13 August 2021

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Dear Sir/Madam

Cost Recovery Implementation Statement (CRIS) 2020-21

We refer to the Cost Recovery Implementation Statement (CRIS) 2020-21 provided for feedback on 26 July 2021.

Morgans is Australia's largest national full-service stockbroking and wealth management network with more than 150,000 client accounts, 540 authorised representatives and 950 employees operating from 60 offices in all states and territories.

The ASIC Act requires ASIC to strive to maintain, facilitate and improve the performance of the financial system, and the entities within it, in the interests of commercial certainty, reducing business costs, and the efficiency and development of the economy. ASIC also has the function of monitoring and promoting market integrity and consumer protection in relation to the Australian financial system.

Commercial certainty: ASIC estimates via the CRIS have grossly underestimated the graduated levy

The levy amount for licensees that provide personal advice on relevant financial products to retail clients has proved to be unpredictable each year, resulting in licensees and financial advisers being unable to budget adequately for the cost. The ASIC estimates via the CRIS have grossly underestimated the graduated levy based on each AFS licensee's share of the total number of advisers registered on the FAR at the end of the financial year, leading to lack of commercial certainty for industry.

As shown in the table below, the indicative graduated levy published in the 2019-20 CRIS was $1,571 per adviser. The actual levy charged for the 2019-20 FY was $2,426.42. That is an increase of $855.40 per adviser (54.5%). For Morgans, with 441 financial advisers providing personal advice to retail clients, this was an unbudgeted increase of $377,231.40.

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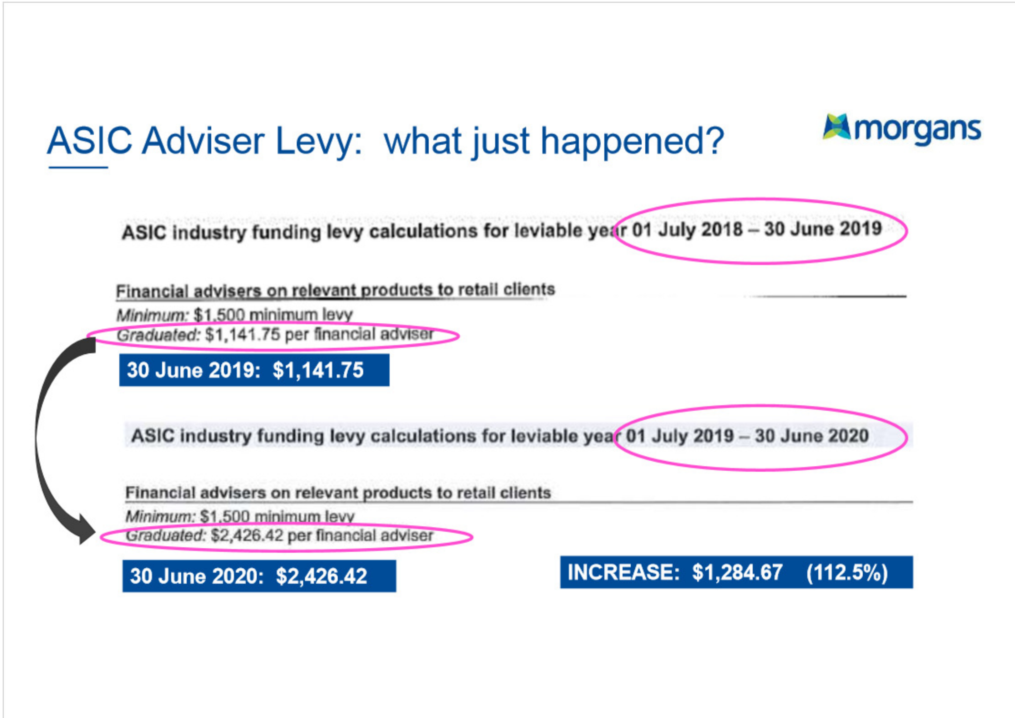
The FY2020-21 indicative levy is $3,138. This represents an increase of $711.58 per adviser (29.3%). For Morgans with 411 advisers, that is an increase of $292,459.

Based on applying last year's difference between the indicative levy and actual levy:

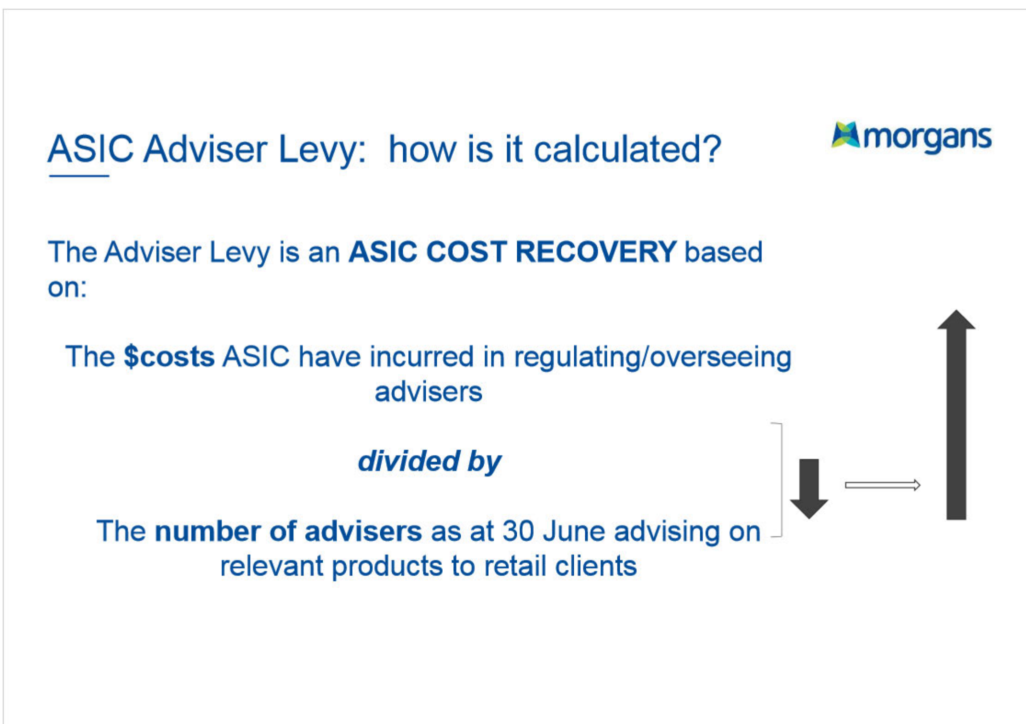
Indicative levy	$3,138.00	
FY2020-21 difference at 54.5%	1,710.21	*Extrapolated for 411 advisers = $703k*
Final levy (if FY2020-21 difference)	$4,848.21	*Extrapolated for 411 advisers = $1.99m*

Reducing business costs
The current formula is not equitable or sustainable. The levy, which is really another tax on business, is increasing at a rate that is much faster than businesses are able to grow revenue – particularly licensees in regional/rural Australia.

As the table below shows, the levy increased by 112.5% between FY2018-19 and the FY2019-20. An indicative levy increase in FY2020-21 of 29.3% is forecast. This is in a period when the pandemic is providing ongoing financial, health and mobility challenges to employers and employees in all sectors of the economy.



As the table below shows, the levy is calculated by dividing the costs ASIC incurs in regulating / overseeing financial advisers, by the number of advisers on the FAR as of 30 June 2021.



An ever-increasing cost borne by an ever-decreasing number of advisers
There are several issues with the current methodology:

1. ASIC costs for regulating the financial advice sector are increasing year on year.
2. ASIC sets the mandate for who and how they are going to regulate the sector. Industry participants, who pay for the cost of regulation, have no input into ASIC's mandate and no ability to take any action to lower such costs for their sector.
3. The number of advisers on the FAR are decreasing quite substantially due to:
    - an ageing adviser population;
    - the increased compliance / regulatory burden in providing personal advice to retail clients; and,
    - the FASEA interpretation of the education requirements for experienced advisers.

That is, an ever-increasing cost borne by an ever-decreasing number of advisers.

Morgans supports ASIC's statutory objectives
Morgans supports ASIC's statutory objectives including enforcing and giving effect to the laws it administers. However, the cost of taking enforcement action, such as court action, against individuals and entities where warranted, should not be borne by those in the sector who are doing the right thing and expending adequate financial, technological and human resources to operate effectively, efficiently and within the bounds of the law.

Unintended consequences
The increase in business costs is likely to result in a number of unintended consequences which do not promote market integrity or consumer protection in this area of the financial system:

- Change in business model from servicing and providing personal advice to retail clients to either exclusively servicing wholesale clients or providing general advice only to retail clients to reduce business costs
- Inability to provide personal advice to average and regional / rural Australians (retail clients). Increasing costs force businesses to increase the costs to retail clients pricing a lot of them out of the market for financial advice
- The loss of excellent advisers and small businesses in the financial services sector as they cannot continue to operate in the cost prohibitive environment (increasing costs for technology, compliance, professional indemnity insurance, licencing and regulatory costs including the ASIC industry funding levies and shortly, the compensation scheme of last resort)
- Increasing incentive to cut corners to reduce cost.

There is an increased willingness to seek financial advice
The ASX Australian Investor Study is an authoritative guide to the evolution of our investment markets and changing investor behaviour. The 2020 study came at a critical moment, as investors responded to the ongoing fallout from the COVID-19 pandemic, and the opportunities and challenges it presented. The 2020 study found that while the resulting market volatility caused many investors to re-examine their financial plans, the research also revealed a renewed focus on diversification and risk management, along with an increased willingness to seek professional advice.

Key findings of the 2020 study
Key findings of the 2020 study were:

- The impact of COVID-19 - 54% of those surveyed have made changes to their portfolios
- Investing in 2020 – 46% (9m) of the total adult population Australians hold investments outside their home and super
- 28% have changed their retirement plans
- 17% have invested all their spare cash
- 3% have increased their allocation to cash
- 57% plan to buy Australian shares
- Top investment challenges:
  - ➔ next generation investors (aged 18-24) – underperformance and hidden fees
  - ➔ wealth accumulators (aged 25-59) – market volatility and information overload
  - ➔ retirees (aged 60+) – market volatility and low interest rates
- 63% of Australians are open to receiving financial advice
- 27% of investors used an adviser, stockbroker or wealth manager in the last 12 months

The 2020 study asked how helpful their financial adviser has been in managing the impact of COVID-19. 84% of advised investors say they have been helpful, with 41% saying they were “extremely” or “very” helpful. There has also been a renewed interest in advice in the wake of recent market volatility, with 17% of non-advised investors saying they are more likely to consult a financial adviser in future.

This demonstrates the need for high quality, professional financial advice which is personal to the individual’s circumstances. Many of these will be retail clients – arguably those most in need of financial advice.

The reality is that due to the ever increasing compliance and regulatory burden, red tape, reduction in the number of experienced qualified financial advisers, less retail clients can be accommodated by the financial services industry for increasing cost.

How is it efficient for ASIC to take litigation action to promote confidence in the financial services sector and then expect those that are doing the right thing to pay for it?
Financial advice licensees which are SMEs are unfairly required to pay high levies that rise year-on-year due to misconduct by large licensees.

The irony of the situation is that the misconduct of the large banks and other large institutions such as AMP (all vertically integrated), which was exposed to the public via the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Royal Commission), and the subsequent remediation programs, litigation and increased regulatory framework have led to the large banks exiting wealth management (personal advice to retail clients). **This had left the remainder of the industry and financial advisers who were doing the right thing to ‘pick up the tab’ for the increased compliance and regulatory costs and enforcement action against those entities.** The funding model should be reformed to take account of large institutions that have exited the sector following the reputational fallout of the Royal Commission, which has also led to a number of legacy misconduct cases being taken to court by ASIC.

Financial advisers that provide personal advice on relevant financial products to retail clients are effectively litigation funders for ASIC.

To account for the mistiming issue due to misconduct of providers who have since left the industry, the graduated levy could be based on adviser numbers 3 years ago. **That is, those that caused the misconduct can’t just move out of the sector and leave others to pay for cleaning up their mess.**

We note ASIC's comment in paragraph 313 of the CRIS that, where possible, ASIC seek to recover their investigation and litigation costs directly from the entity involved when it is successful in a matter before the courts. As noted, not all expenditure is recoverable even where a costs order is awarded due to insufficient assets, and not all legal expenses incurred are recoverable even where successful (typically 60 to 70% may be recoverable). However, where such costs are recovered, ASIC does apply these back to the industry to offset against levy amounts.

In terms of transparency, the total recovered amounts which are offset against levy amounts should be specifically outlined. There will clearly be a timing issue in that some entities who paid the levies in a previous period for investigation and litigation costs may no longer be in operation at the time such cost recoveries are offset against a future levy amount.

Unlicensed personal advice
A further flaw in the methodology is that cases which are actioned for unlicensed personal advice, have the costs of taking the action recovered from licensed entities / advisers. This is not in the spirit of the law. **The public get the benefit of the regulatory oversight of unlicensed operators. If an unlicensed provider is pursued, the costs should be covered by the government / taxpayer, not those who are licenced and bear the costs of such license.**

An alternative approach which is fairer may be to have a higher fixed levy and lower graduated levy in the financial advice sector. For example, a fixed fee of $5,000 per licensee rather than $1,500.

The current funding model is grossly unfair and inequitable. It seeks to recover costs of overseeing businesses that have left the sector (the large banks and wealth management businesses) from those that remain in the sector. It seeks to recover the costs of pursuing unlicensed operators from those that are licensed. And it seeks to recover the unrecovered costs of litigation from compliant licensees. The funding model must be redesigned to remove this unfairness; it must reflect the balance between oversight of existing licensees versus those that have left the industry, those that are unlicensed and those from whom costs are not able to be recovered. Finally, it must provide certainty of cost to licensees. The year-on-year increases and variations to indicative levies is unsustainable.

Yours sincerely
Morgans

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John Clifford
Managing Director | CEO

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