Regulatory Framework for Fintech and Investor Protection

Rob Colquhoun

Friday, 2 November 2018

www.afma.com.au

Australia's Fintech Industry

- Australia's Fintech Industry in its third year
- Greater proportion achieved profitability in 2018
  - 19% profitable, up from 14% in prior year
  - Median revenue growth in last year of 125%
- Types of business varies
  - 24% payments/digital wallets
  - 23% wealth and investment
  - 21% data analytics
- Average capital raised of $4.5M
- Key export markets – UK, US, Singapore, HK

AFMA

Regulatory Opportunities for Fintech

- Open Banking
  - Commencing in 2019
  - Consumer data held by major banks will be accessible to Fintech Participants
  - Subject to consent from the consumer
- Royal Commission into Financial Services
  - Threatens the incumbency of the existing providers
  - Opportunities for new participants
  - But – may overshadow policy innovation
- Equity crowdfunding
  - Small companies (less $25M in assets)
  - Raise up to $5M per annum

AFMA

Regulatory Architecture

- Generally, companies that provide a “financial service” need to hold a licence
  - ASIC (Securities Regulator) – financial services, credit or market infrastructure
  - APRA (Prudential Regulator) – banking licence
- Existing licencing exemptions
  - Spot foreign exchange
  - Some funds transfers
- ASIC Regulatory Sandbox
  - Allows Fintechs to test their products and services prior to obtaining a licence

AFMA

Why Have Regulatory Sandbox?

- ASIC has identified three key barriers to successful Fintechs
  - Speed to market, obtaining licence is a barrier
  - Organisational competence, having a responsible manager (licence condition) is a barrier
  - Access to capital, with proof of concept being the barrier
- ASIC view is that the regulatory sandbox environment addresses these barriers
  - Allows concepts to be validated and refined
  - Provides increased opportunities for investment
  - Allows markets to be fair and efficient

AFMA

How does the Sandbox Work?

- Conditional relief to allow Fintechs to test certain products/services for without a licence
  - Available for new businesses only
  - Relief expires after 12 months
  - Certain prohibitions (previously banned, licence holders)
- Only certain products are covered
  - Deposit/loan products (subject to certain criteria)
  - Payment products issued by an ADI
  - General insurance
  - Liquid investment products
- No formal application – only notification

AFMA

Investor Protection

- Certain criteria included to protect investors
  - Limit of 100 retail clients
  - Caps on exposure per client
    - $10,000 for most products
    - $25,000 for loans
    - $50,000 for general insurance
  - Total exposure for all clients (including wholesale) capped at $5M
  - Requirement to notify clients that don't hold a licence
  - Adequate compensation arrangements
    - Usually through PI insurance
  - Dispute resolution arrangements

AFMA

Is the Balance Right?

- Australia is pro-active in supporting Fintech firms from a policy perspective
- Lack of approval process heightens investor risk
  - Different to Singapore and Hong Kong
- Compensation and dispute resolution arrangements helpful
- Other mechanisms about mitigation, not protection
- However, take up has been low
  - Currently only three firms, and six in total
- Fintechs are looking for more flexibility
  - Further erosion of investor protections?
- Global Developments

AFMA