KPMG

HKMA publishes revised Guideline on Authorization of Virtual Banks

May 2018

On 30 May 2018, the HKMA published a revised *Guideline on Authorization of Virtual Banks* ("the Guideline") following the completion of a public consultation which was launched in February 2018. The key message is that the introduction of virtual banks (VBs) is going ahead in Hong Kong. The HKMA received more than 50 indications of interest, and hopes to start granting licences towards the end of this year or in the first quarter of 2019.

The revised Guideline does not have any major changes compared with the consultation draft. Although no new barriers have been put in the way of VBs being established, none of the requirements in the draft have been relaxed or removed (some of which are additional to the requirements for conventional banks, e.g. the exit plan).

The final version of the Guideline:

- Confirms that financial inclusion must be a key element of an applicant's business case (and that no minimum balance requirements or low-balance fees may be imposed), but clarifies that a VB is not restricted to the retail segment; it can also provide services to SME/corporate clients

- Confirms that VBs will be required to produce an exit plan

- Confirms that the minimum paid-up capital requirement of HKD 300 million cannot/will not be modified in the case of VBs

- Confirms that the existing minimum criteria for authorisation cannot/will not be modified for VBs (i.e. the HKMA will not follow the approach of some other regulators of introducing a phased approach whereby a VB would not have to satisfy the full regulatory requirements during an initial phase, during which phase it would be subject to business restrictions)

- Confirms that VBs that are majority owned by non-financial firms will have to be held through a locally incorporated intermediate holding company (IHC), and provides further detail of the supervisory conditions to be imposed on IHCs

- Revises the wording on the parental support expected of shareholder controllers of VBs to “it is therefore essential that the parent companies of a virtual bank are committed to supporting the bank and are capable of providing strong financial, technology and other support when necessary” – this is to reinforce the point that only applicants with strong parents are allowed to operate a VB

- Revises the wording on the application of supervisory requirements to VBs, confirming that the supervisory requirements applicable to conventional banks will be adapted to suit the business models of VBs under a risk-based and technology neutral approach

- Revises the wording on technology risk to highlight the importance of “system resilience and business continuity management”.

The accompanying press release contains some additional elaboration on the application process. **Effectively, those applicants wishing to be considered as part of the first wave of applications have to submit a substantially complete application by the end of August.**

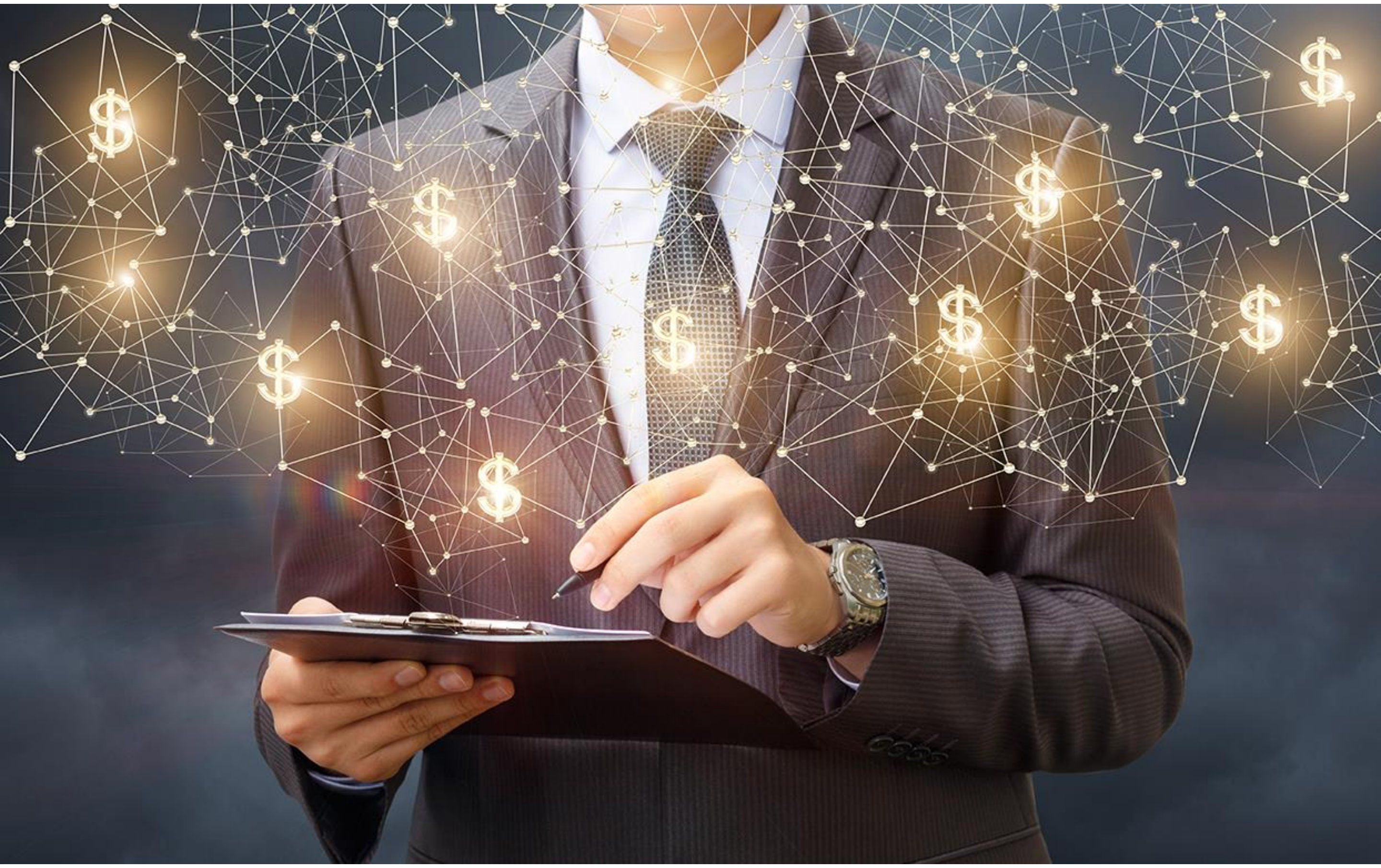
The HKMA sets out four criteria for determining which applications will be given priority when it comes to processing the applications:

(1) The strength of financial, technology and other relevant resources

(2) The credibility and viability of the business plan, providing new customer experience and promoting financial inclusion and fintech

(3) The appropriateness of the IT platform

(4) Readiness to commence operation soon after the licence is granted.



How KPMG can help prospective virtual banks

Development of a viable strategy & business model

Strategic insights into digital banking

Leveraging our experience of working closely with digital and challenger banks in other markets, our Strategy team is able to assist prospective virtual banks to prepare a detailed strategic plan, including three-year financial forecasts, as well as outline business models which are required by the HKMA to support the application for authorisation. For those potential applicants who are deciding whether to proceed with the application, we can prepare a detailed feasibility study.

Support throughout the virtual bank authorisation process

Proven authorisation track record

Our regulatory subject matter experts have deep experience helping banks, stored value facilities and other regulated entities obtain authorisation from the HKMA. We can provide support throughout the process including:

- Preparation or review of application pack
- Preparation or review of key policies
- Preparation or review of exit plan
- Assistance in responding to questions raised by the HKMA on the application.

Independent assessments of the key areas required by the HKMA

Understanding regulatory expectations

We regularly perform independent assessments of technology risk management, business continuity planning, outsourcing, cybersecurity and electronic banking services in accordance with the relevant requirements in the HKMA guidelines. Our teams of IT risk and security specialists have a strong understanding of the banking sector's needs, as well as the HKMA's expectations in these areas.

Designing and implementing an effective IT target operating model

Digital banking technology transformation

Our Advisory team is able to assist applicants in performing a cybersecurity assessment, and developing an appropriate IT target operating model and technology roadmap that are aligned to your business strategy. The team can also support the selection of vendors and technology platforms to fill any gaps in technology capabilities.

Contact us

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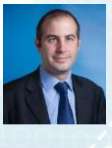

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