



PLAN TO INTRODUCE INTERNET-ONLY BANKS IN KOREA

The FSC announced its detailed plan to introduce Internet-only banks in Korea to enable financial consumers to use more convenient banking services at lower costs and to promote competition and innovation in the banking sector.

KEY POINTS

- ✓ Lower entry barriers and minimize 'ex-ante' regulations to attract more players and encourage diverse, innovative business models
- ✓ Take a two-track approach: (i) pilot operation of one or two Internet-only banks under the current Banking Act; (ii) additional licenses for more diverse companies after a revision to the Banking Act to ease the restriction on shareholding by non-financial companies for Internet-only banks
- ✓ The FSC plans to announce a guideline for an Internet-only banking approval in July, begin to receive applications in September and grant a preliminary license for one or two Internet-only banks by the end of this year.

DETAILED PLAN

1. Easing of shareholding restriction

The current Banking Act bans non-financial companies from holding more than 4% of shares in a bank.¹ The restriction makes it impossible for ICT companies to enter banking business. Therefore, the FSC will ease the restriction on shareholding by non-financial companies² from the current 4% to 50% only for Internet-only banks.

Supplementary measures will be devised to pre-empt possible side effects of easing shareholding restriction. Out of non-financial companies, business groups subject to cross-shareholding restrictions³ will be exempted from the eased shareholding regulation to prevent only a few conglomerates from exercising too much economic control. The FSC will raise the ceiling of shareholding by non-financial companies to a 50% stake necessary for controlling

¹ Article 16-2 of the Banking Act

² 'non-financial business operator' under Article 2.9 of the Banking Act

³ As of end-2014, 61 companies with assets more than 5 trillion won are designated as 'business groups subject to cross-shareholding restrictions.' Among them, those who are not deemed 'non-financial' are not subject to the 4% shareholding restriction under the current Banking Act.

power over management while keeping them in check by other shareholders.⁴ To avoid a conflict of interest, Internet-only banks will be subject to stricter regulations in regard with a large shareholder. The credit ceiling that a bank can provide its large shareholder will be cut from the current 25% of the bank's equity capital to 10%. Internet-only banks will be prohibited from acquiring shares issued by a large shareholder.

2. Equity capital requirement

The minimum equity capital requirement will be lowered to KRW 50 billion for an Internet-only bank, half of the requirement for a commercial bank under the current Banking Act.

3. Business scope

Internet-only banks will be allowed to engage in businesses same as commercial banks do.⁵

4. Prudential regulations

In principle, Internet-only banks will be subject to the same regulations on financial soundness and business operations as commercial banks. However, they will be granted a grace period for some regulations that could be excessive burden in the early stage of operation. For example, Basel I standards will be applied to Internet-only banks in regard with BIS capital requirements, while Basel III standards are applied to commercial banks. Regarding liquidity coverage ratios, Internet-only banks will be required to meet 60%, while commercial banks are required to meet 80% in 2015 and 100% by 2019. After the grace period, such regulations will be gradually strengthened to the levels of commercial banks.

5. Outsourcing of IT Facilities, etc.

Outsourcing

Internet-only banks will be allowed to outsource their IT facilities to IT companies to reduce initial costs.⁶

Credit card business

Internet-only banks will be allowed to engage in credit card business as concurrent service.

Non-face-to-face identification

The FSC has decided in May to loosen the strict requirement of face-to-face identification when customers open a new bank account by allowing alternative methods of non-face-to-face identification.⁷ The eased identification rules, expected to be implemented from December this year, will facilitate the establishment of Internet-only banks.

⁴ The Commercial Act(Article 434) requires affirmative votes by more than two thirds shareholders to make a critical decision in management at a general shareholders' meeting.

⁵ Articles 27, 27-2, 28 of the Banking Act

⁶ Notice of Revision to 「Regulation on Financial Institutions' Outsourcing of Data Processing Business & IT Facilities」 (press release, June 10)

⁷ Banks will be required to choose at least two out of four alternative methods of non-face-to-face identification: (i) a copy of ID cards, (ii) video call, (iii) ID verification upon delivery of a debit card, or (iv) use of information on existing accounts

6. Regulatory approval

The same standards under the current Regulation on Supervision of Banking Business will be applied to Internet-only banks. However, given the purpose of introducing Internet-only banks, review will be focused on the following factors: (i) innovativeness of business plan, (ii) stability of business model, (iii) consumer convenience, (iv) contribution to competitiveness of Korea's financial sector and (v) possibility of global expansion. Supplementary criteria will be added for an Internet-only bank to review whether it has a proper response system in emergencies such as electronic failures or whether large shareholders have a proper plan to recapitalize in the case of liquidity crunch. A detailed guideline will be out in July.

SCHEDULE

Step1: Pilot operation

The FSC plans to grant a preliminary license to one or two Internet-only banks under the current Banking Act within this year as pilot cases to test the viability of Internet-only banking business.

- ✓ Present a detailed guideline on regulatory approval (July 2015)
- ✓ Receive applications for preliminary license (September 2015)
- ✓ Review for regulatory approval (October - November 2015)
- ✓ Grant a preliminary license (December 2015)
- ✓ Issue a license for Internet-only banking business (1st half of 2016)

Step2: Revision to Banking Act

The FSC will push forward a revision to the Banking Act to ease the ban on shareholding by non-financial company to attract more diverse business providers into banking business.

- ✓ Draft a revision bill to the Banking Act (June - July 2015)
- ✓ Discuss the revision bill in the regular session of the National Assembly (Sept. 2015)
- ✓ Receive applications and grant preliminary license (within 6 months after the revised Banking Act would take effect)

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