



COVERSHEET

Minister	Hon Dr David Clark	Portfolio	Commerce and Consumer Affairs
Title of Cabinet paper	Regulations to support the new financial advice regime and other recent financial markets legislation changes	Date to be published	5 February 2021

List of documents that have been proactively released

Date	Title	Author
December 2020	Cabinet paper: Regulations to support the new financial advice regime and other recent financial markets legislation changes	Office of the Minister of Commerce and Consumer Affairs
9 December 2020	DEV-20-MIN-0176: New Financial Advice Regime and Other Financial Markets Legislation Changes: Regulations	Cabinet Office
19 November 2020	Cost Recovery Impact Statement: Licensing fees for benchmark administrators	MBIE

Information redacted

YES

Any information redacted in this document is redacted in accordance with MBIE's policy on Proactive Release and is labelled with the reason for redaction. This may include information that would be redacted if this information was requested under Official Information Act 1982. Where this is the case, the reasons for withholding information are listed below. Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Some information has been withheld due to confidentiality of advice and some information has been withheld due to legal professional privilege.

Cost Recovery Impact Statement

Licensing fees for benchmark administrators

Agency Disclosure Statement

This Cost Recovery Impact Statement has been prepared by the Ministry of Business, Innovation and Employment. It provides an analysis of options to recover the costs of licensing benchmark administrators under the Financial Markets Conduct Act 2013.

- The analysis in this CRIS has been informed by targeted consultation only. MBIE consulted the benchmark administrator that is likely to seek to be licensed. However those licensing costs may be passed on to those that use the benchmark generated by the licensee through user fees. We did not seek the feedback of those institutions and individuals that may face higher user fees through licensing costs being passed through to them to access the benchmark. Therefore the analysis does not incorporate the views of all those that could be affected by the costs of licensing.
- The estimate of time spent on processing a benchmark administrator licensing application is based on information provided by the FMA. This estimate is based on previous experience the FMA has in processing licensing applications from other financial markets participants, however the actual time spent on processing an application may differ from the estimate provided.

Sharon Corbett

Financial Markets Policy

Ministry of Business, Innovation and Employment

19 November 2020

Quality Assurance Reviewing Agency:

Ministry of Business, Innovation and Employment (MBIE)

Quality Assurance Assessment:

MBIE's Regulatory Impact Analysis Review Panel has reviewed the attached Cost Recovery Impact Statement prepared by MBIE. The Panel considers that the information and analysis summarised in the Statement meets the criteria necessary for Ministers to make informed decisions on the proposals in this paper.

Executive summary

- This analysis proposes a licensing fee for benchmark administrators. This is a new licensing category under the Financial Markets Conduct Act 2013. Licences will be issued by the Financial Markets Authority.
- The purpose of the licensing regime is to address potential conflicts of interest and the manipulation of financial benchmarks that have been seen in cases overseas. In particular the licensing regime seeks regulatory equivalence with European Union counterparts so that New Zealand's financial benchmarks will continue to be accepted in financial instruments overseas.
- The proposed fee will be charged on an hourly basis for the time FMA spends assessing licence applications.
- To give proposed applicants transparency and provide some certainty about the likely fee charged, the FMA will provide regular updates and communicate with applicants throughout the licensing process.

Status quo

- On 30 August 2019 the Financial Markets (Derivatives Margin and Benchmarking) Reform Amendment Act 2019 (FMRAA) received Royal assent. FMRAA introduces a licensing regime for administrators of financial benchmarks under the Financial Markets Conduct Act 2013.
- Financial benchmarks are figures or indexes, such as interest rates, that are referenced in financial products or contracts to set the price or determine the value of those financial products. They are critically important to New Zealand's and international financial markets and, by implication, to broader economic activities. For example, financial benchmarks are a key part of setting the price under derivatives, which are used by banks, financial institutions and public sector asset managers for risk management and investment purposes.
- In 2016, the European Union (EU) responded to concerns about conflicts of interest and the manipulation of benchmarks by publishing new regulations relating to financial benchmarks. The EU regulations have significant implications for New Zealand. Government intervention was required in order to create a licensing regime so that New Zealand's administrator of New Zealand benchmarks, the New Zealand Financial Markets Association (NZFMA), can meet the standards set in the EU regulations. Unless equivalence with the EU is achieved, New Zealand benchmarks will not be able to be used in critical financial contracts with EU parties.
- The benchmark administrator licence will be issued by the Financial Markets Authority (the FMA) under the Financial Markets Conduct Act 2013 (FMC Act). This is a new type of licence under the FMC Act and therefore a new fee. The ability to recover the FMA's costs associated with the assessment and issue of the licence is provided for under the Financial Markets Authority Act 2011 and the FMC Act. The FMA has an hourly rate of \$178.25 (incl. GST) that is used to determine fee charges. This rate is set in regulations.

Cost Recovery Objectives

- The following objectives will guide the assessment of the cost recovery proposal for the benchmark administrator licence fee:

- **The fee recovers the cost of the FMA's assessment of the licence application.**

This objective has been given a high weighting in the analysis below relative to the other objectives, which have been given a much lower weighting. The reason for giving this objective a higher weighting is due to the nature of the licence application process. It is expected that the licence type and application will be a non-standard process for which there is more uncertainty in terms of time spent on the application than there would be for other licence types issued by the FMA. The ability for the FMA to recover its costs in issuing the licence takes priority over the other objectives so that FMA can accurately recover the costs of issuing the licence (and avoid subsidising the cost of issuing the licence from other revenue or funding streams).

- **Prospective licensees have clarity about the amount of fee they are likely to pay.**
- **The FMA is incentivised to deliver services associated with licensing in an efficient and effective manner.**
- **The fee is efficient to administer.**

Why a user charge? And what type is most appropriate?

- A market services licence issued under the Financial Markets Conduct Act 2013 is a private good. It allows the licensee to operate in an environment that is regulated by the FMA.
- New Zealand's benchmark administrator, NZFMA (currently unlicensed, but operating in New Zealand already) operates as a not-for-profit incorporated society. Its primary members are large financial institutions and participants from New Zealand and overseas (such as major banks). NZFMA is the administrator and calculation agent for the BKBM Benchmark. Members and subscribers pay a fee to the NZFMA to gain access to the BKBM benchmark so that it can be utilised in financial instruments here and overseas.
- Whilst the NZFMA is run on a not-for-profit basis, it is still appropriate for the cost of the licensing fee to be recovered from the NZFMA as those members and subscribers that access the benchmark utilise it in financial instruments. Licensing costs are likely to be passed on to those utilising the benchmark and we consider this to be appropriate given the benefit they derive from access to that benchmark and its continued use in financial contracts throughout the EU.

Assessment of proposed user charge against objectives

	Status Quo	Flat fee charged	Fee charged on an hourly basis
<p>The fee recovers the cost of the FMA's assessment of the licence application.</p> <p><i>This objective has been given the highest priority in the analysis and the preferred option under this objective has guided MBIE's recommendation for the fee model.</i></p>	0	<p>A flat fee would be calculated based on an estimate of time spent on assessing the application, however, because it is expected that the assessment process will be non-standard, the estimate may not be as accurate as it could be to allow the FMA to recover its costs. There is a risk of over or under recovery with this option. This option is better than the status quo because it will allow the FMA to recover some of its costs of licensing (as long as the estimated fee is accurate).</p> <p style="text-align: center;">+</p>	<p>Because the fee would be charged on an hourly basis the FMA could accurately recover the cost of assessing the licence. This option is much better than the status quo because it allows the FMA to accurately recover the costs of licensing.</p> <p style="text-align: center;">++</p>
Prospective licensees have clarity about the amount of fee they are likely to pay.	0	<p>A flat fee provides certainty to prospective licensees about the costs of licensing.</p> <p style="text-align: center;">++</p>	<p>The applicant would not know the total cost of licensing until the application had been assessed and so they would not have certainty about the costs of licensing. However, the FMA intends to communicate directly with the applicant throughout the licensing process about the fee associated with assessing the application so that the applicant has some clarity about the likely fee it will pay.</p> <p style="text-align: center;">+</p>
The FMA is incentivised to deliver services associated with licensing in an efficient and effective manner.	0	<p>A flat fee provides more incentive for the FMA to deliver services in a way that ensures the application is assessed within the estimated time so as to minimise under-recovery.</p> <p style="text-align: center;">++</p>	<p>Because the FMA can recover costs for every hour spent on assessing the application there may be fewer incentives to search for efficiencies throughout the process in order to reduce hours spent on the application.</p> <p style="text-align: center;">+</p>
The fee is efficient to administer.	0	<p>A flat fee would require less time to administer in terms of recording of hours and billing in comparison to a fee charged on an hourly basis.</p> <p style="text-align: center;">++</p>	<p>There would be some costs associated with administering the licence (such as accurate recording of hours and regular communication about the likely cost of the licensing fee).</p> <p style="text-align: center;">+</p>
Overall assessment	0	+++++++	+++++

Key:

- ++ much better than doing nothing/the status quo
- + better than doing nothing/the status quo
- 0 about the same as doing nothing/the status quo
- worse than doing nothing/the status quo
- much worse than doing nothing/the status quo

The level of the proposed fee and its cost components (cost recovery model)

- As noted above, the FMA's hourly rate is set in regulations. The hourly rate incorporates both indirect and direct costs associated with the operation of the FMA. The proposals addressed in this analysis do not propose a change to the hourly rate.
- The FMA has supplied an estimate for the fee it expects to charge in order to assess applications for benchmark administrator licences. It estimates this fee will be approximately 0.5 FTE for six months. However some of this time will be spent establishing the licensing process (with policy and legal support) in order to determine exactly what must be assessed. Licence application fees do not typically recover these implementation costs and will not be charged to the applicant.

Impact analysis

- The licensing process will be an isolated cost. Once a benchmark administrator is licensed it does not need to apply for a renewal of licence. Analysis undertaken at the time a licensing regime was proposed estimated the impact of the licensing fee to be low. This previous analysis can be found here:

<https://www.mbie.govt.nz/assets/8df512db8a/impact-summary-introduction-of-a-new-regulatory-regime-for-financial-benchmarks.pdf>

Consultation

- Targeted consultation was undertaken with the NZFMA as the likely potential applicant for a licence. MBIE is not aware of any other New Zealand based benchmark administrators that may seek to be licensed in the near future.
- It is possible that some international benchmark administrators may seek to obtain a licence here in New Zealand, but as they will be licensed in their home jurisdictions the incentive to do so is not strong.
- NZFMA's feedback was that if the licensing fee was calculated on an hourly basis, that they would like transparency about the likely fee charged for an assessment of their application.

Conclusions and recommendations

- MBIE recommends that the fee for licensing benchmark administrators should be calculated on an hourly rate basis, at the current FMA hourly rate. This method of charging is the most accurate form of cost recovery for the FMA and this objective has been given a higher priority in the assessment of the two proposed fee models for the reasons outlined earlier in this analysis. The weighting given to this objective has meant that the hourly rate model of charging is MBIE's preferred option. Had less priority been given to the first objective then the flat fee model of charging would be the preferred option.
- MBIE considers that a fee charged on an hourly rate basis is appropriate in this instance because the licensing process will not be a standardised process for which a flat fee could reliably be estimated.

- The hourly rate fee model is currently used by the FMA where the nature of the assessment is difficult to predict and so a flat fee would risk potential over and under recovery. The FMA has a number of fees that it charges on an hourly basis for this reason, notably the licence fee for market operators (such as NZX) and assessments for exemptions and variations of licence. MBIE considers the assessment of a licence application to act as a benchmark administrator is similar in nature to those types of applications already charged on an hourly basis.

Implementation plan

- The main implementation risk with the proposed fee is the uncertainty that the applicant will have about the final fee they will be required to pay. To manage this risk FMA plans to provide regular updates to prospective benchmark administrator licensees as it processes the licence application so as to give licensees more certainty through the licence application process.

Monitoring and evaluation

- As a Crown entity, the FMA is required to report to the Minister of Commerce and Consumer Affairs and to the general public about its performance. The FMA currently collects and reports annually on a range of non-financial performance measures relating to the completion of licence applications and the time taken to process those applications. The FMA is also required to separately record and report on the revenue that it generates from licensing fees in its Annual Report.

Review

- Due to the low number of expected applicants under this licence category, we do not expect to undertake a review of the fee model. A fee charged on an hourly basis is appropriate where the licence application process is not standardised.