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Ms Shellie Davis
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The Treasury
Langton Cres
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By email: Shellie.Davis@TREASURY.GOV.AU

Dear Shellie

Enhanced regulatory sandbox proposal – ASIC submission

This submission is in response to the consultation on the proposed enhanced regulatory sandbox framework issued on 24 October 2017 (the 'proposed enhanced sandbox').

ASIC's commitment to innovation

ASIC is committed to facilitating innovation in financial services and credit. We set up our Innovation Hub initiative in 2015 to assist innovative new businesses, improve our engagement with the Fintech sector and cut red tape.

ASIC sees the promise of a growing fintech sector to increase choice in services and reduce costs to the benefit of consumers. This is a key reason why we look to facilitate this part of the financial sector. To date, through the Innovation Hub, ASIC has provided informal assistance to over 200 fintech startups; granted 38 licences to new fintech business and provided 11 variations to licences of new fintech businesses. Further, licence applicants that have received informal assistance from ASIC staff through the Innovation Hub have obtained licensing decisions in about 40% less than time than if they applied without first obtaining informal assistance.

ASIC's regulatory sandbox issued in December 2016 is a class waiver from licensing requirements (the 'ASIC sandbox licensing exemption'). In making that waiver ASIC was mindful to both balance the benefits of concept validation testing for eligible innovative businesses against the risks of consumer harm from poor conduct by unlicensed businesses and also not to make far reaching policy decisions in the nature of law reform. For that reason our waiver, while a world first, has a number of limitations. To date, four fintech startups have made use of the exemption and in addition over 12 fintech startups have contacted us about using the exemption. The 2017 Fintech Australia census reports that 9% of Australian fintechs plan to use ASIC's sandbox in the next 12 months. Separately, ASIC has issued individual waivers from certain legislative requirements for over 10 fintech startups including most retail marketplace lenders.

ASIC has also entered into over 12 cooperation and referral agreements with international regulators to promote information sharing and more efficient access to foreign markets for Australian innovative businesses. To date, ASIC has referred five businesses to foreign regulators.

ASIC's overarching aim is to maintain sound and appropriate regulatory frameworks that harvest the benefits of innovation while fostering consumer trust and confidence in financial services. The recent Fintech Australia census noted that 'Australia's sophisticated and trusted regulation of financial services' provides a potential competitive advantage for Australian businesses.

Scope of the proposed enhanced regulatory sandbox

ASIC notes a key goal of the proposed enhanced regulatory sandbox is to allow a broad scope of activities without the need to meet existing licensing requirements under legislation that ASIC administers.

Under the proposals, businesses would be able to test a wider range of services than under the existing ASIC sandbox licensing exemption whilst being required to adhere to certain consumer protections and disclosure requirements.

The proposed enhanced regulatory sandbox will extend the scope of the class waiver beyond that under the ASIC sandbox licensing exemption in a number of key areas:

- the testing period is up to 24 months;
- businesses (including very large financial institutions) are able to access the Sandbox multiple times, where they can test a broader range of 'kinds' of products and services they are not already licensed to provide, or have not previously tested;
- the type of service is expanded to include issuing non-cash payment facilities (up to $10,000 per client wallet), providing a crowd-funding service and providing credit (up to $25,000 for contracts up to 4 years);
- the type of services offered to retail clients is expanded to include advice and dealing on: international securities (up to $10,000 investment), life risk insurance products (up to $300,000 cover) and, significantly, superannuation products (up to $40,000 investment) ; and
- for wholesale clients, services can be tested in relation to all products except derivatives and margin lending facilities.

Importantly, the proposal maintains the total client exposure ($5 million) and the consumer protection conditions (such as external dispute resolution membership; the professional indemnity insurance requirement; and conduct and disclosure obligations) that exist under the ASIC sandbox licensing exemption.

The breadth of proposed enhanced regulatory sandbox can be illustrated in a couple of examples:

- an unlicensed business could provide exempted advice/dealing services for up to 500 clients (each investing up $10,000) over 10 years for investments (up to an overall cap of $5M) using the exemption on multiple occasions (in relation to simple managed investment schemes; then domestic securities; then international securities; then Government bonds and then deposits); and

- An existing licensed financial securities dealer firm provides exempted advice/dealing for 10 clients for superannuation investment advice (up to $40,000 per client) for up to 2 years; then for 15 clients for general insurance personal assets cover (at $75,000 per client) for up to 2 years; then for less than 10 clients for life insurance cover (at $300,000 per client) for up to 2 years and then issues credit for less than 15 clients (for $25,000 loans) for up to 2 years. Potentially the same retail client in this case could be provided with all of these products/services with total exposure of $440,000.

Potential scale of the use of the proposed enhanced regulatory sandbox

As a guide to the potential use of the proposed enhanced regulatory sandbox:

- ASIC approved 711 AFS Licence applications (including variations) in the 2016-2017 financial year relating to the financial services and products within the scope of the proposal (this does not count credit related licence authorisations); and

- As stated above, ASIC has provided informal assistance to over 200 fintech businesses over the last two years.

Potentially, a material portion of these businesses could decide to rely on the proposed enhanced regulatory sandbox. This could be in the hundreds per year.

These will be unlicensed entities and as such ASIC will not monitor or supervise them. This is consistent with our approach to the ASIC regulatory sandbox. While ASIC does monitor and supervise existing licensed businesses this is supported by a broad regulatory toolkit and framework applicable to licensed financial services. We do not have this capacity or capability for unlicensed entities.

There is a draft power under the proposed enhanced regulatory sandbox that ASIC could notify a business that it is excluded from the exemption. Given the policy approach that the entities in the sandbox be unlicensed and the approach to supervision set out above we envisage this power will not be commonly used. There are also questions about the power given the broad scope of the proposed enhanced regulatory sandbox; the potential large numbers relying on it and the fact it might confuse consumers by suggesting that ASIC supervises these businesses. For these reasons it may be worth considering removal of the power.

Some further matters that might also be considered in finalising the proposed enhanced regulatory sandbox include the merits of:

- limiting the overall number of retail clients to 100 even if a business uses the exemption on multiple occasions. This would be in addition to the overall limit of $5M contemplated under the proposal;

- not allowing services in relation to superannuation given the longer term significance of such a product to a client. Any form of limiting a service to a cap of superannuation investment may be artificial as it might not adequately contemplate the existing superannuation position of a retail client. An alternative is to limit services in relation to superannuation to general advice;

- narrowing the 'kinds' of products for which exempted services could be provided on multiple occasions (for example, to kinds of products such as for investments; risk management products; credit and non-cash payments) so that businesses could not make multiple use of the exemption for similar kinds of products. The proposal currently has a much broader set of product kinds that could enable a wider multiple use of the proposed sandbox potentially as an avoidance mechanism; and

- limiting investment in international securities to those securities on an ASIC approved foreign market (not just any international market).

Please contact me or Mark Adams (02) 9911 2050 if you would like to discuss this letter.

Yours sincerely

John Price
Commissioner

Cc. Diane Brown, Division Head, Financial System Division, The Treasury