder**) is used throughout the Corporations Act to impose regulatory obligations on AFSL holders. However, such terms are also used in other legislative regimes to impose obligations on AFSL holders which are not regulated by ASIC.

By way of example, section 6 of the *Anti-Money Laundering and Counter-Terrorism Financing Act* 2006 (Cth) (**AML/CTF Act**) provides that a person is a 'reportable entity' for the purpose of the AML/CTF Act in relation to the provision of a designated service. In this regard, item 54 of section 6 of the AML/CTF Act prescribes the following as a designated service:

> *in the capacity of holder of an Australian financial services licence, making arrangements for a person to receive a designated service (other than a service covered by this item).*

Item 54 as extracted above prescribes that AFSL licensees in certain circumstances provide a 'designated service' for the purpose of the AML/CTF Act and accordingly, absent a specific exclusion being introduced to the AML/CTF Act, a foreign AFSL holder will be subject to the scope of the AML/CTF Act and may be required to register with the Australian Transaction Reports and Analysis Centre (**AUSTRAC**) and comply with the significant and detailed obligations under the AML/CTF Act.

If this outcome was not contemplated or intended by ASIC in relation to the foreign AFSL regime then we suggest that the CP 301 proposals are extended to identify this and other unintended consequences of an expansion to the AFSL regime, and provide proposals, for further public consultation, in relation to how to deal with them.

Given the potential ramifications of even a potentially small extension to the AFSL regime because of the knock on impact on other legislative regimes, we request that further analysis is undertaken to ensure that the consequences and impact of the foreign AFSL proposals are fully identified and consulted on.

8 Transitional period

We understand that it is ASIC's proposal in CP 301 that the FFSP Relief will be extended to September 2019 with a further 12 month transition period applying to September 2020.

We would like to invite ASIC to revisit whether the proposed transition period is appropriate given:

(a) the time needed by FFSPs to undertake their cost/benefit analysis and prepare for these significant reforms, if introduced as proposed;

(b) the time needed for ASIC to prepare and finalise the foreign AFSL application forms, kits and guidance;

(c) the time currently being taken to process AFSL applications (which can be up to 8 months we understand);

(d) the volume of applications expected for foreign AFSLs (which CP 301 referred to as 'significant) and which could form a bottleneck once the application process opens; and

(e) we understand that a safe harbour will not be available to FFSPs whose foreign AFSL applications are still being processed in September 2020, to enable them to continue to provide financial services under the FFSP Relief after September 2020 for the duration of their application processing period.

It is proposed that foreign AFSL holder FFSPs will be required to demonstrate compliance with, among other things, Australia's financial services laws and ensure that they have in place adequate conflicts and risk management processes and systems in order to comply with their foreign AFSL conditions. If there are unintended consequences which are enlivened for foreign AFSL holders (for example as set out in section 7 above) then FFSPs will require an adequate transition period to ensure that FFSPs:

(f) are aware of such obligations; and

(g) have in place adequate and robust control mechanisms to ensure compliance with such obligations.

For the above reasons, we would like to invite ASIC to consider extending the transition period from 12 to 24 months, to September 2021.

Yours sincerely

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