RESPONSE TO FEEDBACK RECEIVED

28 February 2022

Proposed Amendments to the Capital Requirements for Locally Incorporated Recognised Market Operators

Monetary Authority of Singapore

Contents

1 Preface

1.1 On 23 October 2020, the Monetary Authority of Singapore ("MAS") issued a consultation paper on proposed amendments to the capital requirements for locally incorporated Recognised Market Operators ("RMOs"). The review aimed to ensure that capital requirements for market operators remain adequate and commensurate with pertinent risks that RMOs may pose to the financial system. As part of this review, MAS will also issue a Notice with definitions related to capital adequacy that are aligned with other regimes administered by MAS.

1.2 The consultation period closed on 4 December 2020, and MAS would like to thank all respondents for their contributions. The list of respondents (excluding those who have indicated anonymity) and their submissions are provided in Annex A and Annex B, respectively.

1.3 MAS has considered carefully the feedback received and will incorporate them where appropriate. Comments that are of wider interest, together with MAS' responses are set out below.

2 Proposed Introduction of a Liquidity Requirement

2.1 MAS had proposed to introduce a liquidity requirement, which would require RMOs to hold cash and cash equivalents of at least 25% of their annual operating costs[1] ("proposed liquidity requirement").

(a) The liquidity requirement

2.2 While most respondents agreed with the proposed liquidity requirement, one respondent felt that the 25% threshold of annual operating costs should be higher, and some respondents felt that the threshold should be lowered to 18% instead. Two respondents proposed a "tiered risk-based threshold", where the threshold would vary depending on factors such as the stage of the RMO 's development, size of the RMO, or type of activities conducted by the RMO.

[1] MAS has referred to this as "annual operating expenses" in the Notice, but there is no material difference between both phrases.

MAS' Response

2.3 MAS intends for the proposed liquidity requirement to be objective and simple to administer. Using the RMO's annual operating costs as a proxy for its size builds in scalability in the proposed liquidity requirement; it allows for the quantum of required liquid resources to be adjusted such that the costs would be commensurate with the scale of the activities conducted by the RMO.

2.4 MAS will procced with the proposal to set the threshold of 25% of annual operating costs for the proposed liquidity requirement, as we are of the view that this would provide RMOs with adequate resources to wind down its operations in an orderly fashion and provide participants of the RMO with sufficient time to switch to alternative trading platforms. We note that such a requirement is consistent with the practice in other major jurisdictions.

(b) Computation of annual operating costs

2.5 On computation of annual operating costs for the purpose of the proposed liquidity requirement, two respondents proposed for an annualised average of total operating costs, based on the total operating costs in the RMO's latest three audited financial statements, to cater to instances of fluctuating financial resources and operating costs. Separately, two respondents also asked if depreciation and amortisation ("D&A") expenses and discretionary bonuses could be removed for the purposes of calculating annual operating costs.

MAS' Response

2.6 MAS has considered whether the calculation of annual operating costs should be based on an average of total operating costs over a number of past years. However, in the case of fast-growing RMOs, such an average is likely to underestimate the current level of operating costs, thus failing to reflect the actual liquidity risks faced by the RMO. As such, we are of the view that it would be more prudent that the annual operating costs should take reference only from costs that are incurred in the preceding financial year.

2.7 MAS has considered the feedback from respondents, and will **exclude D&A expenses from the calculation of annual operating costs for the purpose of the proposed liquidity requirement**. D&A expenses, which generally do not result in a cash outflow, may be excluded as liquid resources are not reduced by such non-cash events. However, any lease payments that have been made must be added to annual operating costs to the extent that they are not already included. This addition of lease payments ensures that liquid resources continue to be set aside for meeting lease obligations even though lease payments are now capitalised and depreciated under Singapore Financial Reporting Standards ("FRS") 116[2].

2.8 MAS does not agree with the feedback to exclude discretionary bonuses from the computation of annual operating costs for the purpose of the proposed liquidity requirement. There may be expectations and/or contractual agreements for bonuses to be paid once declared. Declared bonuses should be accrued in accordance with accounting standards, and the annual operating costs should reflect the total operating expenses of the RMO as stated in the audited financial statements. Any costs that are not incurred from the ordinary activities of the RMO and are not expected to recur frequently or regularly can, however, be deducted from the computation of operating costs.

(c) Assets that can be used to meet the proposed liquidity requirement

2.9 As regards the assets that can be used to meet the proposed liquidity requirement ("liquid assets"), one respondent asked if the cash and cash equivalents may be held in the RMO's operating account, or if it must be segregated from other assets in a separate account. Another respondent asked if intercompany receivables could be included as part of liquid assets.

<u>MAS' Response</u>

2.10 We do not intend to require that cash and cash equivalents be kept in an operating account or segregated in a separate bank account. On intercompany receivables, MAS does not view such receivables as liquid assets. Intercompany receivables run the risk of being ring-fenced within its affiliated holding company in periods of stress, potentially leaving the RMO without ready access to these funds when needed.

[2] Under FRS 116 on leases, effective from financial period beginning 1 January 2019, all leases are required to be recorded on the balance sheet as lease assets and liabilities, with exemptions for short term leases or leases with an underlying asset that is of low value. Such assets are to be depreciated over its lease term. Any cash outflow amounts from regular lease payments, regardless of the depreciation amount from lease assets, must be included in "annual operating expenses" under the Notice.

3 Proposed Recalibration of a Solvency Requirement

3.1 With the introduction of a new liquidity requirement, MAS proposed to recalibrate the existing solvency requirements and remove the exclusion of illiquid assets from the computation. The revised solvency requirement would require RMOs to hold eligible capital of at least the higher of (i) 25% of their annual operating costs, or (ii) $250,000 (“the proposed solvency requirement”).

3.2 Respondents agreed with the proposed solvency requirement. A respondent commented that the proposed solvency requirement would make it less capital intensive for new RMOs, and is consistent with MAS’ intention to balance market innovation/ fintech adoption with the risks posed by different types of entities.

3.3 A few respondents suggested to further lower the proposed solvency requirement to the higher of (i) 18% of their annual operating costs, or (ii) $250,000, or that a tiered risk-based threshold be adopted.

3.4 One respondent asked if tangible assets, such as Plant, Property & Equipment and Right-of-Use assets arising from the adoption of FRS116 could be included in the computation of eligible capital.

3.5 One respondent asked if discretionary bonuses could be excluded from annual operating costs for purposes of calculating the proposed solvency requirement.

<u>MAS’ Response</u>

3.6 In view of the supportive feedback received, MAS will proceed with the proposed solvency requirement.

3.7 MAS recognises that RMOs typically pose little financial risks to other entities in the financial system. However, a baseline solvency requirement remains necessary, and any further lowering or tiering of the threshold would not be appropriate. As such, the proposed solvency requirement will remain at the higher of (i) 25% of the RMO’s annual operating costs, or (ii) $250,000. This is comparable with the requirements imposed in other major jurisdictions.

3.8 MAS wishes to clarify that tangible assets such as Plant, Property & Equipment and Right-of-Use assets would not need to be deducted from eligible capital for the computation of the proposed solvency requirement, as the concern with having adequate liquid assets is now addressed through the introduction of the proposed liquidity requirement.

3.9 Unlike the treatment of D&A expenses in paragraph 2.7 for the proposed liquidity requirement, MAS will not be excluding D&A from annual operating costs for calculating the proposed solvency requirement. MAS views the proposed solvency requirement as a reflection of financial viability, and given this, RMOs should hold adequate capital to replenish depreciating assets.

3.10 As in the case of the liquidity requirement, discretionary bonuses should not be deducted from annual operating costs for the purposes of calculating the proposed solvency requirement.

MONETARY AUTHORITY OF SINGAPORE

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Annex A

LIST OF RESPONDENTS TO THE CONSULTATION PAPER ON

PROPOSED AMENDMENTS TO THE CAPITAL REQUIRMENTS FOR LOCALLY INCORPORATED RECOGNISED MARKET OPERATORS

1. Joint response from: HGX Pte. Ltd., Prime PrimePartners Corporate Finance Holding Pte. Ltd., Phillip Securities Pte. Ltd., Fundnel Pte. Ltd.
2. IC SG Pte. Ltd.
3. RHTLaw Asia LLP, jointly with RHT Compliance Solutions Pte Ltd.
4. TSMP Law Corporation
5. 1 respondent requested confidentiality of their identity
6. 2 respondents requested confidentiality of their identity and submission

Please refer to Annex B for the submissions.

Annex B

FULL SUBMISSION FROM RESPONDENTS TO THE CONSULTATION PAPER ON

PROPOSED AMENDMENTS TO THE CAPITAL REQUIRMENTS FOR LOCALLY INCORPORATED RECOGNISED MARKET OPERATORS

S/N	Respondent	Response from Respondent
1	Joint response from - HGX Pte. Ltd., - Prime PrimePartners Corporate Finance Holding Pte. Ltd., - Phillip Securities Pte. Ltd., - Fundnel Pte. Ltd.	**General comments** None. **Question 1: Introduction of the liquidity requirement** **Joint response**: We agree with the introduction of a direct liquidity requirement, but wishes to note that requiring RMOs to hold cash and cash equivalents of at least a quarter of their annual operating costs can place substantial demand on their resources given that cash and cash equivalents can fluctuate significantly on a daily basis depending on operational events (e.g., payment of salaries). This is of particular importance to RMOs operating on a restricted basis. We therefore propose that the minimum percentage of annual operating costs be lowered to 18% from the proposed 25% in light of the fact that operational demands will have a greater impact on such RMOs' amount of cash and cash equivalents than for RMOs that have a larger scale of operations. We believe 18% should be an acceptable threshold as 18% of annual operating revenue is presently one of the accepted calculation methods for required financial resources. **Question 2: Recalibration of the solvency requirement** **Joint response**: We agree that illiquid assets should not be deducted from eligible capital should the liquidity requirement be implemented, and welcome the proposal to confine deductions from eligible capital to assets that are unlikely to be realisable upon insolvency of an RMO. However, we propose that the revised solvency requirement for eligible capital be, instead, the higher of (i) 18% of annual

		operating costs or (ii) $250,000 for RMOs that have a restricted scale of operations. This is, as explained in our response to Question 1, due to the fact that operational demands have a comparatively greater influence on the level of operating costs for such RMOs. Our reason for proposing 18% is likewise due to the fact that 18% of annual operating revenue is presently an accepted calculation method for required financial resources. **Question 3: Draft of Notice** **Joint response**: No comments on specific wording beyond what would be required to effect our responses to Questions 1 (minimum percentage of annual operating costs to be lowered to 18% instead of 25%) and 2 (eligible capital required to be the higher of 18% of annual operating costs or $250,000).
2	IC SG Pte. Ltd.	**General comments** InvestaX is a digital securities platform based in Singapore offering end-to-end solutions of the issuance, trading and custody of digital securities for private markets, including real estate, private equity and other alternative investments. Founded in 2015, InvestaX is an early pioneer in the use of blockchain technologies to develop leading technology-driven investment vehicles, removing friction and delivering secondary market trading to the private markets. InvestaX currently holds a capital markets services license (“CMSL”) for dealing in securities issued by the MAS, and has submitted an application for the RMO sandbox which is pending approval. **Question 1: Introduction of the liquidity requirement** We welcome the proactive and consultative approach taken by MAS to introduce liquidity requirements for RMOs. We believe this will bolster greater stability and confidence among all market participants and drive wider adoption of such platforms. However, if the purpose of such an amendment is to encourage smaller Fintechs to participate, we think the current requirements may be too high for startups to meet. While more established players have an

		existing customer base and operational model, smaller Fintechs are generally still in growth mode, recruiting talent, focusing on the acquisition of new customers, and demonstrating product-market fit, which require these startups to utilise as much of the funding raised towards future development. As such, 25% of annual operating costs as a liquidity requirement may be an unnecessary and burdensome imposition depending on the stage of the startup and the risk exposure posed by a smaller operator. Therefore we believe that RMOs should be allowed to meet the full liquidity requirements in phases and certainly before they grow big enough to pose any systemic risk or impact a large number of consumers. Specifically, we suggest the following tiered structure for implementing the liquidity requirements: 1. Tier 1 - Entry phase (when an applicant first receives an RMO licence)- liquidity requirements to be lowered (e.g. 15% of annual operating costs) 2. Tier 2 - Progression Phase (12 months post entry phase)- liquidity requirements are increased (e.g. 20% of annual operating costs) 3. Tier 3 - Fully Functional Phase (12 months after progression phase)- RMO required to meet full liquidity requirements of 25% of the annual operating cost. This would provide balance between safeguarding the interests of various stakeholders while promoting innovation and healthy competition from new entrants. The above approach is just an example and MAS could also consider graduating startups to fully functional phase upon hitting a certain threshold financially (revenue, trading value etc.) or operationally (e.g. customers etc.). **Question 2: Recalibration of the solvency requirement** Recalibration of solvency requirements is a welcome measure. There is a considerable reduction in eligible capital requirements from higher of a) 18% of annual operating revenue b) 50% of annual operating or $500,000 to higher of 25% of annual operating cost or $250,000. Again, a phased approach can be adopted here which would encourage more

		Fintech startups to compete in this space. Specifically, we suggest the following tiered structure for implementing the solvency requirements: 1. Tier 1 -Entry phase (when an applicant first receives an RMO licence)- solvency requirements to be lowered (e.g. the higher of 15% of annual operating costs or $150,000) 2. Tier 2- Progression Phase (12 months post entry phase)- solvency requirements are increased (e.g. the higher of 20% of annual operating costs or $200,000) 3. Tier 3- Fully Functional Phase (12 months after progression phase)- RMO required to meet full solvency requirements of the higher of 25% of the annual operating costs or $250,000. For the eligible capital requirements, we would want to seek clarity on what would be the eligible capital requirement for an RMO which is also holding a CMSL licence like ourselves. In the situation where an entity holds both an RMO and CMSL, would we be required to keep the higher of the two capital requirements or a consolidated amount for capital requirements under both CMSL and RMO licence? We note that existing interpretation has been that a licensee would be required to meet the higher capital requirements under the applicable licenses it holds. **Question 3: Draft of Notice** Annex B lacks clarity on where the cash or cash equivalent for liquidity is required to be maintained. Can it be kept in the Company's operating account or is it required to be maintained in a separate account totally untouched at all times. Annex B clause 2.2- The calculation of liquid assets and eligible capital on a daily basis and keeping its records would be too cumbersome a process and involve unnecessary administrative work on the part of a small RMO startup. This should be made a monthly or a quarterly exercise. Even under the Securities and Futures (Financial and Margin Requirements for Holders of Capital Market Services Licences) Regulations there is no requirement for a CMSL holder to do calculation of financial resources on a daily basis,

		such calculations are typically done on a quarterly basis unless the licensee falls below 120% of its total risk requirement, at which point, a monthly requirement may be imposed. We think a similar approach would be more in line with what licensed entities are accustomed to. We would also like to note that the requirement in 2.1(c) means the baseline liquidity and solvency requirements are actually higher, meaning the actual requirement is 120% of (i) $250K solvency requirement and (ii) 25% of the annual operating costs. Which goes back to our overall support for a downward recalibration of the solvency requirement and also the adoption of a phased approach.
3	RHTLaw Asia LLP, jointly with RHT Compliance Solutions Pte Ltd.	Respondent wishes to keep entire submission confidential
4	TSMP Law Corporation	Respondent wishes to keep entire submission confidential

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