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BY EMAIL

Mr Alan Worsley
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ashurst

Dear Alan

Foreign financial service providers – Submissions in response to Consultation Paper 301

We refer to the Consultation Paper 301 *Foreign financial services providers* dated 1 June 2018 (**CP 301**) which calls for submissions to provide feedback and comments on the proposals set out in the paper. We welcome the opportunity to make submissions in relation to CP 301.

We are a global law firm with offices in most of the world's leading financial centres (including London, Hong Kong, Tokyo, Singapore, Frankfurt, Paris, New York, Sydney and Melbourne among others). We are commonly asked to advise foreign financial services providers on the way in which they provide financial services to Australian clients in compliance with Australian financial services laws. In particular, our work includes the following:

- We advise clients on licensing requirements and the availability of exemptions;
- We advise on the structuring of global servicing and booking arrangements, so as to comply with Australian financial services laws;
- We advise on complex cross border issues which arise when servicing clients from offshore, such as capital requirements, client money requirements and conduct of business rules; and
- We have advised a number of global financial institutions which have given Enforceable Undertakings in relation to non-compliance with conditions of the current exemptions.

Through this work, we are well placed to comment on the proposals. We understand and appreciate the practical impact that exemptions have on offshore providers servicing the Australian market.

1. WHY THE EXEMPTIONS ARE REQUIRED

The need for appropriately balanced relief arises from section 911D of the *Corporations Act 2001* (**Corporations Act**). This section is an extended jurisdiction provision which draws activity conducted outside of Australia into the Australian regulatory framework in circumstances where that activity is intended to induce Australian clients to use financial services, or likely to have that effect.

Parliament has itself recognised the need for a number of exemptions for offshore financial services providers. A number of exemptions have been included in the Corporations Act and the *Corporations Regulations 2001* (**Corporations Regulations**) to exempt offshore financial services providers where they are "not in the jurisdiction".

Parliament also considered it appropriate to vest ASIC with the power to grant relief by way of ASIC instrument. As noted in CP 301, ASIC proposes to revoke two key relief instruments which have been in place for many years, in particular:

(a) The sufficient equivalence relief (a number of ASIC Class Orders, as extended by ASIC instrument 2016/396) (**Sufficient Equivalence Relief**); and

(b) The limited connection relief (ASIC Class Order 03/824, as extended by ASIC instrument 2017/182) (**Limited Connection Relief**).

We consider that both the the Sufficient Equivalence Relief and Limited Connection Relief continue to have a sound policy basis, in that they mitigate the impact of section 911D in circumstances where the services are limited to wholesale clients.

If the Sufficient Equivalence Relief and the Limited Connection Relief were revoked, the result would be that many activities undertaken pursuant to these exemptions would not fall within other exemptions. If they were revoked, consideration should be given to whether other, more tailored exemptions might be introduced to accommodate activities where there is a sound policy basis for such an exemption. Failure to do so would lead to inconsistencies within Australian regulatory policy which would seem difficult to justify.

For example, why should an offshore provider of services in respect of foreign exchange contracts have the benefit of an exemption (under section 911A(2E)), when the same provider would require a licence for providing services in relation to securities or interests in managed investment schemes to the same clients? The underlying policy of the Financial Services Reforms in 2002 was to deliver a consistent regulatory regime for the provision of financial services. The Sufficient Equivalence Relief and the Limited Connection Relief are both reasonably generic in their application to a range of financial products and services. Revoking them will lead to a more piecemeal approach to regulation.

2. SUFFICIENT EQUIVALENCE RELIEF

2.1 Benefits of the Sufficient Equivalence Relief

The Sufficient Equivalence Relief has a solid policy foundation, which is to recognise that financial services providers regulated in jurisdictions of sufficient equivalence to Australia should have the benefit of an exemption from the requirement to have an Australian financial services licence provided they only provide financial services to wholesale clients.

The current relief operates very efficiently and effectively. Reliance can be achieved quickly, through the filing of compliant documents with ASIC. We are concerned that a licensing process will be cumbersome and inefficient in its application. ASIC's existing licence process is already under strain, with some simple licence or variation applications taking many months to obtain. If a new "foreign AFS licence" regime is to be introduced, it is important that ASIC is resourced to be able to implement it efficiently.

2.2 **Do the reasons advanced in CP 301 support the revocation of the Sufficient Equivalence Relief?**

ASIC has set out in CP 301 a number of reasons which it considers support the proposal that the Sufficient Equivalence Relief should be revoked in favour of introducing a "foreign AFS licence". These include:

- the need for wholesale clients to be afforded many of the regulatory protections which are afforded to clients of licensees;
- the need for ASIC to achieve greater clarity in relation to the activities of offshore providers; and
- the need for ASIC to have available to it the full suite of licensing and administrative powers to enforce the law, given that there may be practical challenges that limit overseas regulators' ability to take action to monitor and supervise the conduct of foreign providers in Australia.

We acknowledge that these represent good reasons to *revisit* the current Sufficient Equivalence Relief. However, we do not consider that these reasons support the *revocation* of the relief. We briefly address each of the three reasons below.

(a) **Wholesale clients should be afforded the protections which a licence would provide**

The need for greater regulatory protection for wholesale clients is not supported by the general scheme of Chapter 7 of the Corporations Act. There are a raft of regulatory protections which do not apply to wholesale clients. There are also a number of licensing exemptions which are available where services are limited to wholesale clients (or sub-categories of wholesale clients, such as professional investors).

One such exemption is that referred to above - section 911A(2E) – why should professional investors who receive services from offshore providers in respect of securities and interests in managed investment schemes be afforded these protections (through the requirement for a licence), in circumstances where those same professional investors receive services in respect of derivatives and foreign exchange contracts from the provider (under the exemption in section 911A(2E))? This distinction is hard to justify in policy terms, given that derivatives and foreign exchange contracts are the riskier classes of financial products.

Furthermore, where the Sufficient Equivalence Relief is based on an assessment of sufficient equivalence with the providers offshore jurisdiction, how does it follow that additional regulatory protections are required? Should it not follow that the assessment would support recognition of the regulatory protections as being adequate? Is it not sufficient that wholesale clients are made aware of this, as is the case under the conditions of the Sufficient Equivalence Relief?

(b) **The need for ASIC to achieve greater clarity in relation to the activities of offshore providers**

We consider this is a very good reason to consider whether the conditions of the Sufficient Equivalence Relief are appropriate, but it does not support the revocation of the relief.

The issue here is not so much a flaw in the policy which underpins the relief, but rather the process by which the relief has been implemented. If the Sufficient Equivalence Relief were to continue, any concern ASIC may have in relation to the level of information it has regarding the offshore providers' activities with Australian clients could be addressed through additional conditions to compel the provision of the information ASIC considers necessary. Such information could be provided at the time the relief is sought, and on an ongoing (say, annual) basis.

(c) **The need for ASIC to have available to it the full suite of licensing and administrative powers to enforce the law**

Again, we consider this is a very good reason to consider whether the conditions of the Sufficient Equivalence Relief are appropriate, but it does not support the revocation of the relief.

If ASIC considers that its powers (such as enforcement and information gathering powers) should be enhanced, we consider that this could be achieved through additional conditions on an exemption.

2.3 **Parliament itself considered exemptions of this nature appropriate**

The Sufficient Equivalence Relief is provided through instruments issued under section 911A(2)(l) of the Corporations Act (as is apparent on the face of the relevant Class Orders and ASIC instruments).

There is also another exemption under section 911A(2)(h) which provides an exemption 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 limited to wholesale clients.*

In other words, Parliament *specifically contemplated* that ASIC would be able to create an exemption in favour of financial services providers who are regulated offshore. This signals that Parliament itself considered that such an exemption can be appropriate. Further, if one considers two of the reasons advanced by ASIC and discussed in paragraph 2.2 for revoking the exemptions:

(a) Parliament did not seem concerned that wholesale clients would not have the benefit of the regulatory protections which a licence would provide; and

(b) Parliament did not seem concerned that ASIC would not have available to it the full suite of licensing and administrative powers to enforce the law.

Indeed, on (a), the same can be said for all of the other licence exemptions which relate to services provided by wholesale clients. And on (b) the same can be said of all other licence exemptions.

Whilst ASIC has not exercised its power to grant the Sufficient Equivalence Relief under section 911A(2)(h), its revocation would, in the absence of further action, leave a gap in the overall exemption framework which was specifically contemplated by Parliament.

2.4 An alternative approach for consideration – extend the relief

We consider that the current conditions of the Sufficient Equivalence Relief are cumbersome and lack clarity in a number of respects. We have no doubt the current conditions can be improved, and should be improved, to enhance their effectiveness and to achieve the policy objectives as stated by ASIC in CP 301.

We set out below, some items which could be considered in the context of proposing new conditions for the Sufficient Equivalence Relief, should they be extended.

Issue/concern to address	Proposal to address in an extended relief instrument
ASIC may be concerned that the definition of "wholesale client" allows an offshore provider to service a broader range of clients than is appropriate.	The exemption could be limited to sub-categories of wholesale clients (such as to "professional investors" and other discrete categories).
ASIC may be concerned that examples of non-compliance with the current relief suggests that the relief does not carry a sufficient emphasis on compliance with Australian regulatory requirements.	Additional compliance monitoring conditions could be introduced (such as an annual compliance attestation (as is required for Australian Credit Licence holders).
ASIC suggests that due to restricted monitoring and supervision arrangements, ASIC is not able to obtain sufficient information in relation to the activities of offshore providers with Australian clients.	A condition could be introduced to require periodic reporting on the nature and extent of services provided in reliance on the exemption (as has been historically required of exempt market operators).
ASIC does not have sufficient enforcement powers	Conditions could be introduced to allow ASIC to enforce specified rights, or impose other conditions by notice to the provider to address any particular concerns ASIC may have (in the same way as ASIC has done for AFS licence holders).
ASIC may be concerned that there are provisions of the Corporations Act or ASIC Act which ought to apply to providers who provide services under the relief (but currently do not apply as they are expressed to apply only to AFS licensees).	Consideration could be given to amending the Corporations Act or ASIC Act or inserting provisions through the Corporations Regulations to apply such provisions to the exempt provider as if they were a licensee or through including terms in the condition of the exemption itself. For example, it could be a condition that the provider comply with [specified provisions] *as if it were a licensee*.

We consider that this approach would strike the appropriate balance between maintaining the vital benefits of the current Sufficient Equivalence Relief to promote access by Australian wholesale clients to services, investments and markets offshore, while also addressing ASIC's key concerns in relation to market integrity and investor protection.

2.5 An alternative approach for consideration – Regulations

As an alternative to extending the Sufficient Equivalence Relief, or providing alternative relief via ASIC instrument, consideration could also be given to promoting amendments to the Corporations Regulations to introduce exemptions to achieve the same effect. In other words, this would be consistent with the introduction of reg 7.6.02AG of the Corporations Regulations.

3. LIMITED CONNECTION RELIEF

3.1 The need for the Limited Connection Relief

As noted briefly above, we consider that the underlying policy considerations which supported the Limited Connection Relief when it was first introduced in 2003 remain.

While ASIC has suggested that the Limited Connection Relief is no longer required by virtue of a number of other exemptions inserted by reg 7.6.02AG of the Corporations Regulations (limiting the operation of section 911D), there are still a number of foreign financial services providers who do not have a place of business in Australia and are not able to rely on these exemptions. ASIC has not indicated how the concerns which were alleviated through the introduction of the Limited Connection Relief will be addressed if the relief is revoked.

There are many providers, including many clients of Ashurst, who rely on this exemption and we consider there is a sound basis for them to be able to continue to do so. The exemption is commonly relied upon to support the following activities (by way of example):

(a) The distribution of research in respect of offshore markets to Australian wholesale clients;

(b) The provision of access to Australian corporations and institutions to global capital markets for the raising of debt and equity capital; and

(c) The provision of access to Australian corporations, institutions and large superannuation funds to offshore investment opportunities, including associated custody services.

In each of the above cases, the Limited Connection Relief provides Australian investors, corporates and institutions with opportunities to access investments and services which they may not otherwise be able to access (including in jurisdictions which do not qualify for sufficient equivalence).

As ASIC has already heard from respondents to its previous Consultation Paper 268 *Licensing relief for foreign financial services providers with a limited connection to Australia,* in the absence of the Limited Connection Relief, there would be no viable alternatives for many entities who rely on this exemption to continue their offshore activities without an AFS licence.

We note in particular the unique position of foreign investment managers, who are not able to rely on relief to which ASIC has referred in its consultation paper as relieving the need for ASIC to maintain the limited connection relief.

Specifically, Regulation 7.6.02AG(2C) makes available an exemption from the requirement to hold an AFS licence to a financial service provider who is not in the jurisdiction, who provides financial services to the holder of an Australian financial services licence or someone who is exempt from the requirement to hold the licence, but only where that person is not acting as a trustee or acting as a responsible entity of a registered managing investment scheme or otherwise acting on someone else's behalf.

Foreign investment managers in almost all cases provide services to persons who are acting as a trustee (eg. trustees of public office superannuation funds) or persons who are acting as trustees of wholesale schemes or responsible entities of retail registered schemes. That means this exemption is not available to foreign investment managers, many of whom have had to rely on the Limited Connection Relief in the absence of a suitable exemption.

In circumstances where a foreign provider has no place of business in Australia, requiring them to obtain an AFS licence would be a significant regulatory burden. As a result, it may well be that a number of these providers who otherwise have no connection with Australia, would struggle to justify obtaining an AFS licence to continue to service the Australian market. This would result in Australian corporations and institutions ceasing to have access to their services.

If the Limited Connection Relief were to be revoked, we would urge ASIC to seriously consider specific exemptions to accommodate the above activities, rather than force these providers to obtain a full AFS licence (as many of them would not be able to avail themselves of the proposed 'foreign AFS licence').

3.2 **Alternative to revoking the Limited Connection Relief**

Consistent with our comments in respect of the Sufficient Equivalence Relief, if the Limited Connection Relief were to be extended, additional conditions could be added to achieve ASIC's regulatory objectives. For example, additional conditions could:

(a) enhance ASIC's supervisory and enforcement powers in respect of providers which rely on the relief;

(b) limit the provision of services to professional investors or other sub-categories of wholesale client; and/or

(c) require that providers which rely on the relief register with ASIC and provide ASIC with relevant information on a regular basis to facilitate greater transparency.

In our view this approach would appropriately address ASIC's key concerns while maintaining the benefits of the Limited Connection Relief.

4. TRANSITION CONSIDERATIONS IF THE PROPOSALS ARE IMPLEMENTED

We understand that ASIC seeks to ensure a smooth transition should the proposals in CP 301 be implemented. This is important not just for the foreign financial services providers, but also for the Australian clients who use their services. There is a large number of financial services providers who rely on the Limited Connection Relief and the Sufficient Equivalence Relief. The proposed changes will be disruptive and would need to be implemented carefully and sensibly.

We set out below a number of items which we consider are critical to take into account to ensure a smooth transition:

(a) Timing of revocation/transition

CP301 suggests that the Limited Connection Relief would cease in September 2019, with the Sufficient Equivalence Relief ceasing 12 months later. There is currently a lack of clarity regarding the transition period available to providers relying on the Limited Connection Relief. In our view both exemptions should be extended to September 2020 (or a later date if, following the consultation that is considered appropriate) to ensure that they both cease at the same time.

Global financial institutions often operate through a number of entities in different jurisdictions and they structure their regulatory engagement with Australian clients having regard to all available exemptions, and their interaction. Removing one exemption will cause many of these global institutions to restructure their arrangements. Removing a second exemption may then require a subsequent restructuring of their arrangements.

If a 'foreign AFS licence' is introduced, we would suggest that the application process is available as soon as possible in 2019, well ahead of the current relief lapsing in September 2020.

(b) Arrangements to support orderly transition

If a 'foreign AFS licence' is introduced, the two exemptions should have conditions which allow ASIC to grant providers consent to operate under the relevant relief beyond October 2020, if there is a legitimate reason for this. For example, these reasons may include ASIC's own capacity to process a plethora of new licence applications (both foreign and domestic). This approach would be preferable to a hard end date which creates uncertainty if the date is at risk of not being met.

(c) Licence application process

ASIC should ensure that there is a clear and effective process for 'foreign AFS licence' applications. It would be helpful if the process could be streamlined so that ASIC only requires the production of information and documentation which it feels is genuinely required to meet its regulatory objectives. As noted above, reliance on the Sufficient Equivalence Relief is currently very efficient and quick to put in place. A drawn out or cumbersome licence application process would not deliver meaningful regulatory benefit, particularly given the applicant is already regulated in a jurisdiction assessed as being sufficiently equivalent.

For example, we note that in Appendix 1, ASIC proposes that a foreign AFS licence applicant would be required to have in place adequate risk management arrangements. The question arises as to what information ASIC will require of an applicant to demonstrate compliance with this requirement? If ASIC requires

applicants to provide extensive documentation regarding their offshore risk management framework and procedures, we query whether the ASIC licensing team will have the capacity to review comprehensive offshore risk management arrangements (much of which will not relate to Australian activity at all) and, what benefit ASIC would derive from a review of those arrangements.

(d) Sufficient equivalence assessments for other jurisdictions

It would be helpful if ASIC could provide an indication of its capacity and preparedness to consider other jurisdictions for sufficient equivalence. This is particularly important if the Limited Connection Relief is revoked, as there will be entities in many jurisdictions which will lose the benefit of that exemption, and not presently qualify for a foreign AFS licence.

We would be happy to discuss any of these submissions with you through the consultation process.

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