

MAS to Issue Up to Five Digital Banking Licences – Practical Considerations for Potential Applicants

Overview

On 28 June 2019, the Monetary Authority of Singapore ("MAS") announced that it will issue up to five new digital bank licences, comprising:

- **two digital full bank licences**, which would allow licensees to provide a wide range of financial services and take deposits from retail customers; and
- **three digital wholesale bank licences**, which would allow licensees to serve SMEs and other non-retail segments.

The intention behind the issuance of the digital bank licences is to add diversity and help strengthen Singapore's banking system in the digital economy.

Based on MAS' press release, we have set out below the details on the eligibility criteria and safeguards applicable to digital full banks and digital wholesale banks. MAS will provide more details on the eligibility and admission criteria in August 2019, and expects to invite applications at that time.

DIGITAL FULL BANK FRAMEWORK

Eligibility Criteria

Application for a digital full bank license is open to both Singapore and foreign companies.

Companies headquartered in Singapore and controlled by Singaporeans

Application for a digital full bank licence is open to companies headquartered in Singapore and

controlled by Singaporeans. MAS will presume there is control if the Singaporean and/or his related parties hold the largest shareholding and have management control over the joint venture.

Foreign companies

Foreign companies are eligible if:

- they form a joint venture with a local company; and
- the joint venture meets the headquarter and control requirement.

Track record / Proposed business model

In addition, to be eligible to apply, the applicant or its parent group must:

- have a track record in operating an existing business, in their respective technology or e-commerce fields. MAS has indicated that applicants with no existing business will not be considered;
- provide clear value propositions on how it can serve existing unmet or underserved needs; and
- demonstrate that it has a sustainable digital banking business model. MAS has indicated that it will not allow any bank, digital or not, to engage in value-destructive competition to gain market share. MAS will assess the reasonableness of the applicant's business plans and financial projections such as cost-to-income ratio and net interest margin.

Safeguards

A digital full bank will be required to:

- incorporate in Singapore;
- participate in the deposit insurance scheme provided by the Singapore Deposit Insurance Corporation (this will protect deposits of up to S\$75,000 per depositor in the event of the bank's failure);
- comply with the same suite of prudential rules as existing banks, including ongoing risk-based capital and liquidity requirements; and
- submit a viable exit plan to facilitate an orderly wind-up if necessary.

Phasing in of Permissible Activities

MAS will phase in the permissible activities of the digital full bank *via* a two-stage process to minimise risks to retail depositors.

First Stage: Restricted Digital Full Bank ("Restricted DFB")

- The digital bank will commence as a Restricted DFB and will be subject to the following restrictions for one to two years from the point of entry:
 - **Deposit caps** - Aggregate deposits will be capped at S\$50 million and individual's deposits will be capped at S\$75,000. Wholesale deposits will not be subject to the aggregate deposit cap once the Restricted DFB's paid-up capital reaches S\$100 million (in line with wholesale bank's minimum paid-up capital). In addition, the bank can only accept deposits from a small group of persons such as business partners, staff and related parties.

- **Business restrictions** – The bank can only offer simple credit and investment products, and will not be allowed to offer complex investment products such as structured notes, derivatives (other than for risk management purposes) and proprietary trading. Further, the bank should not establish banking operations in more than two overseas markets.
- **Lower minimum paid-up capital** – The initial paid-up capital required at the entry point will be S\$15 million.
- **Capital and liquidity rules** – The bank will be subject to the same capital adequacy requirements as local banks (i.e., 6.5% CET1 Capital Adequacy Ratio, 10% Total CAR, 2.5% capital conservation buffer, up to 2.5% countercyclical capital buffer). It will also be subject to a minimum liquid asset requirement of 16%.

- Business and deposit restrictions will be relaxed once the digital bank has demonstrated ability to manage its risks well, and minimum paid-up capital will be raised in proportion to its risk profile and how the bank is delivering on its value propositions.

Second Stage: Digital Full Bank ("DFB")

- The Restricted DFB will graduate to become a full functioning digital bank (i.e., DFB) with all deposit caps lifted, once it has met all relevant milestones and has been assessed to pose no significant supervisory concerns.
- In assessing the bank's readiness to graduate to become a DFB, MAS will consider factors such as its business and financial performance, quality of loans, products and customer service, ability to serve needs of identified segments, risk management and

compliance track record, and if the business is generally well-managed and profitable.

- A DFB will need to meet the minimum paid-up capital requirement of S\$1.5 billion and it will be subject to the same capital adequacy (i.e., 6.5% CET1 Capital Adequacy Ratio, 10% Total CAR, 2.5% capital conservation buffer, and up to 2.5% countercyclical capital buffer) and liquidity requirements (i.e., 100% net stable funding ratio and 100% liquidity coverage ratio) as local banks.
- MAS will not prescribe a time period within which the Restricted DFB must graduate to DFB. Nonetheless, the Restricted DFB must have a viable plan to meet the requirements to become a DFB.

Other business restrictions

Other business restrictions which will apply to both Restricted DFBs and DFBs include:

- One physical place of business only.
- No minimum account balance and fall below fees.
- Compliance with unsecured credit rules issued by the MAS.
- Allowed to offer cashback services through electronic funds transfer at point of sale ("EFTPOS") terminals at retail merchants, but no access to automated teller machines ("ATMs") or cash deposit machines ("CDMs") network.

DIGITAL WHOLESALE BANK FRAMEWORK

Eligibility Criteria

Application for a digital wholesale bank license is open to both Singapore and foreign companies.

The applicant will need to meet similar eligibility criteria as a digital full bank applicant, i.e., the requirement for it to be headquartered in Singapore and controlled by Singaporeans, as well as the track record and business model requirements – please see "*Eligibility Criteria*" in the *Digital Full Bank Framework* section above.

Safeguards

A digital wholesale bank will be required to:

- incorporate in Singapore;
- provide a viable exit plan during the application stage; and
- comply with the following key requirements:
 - have a minimum paid-up capital of S\$100 million;
 - prohibited from taking Singapore dollar deposits from individuals, except for fixed deposits of at least S\$250,000. It will however be free to open and maintain business deposit accounts for SMEs and corporates;
 - be subject to the same capital and liquidity rules applicable to existing wholesale banks; and
 - be restricted to one physical place of business and to only conduct activities within its initial proposed business scope.

OTHER RELEVANT CONSIDERATIONS

Practical Considerations for Applicants

While full details of the licensing requirements and process have yet to be announced, interested parties should take note of the following requirements for the purposes of their

initial planning and structuring of the prospective applicant entity:

- where foreign shareholders are involved, the shareholdings / holding structure would need to take into account the requirement for the applicant entity to be controlled by Singaporeans;
- where newly-incorporated entities are intended to be applicants, there should be a parent group which can satisfy MAS' track record requirement;
- the proposed business model should include clear value propositions for unmet or underserved banking needs and also be sustainable;
- keeping in mind the initial base capital requirement, and ongoing capital adequacy and liquidity requirements which would apply after the licence is awarded; and
- formulating a viable exit plan – this will be required at the application stage.

While successful applicants would enjoy the benefit of general exemptions from licensing requirements under key legislations such as the PSA, SFA and FAA, applicants seeking to collaborate with other businesses should also bear in mind the statutory prohibitions on carrying on certain non-financial businesses and the limits to the shareholding or control in an entity.

Flexibility

Relatedly and in connection with MAS' aim to embrace a digital economy, the Payment Services Act 2019 ("**PSA**") is expected to commence in January 2020.

As licensed banks, including digital banks, are subject to more stringent prudential regulation and supervision than non-bank payment service

providers, such licensed banks will be exempt from the requirement to hold a licence for providing payment services regulated under the PSA.

Licensed banks are also generally exempt from licensing requirements under the Securities and Futures Act ("**SFA**") for conducting regulated activities such as dealing in capital markets products, and under the Financial Adviser's Act ("**FAA**") for providing financial advisory services.

However, licensed banks would still have to comply with business conduct requirements in relation to the provision of licensable payment services and capital markets services.

Regulatory Constraints as a Licensed Bank

Anti-Commingling Policy

Prospective applicants intending to establish strategic collaborations or joint ventures with non-financial businesses should be aware of the anti-commingling policy embodied in the Banking Act, which prohibits licensed banks in Singapore from:

- carrying on, or entering into any partnership, joint venture or any other arrangement to conduct non-financial businesses;
- acquiring or holding equity investment in a single company engaging in non-financial business, which exceeds in the aggregate 2% of the capital funds of the bank; and
- acquiring or holding a major stake in any company engaging in non-financial business.

Non-financial businesses which a licensed bank is prohibited from conducting, or investing in, include manufacturing and selling of consumer goods, property development, and property management of properties which are not held by it or its major stake entities.

Nonetheless, under Regulation 23G of the Banking Regulations, licensed banks are allowed to carry on, or enter into any partnership or joint venture to carry on, non-financial businesses which are "related or complementary to their core financial business" as long as such activities are not prohibited ("**Permissible Non-Financial Businesses**"). This is subject to the fulfilment of various conditions including, putting in place adequate risk management policies, ensuring that staff possess the relevant expertise, and limiting the aggregate size of all such businesses to 15% of its capital funds.

Where a licensed bank intends to conduct or invest in any business which does not fall within the scope of Permissible Non-Financial Businesses, then it must obtain the specific approval of the MAS before doing so.

Proposed changes to the scope of Permissible Non-Financial Businesses

In September 2017, MAS has proposed to adjust the anti-commingling framework. In particular, MAS has proposed to allow licensed banks to engage in the following businesses under

Regulation 23G of the Banking Regulations, including:

- the operation of online location or electronic platform that matches buyers and sellers of consumer goods or services;
- the sale of consumer goods or services *via* online location or electronic platforms; and
- entering into tie-ups or referral arrangements to sell or provide the products or services of a third party.

While these proposed changes would expand the current scope of permissible services and tie-ups which a bank may engage in under Regulation 23G of the Banking Regulations, they have not been legislatively enacted.

Prospective applicants intending to carry on any non-financial business, either directly or indirectly, may wish to consider the implications of the anti-commingling framework and monitor developments in this area when structuring their business model.

If you would like information and/or assistance on the above or any other area of law, you may wish to contact the partner at WongPartnership that you normally work with or any of the following partners:



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