OFFICE OF THE MINISTER
OF COMMERCE

The Chair

Cabinet Economic Growth and Infrastructure Committee

Financial Markets Conduct Act Licence Fees and Increase of Other Financial Markets Authority Fees

Purpose

1 This paper seeks approval to introduce licensing fees for market services providers under the Financial Markets Conduct Act 2013 (FMC Act) and to increase some existing Financial Markets Authority (FMA) fees. To give effect to these decisions, it also seeks approval for the submission of the Financial Markets Conduct (Fees) Regulations 2014 and Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014 to the Executive Council.

Executive summary

2 The FMC Act is a significant overhaul of securities law in New Zealand. It was passed in September 2013 and will begin coming into force from 1 April 2014. The FMC Act is a key component of the Government's Business Growth Agenda. The FMC Act's main purposes are to promote the confident and informed participation by businesses, investors and consumers in New Zealand's financial markets, and to promote and facilitate the development of fair, efficient, and transparent financial markets.

3 The FMC Act will introduce licensing requirements for market services providers, bringing New Zealand into line with international securities law. In granting licences, FMA will incur a number of costs. As the benefits of holding a licence are received by the market services provider, it is appropriate (and consistent with established fee guidelines) that these costs are fully recovered through licensing fees.

4 I am seeking approval to introduce new fees and amend some existing fees for the following groups of financial markets participants:

- market services providers seeking licences under the FMC Act
- existing financial markets participants who pay FMA fees for certain actions such as exemptions and advice
- trustees and statutory supervisors.

5 Cabinet approved the release of a discussion document for public consultation in November 2013 [EGI Min (13) 28/6 refers]. Following public consultation and analysis of submissions, the preferred fee model (and fee levels) for market services providers in the discussion document has been retained – being a flat fee plus an hourly rate. I expect the majority of applicants will be charged the flat fee, with the hourly rate allowing cost recovery from resource intensive applications (outliers of the regime).

6 The discussion document also proposed an increase to the hourly rate used to calculate some of FMA's fees. The hourly rate has been in place since 1998 and is now too low for FMA to fully recover its costs. I am seeking Cabinet approval to increase FMA's hourly rate from $166.62 to $178.25 (GST inclusive), representing a seven per cent increase. The increased hourly rate will be applied to the proposed fees for licence applications and a number of existing FMA fees.

7 This paper also seeks agreement to adjust the licensing fee model and fee level for statutory supervisors and trustees to align it with the proposed fee model for market services providers. The existing flat fee has resulted in substantial under-recovery. The proposed changes will increase the flat fee from $4,968.00 to $8,021.25 – an increase of just over 60 per cent – and add an hourly rate for resource intensive applications.

8 Because of the tight timeframe before licensing commences on 1 April 2014, I am also seeking approval of the Financial Markets Conduct (Fees) Regulations 2014 and Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014 to give effect to these proposals.

Background

9 The FMC Act is a significant overhaul of securities law in New Zealand. Securities law governs how financial products are promoted and sold, and the on-going responsibilities of those who offer, deal and trade them.

10 The FMC Act is a key component of the Government's Business Growth Agenda. The FMC Act's main purposes are to promote the confident and informed participation by businesses, investors and consumers in New Zealand's financial markets, and to promote and facilitate the development of fair, efficient, and transparent financial markets. Well-functioning financial markets give high-quality investment opportunities for New Zealanders and channel capital to companies to grow their businesses. The FMC Act aims to assist this flow of capital, which is crucial for economic growth.

11 The FMC Act was passed in September 2013. One of the changes made by the FMC Act is the introduction of a licensing regime, to be administered by FMA, for the following market services providers:

- fund managers
- discretionary investment management service (DIMS) providers
- independent trustees of restricted schemes
- derivatives issuers
- licensed intermediaries (such as peer-to-peer lending services and crowd-funding platforms).

12 Introducing licensing for market services providers brings New Zealand into line with international securities law. The value of a licensing regime is its ability to reduce information asymmetry between providers and investors, contributing to transparency within New Zealand's financial markets. I expect that licensing will contribute to the restoration of investor confidence and enable more efficiency within our financial markets.

13 FMA will begin licensing applicants from 1 April 2014, with the FMC Act's requirements to hold licences phased in from 1 December 2014. In addition, licensed peer-to-peer lending services and crowd-funding platforms will be able to operate from 1 April 2014.

Licence fees for market services providers

14 The proposed licensing fee covers licence application, variation, exemption and renewal costs.

15 In line with established fee setting guidelines,[1] the licence can be described as a private good. Therefore the key policy objective in setting licence fees is to fully recover FMA's costs directly from those who will benefit from holding the licence. The benefit market services providers gain from being licensed will be their ability to operate in the improved regulatory environment created under the FMC Act.

16 In addition to the key policy objective to fully recover FMA's costs, the following criteria were used to assess the fee model options:

- ensure a user-pays system that covers FMA resource costs used to process each application, minimising cross-subsidisation and over-recovery
- certainty and fairness to users – including knowing the cost of the fee at the outset
- ease of implementation.

Consultation

17 Public consultation was undertaken from 26 November 2013 until 21 January 2014. A discussion document was published on the Ministry of Business, Innovation and Employment's (MBIE) website and submissions were sought on a specific list of questions about the fee model options and fee levels.

Application fee model options for market services providers

18 The discussion document outlined two main fee models:

- Hourly rate – applicants would be charged according to the number of hours it takes to process their applications.
- Flat fee plus hourly rate (preferred option) – the flat fee would be based on the estimated number of hours it takes to process a standard application. The flat fee can also be described as the mid-point in an estimated range encompassing applications that require a low to medium level of FMA resource to process. Resource intensive applications (the outliers of the regime) would be charged at the hourly rate on top of the flat fee where necessary.

Submissions received on the application fee model for market services providers

19 A total of eight submissions were received on the proposals in the discussion document, mainly from key industry groups. Five of those submitters supported, in principle, the preferred model. Of the other three submitters, Trustees Executors preferred a flat fee, New Zealand Bankers' Association wanted a lower flat fee to be applied within the preferred model and one made no comment on the preferred model.

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[1] The preferred fee model has been developed in line with the Auditor-General's guidelines *Charging fees for public sector goods and services* and Treasury's *Guidelines for Setting Charges in the Public Sector.*

20 Some submitters had concerns about the estimated number of hours used to calculate the flat fee. Their concerns appeared to result from the lack of detail provided on the estimates process in the discussion document rather than an error in the fee model itself. Two submitters proposed a cap should be applied to the hourly rate portion and three wanted assurance that early indication would be given to applicants that the hourly rate would be charged.

Decisions on the application fee model for market services providers

21 Following public consultation, the proposed application fee model for market services providers is a flat fee plus an hourly rate. The objective of the model is to provide certainty through the use of a standard flat fee for the majority of applicants, whilst ensuring that the outliers of the regime pay a fair fee that reflects the FMA resource used in processing their applications. The rationale for the use of a flat fee plus an hourly rate is that it allows a relatively low fee to be charged to the majority of applicants, it allows cost recovery from resource intensive applications, and it mitigates against under-recovery through the use of the hourly rate.

22 In response to submitters' concerns about the estimates used in developing the fee model and levels, I am satisfied the process used to estimate the flat fee has been as robust as possible, utilising FMA's previous experience in licensing financial markets participants. Information currently available about licensing costs and the licensing requirements FMA will be considering in processing applications has been incorporated in the estimates process for market services providers' fees.

Appropriate use of the hourly rate within the fee model for market services providers

23 Introducing an hourly rate into the model for resource intensive applications does provide some flexibility for FMA in recovering costs. To ensure this flexibility is used appropriately, I propose that FMA be required to give written notice to the applicant if they believe an hourly rate may be need to be charged to process the application. The notice will also include a list of reasons why the hourly rate may be charged. This process will provide transparency around the use of the hourly rate and give applicants some certainty about the overall fee level. In addition, I note the FMA is subject to fair charging principles.

24 The FMA will only be able to charge the hourly rate for hours above a set threshold. The threshold is set above the level of a standard application flat fee and represents the maximum number of hours which the flat fee covers.

Proposed application fee levels for market services providers

25 The following table outlines the proposed fee model and levels. The table also includes some additional estimates about the number of licence applications FMA expects to receive under each category of market services provider and sets out the level of hours used to calculate the standard flat fee and the threshold number of hours at which FMA may charge an hourly rate.

Type of market services provider	Approximate number of applications FMA expects to receive	Estimated average number of hours to process a standard application	FMA hourly rate (GST inclusive)	Flat fee (estimated average number of hours per standard application multiplied by FMA's hourly rate)	Threshold number of hours for when FMA may charge the hourly rate if notice is given to the applicant
Fund Manager	220	20 hours	$178.25	$3,565.00	25
DIMS providers	200 - 400	20 hours	$178.25	$3,565.00	25
Independent Trustee of a Restricted Scheme	80	12 hours	$178.25	$2,139.00	15
Derivatives Issuer	50	60 hours	$178.25	$10,695.00	70
Regulated Intermediary (such as peer-to-peer lending services and crowd-funding platforms)	Crowd funders: 10 Person-to-person lenders: 5	35 hours	$178.25	$6,238.75	40

Multiple licence applications for market services providers

26 The discussion document outlined an option in which applicants may receive a discount if they make applications for multiple types of market services provider licences. This discount has been developed to allow for the fact that some information may be duplicated between applications and need only be assessed once. Seven submissions supported this proposal and, of those, four submitters proposed that the discount should also apply within a specified timeframe.

27 The main issue with the use of a timeframe is the degree to which the information supplied in the initial application remains current. FMA considers that information would remain current for a period of up to six months.

28 I propose that a discount be applied to applications for different types of additional market services provider licences made within six months of the initial licence application, taking into account the amount of duplicated information between applications. Based on information supplied by FMA, the discussion document proposed that the most resource intensive type of market services provider licence application would be charged at 100 per cent of the standard flat fee and for any additional applications a discount of 50 per cent would be given on the standard flat fee. The hourly rate would be applied to applications for multiple licence types in the same manner as with initial licence applications.

Renewal fee for market services providers

29 The preferred renewal fee model in the discussion document was a full fee at renewal based on FMA's intention to undertake a full assessment at renewal. FMA is currently finalising licence terms for market services providers, but the proposed term is five years.

30 There was opposition to a full fee charged at renewal. Submitters stated that as they will be subject to monitoring by FMA during their licence term, there was no need to do a full assessment at renewal. However, FMA's intention is to perform 'risk-based' monitoring over the life of a licence. The renewal event may be the only opportunity to do a complete assessment of an entity or individual. Based on this information, I support the proposal to charge a full fee at renewal. The hourly rate would also be applied to renewals of licence in the same manner as the first application, reflecting the level of FMA resource needed to assess the renewal application.

Variations and exemption fees for market services providers

31 I propose that variations and exemptions of licence for market services providers be charged on an hourly rate basis. The reason for this is to allow for the wide range of applications that can be made under variations and exemptions of licence. This approach has been taken in response to submissions - a standard fee is not appropriate if the application itself is not a standard process.

Increase in some existing FMA fees

General increase in hourly rate

32 FMA's main sources of revenue are from Crown and industry levy funding. A small part of FMA's funding is derived from fees charged for certain services, including:

- fees for licensing or authorising certain market participants
- fees relating to applications for exemptions from legislative requirements, for example, exemptions from Securities Act 1978 requirements.

33 The hourly rate on which some of FMA's fees are based has been in place since 1998, at the time of the Securities Commission (FMA's predecessor). FMA has reviewed the costs included in the hourly rate and has advised that it is too low for full cost recovery. To ensure that fees are set at a level that recover FMA's costs, the discussion document released on market services providers' fees also proposed an increase to FMA's hourly rate from $166.62 to $178.25 (GST inclusive). This represents a seven per cent increase.

34 The main reason behind the increase of the hourly rate is general cost increases since the rate was set in 1998. The other main cost driver is FMA's need to employ more specialist staff with a wider range of technical expertise to consider applications under the various regimes that the hourly rate covers. FMA does not believe this factor will be a significant cost driver for fees costs in the future.

35 The increased hourly rate would be applied to some existing FMA fees charged to financial market participants. The new hourly rate would also be used to calculate the licence fees for market services providers.

36 The hourly rate increase relates to work carried out by an employee of the FMA who is qualified in accountancy, auditing, business, commerce, economics, or law. Or for an employee of the FMA who the FMA is satisfied has a professional level of skills, training, or experience in matters of the kind to which the application relates. The proposals do not affect the existing FMA Board member rate of $230.00 (GST inclusive).

Increase in fees for licensing statutory supervisors and trustees

37 I also propose to increase the existing fee for statutory supervisors and trustees. The current flat fee for statutory supervisors and trustees is set too low to fully recover FMA's costs in licensing this group. All of the initial licence applications incurred resource costs exceeding the amount recovered by the flat fee that was charged. I propose an increase to the flat fee for licensing statutory supervisors and trustees from $4,968.00 to $8,021.25, an increase of just over 60 per cent. The discussion document on market services providers also publically consulted on this increase.

38 The new fee is made up of an increased number of hours allocated to each application and the increase in FMA's hourly rate. When combined, this would be a significant increase for statutory supervisors and trustees. However, the increase is justified by the resources used to licence this group.

39 I also propose to change the fee model for statutory supervisors and trustees to a flat fee and hourly rate and to recover costs for variation of licence on an hourly rate basis only. These changes to the application fee model and variation of licence fee model bring the fees in line with the proposed fees for market services providers.

40 Although the proposed fees are a large increase, it is anticipated that this will not have an immediate impact on the market. Aside from requests for a variation, the existing licences will otherwise not need to be reviewed by FMA until 2017 or 2018.

41 The tables below outline the proposed changes to existing FMA fees.

Action specific fees

Type of Fee	Application fee	Current hourly rate (GST inclusive)	Proposed hourly rate (GST inclusive)
Request to waive levy	$115.00	$166.62	$ 178.25
Advice/Decisions/Exemptions under Securities Markets (Fees) Regulations 2003	$115.00	$166.62	$ 178.25
Application for exemption under Securities (Fees) Regulations 1998	$115.00	$166.62	$ 178.25
Auditors Regulations 2012 (Part 2)	various	$166.62	$ 178.25

Trustees and statutory supervisor licence application fee

Type of financial market participant	Current flat fee based on FMA hourly rate $166.62 (GST inclusive)	Estimated average number of hours to process an application	Proposed FMA hourly rate (GST inclusive)	Flat fee (estimated average number of hours per application multiplied by FMA's hourly rate) GST inclusive	Threshold number of hours for when FMA may charge the hourly rate if notice is given to the applicant
Trustees and Statutory Supervisors	$4,968.00 (approximately 30 hours per application)	45 hours	$178.25	$8,021.25	52 hours

Review period for fees

42 A review period of three years is proposed for the fee model and fee level for the new licences issued to market services providers under the FMC Act. This period will allow enough time for the licensing regime to be established and costs to be assessed.

43 A review period of five years is proposed for the fee model and fee level for statutory supervisors and trustees. Because the policy proposals are based on current figures I am satisfied that the fee model and levels do not need to be reviewed as soon as for market services providers.

[redacted]

Regulations to give effect to the proposals

45 Because of the tight timeframe before licensing commences on 1 April 2014 I am also seeking approval for the submission of the regulations to the Executive Council. These have been drafted in advance of this paper:

- Financial Markets Conduct (Fees) Regulations 2014
- Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014.

Fiscal Implications

46 There are no fiscal implications from this paper as the fees proposed are cost-recovery only.

Human Rights

47 There are no human rights implications arising out of the proposals.

Timing

48 The regulations will come into force on 1 April 2014. FMA will begin licensing applicants from this date, with the FMC Act's requirements to hold licences phased in from 1 December 2014.

49 A waiver of the 28-day rule is sought to ensure the purpose of the regulations is not defeated. The purpose of the regulations is to allow FMA to recover its costs from licensing applicants, which will not be possible if the regulations are not in place by 1 April 2014.

Compliance

50 The regulations:

- Comply with the principles of the Treaty of Waitangi;
- Are consistent with the rights and freedoms contained in the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993;
- Are consistent with the principles and guidelines set out in the Privacy Act 1993;
- Comply with relevant international standards and obligations; and
- Comply with the Legislation Advisory Committee Guidelines on Process and Content of Legislation.

Regulations Review Committee

51 I do not consider that there will be grounds for the Regulations Review Committee to draw the Financial Markets Conduct (Fees) Regulations 2014 and Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014 to the attention of the House.

Certification by Parliamentary Counsel

52 The Financial Markets Conduct (Fees) Regulations 2014 and Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014 have been certified by Parliamentary Counsel as being in order for submission to Cabinet.

Regulatory Impact Analysis

53 A Regulatory Impact Statement (RIS) was prepared in accordance with the necessary requirements and is attached.

54 The General Manager, Strategic Policy Branch and the Ministry of Business, Innovation and Employment Regulatory Impact Analysis Review Panel have reviewed the attached RIS prepared by MBIE. They consider that the information and analysis summarised in the RIS meets the criteria necessary for ministers to fairly compare the available policy options and take informed decisions on the proposals in this paper.

Publicity

55 The Financial Markets Conduct (Fees) Regulations 2014 and Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014 will be published in the Gazette on the Thursday following Executive Council approval. I also intend to inform relevant market participants about Cabinet's decisions in respect of this paper by publishing the paper on MBIE's website. [redacted]

Consultation

56 The Treasury, Reserve Bank and FMA have been consulted on the proposals in this paper. The Department of Prime Minister and Cabinet has been informed.

Recommendations

I recommend that the Committee:

1. **Note** that the Financial Markets Conduct Act 2013 (FMC Act) introduces a licensing regime for market services providers, which will come into effect from 1 April 2014.

2. **Agree** to introduce licensing fees for market services providers under the FMC Act as outlined below:

Type of market services provider	Flat fee (GST inclusive)	Renewal fee (GST inclusive)	Hourly rate in excess of any fee (GST inclusive)	Threshold number of hours at which the hourly rate may be charged
Fund Manager	$3,565.00	$3,565.00	$178.25	25 hours
Discretionary Investment Management Services (DIMS) Providers	$3,565.00	$3,565.00	$178.25	25 hours
Independent Trustee of a Restricted Scheme	$2,139.00	$2,139.00	$178.25	15 hours
Derivatives Issuer	$10,695.00	$10,695.00	$178.25	70 hours
Regulated Intermediary (such as person-to-person lending services and crowd-funding platforms)	$6,238.75	$6,238.75	$178.25	40 hours

3. **Agree** that FMA be required to give written notice to an applicant for a market services provider or trustee and statutory supervisor licence if it believes an hourly rate in addition to the flat fee may be charged to process the application. The notice must also include a list of reasons why the hourly rate may be charged.

4. **Agree** that variations of market services providers' licence will be charged on an hourly rate basis, including an application fee of $115.00 (GST inclusive).

5. **Agree** that exemptions of licence for markets services providers will be charged on an hourly rate basis, including an application fee of $115.00 (GST inclusive).

6. **Agree** that FMA be required to waive or refund a percentage of the market services provider flat fee in order to apply a multiple licence discount. The multiple licence discount will take account of the information in a market services provider licence application that has already been assessed as part of another market services provider licence application within six months of the initial application.

7. **Agree** to an increase in the Financial Markets Authority (FMA) hourly rate for FMA officers from $166.62 to $178.25 (GST inclusive).

8. **Agree** to an increase in the licence application fee for statutory supervisors and trustees and to change the fee model to a flat fee and hourly rate as outlined in the table below:

Type of financial markets participant	Flat fee (GST inclusive)	Hourly rate in excess of flat fee (GST inclusive)	Threshold number of hours at which the hourly rate may be charged
Trustees and Statutory Supervisors	$8,021.25	$178.25	52 hours

9. **Agree** that variations of licence for trustees and statutory supervisors will be charged on an hourly rate basis, including an application fee of $115.00 (GST inclusive).

10. **Agree** to an increase in the hourly rate for the following action specific fees. The new fees are as follows:

Type of FMA fee	Hourly rate (GST inclusive)
Request to waive levy	$ 178.25
Advice/Decisions/Exemptions under the Securities Markets (Fees) Regulations 2003	$ 178.25
Application for exemption under Securities (Fees) Regulations 1998	$ 178.25
Auditors Regulations 2012 (Part 2)	$ 178.25

11. **Note** that the decisions set out above fulfil the policy intent for FMA to recover costs for providing certain services to financial market participants.

12. **Note** that the Financial Markets Conduct (Fees) Regulations 2014 and Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014 give effect to the decisions referred to above.

13. **Note** that the Financial Markets Conduct (Fees) Regulations 2014 and Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014 come into force on 1 April 2014.

14. **Authorise** the submission to the Executive Council of the Financial Markets Conduct (Fees) Regulations 2014 and Financial Markets Conduct (Changes to Financial Markets Authority Fees) Regulations 2014.

Hon Craig Foss
Minister of Commerce
11 / 3 / 14