



**BANK NEGARA MALAYSIA**  
CENTRAL BANK OF MALAYSIA

# Licensing Framework for Digital Banks

Applicable to:

1. Applicants under section 10 FSA
2. Applicants under section 10 IFSA
3. Licensed digital banks
4. Licensed Islamic digital banks
5. Shareholders of proposed licensed digital banks or proposed licensed Islamic digital banks
6. Shareholders of licensed digital banks or licensed Islamic digital banks

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## PART A OVERVIEW

### 1 Introduction

- 1.1 Technology-based innovations have become more entrenched within the financial sector, enhancing its service and delivering efficiency gains, and ultimately contributing to the development of the broader economy. The Bank endeavours to ensure the regulatory framework remains conducive for enablement of these innovations in a safe and sound manner that supports transformation of the financial ecosystem to meet future economic needs of the nation, and promote sustainable and inclusive financial sector.
- 1.2 In line with these efforts, the Bank has developed a framework for digital banks to offer banking products and services to underserved or unserved market wholly or almost wholly through digital or electronic means. Licensing of these new players with innovative business models is expected to add dynamism to the banking landscape to serve the economy and contribute to individual well-being. This includes expanding meaningful access to and responsible usage of suitable financial solutions for the underserved and unserved market segments.
- 1.3 The Bank is cognizant that such digital banks have not operated through a full financial and economic cycle. This calls for a balanced approach that enables admission of digital banks with strong value propositions whilst safeguarding the integrity and stability of the financial system as well as depositors' interests.
- 1.4 This licensing framework for digital banks aims to achieve these outcomes through specifying an asset threshold in the initial three to five years of operations of a licensed digital bank. This functions as a 'foundational phase' for the licensed digital banks to demonstrate their viability and sound operations, and for the Bank to observe attendant risks. During the foundational phase, the licensed digital bank will be subject to a more simplified regulatory requirement.
- 1.5 This policy document sets out the requirements relating to applications for the establishment of a digital bank, as follows—
  - (a) Part B sets out the eligibility requirements and application procedures that must be complied with by an applicant intending to carry on digital banking business or Islamic digital banking business. This is in addition to the application and assessment process set out in the policy document

on *Application Procedures for New Licences under Financial Services Act 2013 and Islamic Financial Services Act 2013 (Licensing Procedures)*;

- (b) Part C sets out the business limitations and regulatory framework applicable to a licensed digital bank during the foundational phase; and
- (c) Part D sets out the business activities that must be undertaken and the physical access points that may be established by the licensed digital bank.

1.6 Existing licensed banks or licensed Islamic banks may apply to carry on digital banking business or Islamic digital banking business through a separate corporate body, such as their subsidiary or through a joint venture arrangement with another party. However, this does not preclude existing licensed banks and licensed Islamic banks from digitalising their current business operations, which does not require the application of a separate licence under this policy document.

## 2 Applicability

2.1 This policy document is applicable to–

- (a) an applicant applying for a licence under section 10 of the Financial Services Act 2013 (FSA) or section 10 of the Islamic Financial Services Act 2013 (IFSA) to carry on digital banking business or Islamic digital banking business, as the case may be;
- (b) a licensed digital bank as defined in paragraph 5.2 of this policy document;
- (c) the shareholders who require an approval under section 90 of the FSA or section 102 of the IFSA for the holding of interest in shares of a proposed licensed digital bank; and
- (d) the prospective shareholders who require an approval under section 90 of the FSA or section 102 of the IFSA for the acquisition of interest in shares in a licensed digital bank.

## 3 Legal provisions

3.1 The requirements in this policy document are specified pursuant to–

- (a) sections 9, 25(1), 47(1), 123(1) and 143 of the FSA; and
- (b) sections 9, 22(1), 57(1), 135(1) and 155 of the IFSA.

3.2 The guidance in this policy document is issued pursuant to section 266 of the FSA and section 277 of the IFSA.

#### 4 Effective date

4.1 This policy document comes into effect on 31 December 2020.

#### 5 Interpretation

5.1 The terms and expressions used in this policy document shall have the same meanings assigned to them in the FSA and IFSA, as the case may be, unless otherwise defined in this policy document.

5.2 For the purpose of this policy document–

**“S”** denotes a standard, an obligation, a requirement, specification, direction, condition and any interpretative, supplement and transitional provisions that must be complied with. Non-compliance may result in enforcement action;

**“G”** denotes guidance which may consist of statements or information intended to promote common understanding and advice or recommendations that are encouraged to be adopted;

**“digital banking business”** means banking business as defined in section 2(1) of the FSA which is carried on wholly or almost wholly through digital or electronic means;

**“e-SPICK”** means the national electronic cheque information clearing system operated by Payments Network Malaysia Sdn. Bhd. (PayNet);

**“Islamic digital banking business”** means Islamic banking business as defined in section 2(1) of the IFSA which is carried on wholly or almost wholly through digital or electronic means; and

**“licensed digital bank”** means–

- a person licensed under section 10 of the FSA to carry on digital banking business; and
- a person licensed under section 10 of the IFSA to carry on Islamic digital banking business.

## 6 Related legal instruments and policy documents

6.1 This policy document must be read together with other relevant legal instruments and policy documents that have been issued by the Bank, in particular–

- (a) *Agent Banking;*
- (b) *Licensing Procedures;*
- (c) *Application Procedures for Acquisition of Interest in Shares and to be a Financial Holding Company (Acquisition Procedures);*
- (d) *Approach to Regulating and Supervising Financial Groups;*
- (e) *Outsourcing;*
- (f) *Capital Funds;*
- (g) *Capital Funds for Islamic Banks;*
- (h) *Capital Adequacy Framework (Capital Components);*
- (i) *Capital Adequacy Framework for Islamic Banks (Capital Components);*
- (j) *Capital Adequacy Framework (Basel II – Risk-Weighted Assets);*
- (k) *Capital Adequacy Framework for Islamic Banks (Risk-Weighted Assets);*
- (l) *Liquidity Coverage Ratio; and*
- (m) *Shariah Governance.*

## PART B ELIGIBILITY AND ADDITIONAL APPLICATION PROCEDURES

### 7 Factors for consideration in assessing the best interest of Malaysia criteria

**G** 7.1 In assessing an application to carry on digital banking business or Islamic digital banking business prior to making any recommendation to the Minister of Finance, the Bank will have regard to part B of the *Licensing Procedures*.

**S** 7.2 In assessing the best interest of Malaysia criteria as specified under Schedule 5 of FSA or IFSA, an applicant is required to demonstrate to the Bank's satisfaction a commitment in driving financial inclusion, including ensuring quality access and responsible usage of financial services, particularly to underserved and hard-to-reach segments that may be unserved, which includes retail as well as micro, small and medium enterprises (MSMEs), in a sustainable manner, without jeopardising the interest of depositors.

**G** 7.3 To reflect the commitment to meet the best interest of Malaysia criteria, the shareholders of a proposed licensed digital bank may offer an enforceable undertaking pursuant to section 259 of the FSA or section 270 of the IFSA which effectively incorporate such commitments. Similar commitments may also be incorporated as part of the licensing conditions of the licensed digital bank.

### 8 Factors for consideration in assessing shareholders

**G** 8.1 In assessing the suitability of the shareholders of a proposed licensed digital bank or the prospective shareholders of a licensed digital bank, the Bank will have regard to factors set out in paragraph 7.9 of the *Acquisition Procedures*.

**G** 8.2 Without limiting the generality of paragraph 8.1, the Bank will assess the ability of the applicant and where relevant, other shareholders collectively, to contribute to the proposed licensed digital bank in the following areas–

- (a) robust risk management and compliance capabilities, which may be demonstrated by a track record of operating in a regulated environment;
- (b) application of transformative technology in the development and delivery of financial services, such as scalable and agile technology stack built on microservices architecture;

- (c) access to deep and robust customer analytics that may be utilised to improve and expand access to and responsible usage of financial services;
- (d) ability to continuously serve as a source of financial strength to the proposed licensed digital bank; and
- (e) with respect to proposed licensed Islamic digital banks, the requisite Shariah expertise to effectively carry on Islamic digital banking business.

**G** 8.3 The Bank may require a shareholder who holds an aggregate interest in shares of 50% or more in a proposed licensed digital bank to organise all its financial and financial-related subsidiaries under a financial group, headed by a single apex entity, which may be either a licensed institution or a financial holding company. In this regard, shareholders are encouraged to refer to the Bank's paper on *Approach to Regulating and Supervising Financial Groups* and the *Acquisition Procedures*.

**G** 8.4 The presence of strong and well-managed domestic banking institutions is important for the stability of the financial system and its orderly growth and development. In this respect and in consideration of the factors set out in Schedule 6 of the FSA and IFSA, the Bank will review whether the application will be in the best interest of Malaysia, including the degree and significance of Malaysian participation in the financial sector. In this regard, preference will be accorded to an application where the controlling equity interest in the proposed licensed digital bank are held by Malaysians.

## **9 Application process**

**S** 9.1 In submitting an application pursuant to section 9 of the FSA and IFSA, as the case may be, an applicant shall comply with the procedures set out in Part C of the *Licensing Procedures*.

## **10 Submission of business plan**

**S** 10.1 Pursuant to section 9 of the FSA and IFSA, an applicant shall submit to the Bank the information and documentation required under Part D of the *Licensing Procedures*.

**S** 10.2 With respect to the submission of a business plan, the applicant is required to submit to the Bank a business plan that contains the information required under paragraph 12 of the *Licensing Procedures*, as well as the additional requirements outlined in paragraph 10.3 of this policy document. Notwithstanding that paragraph 12 of the *Licensing Procedures* requires the submission of a three-year business plan, in the case of an application to carry on digital banking business or Islamic digital banking business, the applicant shall submit a business plan that covers a five-year period.

**S** 10.3 The applicant must ensure that the overall business plan shall—

- (a) be aligned with the specified total asset size during the foundational phase, as provided in paragraph 13.1;
- (b) emphasise and be aligned with financial inclusion objectives of serving the unserved and/or underserved segments. The plan shall include—
  - (i) description of the specific unserved and/or underserved target segments. The identification of the target segment must be supported by market studies and an analysis of the market gaps;
  - (ii) proposed financial products and services that will be offered. The applicant must explain how the solutions to be offered will address the specific needs of the target segment, promote responsible usage of financial services and create positive impact to the target segment. An example would be a solution that encourages the build-up of savings or financial buffers, including retirement savings by the unserved and/or underserved segments;
  - (iii) indicate in the pro-forma financial statements, the share of business from the identified unserved and/or underserved segments relative to the overall projected operations; and
  - (iv) performance indicators that reflect the applicant's value proposition in driving the financial inclusion objectives. These indicators must clearly demonstrate the proposed licensed digital bank's progress in fulfilling the financial needs of the target segments identified in paragraphs 10.3(b)(i) and (ii).
- (c) include a projected path to profitability that demonstrates a sustainable business model. Where the applicant does not expect the proposed licensed digital bank to break even within the first five years, the applicant shall indicate in the pro-forma financial statements the expected year that the proposed licensed digital bank will break even;

- (d) include an analysis of the reasonableness of the key assumptions that forms the basis of the pro-forma financial statements;
- (e) identify the risks associated with the business activities and strategies to manage such risks;
- (f) indicate talent requirement (in numbers and type of skills needed) over the five-year period, and how the required numbers and skills will be met in areas related to technology and risk management, and where applicable, requisite Shariah expertise;
- (g) outline the measures to address customers' queries or complaints, given that licensed digital banks are required to be operating wholly or almost wholly through digital or electronic means;
- (h) outline the measures to reach compliance with regulatory requirements at the end of the foundational phase as described in paragraph 15.2. The plan shall include the timeframe and resources required to build the capability for full compliance;
- (i) include, for applicants who intend to offer financial services through agent banking, details on the proposed agent, which at minimum shall cover–
  - (i) description of the unserved and/or underserved segments that would be served through the agent;
  - (ii) description of prevailing conditions that inhibits the offering of financial services through digital or electronic means to these target segments;
  - (iii) locations (the city/ town, sub-district (*mukim*) and state) where the agents are expected to operate in;
  - (iv) type of products and services offered by the proposed licensed digital bank to its customers that would be facilitated through the agent, such as bank accounts or e-wallets;
  - (v) indicate in the pro-forma financial statements, the share of business served through the agent relative to the overall projected operations;
  - (vi) detailed plan to fully migrate the services to digital or electronic channels within five years of the proposed licensed digital bank's commencement of operations; and
- (j) include a description of the plans for deploying the technology, which at minimum should cover–
  - (i) a description of the technology stack used in the cloud arrangement, including–

- (i) overview of system architecture diagram and network architecture diagram; and
- (ii) overview of cloud strategy and its deployment model (Software as a Service, Platform as a Service, Infrastructure as a Service) for critical systems;
- (ii) a description of the applicant's strategy to adopt relevant new technologies and digital innovations such as big data, artificial intelligence, or distributed ledger technology to meet the financial inclusion objectives as well as to gain competitive advantage. The strategy shall clearly outline how the new technologies and digital innovations are used to address the following attributes—
  - (i) flexibility: flexibility of solution to integrate with various platforms or emerging technologies with minimal changes or disruptions to core systems; and
  - (ii) scalability: modularity in design to ensure adaptability to changing market trends;
- (iii) a description of the planned IT governance (including its IT governance structure) to oversee—
  - (i) technology risks and cyber risks;
  - (ii) IT strategic plan and cyber strategic plan;
  - (iii) IT operations;
  - (iv) IT projects; and
  - (v) third party service providers including IT outsourcing as well as cloud arrangements;
- (iv) a description of the planned IT operational management to effectively support business operations including—
  - (i) overview of end-to-end IT operational management covering IT operational arrangement to outsource or procure from third party service providers (including cloud service providers);
  - (ii) proposed IT organisation structure; and
  - (iii) business continuity plan and disaster recovery plan;
- (v) a description of the planned measures (technology, people and process) to ensure system resiliency and high availability of services to its customer; and
- (vi) a description of the planned measures (technology, people and process) to effectively manage cybersecurity threat and cyber attacks including the arrangement to identify, protect, detect, response and recover from cybersecurity threats and cyber incidents.

**S** 10.4 At the application stage, an applicant is required to obtain an independent external review on the feasibility of the business plan, that includes–

- (a) evaluation on the comprehensiveness of the business plan in capturing the Bank's requirements in paragraphs 10.2 and 10.3, and identification of key gaps, if any;
- (b) assurance<sup>1</sup> in accordance with applicable professional standards that–
  - (i) the pro-forma financial statements are accurately prepared in line with the assumptions used by the applicant and the key assumptions are adequately disclosed to the Bank, and
  - (ii) the basis of preparation and presentation of the pro-forma financial statements is in accordance with the Malaysian Financial Reporting Standards and the assumptions referred to in paragraph 10.4(b)(i); and
- (c) the external independent report shall provide commentary on suitability of the assumptions used in preparation of the pro-forma financial statements, having regard to the applicant's business plan, including–
  - (i) the relevance and reliability of the assumptions and their effects on the line items in the pro-forma financial statements;
  - (ii) sufficiency and appropriateness of the supporting information used in deriving the key assumptions, which may include historical track records, commissioned market studies, internal documentation of views, basis and calculations of the applicant; and
  - (iii) the extent of procedures performed by the external independent expert to validate each available supporting information, as well as any limitations in performing the said procedures.

The independent external party is required to have a good track record and expertise or relevant experience in assessing business plan financial projections.

**S** 10.5 After a licence is granted by the Minister of Finance and prior to the commencement of operations, the licensed digital bank is required to undergo an operational readiness review as described in paragraphs 10.17 and 10.18 of the *Licensing Procedures*. In addition, the licensed digital bank is required to obtain an independent external assurance that the internal controls and IT systems of the licensed digital bank are in place to support its operations in a sound and prudent manner and submit such assurance to the Bank. These include controls and IT systems to ensure compliance with the prudential standards issued by the

<sup>1</sup> At least a moderate level of assurance (refers to a limited or negative assurance) under the applicable professional standards in the context of the financial projection prepared in accordance with the assumptions for events and actions that have not yet occurred.

Bank on capital, liquidity, risk management, consumer protection, AML/CFT, Shariah matters and cyber security. The independent external party is required to have a good track record and expertise or relevant experience in assessing adequacy of internal controls and IT systems for compliance with prudential standards.

**S** 10.6 The independent external party referred to in paragraphs 10.4 and 10.5 must be free from any conflict of interest or potential conflict of interest that could impair the ability to provide an objective assurance and/or assessments on the applicant's business plan and operational readiness.

## 11 Submission of exit plan

**S** 11.1 With the adoption of new and untested business models, applicants shall be prepared to exit the business in the event that such business models prove to be unsustainable or ineffectual. An exit plan is thus necessary to ensure that the licensed digital bank is able to voluntarily unwind its business operations without any regulatory intervention and in an orderly manner without causing any disruption to its customers and the financial system.

**S** 11.2 At the point of application, an applicant shall submit to the Bank an exit plan for the first five years of the applicant's operations. In this regard, the exit plan must include the following—

- (a) potential management triggers for exiting the business which clearly defines unsustainable business models and/or the materialisation of risks beyond the applicant's own risk appetite. These indicators may comprise of, but are not limited to—
  - (i) capital-related triggers such as leverage ratio and common-equity Tier 1 ratio;
  - (ii) liquidity-related triggers such as loan-to-funds ratio;
  - (iii) earnings-related triggers such as return on assets and return on equity; and
  - (iv) asset quality-related triggers such as non-performing loan ratio;
- (b) likely options and related measures to be taken for exiting that minimises disruption to its customers and the financial system;
- (c) potential impediments to the execution of identified exit options and preparatory measures to mitigate the impact of such impediments; and

(d) sources of funding and liquidity for exit (excluding any form of assistance from the Bank) and the estimated timeframe to exit the business.

The full implementation of the exit plan must result in the winding down or transfer of the licensed digital bank's business.

**S** 11.3 For purposes of paragraph 11.2, within the exit plan, the applicant is required to demonstrate the following—

- (a) the necessary capabilities required to extract and aggregate real time data on depositors and customers upon request, including up-to-date contact information and alternative bank accounts to facilitate any pay-out; and
- (b) the necessary capabilities and resources required to ensure continuity of services throughout the implementation of the exit plan, with a specific focus on continuity of services under outsourcing arrangements.

**S** 11.4 For the purpose of the requirements under paragraphs 11.2 and 11.3, an applicant shall provide a comprehensive description of its exit plan which includes the following information—

*Table 1: Required content of the exit plan*

Coverage	Details
Governance to support informed decision making in the activation of exit plan	<ul style="list-style-type: none"> <li>• Well-defined roles and responsibilities of the board, senior management and business units</li> <li>• Policies, procedures and management information systems to inform and support decision making and smooth coordination of exit plan execution</li> </ul>
Exit triggers	<ul style="list-style-type: none"> <li>• Identification of factors and indicators/thresholds that will prompt activation/execution of the exit plan including, but not limited to, material underachievement of interim targets towards compliance to regulatory requirement at the end of the 5-year observation period</li> <li>• Processes for continuous monitoring of factors and indicators/thresholds</li> </ul>
Execution of measures that enable an orderly exit from the	<ul style="list-style-type: none"> <li>• Identification of possible actions that can be undertaken under different scenarios, taking into account cross-border considerations and stages of development/complexity of the applicant's business</li> </ul>

business without causing disruption to third-parties, in particular customers and counterparties	<ul style="list-style-type: none"> <li>Identification of possible and credible funding sources to implement the exit plan</li> <li>Description of operational dependencies on external parties (i.e. applicant's dependence on external service providers) and its associated costs throughout the exit phase to ensure smooth operational continuity throughout the exit phase</li> </ul>
Communication and engagement strategy (including to the Bank) to mitigate unintended consequences	<ul style="list-style-type: none"> <li>Identification of key stakeholders, including depositors, relevant regulators and authorities, counterparties, service providers, general public, etc.</li> <li>Information needs of respective stakeholders</li> <li>Medium, timing and frequency of communication</li> <li>Person(s) responsible for ensuring the effective coordination and execution of the communication and engagement strategy</li> </ul>

**G** 11.5 As a starting point in developing the exit plan, an applicant may refer to the exposure draft on *Recovery Planning* issued by the Bank to guide the applicant's selection and calibration of exit triggers as well as assessment of efficacy and feasibility of its measures.

**S** 11.6 An applicant is required to submit an exit plan which broadly covers all aspects specified in paragraph 11.4 and with detailed elaboration on exit triggers and execution of measures. Further details on the operational aspects such as the exact governance policies, technical details of the management information system and detailed information needs of respective stakeholders may be submitted later for the Bank's review, prior to the commencement of its operations.

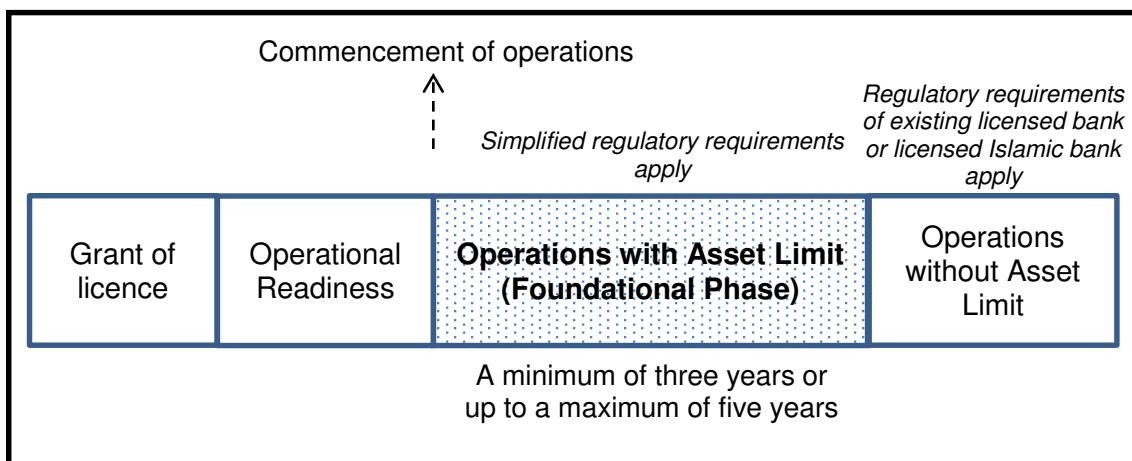
**S** 11.7 Prior to the commencement of operations, the Board of the licensed digital bank is required to endorse the exit plan including the refined operational details as stated in paragraph 11.6. The licensed digital bank is required to keep its exit plan updated and to notify the Bank as and when there are material changes to its structure or operations that will significantly affect its exit plan. The Board of the licensed digital bank is required to review the exit plan on an annual basis to

ensure it remains feasible and credible, taking into account developments in the operations of the licensed digital bank.

## PART C REGULATORY REQUIREMENTS

### 12 Overview

**S** 12.1 A licensed digital bank shall operate with an asset limit for a period of up to five years from its commencement of operations ('foundational phase'). An overview of the timeline of the operational progression of the licensed digital bank is illustrated below.



**S** 12.2 During the foundational phase, a licensed digital bank shall–

- maintain at all times a minimum amount of capital funds of RM100 million unimpaired by losses; and
- be subject to the business limitation as described in paragraph 13 and the regulatory framework as described in paragraph 14.

### 13 Business limitation

**S** 13.1 A licensed digital bank shall ensure that its total size of assets do not at all times exceed the limit of RM3 billion during the foundational phase. In complying with the asset limit, the licensed digital bank shall monitor its off-balance sheet items to ensure any potential crystallisation of off-balance sheet items into on-balance sheet items does not result in a total size of assets that exceed the asset limit.

## 14 Regulatory framework

**S** 14.1 A licensed digital bank shall comply with the regulatory requirements applicable to an existing licensed bank or licensed Islamic bank, except where specified below.

Areas of simplification or exemption to the existing regulatory framework	
(A) Capital Adequacy	<p>(a) A licensed digital bank shall maintain a minimum Total Capital Ratio (TCR) of 8%, computed based on the following–</p> <p><i><u>Capital Components</u></i></p> <p>(i) All requirements in the policy documents on <i>Capital Adequacy Framework (Capital Components)</i> and <i>Capital Adequacy Framework for Islamic Banks (Capital Components)</i> shall apply, except where stated otherwise below.</p> <p>(ii) Only Common Equity Tier 1 (CET1) capital shall be recognised as eligible regulatory capital.</p> <p>(iii) Capital buffer requirements, including the Capital Conservation Buffer and Countercyclical Capital Buffer, shall not apply.</p> <p><i><u>Risk-weighted assets</u></i></p> <p>(iv) All requirements in the policy documents on <i>Capital Adequacy Framework (Basel II – Risk-Weighted Assets)</i> and <i>Capital Adequacy Framework for Islamic Banks (Risk-Weighted Assets)</i> shall apply, except where stated otherwise below.</p> <p>(v) For credit risk, only the Standardised Approach shall apply, with modifications as set out in Appendix 1.</p> <p>(vi) For operational risk, only the Basic Indicator Approach shall apply.</p>

	<p>(vii) For market risk, only the Standardised Market Risk Approach shall apply, with the following modifications—</p> <ul style="list-style-type: none"> <li>i. For interest/profit rate risk exposures, the requirements as set out in Appendix 2 shall apply.</li> <li>ii. Equity, commodity and inventory risk exposures shall be treated as banking book exposures, and subject to requirements in Appendix 1<sup>2</sup>; and</li> <li>iii. For options risk exposures, only the delta-plus method<sup>3</sup> shall apply.</li> </ul> <p>(viii) The large exposure risk requirement (LERR) shall not apply.</p>
(B) Liquidity	<p>(a) A licensed digital bank shall hold an adequate stock of unencumbered Level 1 and Level 2A high-quality liquid assets (HQLA) equivalent to at least 25% of its total on-balance sheet liabilities.</p> <p>(b) All general and operational requirements relating to the eligibility of Level 1 and Level 2 HQLA shall refer to those set out in the policy document on <i>Liquidity Coverage Ratio (LCR)</i><sup>4</sup>.</p>
(C) Stress testing	<p>(a) A licensed digital bank shall be exempted from the requirements under the policy document on <i>Stress Testing</i>.</p>

<sup>2</sup> For commodity and inventory risk exposures, this will fall under the “Other Assets” category.

<sup>3</sup> For the avoidance of doubt, all delta-weighted positions in the banking book should be recorded using the absolute values (i.e. non-negative).

<sup>4</sup> Paragraph 10 of the policy document on LCR defines the scope of eligible assets for each level, while paragraphs 11 and 12 set out operational requirements and encumbrance criteria in maintaining the HQLA stock.

(D) Public Disclosures (Pillar 3)	<p>(a) A licensed digital bank shall be exempted from the requirements under the policy documents on <i>Risk-Weighted Capital Adequacy Framework (Basel II)– Disclosure Requirements (Pillar 3)</i> and <i>Capital Adequacy Framework for Islamic Banks (CAFIB)– Disclosure Requirements (Pillar 3)</i>.</p> <p>(b) A licensed digital bank shall include the following information as part of the explanatory notes in the financial statements–</p> <ul style="list-style-type: none"> <li>(i) Breakdown of gross risk-weighted assets for each risk component; and</li> <li>(ii) For credit risk-weighted assets, the breakdown of the various categories of risk weights.</li> </ul>
(E) Shariah Governance	<p>(a) All requirements in the policy document on <i>Shariah Governance</i> shall apply to a licensed digital bank carrying on Islamic digital banking business, except where stated otherwise below–</p> <ul style="list-style-type: none"> <li>(i) Shariah Committee must comprise at least three members; and</li> <li>(ii) Shariah Committee must convene at least two times a year.</li> </ul>

**S** 14.2 A licensed digital bank shall have regular engagements with the Bank during the foundational phase. This is to ensure that the licensed digital bank achieves consistent and steady progress in complying with regulatory requirements applicable to an existing licensed bank or licensed Islamic bank.

**S** 14.3 Notwithstanding paragraph 14.1, a licensed digital bank must obtain the Bank's prior written approval if it wishes to adopt the regulatory framework applicable to an existing licensed bank or licensed Islamic bank during the foundational phase<sup>5</sup>.

<sup>5</sup> For the avoidance of doubt, this will only apply to the adoption of regulatory requirements, and does not supersede paragraphs 12.2(a) and 13.1 upon the Bank's approval.

**G** 14.4 In considering the application under paragraph 14.3, the Bank will assess, among others—

- (a) the robustness of the licensed digital bank's overall risk management and compliance policies and practices; and
- (b) the size and complexity of the licensed digital bank's operations and business model.

**G** 14.5 For requirements other than those set out in paragraph 14.1, the Bank will apply the requirements applicable to an existing licensed bank or licensed Islamic bank<sup>6</sup> in a manner that is proportionate and commensurate to the risks undertaken by the licensed digital bank.

**S** 14.6 A licensed digital bank shall comply with any additional requirements as specified by the Bank, after having regard to specific risk profile or business model of a licensed digital bank and the Bank's ongoing supervisory monitoring and assessments of the licensed digital bank.

## 15 End of the foundational phase

**G** 15.1 A licensed digital bank may after three years from the commencement of its operations, submit an application to the Bank for the foundational phase to end and for the business limitation to be uplifted.

**G** 15.2 In considering the application under paragraph 15.1, the Bank will assess whether the licensed digital bank has to the Bank's satisfaction—

- (a) complied with all applicable laws and regulatory requirements;
- (b) achieved a minimum amount of capital funds of RM300 million unimpaired by losses; and
- (c) shown satisfactory progress in achieving the committed value propositions as described in its business plan.

**S** 15.3 By the end of the fifth year from the commencement of its operation, a licensed digital bank shall comply with all regulatory requirements applicable to an existing licensed bank or licensed Islamic bank and achieve a minimum amount of capital funds of RM300 million unimpaired by losses. The business limitation referred to under paragraph 13 shall no longer be applicable.

<sup>6</sup> This includes requirements relating to consumer protection and AML/CFT.

- S** 15.4 A licensed digital bank must ensure that systems and processes are put in place to comply with the regulatory requirements specified in paragraph 15.3.
- S** 15.5 Without prejudice to the Bank's power to take an enforcement action against any breaches of this policy document, a licensed digital bank that fails to fulfil the requirements under paragraph 15.2 by the end of the fifth year from the commencement of its operation shall implement its exit plan, failing which enforcement actions may be taken by the Bank, including the revocation of the digital bank's licence.
- G** 15.6 The Bank generally expects for a licensed digital bank to continue serving the underserved or unserved segments as part of its business operations, even after the end of the foundational phase.

## PART D BUSINESS ACTIVITIES AND PRESENCE

### 16 Business of paying or collecting cheques

**G** 16.1 To facilitate the performance of its business of paying or collecting cheques, a licensed digital bank may become a member of e-SPICK or enter into a commercial arrangement to appoint an existing licensed bank or licensed Islamic bank that is an e-SPICK member.

**S** 16.2 For the purpose of paragraph 16.1, the licensed digital bank shall ensure that any of its commercial arrangements comply with all the policy documents applicable to existing licensed banks and licensed Islamic banks including the policy document on *Outsourcing*.

### 17 Physical access points

**S** 17.1 In line with section 46(1) of the Companies Act 2016, a licensed digital bank is required to establish a registered office in Malaysia. A licensed digital bank shall ensure that its registered office sufficiently allows the Bank to communicate with the licensed digital bank during the supervisory process, including for the purposes of examination and engagement with senior management and the board. A licensed digital bank is permitted to establish physical offices for administrative purposes. If the licensed digital bank intends to facilitate face-to-face customer complaints, the registered office and physical offices shall also serve as a centre for this purpose. For the avoidance of doubt, a licensed digital bank is not allowed to establish a branch i.e. a fixed place of business to facilitate customer transactions.

**S** 17.2 The establishment of offices referred to in paragraph 17.1 is subject to the requirements of section 25(1) of the FSA and section 22(1) of the IFSA.

**G** 17.3 A licensed digital bank may participate in the Shared ATM Network and any other cash-out services, as well as enter in commercial arrangements with licensed banks and licensed Islamic banks for the use of the respective banks' network of self-service terminals, including ATMs, cash deposit machines, cash recycler machines and cheque deposit machines.

**S** 17.4 For the purpose of paragraph 17.3, the licensed digital bank shall ensure that any of its commercial arrangements comply with all the policy documents

applicable to existing licensed banks and licensed Islamic banks including the policy document on *Outsourcing*.

**S** 17.5 A licensed digital bank may be permitted to offer banking services through agent banking, subject to the requirements in the policy document on *Agent Banking*. A licensed digital bank may appoint an agent beyond the allowable locations/criteria specified in the policy document on *Agent Banking*. Where an agent is appointed in a location beyond the allowable locations/criteria specified in the policy document on *Agent Banking*, such appointed agent can only perform the services of accepting deposits and facilitating withdrawal of funds for the customers of the licensed digital bank. In view that licensed digital banks are required to offer services wholly or almost wholly through digital or electronic means, reliance on agent, if any, to reach out to the unserved and/or underserved segment shall be minimal and shall not serve as a primary channel for transacting with customers.

## APPENDIX 1 CREDIT RISK COMPONENT OF CAPITAL ADEQUACY FRAMEWORK (RISK-WEIGHTED ASSETS)

### 1 On-balance sheet exposures

**S** 1.1 A licensed digital bank shall apply the risk weight for exposures that are not deducted from regulatory capital as follows—

	Categories of Exposures	Risk weight (%)
(a)	Federal Government of Malaysia and Bank Negara Malaysia	
	(i) Denominated and funded in Ringgit Malaysia	0
	(ii) Denominated in foreign currencies	20
(b)	Cash and gold	0
(c)	Banking institutions	
	(i) Exposure with an original maturity of three months or less <sup>7</sup>	20
(d)	(ii) Exposure with an original maturity of more than three months	50
(e)	Corporates	100
(f)	Small and medium enterprises (SMEs) <sup>8,10</sup>	75
(g)	Retail <sup>9,10</sup>	
	(i) Exposure with an original maturity of more than five years	100
(h)	(ii) Other retail exposure	75
(i)	(i) Retail exposure secured by residential property	
	(ii) Equity	Similar to the existing requirements <sup>11</sup>
(j)	(iii) Defaulted exposure	
	(iv) Exposure to Credit Guarantee Corporation Malaysia Berhad	
(k)	Other assets	100

<sup>7</sup> This excludes exposures which are expected to be rolled-over beyond their original maturity.

<sup>8</sup> Definition of SMEs are as specified in the policy documents on *Capital Adequacy Framework (Basel II – Risk-Weighted Assets)* and *Capital Adequacy Framework for Islamic Banks (Risk-Weighted Assets)*.

<sup>9</sup> Covers exposure to individuals, except those that qualify as exposure to residential property.

<sup>10</sup> For Islamic banking assets, the exposure must be based on either *Murābahah* or *Ijārah* contract or any other Shariah contract provided that the credit risk profile of such exposure is similar to *Murābahah* or *Ijārah* contract.

<sup>11</sup> As specified in the policy documents on *Capital Adequacy Framework (Basel II – Risk-Weighted Assets)* and *Capital Adequacy Framework for Islamic Banks (Risk-Weighted Assets)*.

## 2 Off-balance sheet exposures

**S** 2.1 A licensed digital bank shall apply the credit conversion factors to its off-balance sheet exposures in accordance with the requirements specified in Part B.2.4 of the policy documents on the *Capital Adequacy Framework (Basel II – Risk-Weighted Assets)* and *Capital Adequacy Framework for Islamic Banks (Risk-Weighted Assets)*.

## 3 Credit risk mitigation

**S** 3.1 A licensed digital bank shall ensure that there are no mismatches in maturity<sup>12</sup> or currency between the underlying exposures and the collateral.

**S** 3.2 A licensed digital bank shall only adopt the Simple Approach in the treatment for Credit Risk Mitigation.

### ***Collateralised transactions***

**S** 3.3 A licensed digital bank shall only recognise the following instruments as eligible collateral–

- (a) cash (as well as certificates of deposit or comparable instruments issued by the lending bank) on deposit;
- (b) gold; and
- (c) debt securities issued by the Federal Government of Malaysia or Bank Negara Malaysia.

### ***Guarantees***

**S** 3.4 A licensed digital bank shall only recognise guarantee provided by–

- (a) Federal Government of Malaysia;
- (b) Bank Negara Malaysia; and
- (c) Credit Guarantee Corporation Malaysia Berhad.

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<sup>12</sup> i.e. Residual maturity of a hedge is less than that of the underlying exposure.

## APPENDIX 2 MARKET RISK COMPONENT OF CAPITAL ADEQUACY FRAMEWORK (RISK-WEIGHTED ASSETS)

### 1 Specific risk capital charges

**S** 1.1 In computing the specific risk capital charges, a licensed digital bank shall apply the risk weights as specified below.

Time Bands	6 months or less	>6 months to 1 year	>1 to 2 years	>2 to 5 years	>5 years
Risk Weights for Federal Government of Malaysia and Bank Negara Malaysia Debt Securities			0%		
Risk Weights for Investment Grade Debt Securities <sup>13</sup>	0.25%	1.00%	2.00%	3.50%	4.50%
Unrated and Non-Investment Grade Debt Securities	Classified as banking book exposures				

**S** 1.2 Exposures to unrated and non-investment grade debt securities shall be treated as banking book exposures and subject to the applicable risk weights as set out in Appendix 1.

### 2 General risk capital charges

**S** 2.1 A licensed digital bank shall use the maturity method<sup>14</sup> in computing the general interest/profit rate risk charge.

**S** 2.2 A licensed digital bank shall compute the total general interest/profit rate risk charge as the sum of the following two components—

<sup>13</sup> This includes investment grade foreign sovereign debt securities.

<sup>14</sup> Refer to paragraphs 5.64 to 5.69 of the policy document on *Capital Adequacy Framework (Basel II – Risk-Weighted Assets)* and paragraphs 5.53 to 5.58 of the policy document on *Capital Adequacy Framework for Islamic Banks (Risk-Weighted Assets)*.

- (a) the overall net open position charge<sup>15</sup>; and
- (b) the vertical disallowance<sup>16</sup> of 10%.

2.3 In computing the overall net open position component under paragraph 2.2(a), a licensed digital bank shall apply the risk weights specified below.

Time Bands	6 months or less	>6 months to 1 year	>1 to 2 years	>2 to 5 years	>5 years
Risk Weights	0.20%	0.80%	1.30%	2.70%	6.00%

<sup>15</sup> This is computed by summing the weighted net positions of each time band. The weighted net position in each time band is the net position multiplied by the relevant risk weight as specified in paragraph 2.3 of Appendix 2.

<sup>16</sup> This is computed by weighting the smaller of the absolute values of the long and short positions in each time band (i.e. hedged positions) with the relevant risk weight.