MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

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List of documents that have been proactively released		
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Information redacted **NO**

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In Confidence

Office of the Minister of Commerce and Consumer Affairs

Chair, Cabinet Business Committee

Policy decisions on the Financial Markets Authority's levy

Proposal

1. This paper seeks approval to make changes to the Financial Markets Authority's (FMA) levy as a result of the recently agreed increase to its baseline funding through Budget 2020.

Relation to government priorities

2. The proposals in this paper and associated baseline funding increase have been adjusted to take into account the impact, and the Government's response to, COVID-19. The main change is that the FMA's funding increase will now be phased in over three years instead of two so as to reduce the impact a levy increase would have on the financial services sector at a time when revenues and profitability may be reduced.

3. The Government's economic plan identifies key shifts and policy actions. One of these is that 'deeper pools of capital are available'. Having a well-resourced financial markets regulator is a key part of the infrastructure needed to support New Zealanders to have confidence to invest in financial markets and to facilitate greater access to capital for innovative New Zealand firms. The levy changes also take into account supporting early-stage capital availability by creating a levy class tailored to 'growth market operators'.

Executive Summary

4. The FMA is New Zealand's main conduct regulator of financial markets. In recent years the FMA has faced an expansion of its remit and broader cost pressures. Accordingly, on 6 April 2020, Cabinet agreed to increase the FMA's appropriation by $24.805 million per annum by 2022/23, taking the FMA's operational funding to $60.805 million from 2022/23 and outyears.

5. Cabinet also agreed that the majority of this increase - $23.501 million per annum by 2022/23 - will be funded via an increase in the existing levy on financial service providers. However, some financial service providers may be experiencing a decline in revenue due to the impact COVID-19 is having on the economy. To lessen the impact that an increase in levy may have on financial service providers, Cabinet agreed to phase the increase in the FMA's appropriation over a three-year period, being:

   a. $12.500 million in 2020/21 (effective July 1 2020);

   b. $17.500 million in 2021/22;

c. $24.805 million in 2022/23 and outyears.

6. Changes are now proposed to the FMA levy model to give effect to the above increase in appropriation and the amount to be recovered via the levy, specifically to:

   a. increase levy amounts to recover the increase in FMA funding;

   b. revise figures for each levy class's portion of the total amount of FMA levy recovered;

   c. update forecasts of the estimated populations within each levy class; and

   d. add or adjust classes to reflect market developments.

7. This paper seeks Cabinet's agreement to adjust the levy model and amounts paid by financial markets participants. A full list of the changes is attached as Annex One. The figures outlined in the levy model are for the first year of phasing only. Further decisions will need to be made in regards to the levy model to give effect to the remaining two years of phasing and the commencement of the new financial advice regime in early 2021.

8. The adjustments to the levy model will require amendments to, or replacement of, the Financial Markets Authority (Levies) Regulations 2012. These amendment regulations will be made over the next few months, and the new levy amounts will be charged from 1 July 2020, however this timing may be slightly delayed given the impact the Government's priorities for urgent COVID-19 related law changes is having on the capacity of the Parliamentary Counsel Office.

Background

Recent review of the FMA's funding and levy

9. The FMA was established in 2011 and is New Zealand's principal conduct regulator of financial markets. The FMA's overarching statutory purpose is to promote and facilitate the development of fair, efficient and transparent financial markets. Well-regulated financial markets are vitally important to New Zealand's economy and the financial wellbeing of every New Zealander.

10. In 2019, the Ministry of Business, Innovation and Employment (MBIE) and the FMA initiated a review of the FMA's funding requirements and the FMA levy. The reason for the review was that the FMA's operational funding has come under significant pressure over recent years. The FMA is forecasting an operating deficit for 2019/20 of approximately $4 million, which will need to be met by its cash reserves.

11. The driving force behind the FMA's cost pressures is that its regulatory remit and responsibilities have expanded but it has not received any additional funding to account for this. For example:

    a. The FMA has been devoting resources to the upcoming changes to the financial advice regime. Implementation of these changes has already begun, with transitional licensing of advisers underway.

b. The FMA has also been responding to declining levels of trust in financial services, spurred by the findings of Australian Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (ARC). These high-profile failings and criticisms of the Australian regulators have received significant coverage in New Zealand and magnified concern about the regulation of financial services here and the FMA's ability to respond to misconduct. Following this, the FMA dedicated resources to areas such as the recent conduct and culture reviews of banks and life insurers.

12. On 6 April Cabinet agreed to increase the FMA's appropriation by $24.805 million by 2022/23, taking the FMA's operational funding to $60.805 million per annum in 2022/23 and outyears. This will enable the FMA to meet its existing organisational pressures, be better prepared to unexpected market developments or events, be able to undertake effective and swift implementation of the new financial advice regime, and enable more cross-agency collaboration to improve coordination and efficiencies in the financial system.

13. This funding increase is to be phased in over three years as follows:

    a. $12.500 million in 2020/21 (effective July 1 2020);

    b. $17.500 million in 2021/22;

    c. $24.805 million in 2022/23 and outyears.

14. Cabinet also agreed that the majority of the FMA's operational funding would continue to be recovered via a levy on financial services industry. The Crown currently contributes approximately 25 percent of the FMA's funding, with the remaining 75 percent recovered via a levy on financial markets participants. Cabinet has confirmed through a Budget 2020 bid to increase the Crown's contribution to the FMA's operational funding appropriation by $1.304 million per annum on an ongoing basis and $3.000 million per annum on an ongoing basis to its litigation fund.

15. With the above increase in the FMA's funding and the Crown's contribution, the new split of the FMA's operational funding in 2020/21 will be approximately 21 percent Crown and 79 percent levy (decreasing to 17 percent Crown and 83 percent levy with the fully phased-in funding increase).

Recent changes have been made to FMA's funding proposals as a result of COVID-19

16. The proposals in this Cabinet paper and the corresponding funding increase have recently been adjusted to take into account the potential economic impact of COVID-19 on the financial services sector. I note that a large number of financial services firms are essential services and so are continuing to operate their business in some form.

17. The main change is that the increase in funding will now be phased in over three years instead of two. This is to lessen the impact an increase in levy would have upon financial services businesses at a time when revenues may be lower because of the economic impact of COVID-19. This adjustment complements the many other lines of support the Government is currently providing businesses to cushion the impact of COVID-19.

18. The revised proposals also take into account the fact that the Government has recently decided to slow the pace of regulatory change for the financial services sector in response to COVID-19. This will relieve the FMA of some immediate resourcing pressure, but work on upcoming regulatory reforms and implementation will still need to continue, albeit at a slower pace.

19. I would like to emphasise that a well-resourced financial conduct regulator is particularly important in times of market stress and potential economic downturn. The FMA has advised that it will be allocating its resources in response to current and upcoming market conditions. This is needed because the risk of misconduct increases in times of market stress. More supervision and engagement is needed with the financial services sector at this time, and the FMA needs to be resourced to do this.

Risk of increasing the levy

20. When consultation was undertaken on the funding proposals the vast majority of submitters stated that the Crown should maintain at least its current percentage of the FMA's funding (25 per cent). As a result, there may be a strong reaction from financial services providers about any levy increase at all, especially given the Crown will be reducing the portion of the FMA's funding it pays.

21. There is also a risk that an increase in the levy on the financial services sector will put additional stress on financial services businesses in the context of COVID-19. However, in addition to phasing the FMA's appropriation increase over three years, most financial services are essential services and are continuing to operate in some form. I believe these factors, when combined with the Government's other COVID-19 business support measures should sufficiently minimise the potential impact of higher levies on financial service providers.

Changes to the FMA levy

22. In order to implement the agreed changes to the FMA's funding, adjustments to the FMA levy model are needed. The full levy model and proposed changes necessary to implement the first phase of the increase in funding are outlined in Appendix One.

23. Further levy increases and changes to the model will be necessary next year to account for the remaining years of phased increases, the introduction of the new financial advice regime, and for changes that could not be made this year due to constraints on adjusting the register system that supports the collection of the levy (the Financial Services Provider Register).

The FMA levy model

24. The FMA oversees a wide range of financial markets participants. Financial markets participants make a contribution to the FMA levy for each financial service they provide. For example, a registered bank that is also an insurer and has a managed investment scheme (such as KiwiSaver) will pay a levy for all three activities.

25. Where appropriate, levy amounts are also tiered within a levy class to recognise variations in participant's size and nature. This means that the amount of levy charged is typically proportionate to the size of the business. For example, a large KiwiSaver scheme pays more than a smaller boutique KiwiSaver manager and a large bank pays more than a smaller bank or credit union.

26. When setting and reviewing the FMA levy model the following objectives have been taken into account:

    a. The cost of the levy for market participants is consistent with the benefits they receive from well-regulated financial markets;

    b. The levy does not discourage entry into the market for, and the supply of, financial products or services; and

    c. The levy is practical in respect of its implementation and collection, and also avoids large over or under-collections.

27. The forecast populations for each levy class and tier (where applicable) have been updated with more accurate figures based on actual collections. This will ensure that the levy does not over or under-collect by large amounts.

28. Adjustments have been made to certain levy classes to better align the levy with the objectives above. In particular, the following significant adjustments are proposed:

    a. Registered banks and non-bank deposit takers, licensed insurers, discretionary investment management services, and registered or incorporated persons will experience notable increases in the portion of the levy they pay because of the level of benefit these organisations receive from participating in well-regulated financial markets.

    b. New financial service providers, licensed supervisors, authorised financial advisers and financial service providers not included in any of classes 2 - 6 will see notable decreases in the portion of the levy they pay so that the levy does not discourage entry into or the ongoing operation of financial service businesses or impact access to high-quality financial advice.

    c. The levy for licensed market operators will be split to provide for a lower levy for operators of a growth market to reflect their smaller size and provide a platform for small and medium businesses to list and access capital.

    d. The levy for listed issuers will be split so that small issuers pay a lower levy reflecting the smaller size of their businesses and to encourage more small and medium businesses to list on markets and access to capital.

    e. A new levy class will be added for administrators of financial benchmarks that will have to be licensed by the FMA and registered on the financial service providers register.

29. The full updated FMA levy model is attached as Appendix One.

Consultation on the changes to the FMA levy

30. Consultation on the changes to the FMA levy was undertaken with levy payers through a discussion document between January and February 2020. MBIE and the FMA also held targeted stakeholder workshops with key financial services sector associations and online webinars to ensure stakeholders had the opportunity to provide feedback. Feedback was sought on the following:

    a. three different baseline funding options for the FMA;

    b. how any increase in funding is sourced between the Crown and industry; and

    c. administrative changes to the FMA levy model.

Submissions on the changes to the FMA levy model

31. 49 written submissions were received on the discussion document. Feedback on the levy model mainly related to why individual participants or sectors were paying more in levies than others. There was support from submitters for the adjustments to levy classes to improve access to capital raising.

Consultation

32. The FMA, the Reserve Bank of New Zealand, and the Treasury were consulted on this paper. The Department of the Prime Minister and Cabinet (Policy Advisory Group) were also advised of, and provided, this paper.

Financial Implications

33. The financial implications for the FMA funding and levy changes were considered by Cabinet as part of the Budget Significant Initiatives Paper on 6 April 2020.

Legislative Implications

34. The changes to the FMA levy will require the Financial Markets Authority (Levies) Regulations 2012 to be amended or replaced. Given the decision to delay commencement of the new financial advice regime to early 2021, the amendment regulations will also need to repeal the levy changes made for the purpose of the financial advice regime (the Financial Markets Authority (Levies) Amendment Regulations 2019) which are due to come into force on 29 June 2020.

35. These amendment regulations will be made over the next few months, and the new levy amounts will be charged from 1 July 2020, however this timing may be slightly delayed given the impact on the Parliamentary Counsel Office's capacity of the Government's priorities for urgent COVID-19 related law changes.

Regulatory Impact Analysis

36. The Regulatory Impact Analysis requirements apply to the proposals in this paper. A Regulatory Impact Assessment (RIA) has been prepared and is attached.

37. A Quality Assurance Panel with representatives from the Regulatory Quality Team at the Treasury, the Ministry for Primary Industries, and MBIE has reviewed the 'Financial Markets Authority funding and levy' RIA produced by MBIE in March 2020. The Panel considers that the RIA meets the Cabinet requirements to support its decision.

38. Given the complexity of the proposal, this RIA is well structured and provides transparency to the proposed changes. However, while stakeholders supporting the enhanced case have a small majority, the additional benefits of the enhanced case over and above the base case are not always obvious. Further specific information about the activities undertaken by the FMA and the associated extra level of services to be delivered would aid clarity. Additional time for consultation would have allowed better understanding of the impact on regulated parties (there was also little to no feedback on some levy classes).

Population Implications

39. No significant impacts for specific population groups have been identified during the course of the analysis of the FMA's levy model.

Communications

40. This paper will be proactively released on MBIE's website as soon as possible after the Budget has been delivered so that levy payers can plan and prepare for the new levies. This will be combined with communications to the industry emphasising the changes made following COVID-19.

Proactive Release

41. This paper will be published on MBIE's website after delivery of the Budget, subject to withholdings as appropriate and consistent with the Official Information Act 1982.

Recommendations

The Minister of Commerce and Consumer Affairs recommends that the Committee:

1. **note** that the Ministry of Business, Innovation and Employment and the Financial Markets Authority (FMA) publicly consulted on the FMA's funding and the FMA levy between January and February 2020 [CBC-MIN-0001];

2. **note** that on 6 April 2020 Cabinet agreed to increase the FMA's Multi-Category Appropriation by $24.805 million by 2022/23 and outyears to a total of $60.805 million per annum and that by 2022/23 and outyears, $23.501 million of this will be recovered from financial markets participants through the FMA levy;

3. **note** that on 6 April 2020 Cabinet also agreed to phase the increase to the FMA's appropriation by $12.500 million in 2020/21, $17.500 million in 2021/22 and $24.805 million in 2022/23 and outyears;

4. **agree** to make changes to the FMA levy model structure as set out in Appendix One of this paper to reflect:

a. the amount of the FMA’s funding increase that is to be recovered via the levy;

b. revised forecasts of the estimated populations within each levy class;

c. new or adjusted classes to reflect market developments; and

d. revised figures for each levy class’s portion of the total amount of FMA levy recovered;

5. **note** that changes will be proposed to the levy model next year to increase the amount to recover via the levy for the second and third years of the phased FMA funding increase, to take into account the impact of upcoming regulatory reforms, and for changes not possible this year due to constraints in adjusting the levy register system;

6. **authorise** the Minister of Commerce and Consumer Affairs to issue drafting instructions to the Parliamentary Counsel Office to draft regulations to give effect to decisions in this paper;

7. **authorise** the Minister of Commerce and Consumer Affairs to make minor or technical changes to the FMA levy model consistent with the policy decisions in this paper.

Authorised for lodgement

Hon Kris Faafoi

Minister of Commerce and Consumer Affairs

Appendix One: The FMA levy model structure

Levy class	Type of levy (fixed levy or tiers)	Current approx. % of total revenue	New approx. % of total revenue	Current levy (excl. GST)	New 2020/21 levy (excl. GST)
Class 1 New financial service provider (FSP) registrations	Fixed levy	4.09%	2.73%	$460	$480
Class 2 Registered FSPs that are registered banks or licensed NBDTs	Total assets exceed $50 billion	11.11%	13.46%	$535,000	$900,000
	Total assets exceed $10 billion but not $50 billion			$130,000	$240,000
	Total assets exceed $2 billion but not $10 billion			$38,000	$72,600
	Total assets exceed $1 billion but not $2 billion			$22,000	$37,000
	Total assets exceed $500 million but not $1 billion			$10,500	$13,300
	Total assets exceed $40 million but not $500 million			$7,700	$8,400
	Total assets do not exceed $40 million			$2,400	$2,500
Class 3 Registered FSPs that are licensed insurers	Annual gross premium revenue exceeds $500 million	7.36%	9.05%	$150,000	$300,000
	Annual gross premium revenue exceeds $100 million but not $500 million			$38,000	$70,000
	Annual gross premium revenue exceeds $50 million but not $100 million			$24,000	$41,000
	Annual gross premium revenue exceeds $10 million but not $50 million			$11,000	$16,000
	Annual gross premium revenue does not exceed $10 million			$2,200	$4,200
Class 4 Registered FSPs that are supervisors licensed in respect of the supervision of debt securities and managed investment products in registered	Total supervised interests exceed $5 billion	2.24%	2.19%	$138,000	$200,000
	Total supervised interests exceed $1 billion but not $5 billion			$76,000	$90,000

schemes	Total supervised interests exceed $100 million but not $1 billion			$26,000	$35,000
	Total supervised interests do not exceed $100 million			$6,400	$9,200
Class 5 Registered FSPs that are managers	Total managed assets exceed $10 billion	20.99%	20.35%	$380,000	$460,000
	Total managed assets exceed $5 billion but not $10 billion			$270,000	$320,000
	Total managed assets exceed $2 billion but not $5 billion			$120,000	$160,000
	Total managed assets exceed $1 billion but not $2 billion			$80,000	$100,000
	Total managed assets exceed $500 million but not $1 billion			$45,000	$58,000
	Total managed assets exceed $100 million but not $500 million			$25,000	$26,500
	Total managed assets exceed $20 million but not $100 million			$6,400	$7,200
	Total managed assets do not exceed $20 million			$1,400	$1,700
Class 6 Registered FSPs where One of the following amounts (being whichever applicable amount is the greatest):	(a) the person is an entity authorised to undertake trading activities on licensed markets	0.25%	0.12%	$4,500	$6,600
	(b) the person is a contributory mortgage broker	0.11%	0.16%	$1,800	$2,700
	(c) the person is registered for the financial service described in section 5(1)(k) of the FSP Act, other than— (i) persons included in class 6A, 6B, 6C, or 6D; and (ii) DIMS wholesale providers	3.34%	0.80%	$5,300	$8,000
	(d) the person holds a market services licence that covers the service of acting	0.57%	0.91%	$9,600	$13,500

	as a derivatives issuer				
	(e) authorised financial advisers	2.77%	2.26%	$330	$380
Class 6A Registered FSPs that are DIMS retail providers	Funds under management exceed $2 billion			$36,000	$57,000
	Funds under management exceed $500 million but not $2 billion			$14,000	$24,000
	Funds under management exceed $100 million but not $500 million	1.28%	1.42%	$4,800	$8,100
	Funds under management exceed $50 million but not $100 million			$2,400	$3,900
	Funds under management do not exceed $50 million			$950	$1,600
Class 6B Registered FSPs that are providers of a regulated client money or property service other than persons in class 6(a) or 6C	Fixed levy	0.71%	0.77%	$1,800	$2,800
Class 6C Registered FSPs that are custodians and persons providing custodial services	Fixed levy	5.29%	1.06%	$6,300	$9,100
Class 6D Registered FSPs that provide a crowd funding service or a peer-to-peer lending service	Fixed levy	0.12%	0.16%	$2,600	$2,900
Class 7 Registered FSPs that are not included in any of classes 2 to 6D	Fixed levy	13.44%	11.83 %	$460	$540
Class 8 Listed issuers	Fixed levy plus any debt collection costs incurred in relation to the persons	1.99%	1.23%	$2,600	$3,600
Class 9 Persons that lodge a PDS	All except for PDS of a managed fund			$2,600	$3,500
	Per fund, multi-fund investment option, or life-cycle stage covered by a PDS, in the case of a managed fund	2.79%	0.59%	$530	$700
Class 10	Fixed levy plus any debt collection costs	0.57%	0.13%	$29,000	$48,000

Licensed market operators	incurred in relation to the persons				
Class 11 FMC reporting entity	Fixed levy	0.13%	0.11%	$48	$60
Class 12 Accredited bodies	Fixed levy per specified licence	1.49%	1.50%	$2,600	$4,000
Class 13 Overseas auditors holding a specified licence	Fixed levy plus any debt collection costs incurred in relation to the persons	0.21%	0.31%	$2,600	$4,400
Class 14 Persons that apply for registration or incorporation	The Building Societies Act 1965	1.76%	2.56%	$9	$17.39
	The Companies Act 1993			$9	$17.39
	The Friendly Societies And Credit Unions Act 1982			$9	$17.39
	The Limited Partnerships Act 2008			$9	$17.39
Class 15 Persons that are registered or incorporated, and make an annual return	The Building Societies Act 1965	17.37%	25.54 %	$9	$17.39
	The Companies Act 1993			$9	$17.39
	The Friendly Societies And Credit Unions Act 1982			$9	$17.39
	The Limited Partnerships Act 2008			$9	$17.39
New levy Growth market operators	Market operators licensed with conditions imposing a limit on the size of issuers that may remain listed on its market	n/a – new levy	0.02%	n/a – new levy	$7,000
New levy Benchmark administrators	Fixed levy		0.05%		$17,500
New levy Small issuers	With a market capitalisation less than $60 million		0.12%		$900