

W5 Post-Global Financial Crisis Regulation of Banking in Australia: Reforms and Emerging Challenges (II)

1. What is Fintech? How does the Australia government regulate Fintech (e.g., Fintech licensing exemption- general requirements)?

What is the “Fintech”? How does it evolve?

Financial technology (Fintech) describes an emerging financial services sector in the 21st century. Originally, the term applied to technology applied to the back-end of established consumer and trade financial institutions. Since the end of the first decade of the 21st century, the term has expanded to include any technological innovation in the financial sector, including innovations in financial literacy and education, retail banking, investment and even crypto-currencies like bitcoin.

The term financial technology can apply to any innovation in how people transact business, from the invention of digital money to double-entry bookkeeping. Since the internet revolution and the mobile internet revolution, however, financial technology has grown explosively, and fintech, which originally referred to computer technology applied to the back office of banks or trading firms, now describes a broad variety of technological interventions into personal and commercial finance. ASIC has released a world-first class waiver to allow eligible fintech businesses to test certain specified services for up to 12 months without an Australian financial services or credit licence.

Fintech general requirements

There are some legal hurdle requirements if a business wish to apply for the fintech exemption. For financial services, an Australian financial services (AFS) license is generally required; alternatively, providing financial services on behalf of an AFS licensee as a representative. Financial services generally provide financial product advice; deal in a financial product; make a market for a financial product; operate a registered managed investment scheme; provide a custodial/depository service; or provide traditional trustee company services. For consumer credit, an Australian credit license is generally required; alternatively, acting as a representative of a credit licensee. There are two broader categories of credit activities, including credit activities relating to the provision of a credit contract or consumer lease and securing obligation thereunder; or assisting persons to enter into a credit contract.

Fintech licensing exemption

Australia’s regulatory sandbox framework is comprised of three broad options for testing a new product or service without a licence. Those options include relying on existing statutory exemptions or flexibility in the law, such as by acting on behalf of an existing licensee; relying on ASIC’s ‘fintech licensing exemption’ for the testing of certain specified products and services; and for other services, relying on individual relief from ASIC. The aim of the fintech licensing exemption is to facilitate innovation in financial services and credit by allowing businesses to test certain product and service offerings without holding a license for a testing period of 12 months (RG257.45).

Overview

The legal Instruments include the ASIC Corporations (Concept Validation Licensing Exemption) Instrument 2016/1175 and ASIC Credit (Concept Validation Licensing Exemption) Instrument 2016/1176. There is no need to apply to obtain the benefit of this exemption. As long as the business satisfy the requirements in the exemptions, they are legally entitled to rely on this exemption for 12 months (RG257.41). However, businesses wishing to apply for the exemption must notify before starting relying on this exemption and provide certain information, business can commence after 14 days (RG257.42). It is also important to note that it is prohibited to suggest to consumers that your business/business model has been licensed, authorized or approved by the ASIC (RG257.43).

Eligibility

- [RG257.51) Financial Services: The person seeking to provide financial services must not:
 - (a) be banned from providing financial services;
 - (b) already hold an AFS license;
 - (c) already be an authorized representative of an AFS licensee that is authorized to provide the services covered by the exemption; or
 - (d) a related body corporate of an AFS licensee (see s 50 of the Corporations Act)
- [RG257.52) Credit Activities: The person seeking to engage in the credit activities must not:
 - (a) be banned from engaging in credit activities;
 - (b) already hold a credit license;
 - (c) already be a credit representative of a credit licensee; or
 - (d) be a related body corporate of a credit licensee (see s 50 of the Corporations Act).

What Products and services Can Be Tested?

1. Financial Services [RG 257.56-257.60]

- [RG257.57] The fintech licensing exemption applies to specified services. It does not apply to all financial services or credit activities. It is permitted to provide the following services without holding an AFS license:
 - (a) Giving financial product advice in relation to those listed at RG 257.58, and
 - (b) dealing in the products listed at RG 257.58, other than by issuing those products.
 - [RG 257.58] The fintech licensing exemption for advice and dealing (other than acting as a product issuer) applies in relation to:
 - (a) Listed or quoted Australian securities;
 - (b) Debentures, stocks or bonds issued or proposed to be issued by the Australian Government
 - (c) Simple managed investment schemes;
 - (d) Deposit products;
 - (e) Some kinds of general insurance products; and
 - (f) Payment products issued by authorized deposit-taking institutions (ADIs)
 - [RG257.59] It is important to note that this exemption is NOT available for issuing financial products.
2. Credit Services [RG 257.61-257.64]
- [RG 257.61] The fintech licensing exemption allows you to provide credit services in relation to certain types of credit contracts without needing to hold a credit licence.
 - [RG 257.62] The exemption allows you to act as an intermediary or to provide credit assistance in relation to a credit contract that:
 - (a) has a maximum amount of credit of no more than \$25,000;
 - (b) has a maximum annual cost rate of 24%;
 - (c) is not subject to tailored responsible lending obligations (i.e. is not a reverse mortgage or a small amount credit contract); ; and
 - (d) is not a consumer lease
 - [RG 257.63] This exemption is NOT available for providing credit.

Providing services that are not covered by the fintech licensing exemption [RG 257.69]

[RG257.70] If you want to provide products and services that are not covered by the fintech licensing exemption, as well as offering services that are covered by the exemption, you can do one of the following:

- (a) rely on another exemption, for example, existing flexibility in the laws;
- (b) hold an AFS or credit licence with appropriate authorisations covering all of the services you intend to provide; or
- (c) obtain individual relief (Section G and RG 51).

Testing period

[RG 257.71] If a business rely on the fintech licensing exemption, they do not need to hold a licence for one 12-month period (testing period). The testing period commences 14 days after the business advise ASIC that they intend to rely on the exemption (unless we take further action). They will be notified in writing of the date on which your testing period commences.

[RG 257.72] ASIC consider 12 months is sufficient time for businesses to be able to test the viability of the business model or idea and, at the same time, begin the process of applying for an AFS or credit licence.

[RG257.73] After the 12-month testing period ends, businesses will need to cease operations unless:

- (a) they have been granted an AFS or credit licence;
- (b) they have entered into an arrangement to provide services on behalf of an AFS or credit licensee (see RG 257.26–RG 257.28); or
- (c) ASIC have given individual relief extending the testing period.

[RG257.74] After the end of the testing period, you will no longer be able to offer financial services or engage in credit activities unless you comply with the law like other businesses. This includes financial services or credit activities you provide to your current clients.

General Conditions

- [RG257.82] Have no more than 100 retail clients (no limit wholesale): The fintech licensing exemption is subject to a limit on the number of retail clients that a testing business can engage and the exposure of each client. Testing businesses relying on the exemption can provide services to up to 100 retail clients.
- Plan to test for no more than 12 months and meet disclosure and conduct requirements
- [RG257.83] Have total customer exposure of no more than \$5 million (see also individual exposure for retail investors).
- [RG257.96] Have adequate compensation arrangements (e.g., professional indemnity insurance);
- [RG257.103] Have dispute resolution processes in place;

What if the business need more time or other flexibility?

- The ASIC will accept and consider applications for:
 - an extension to the testing period (e.g. to allow you to test your services for an additional 12 mths);
 - an increase in the client limits (e.g. to allow you to provide services to up to 200 retail clients); or
 - variations to other conditions of the relief.

[RG 257.129] Factors for extending the testing period or increasing the client limits are:

- (a) the nature of the extension or variation you are seeking;
- (b) the reasons you are seeking an extension to the testing period or an increase in the client limits;
- (c) how the extension you seek (e.g. additional testing time or testing with additional clients) will allow you to validate your business model, and not just extend the scope of your operations;
- (d) the date at which your testing period began;
- (e) whether you have applied for a licence and, if so, the date on which you submitted your application; and
- (f) your experience to date in providing services during your testing period, including whether there have been any material disputes with consumers or reports of misconduct to ASIC; and
- (g) the normal matters we consider when deciding whether or not to grant an exemption—these are outlined at RG 51.57–RG 51.62.

Extra content

ASIC Innovation Hub

Innovation hub is an ASIC initiative for new fintech businesses that are developing innovative financial products or services. Via the Hub, eligible fintech start-ups receive informal assistance to navigate the regulatory system. Assistance offered is not legal or financial assistance. They are informal guidance during the pre-license application phase, for instance, the obligations under the financial services regulatory framework, how the ASIC administers this framework (e.g., how to obtain a license). Business that is eligible to use the services of Innovation Hub include a financial technology (Fintech) business; has not been trading under a license from ASIC for over 12 months; offers a potentially ground-breaking innovation; and offers an innovation that provides a potentially better outcome for investors and consumers.

Are foreign clients counted in the 100 retail cap?

ASIC expect where the service provider provides services to foreign retail clients or foreign consumers in the course of its Australian financial services business or credit services business, those clients or consumers would generally need to be included in the 100 retail clients or 100 consumers cap.

Can business refer publicly to assistance ASIC provides through the Innovation Hub?

ASIC does not object to you mentioning that we have provided informal assistance to you via the Hub. However, you should not create an impression (explicitly or implicitly) that your business or services are in any way endorsed or approved by ASIC and you must not reproduce ASIC's logo without our express approval.

What do I need to tell consumers about my reliance on the sandbox exemption and not being licensed?

- Under the fintech licensing exemption, you will need to comply with key consumer protection provisions in the financial services and credit laws: [RG 257.86 -87].
- You will also need to tell your clients that [RG 257.88]
 - you do NOT hold a license;
 - the service you will provide is being tested under the fintech licensing exemption; and
 - some of the normal protections associated with receiving services from a licensee will not apply.

UK Approach in Fintech

The regulator of UK is the Financial Conduct Authority (FCA). It is required to apply for participation in the regulatory sandbox to get authorization in order to test.

The general criteria are:

- Scope: Are you looking to deliver innovation that is either regulated business or supports regulated business in the UK financial services market?
- Genuine Innovation: Is your innovation ground-breaking or a significantly different offering in the marketplace?
- Consumer Benefit: Does the innovation offer a good prospect of identifiable benefit to consumers (either directly or via heightened competition)?
- Need for a Sandbox: Do you have a genuine need to test the innovation in our sandbox? Applicants aren't required to need a sandbox tool to meet this criteria
- Ready for Testing: Are you ready to test the innovation in the real market with real consumers?

Any authorization or registration will be restricted to allow firms to test only their ideas as agreed with us.