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Executive Summary

Fintech opportunities and challenges in the Malaysian capital market

The Fintech revolution has come of age globally. This issue of *The Reporter* focuses on Fintech and explores its outlook for the Malaysian capital market, and what market participants can accomplish from Fintech. It also discusses how market participants can utilise RegTech, technological innovations for regulatory compliance, to meet and reduce the costs of meeting regulatory requirements.

The lead article further discusses:

- Initiatives that the SC has introduced to facilitate full adoption of digital technology and innovation across the Malaysian capital market;
- The SC's concerns and assessment on the emergence of Fintech, and makes practical suggestions for intermediaries, investors and issuers on what can be done to benefit most from the Fintech revolution; and
- Useful reminders on what to look out for to protect yourself from scams and fraudulent activities.

We hope you will find the articles in this issue informative and helpful. As always, we would like to hear from you. If you have any comments, feedback or ideas for future editions, please email the Editorial Team at reporter@seccom.com.my

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Opportunities and Challenges: Financial innovation and the Fintech landscape in Malaysian Capital Market

Background

Fintech – technology in financial services, until recently, has been focusing mainly in the areas of payments, deposits and remittances, i.e. in the retail banking segment of the financial services industry. However, over the last few years, there has been an expansion of Fintech activities into other segments of the financial services industry e.g. insurance and the capital markets. For example, the auto insurance companies have started using new technology, where they take into account current driving habits of customers instead of depending solely on customers' past driving records, when pricing and quoting insurance premiums. Investment banks have begun using Fintech applications as part of a solution to create new product offerings and enhance service delivery. Fund managers and asset-management companies are embracing innovations such as robo-advisors, to gain an edge to generate alpha over their competitors. Meanwhile, securities brokers have introduced integrated and innovative online brokerages, to increase revenue and gain customer loyalty.

This article explores growth opportunities that the Malaysian capital market and market participants can get out from Fintech. It also discusses how market participants can utilise Regtech to meet and reduce the costs of meeting regulatory requirements.

Lastly, the article highlights concerns of the SC and SC's assessment on the impact of the emergence of Fintech in the capital markets to the investors, market participants and market institutions.

> "Investment banks have begun using Fintech applications as part of a solution to create new product offerings and enhance service delivery."

Driving factors of Fintech in recent years

Various factors have come together, at first gradually and then suddenly, to result in what we now witness as a surge of technological innovations occurring in the financial sector shortly after the global financial crisis (GFC) of 2007-2008, more notably, in the last few years. Practitioners, intellectuals and financial literature writers commonly group these factors into the following dynamics:

- First, there has been a sharp increase in technological capabilities coupled with an attendant decrease in costs. This is evident in the increase in computing capacity of computers as well as other online and communication devices (such as smart phones and tablets) to process and store large volume of data, which combined nicely with sharp falls in the costs of hardware, software and storage of data;

- Second, the effect of 'innovation spiral' has played out most prominently in the tech-industry. This spiral effect is major as an invention of one technology that may or may not be successful commercially, can become an important driver to condition further product market innovation that becomes more useful or more successful. The 'innovation spiral' effect spawned by the tech-industry has extended to and is a significant driver that fuels better market innovation and product evolution in the financial services sector. Such development only goes to prove the adage that innovation is not a linear process but a continuous cycle where inputs from difference places and parties can be leveraged by various other parties, including regulators and businesses to meet own needs. For example, distributed ledger technology (DLT) has created much interest in the financial services industry as it projects a huge potential to change the way we carry out and record transactions in a decentralised and secured manner, without having to go through a central authority. Potential areas identified for DLT application in the capital markets are, for now, in the areas of securities trading, clearing and settlement. Regulators have also started mulling over whether they could use the same technology to plug into the network of financial institutions (FIs) to conduct risks surveillance and track transactions to detect anti-money laundering and counter-terrorist financing (AML-CTF).

- Third, the withdrawal of traditional FIs from some segments of the financial markets after GFC has opened a door of opportunity to new entrants. For example, the retreat of many traditional banks from certain risky lending activities (owing to more stringent capital requirements and rigorous risk management post GFC) is the window allowing online platform-lenders to occupy that space. Often these entrants arrive with novel idea of providing a service the incumbents may have overlooked or did not contemplate possible. New entrants like Fintech firms have an advantage as they often come unburdened by regulatory incumbency, compliance costs and capital requirements, or having to deal with legacy systems, processes and infrastructure. As a result, Fintech firms are more able to move faster, focus their resources on developing solutions and compete directly with traditional financial service providers. A number of these new entrants were able to scale up quickly using new technology before traditional service providers have time to defend their turf, much less consider any counter-attack or strike-back strategy;

- Fourth, consumer trust in traditional FIs e.g. the banks has been on a decline since the GFC erupted in 2007-2008. This is significant, as it is the trust that has hitherto acted as a barrier to entry for new entrants to financial services industry. Consumers blame the financiers and their insatiable greed to maximise profits as the main cause of GFC that had caused havoc to the financial system and in doing so brought about a global economic downturn and hardship to many. As a result, consumers are more willing to engage services of new entrants. More crucially, they are more willing to use new specialist-providers on specific services on an

“The innovation spiral effect spawned by the tech-industry has extended to and is a significant driver that fuels better market innovation and product evolution in the financial services sector.”

'a la carte' basis, (e.g. on payments, saving and investment products) that were previously offered by a single bank. The negative consumer sentiments towards traditional FIs is most notable in developed markets like the US and Europe where the financial crisis began and accelerated, and where there had been huge taxpayer-financed bailouts; and

- Fifth, the increasingly wider access to internet connections and spread of high-speed mobile devices world-wide allowing real-time transactions to take place on the go at any time, have provided consumers a totally new and enhanced customer experience. More crucially, the distribution efficiency of the web, the proliferation of websites and the exponential growth of social media from a passing trend to global obsession, have empowered consumers by the ease of sharing of digestible financial education/information to a much wider audience on the net and the quick access to choices of financial products and services. Consumers now feel they have the power to make a Buy decision, rather than being Sold financial products.

This experience has given rise to higher customer expectations with regard to convenience, speed, costs and user-friendliness of online financial services, which has in turn become one of the most important factors in transforming consumer purchasing-decisions on products and services. Furthermore, as consumers become increasingly accustomed to using online devices to undertake financial transactions, they are more willing to log on and use other services and new product offerings of these new entrants.

Thus, much like a symphony with multiple and distinct movements and instruments, all of the above dynamics have worked together to result in what seems like a sudden surge of Fintech activities in various aspects of financial services sector in recent years, which evolution has in actual fact begun decades ago when one looks closer.

Fintech outlook for the Malaysian capital market

If we view Fintech as a movement that has brought about transformative changes to the financial services industry globally in a way that has not happened before, we must then ask ourselves, "What is Malaysia's Fintech journey, where we are, what is next?"

Fintech has become one of the biggest growth industries in the world. According to the latest analysis by Accenture on the data published by CB Insights (a global finance data and analytics firm), investment in Fintech ventures reached an all-time high in 2017, buoyed by a surge in funding for start-ups in the US, UK and India.[1]

"...investment in Fintech ventures reached an all-time high in 2017, buoyed by a surge in funding for start-ups in the US, UK and India."

[1] https://newsroom.accenture.com/news/global-venture-capital-investment-in-Fintech-industry-set-record-in-2017-driven-by-surge-in-india-us-and-uk-accenture-analysis-finds.htm

Another report dated 2017 indicates that[2]:

- In May 2016, London was ranked as the largest Fintech hub in the world, employing 61,000 people and generating £6.6 billion (US$8.5 billion) in revenue. The report states further that the UK government's support for Fintech sector remained strong even in the post-Brexit era; and
- In 2016, 35 New York Fintech companies have raised financing US$59 million. It was reported that in New York the average early-stage funding per start-up was US$568,000, more than double of global average amounting US$252,000 per start-up.

The data tells us one thing: while nobody can predict precisely how Fintech will change the future of the financial services sector, investors' interest are high in the Fintech sector as shown by the amount of venture capital pumped into the sector. In view of the venture investors' interest in the Fintech sector, we can only expect more innovations and cutting-edge technologies coming out of Fintech labs and hubs, and flowing into and disrupting the financial services sector further. The only question is how fast.

In the Asia-Pacific region alone, we see a flourishing of activities taking place where large sums of venture money have flowed into investing in the future of Fintech. Though these ventures are driven by the private sector, they are eagerly supported by the public sector:

- In 2014, Hong Kong launched a new Asia-Pacific Fintech Innovation Lab, where eight start-ups offering a wide range of solutions from security to analysis and risks were selected to participate in the Lab. The Lab is a 12-week annual programme that helps early-and growth-stage Fintech entrepreneurs to gain exposure to top financial institution executives' thoughts, ideas and mentorship. The Lab marks its fifth year of operation into 2018 with alumni participants having raised up to US$288 million as at 2017;

- In 2015, Sydney launched a Financial Services Knowledge Hub to provide start-ups with office space, mentoring, networking, export support and opportunities to access capital. In terms of growth figures, the number of Fintech start-ups in Australia has increased from less than 100 in 2014 to 579 companies as at July 2017. In addition, the latest numbers indicate that Fintech investment in Australia has remained steady with US$675 million invested across 25 deals in 2016;

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[2] https://assets.kpmg.com/content/dam/kpmg/au/pdf/2017/scaling-Fintech-opportunity-sydney-australia.pdf

- In Singapore, the Monetary Authority of Singapore (MAS) has established a new Fintech & Innovation Group (FTIG) within its own organisation structure in August 2015. The FTIG is tasked to develop regulatory policies and strategies to facilitate the use of technology and innovation in managing risks and strengthening competitiveness in the financial sector. MAS also announced its commitment of SGD225 million (US$160 million) worth of fund to be disbursed over a period of five years from 2015 to 2020, to support the private sector in creating a vibrant innovation ecosystem in Singapore. The fund targets three core areas:

1. Attract FIs to set up their R&D and innovation labs in Singapore.
2. Catalyse the development of innovative solutions that can potentially promote FI's growth, efficiency and competitiveness.
3. Support the building of industry-wide technology infrastructure required for the delivery of new and integrated services in Singapore financial services industry.

The SC's initiatives in Fintech

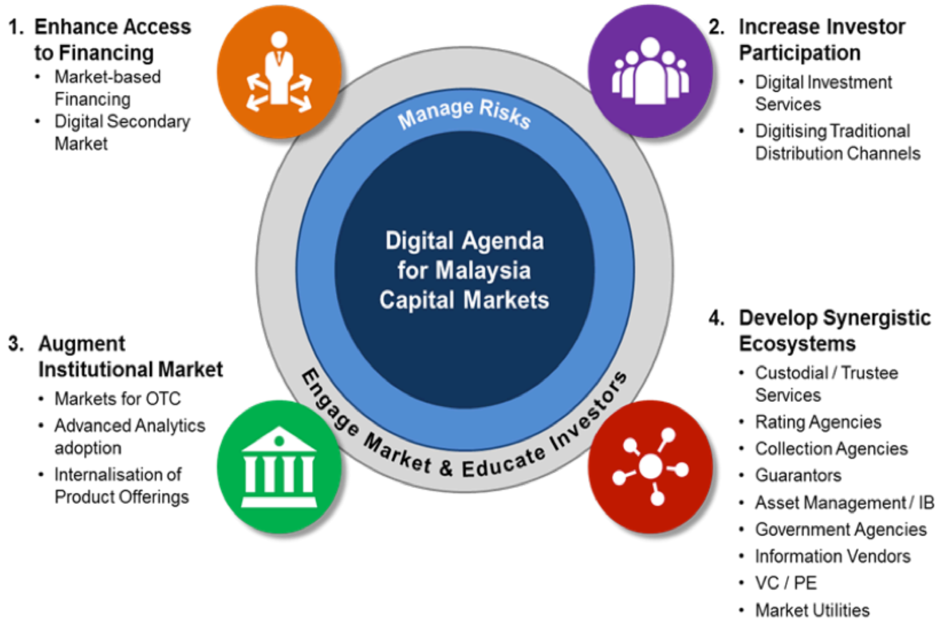
- In 2014, the SC hosted a public conference called **SCxSC** to generate interest and create awareness among local tech firms and enthusiasts, the investing public including business world at large, on the potential of using technologies and innovations to tap the Malaysian capital markets for funding. This annual public conference marks the SC's first attempt to reach out and bring together all stakeholders of digital finance i.e. the issuers, Fintech firms, angel investors, venture companies and retail investors, to one forum. This annual event has created much hypes among all stakeholders and more importantly, it serves to raise profiles of the local niche growth sectors and attract Fintech talents and vital capital to our ecosystems;

- In 2016, the SC published an agenda on Fintech by sharing with market participants a comprehensive plan called **Digital Agenda for Malaysia's Capital Market**[3]. The plan is a roadmap that sets out the SC's vision for a holistic development of Fintech for the Malaysian capital markets. It identified four strategic objectives that the SC seeks to achieve, in facilitating full adoption of digital technology and innovation across the entire capital markets, and underpinned by a three-pronged regulatory principles of managing risks, engaging markets, and educating investors. Diagram below presents a snapshot of the SC's Digital Agenda:

"The plan is a roadmap that sets out the SC's vision for a holistic development of Fintech for the Malaysian capital markets."

[3] For more information on the digital agenda, please refer to the SC's *2016 Annual Report*.

Diagram 1:



- Prior to rolling out the Digital Agenda, Malaysia became the first ASEAN country to introduce a legal framework on Equity Crowdfunding (ECF) when the SC released its ECF regulatory framework in February 2015. The framework was well received with keen interest in the new framework from among start-ups and incumbent market participants. In June 2015, the SC announced the approval of seven ECF operators in the country as 'recognised market operators'. They were selected from a list of 27 applicants and the selection process assessed, among others, the ability of the approved operators to bring unique strength, expertise and different flavour to our capital markets;

- In August 2016, the SC followed up with a legal framework on peer-to-peer debt financing (P2P). Both the ECF and P2P regulatory frameworks were introduced to encourage and enhance access to capital market financing by smaller enterprises, particularly micro, small and medium enterprises (MSMEs).[4]

The ECF and P2P frameworks have gained traction especially among start-ups and MSMEs. They have proven to be viable alternative routes to fundraising for smaller enterprises from our capital markets. These new avenues also provide retail as well as sophisticated investors with an alternative channel for investment. More significantly, both the online fundraising platforms have attracted a strong following of young investors of less than 35 years old. Both these alternative online platforms have seen 38% youth participation compared to the traditional stock market where youth participation on Bursa Malaysia is just over 20%.

“The ECF and P2P frameworks have gained traction especially among start-ups and MSMEs.”

[4] For more information on ECF and P2P, please refer to the April 2016 and January 2017 issues of *The Reporter* respectively

Key statistics on the performance of ECF and P2P are summarised below:

Alternative Market-based Financing Avenues

1,200 Successful deals across ECF and P2P Financing
ECF: 40 campaigns
P2P: 1,160 campaigns

309 MSMEs successfully raised funds
ECF: 40 issuers
P2P: 296 unique issuers

118M Total funds raised thus far across ECF and P2P
ECF: RM38 million
P2P: RM80 million

75% Issuers have women or youth founders

5,000 Investors participating in ECP and P2P

38% of participating investors are less than 35 years old

- Recognising the early success of this segment, the Malaysia Government has announced in Budget 2019 the establishment of a RM50 million Co-Investment Fund (CIF) to be co-invested in MSMEs alongside private investors through ECF and P2P platforms. The CIF will leverage the collective wisdom of the crowd and will only co-invest in MSMEs that have gained significant traction with private investors. Doing so will allow for greater transparency on how the funds are utilised, where the CIF is targeted to be eventually self-sustaining on the returns generated from its investors.

- In 2015, the SC initiated the setting up of an industry-wide networking group called **aFINity** (Alliance of Fintech Community) to spur further financial innovations and depth to our capital markets. aFINity is a developmental cum advocate group led by the industry. The SC supports aFINity by providing policy and regulatory clarity, and facilitating Fintech discussions with other relevant authorities and government agencies, with the objective to help Fintech entrepreneurs move up the value-chain from solutions-designing, setting up businesses to commercialising innovations. Since the launch, aFINity now counts for more than 200 registered industry participants drawing from existing market participants, techno-preneurs and start-ups as well as from the surrounding ecosystem players.

  The SC has facilitated more than 100 engagement sessions with aFINity since its inception on a wide range of topics, which included larger community-wide information sharing, targeted focus group discussion, to even one-on-one engagement. The SC continues to encourage financial services community, innovation community, researchers and academia, and Fintech start-ups including industry

“The SC has facilitated more than 100 engagement sessions with aFINity.”

experts and emerging disruptors, to use this network to link up and explore insights and opportunities for more mutually beneficial collaborative actions;

- In May 2017, the SC launched the Digital Investment Management (DIM) framework to give retail investors access to specialist services of investment management industry i.e. the portfolio management services. Traditionally, only high net worth (HNW) investors get to access and enjoy professional services of portfolio managers. The DIM regulatory framework democratises it by allowing the offering of automated portfolio management services to all Malaysian, regardless of their net-worth or income level. The idea is to liberalise the retail investment framework at low costs and in an affordable manner without compromising safeguards for investor protection. So far, the SC has registered one DIM operator.

Where are we at now?

The Fintech movement and disruptive innovations it brings about has indeed reshaped the way financial services are structured, provisioned and consumed globally. It has forced open the capital markets to serve a wider cross-section of issuers and investors than ever before imagined. In Malaysia, new business models using innovative technology platforms such as ECF, P2P and DIM are just some of the financial services and channels that the SC has facilitated, as part of the overall initiatives to continuously grow and develop our Malaysian capital markets. We anticipate more innovative Fintech entrepreneurs coming to Malaysian shores to tap on hitherto untapped segments of the Malaysian capital market, e.g. the segments on financial planning, investment advice, social investing and automated trading space.

For completeness, other innovations that have come before the SC for approval and/or consultation are summarised below:

- In April 2017, the SC approved Rakuten Trade, the first digital only equities broker for the Malaysian market. Rakuten Trade has received positive response from investors since its launch with more than 10,000 accounts opened by end 2017. More encouragingly, a big portion of these are new-to-market investors.
- Stockbit, an Indonesian start-up has arrived at our shore in early 2018 with an investment-focused social media platform that aims at facilitating public-listed companies (PLCs), equities analysts, investors' engagement and exchange of information on its social media page.
- In July 2018, the Financial Planning Association of Malaysia (FPAM) has launched Smartfinance.my, a digital portal with attached tools that allow consumers to gain a snapshot of their current financial position and connect users with licensed financial planners.

The emergence of other innovations such as cryptocurrencies and initial coin offerings (ICOs) has unleashed a renewed wave of interest, notably among retail interest on investment activities. Cryptocurrencies and ICOs are digital assets and a new method of financing for start-ups and new businesses where digital tokens or coins are issued to raise funding, instead of these enterprises having to turn to traditional funding avenues such as public stock markets, private equities (PEs) or venture capitals. We note from the engagements the SC had with the industry and the volume of queries received on cryptocurrencies and ICOs from various parties that there are keen interest in the investment and trading of digital assets.

What's Next: An Expanded Horizon for Incumbents

While the recent financial innovation brings in new entrants, which means increased competition for incumbents, it also brings about an opportunity for incumbents to rethink their business models and strategy. Yes, incumbents may have misgivings on this development, however as more technologies become available in the market, these technologies could become new tools to be leveraged by incumbents to evolve their own product offerings and improve service delivery to protect their core business from further erosion. The development also serves as a good reminder for incumbents to review how they conduct business compared with new entrants in order to stay nimble, efficient and on top of the game.

Some incumbents are already taking advantage of the proliferation of digital devices as an opportunity to capture and engage with clients in building stronger relationships and enhance 'stickiness' i.e. creating longer-term customer loyalty. Others responded to the shift in customer behaviour by improving product offerings towards more customisation and personalisation. As social media become more common and pervasive in consumers' everyday life, we also see market participants responded by using social media more extensively as a marketing tool and a feedback loop when engaging clients while some firms have started experimenting with chatbots for customer servicing. These initiatives are already happening in Malaysia. Globally, some markets have evolved where market participants have moved towards pure digital, self-directed offerings while others are equipping their sales-force with digital tools to enhance marketing capabilities. We are seeing the emergence of this trend in Malaysia as well, and expect further adoption in years to come.

> "Some incumbents are already taking advantage of the proliferation of digital devices as an opportunity to capture and engage with clients in building stronger relationships and enhance 'stickiness' i.e. creating longer-term customer loyalty."

The potential for Fintech to drastically improve the middle-and-back office are often not stressed enough. While cost reduction and regulatory compliance remain a priority for market participants, the two objectives can be met with the help of technology. There can indeed be lessons learned from start-ups in running lean and efficient operations, enabled by technology. It could be as simple as getting systems to become more integrated to enable straight-through processing, deploying bots to automate repetitive tasks, using biometric information for identity verification, or even leveraging artificial intelligence (AI) and analytics for better risk management.

As technologies allow operations to scale efficiently, we also see the emergence of market utility firms whether in know-your client (KYC) best practices, post-trade reporting or other areas, to service incumbents. A *September 2018 Report* published by the Financial Industry Regulatory Authority (FINRA)[5] showed that a growing number of Fintech start-ups have leveraged a variety of innovative technologies to assist incumbent providers in cutting costs and reducing compliance burden. Some incumbents are seen developing a variety of Regtech tools in-house, in meeting their compliance obligations particularly in the compliance of KYC and AMLA-CTC.[6] Regtech solutions are getting popular among financial service providers as they offer higher level of information accuracy, granularity and availability, which help to improve incumbents' responsiveness to regulatory changes and in monitoring systemic risk, which in turn brings uniformity to risk management and regulatory reporting. For example, in the same report several market participants have noted significant reductions in false alerts generated by their surveillance systems after utilising Regtech tools.

Besides market participants, Fintech innovations have also made inroads into market infrastructure institutions i.e. the exchanges and other trading avenues, central counterparty clearing-houses (CCPs), securities depositories and index providers that have provided essential infrastructure for the efficient operation of a modern capital market. A 2018 joint report by World Federation of Exchanges (WFE) and McKinsey & Company indicates that Fintech-led innovations are already found across the entire capital market infrastructure value chain. Market institutions are advised to adopt a focused and proactive approach when considering how best to engage and work with Fintech companies, to drive further capital market efficiency.[7]

While incumbents will struggle with legacy processes, systems and infrastructure, it is important that incumbents recognise that their entrenched position also means it comes with a trove of data stretching back decades. How they use and mine these untapped data for strong actionable business insights could potentially be a key differentiator for incumbents. The idea is to take advantage of Fintech by modernising existing business operations and generate new sources of revenue by exploring and capturing new business opportunities through Fintech.

Given the sweeping scope of change and the nascent demand in the Malaysian capital market, we believe collaboration between industry participants, both incumbents and new entrants, is key. The SC continues to encourage the industry to explore mutually beneficial partnerships, collaborations and arrangements to deliver the greatest value and experience to our investors and issuers.

"As technologies allow operations to scale efficiently, we also see the emergence of market utility firms whether in know-your client (KYC) best practices, post-trade reporting or other areas, to service incumbents."

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5 FINRA is a self-regulatory body that provides first line of oversight over broker-dealers firms and professionals who deal in securities in the US markets

6 http://www.finra.org/sites/default/files/2018_RegTech_Report.pdf

7 https://focus.world-exchanges.org/articles/wfe-mckinsey-joint-report-fintech-capital-markets-infrastructure-industry-reveals-likely-future-innovations-opportunities

Regulatory concerns

While we look forward to the promises in which Fintech can potentially deliver to improve ways in which the financial system operates to make our capital markets a more inclusive and vibrant marketplace, at the same time, we are aware that such promises are not without risks. These potential risks include:

Cyber security and privacy protection – As Fintech's growth largely involves growth using online platforms, it makes this industry uniquely vulnerable to security breaches. Incidents of security breaches at large companies like Yahoo, Uber, Equifax and Google resulting in privacy of customers' personal data being compromised, only add to the worries. Until Fintech firms upgrade their security architecture on data protection and compliance, cyber security will remain a concern to regulators;

AML and cross-border transactions – Convenience and fast transactions is much more complex in cross-border transactions as recipient identification relies on processes in another country. Thus, the standard of regulations on AML-CTF of a country, and capacity of Fintech firms to comply with AML-CTF regulations will continue to be a regulatory concern. The FATF, the international body responsible for combating money laundering, has been spearheading efforts to prevent the misuse of virtual assets (such as virtual currencies, wallet providers and ICOs) for financing illicit activities. This includes enhancing its existing standards to ensure virtual asset service providers are subject to AML-CFT regulations which involves monitoring, record-keeping and reporting of suspicious transactions;

Corporate governance (CG) – Compliance culture of tech firms that are now operating in the space of financial sector will be a concern to regulators as tech firm have been operating in less regulated environment, and may not have cultivated the stringent compliance culture required to operate in a highly regulated environment like the financial sector. The recent failure of the founder cum chief executive of the largest online P2P lender, Lending Club, to disclose personal interest in a sale of loans to a big investor, is a highly publicised governance breach that serves to intensify the point; and

Investor education – Investors need better education and constant reminders on the fundamental correlation between investment risk and returns so that they are not blindsided by the appeal and shine of new technologies. The dotcom bubble of the late '90s is a good reminder of hypes over information technology resulting in exuberant and excessive speculation by investors on dotcom stocks. Recent reports on thousands of retail investors across China suffering losses as fraudulent Chinese P2P platform lenders collapsed in the midst of tighter regulatory environment, only goes to expose the vulnerability of retail investors and the need for regulators to continuously enhance investor education programmes.

> "Fintech can potentially deliver to improve ways in which the financial system operates to make our capital markets a more inclusive and vibrant marketplace."

Final Thoughts

As regulator of the Malaysian capital market, the SC is responsible for designing and supervising rules of conduct by which market participants operate. These rules are aimed at minimising harm to investors, market participants and systems. In return for gaining access to the markets, market participants are obligated to observe regulatory standards when dealing with clients, or suffer penalties and other more stringent sanctions including suspension and revocation of licence or registration.

We are aware that as regulator our level of understanding and how we respond to market innovations will be of interest to market participants. While we continue to be flexible and adaptive to market developments, the safety and investor protection will remain as imperatives. For the orderly development of the Malaysian capital market, the SC will continue to facilitate innovative financing activities only if they meet the needs of the market with appropriate safeguards in place for investor protection and market stability. We continue to work to understand the kind of risks that new entrants may introduce and remain cautious in allowing innovations where the operators cannot demonstrate minimum fit and proper attributes, or articulate a viable business plan. Of equal importance is to see existing market participants and new entrants make it a part of their business strategy to give consumers better service, experience and outcome in undertaking capital market activities.

Message to Intermediaries

1. Be mindful of addressing the risks of your services or products being exploited by unscrupulous parties. This include having robust AML-CFT process in place to address the risk of misuse of virtual financial products and services for illicit activities. Cyber security and governance should also be focused upon to combat risks of being a victim of cyber security breaches and data theft.

2. Ensure good corporate governance and compliance practices are in place from the very outset. As the Fintech arena is coming under increasing scrutiny by regulators and it is best to cultivate a high culture of compliance in order to succeed in the longer term.

3. While pursuing the next wave or breakthrough, technology firms should focus on how it can best serve the needs of the investors, especially where retail investors are involved, as well as focus on providing a seamless investing experience. For new products and services, this also includes running investor education programmes, as well as using innovative channels to deliver education messages, in order to help investors understand the opportunities and risks of using Fintech products and services.

Message to Investors and Issuers

1. Through the digital agenda, new innovative avenues for fundraising and investments such as ECF, P2P, DIM and digital stockbroking are being introduced to the Malaysian capital market. We encourage you to explore these new avenues to see if any of these meet your fundraising and investment needs.

2. At the same time, before investing or fundraising, do check that the digital platform or operator of your choice is registered with the SC. An up to date list is published on the SC's website at https://www.sc.com.my/digital/list_rmo/

3. For issuers, understand that fundraising from the public through ECF or P2P is a regulated activity and a serious exercise. Be prepared by:

   a. Understanding your obligations to new shareholders or debtors;
   b. Having your company's financial information in good order;
   c. Crafting a holistic business plan outlining the company's goals;
   d. Planning for how the newly raised funds will be utilised; and
   e. Getting ready to pitch your business and value proposition to potential investors.

4. For investors, as these are new products and services being introduced to the market:

   a. Be sure to ascertain your own risk profile. Only choose products and services which commensurate with the investment risk you are willing to take;
   b. If you are investing in a company through ECF or P2P, understand your rights as a shareholder or debtor; and
   c. If you are using the services of a digital stockbroker or DIM, read the relevant disclosures to understand the nature of the service provided and fees involved before signing up.

Message to Investors and Issuers *(continued)*

5. There could be government incentives offered related to these digital businesses, for example the Malaysian Business Angels Network (MBAN) Tax Incentive which covers angel investors participating in ECF. Issuers and investors should take the opportunity to benefit from these incentives.

6. All licensed or registered digital platform operators are members of the Securities Industry Dispute Resolution Center (SIDREC). If there are any disputes arising between investors or issuers with the operators which cannot be resolved bilaterally, the case can be brought up to SIDREC.

Administrative Actions and Supervisory Engagements

ADMINISTRATIVE ACTIONS

For the period of 1 January 2018 to 30 June 2018, the SC has imposed 34 administrative actions against:

- 7 Capital Markets Services Licence holders;
- 3 public-listed companies (PLC);
- 1 licensed person; and
- 12 individuals.

The sanctions were imposed for breaches relating to the SC's guidelines and licensing conditions, as well as non-compliances with approved accounting standards.

Table 1

Administrative actions from 1 January 2018 to 30 June 2018 by types of sanction and parties in breach

Parties in breach	Types of sanction				
	Directive	Reprimand	Penalty	Suspension/ revocation of licence	Public Statement
CMSL holders	–	–	7	–	–
PLCs	3	3	–	–	–
Listed person	–	–	1	1	–
Individuals	–	12	5	–	2
TOTAL	**3**	**15**	**13**	**1**	**2**

Table 2

Penalties imposed from 1 January 2018 to 30 June 2018

Party in breach	Amount (RM)
Shaiful Nazren Kassim	123,750
MTC Asset Management (M) Sdn Bhd	2,000
AmFunds Management Bhd	2,000
AmIslamic Funds Management Sdn Bhd	1,000
RHB Asset Management Sdn Bhd	3,000
Dato' Sri Liew Kuek Hin	392,000
Huang Yan Teo	392,000
Leslie Looi Meng	392,000
Dato' Sri Liew Yew Chung	343,000
Liew Yet Mei	343,000
HSBC Bank Malaysia Bhd	8,000
HSBC Amanah Malaysia Bhd	1,000
Muamalat Invest Sdn Bhd	1,000
TOTAL	**2,003,750**

Enforcing requirements under the LOLA Framework

The *Guidelines on Unlisted Capital Market Products under the Lodge and Launch Framework* (LOLA Guidelines) require an issuer of a wholesale fund to submit to the SC monthly statistical returns of the wholesale fund within the period prescribed in the LOLA Guidelines. For this reporting period, we have imposed a penalty of RM1,000 for each day of delay per fund on the following fund management companies for their failure to submit monthly statistical returns of wholesale fund as required under the LOLA Guidelines:

- MTC Asset Management (M) Sdn Bhd;
- AmFunds Management Bhd;
- AmIslamic Funds Management Bhd;
- RHB Asset Management Sdn Bhd; and
- Muamalat Invest Sdn Bhd.

The LOLA Guidelines also require an issuer of a structured product to submit to the SC a monthly post-issuance report within the guidelines' prescribed period. On this matter, HSBC Bank Malaysia Bhd and HSBC Amanah Malaysia Bhd were imposed a penalty of RM8,000 and RM1,000 respectively due to delayed submission of their monthly post-issuance reports to the SC.

Observing Fit and Proper Requirements for CMSRL Holders

The SC is vigilant in ensuring that the licence holders remain fit and proper. CMSRL holders are expected to meet the SC's requirements in conducting their respective regulated activities.

In relation to this, the SC has taken an action again Shaiful Nazreen Kassim, a CMSRL holder, for conducting discretionary trading of three clients' account without obtaining prior approval from the senior management of his stockbroking company. He has failed to fulfil a client's requests, including instructions for withdrawal of monies from the client's accounts.

The SC has revoked his CMSRL for dealing in securities and imposed a penalty of RM123,750.

Compliance with Malaysian Financial Reporting Standards

PLCs are obligated to comply with the Malaysian Financial Reporting Standards (MFRS) in the publication and submission of their Audited Financial Statements (AFS).

In light of this, the SC has reprimanded NetX Holdings Bhd (NetX) for this particular breach relating to NetX's AFS for the financial years ended 30 June 2014 and 30 June 2015. The SC also reprimanded all four NetX's directors at the time of breach. They are YM Tengku Ahmad Badli Shah Raja Hussin, Tan Sik Eek, Chu Chee Peng and Yong Ket Inn.

In addition, the SC has also reprimanded Khee San Bhd (Khee San) for failing to comply with the MFRS relating to its AFS for the financial years ended 30 June 2015 and 30 June 2016. The SC has also issued directives for Khee San to rectify and reissue its AFS for 2015 and 2016. Khee San was also directed to seek appropriate independent professional advice to reconstitute an effective Audit Committee and address its financial reporting functions. The SC also reprimanded the directors of Khee San, namely Dato' Sri Liew Kuek Hin, Huang Yan Teo, Leslie Looi Meng, Dato' Sei Liew Yew Chung and Liew Yet Mei and imposed a total penalty of RM1,862,000 on them.

The SC also reprimanded Multi Sports Holdings Bhd (Multi Sports), its two executive directors and an independent non-executive director for knowingly authorising the furnishing of its financial statements that is false or misleading to

> "The SC is vigilant in ensuring that the licence holders remain fit and proper. CMSRL holders are expected to meet the SC's requirements in conducting their respective regulated activities."

Bursa Malaysia. The financial statements concerned were Multi Sports' Q1 2015 until Q4 2015. Further, the SC issued public statements to the effect that, in the SC's opinion, the retention of office by the two executive directors of Multi Sports were prejudicial to the public interest.

Infringement Notices

During this period, SC issued 29 Infringement Notices[1] in relation to, among others–

- non-compliances with approved accounting standards;
- non-compliances with licensing conditions;
- weaknesses in compliance, risk and audit functions; and
- non-compliance with the *Rules on Take-overs, Mergers and Compulsory Acquisitions*

Table 3

Infringement notices issued from 1 January 2018 to 30 June 2018

Type of infringement notices	Jan	Feb	Mac	Apr	May	Jun	Total
Supervisory Letter	–	–	–	–	–	11	11
Warning Letter	–	–	3	–	1	–	4
Non-compliance Letter	6	2	2	–	–	–	10
Cease and Desist Letter	1	–	–	2	1	–	4
TOTAL	**7**	**2**	**5**	**2**	**2**	**11**	**29**

Supervisory Examinations and Engagements

In carrying out our oversight and supervisory functions on intermediaries and market institutions, we rely on a variety of supervisory tools for detection of risks and market irregularities. Besides carrying out on-site examinations, the SC also relies on engagements with market participants to address concerns, supervisory findings as well as communicate regulatory expectations of the SC.

8 Non-statutory enforcement tools issued where the breaches of securities law detected do not warrant the initiation of a formal enforcement action or imposition of administrative action.

Table 4

Number of supervisory examinations and engagements conducted by the SC from 1 January 2018 to 30 June 2018

Entity	Number of examinations conducted	Number of engagements conducted
Firms[2] (securities, derivatives, fund management, REITs & corporate finance)	53[3] (including 1 on cybersecurity)	22
Bond market service providers[4]	–	–
Bursa Malaysia Bhd	–	33
Market institutions[5]	–	37
PLCs	13[6]	8
Auditors	–	10
CMSL holders	Not applicable	35[7]
Other stakeholders (recognised market operators)[8]	–	28

[2] Firms involved in regulated activities including dealing in securities and derivatives, fund management, investment advice and advising on corporate finance.
[3] Examinations include thematic reviews and for-cause assessments.
[4] Rating agencies, bond pricing agency and trustees.
[5] Federation of Investment Managers Malaysia and Private Pension Administrator Malaysia.
[6] This refers to the number of new cases initiated within the reporting period.
[7] This refers to the number of engagement undertaken by the Authorisation and Licensing Department.
[8] Operator of the stock market or derivatives market.

Criminal Prosecutions and Outcomes, Civil Enforcement and Regulatory Settlements

Introduction

From 1 January 2018 to 30 June 2018, we instituted criminal charges against eight individuals for various securities offences. Five individuals were charged for insider trading while two individuals were charged under the *Securities Industry (Central Depositories) Act 1991* for allowing their accounts to be utilised to effect the acquisition of shares related to insider trading. One individual was charged for engaging in an act which operated as a fraud in connection with the purchase of securities by a co-operative society established for employees of a listed corporation.

A testament of the SC's active enforcement efforts was also demonstrated by the Court of Appeal's decision to affirm a conviction and sentence meted out by the Sessions Court against an individual for knowingly permitting the furnishing of false statements to Bursa Malaysia Securities Bhd (Bursa Malaysia).

Criminal Prosecutions

In January 2018, the SC preferred two charges against Ismail Basir for defrauding Koperasi Pelaburan Pekerja-Pekerja Proton Bhd (KOPRO) between August 2007 and November 2008 of its investments amounting to RM350,000. Ismail had defrauded KOPRO by acts which included representing himself as a dealer's representative at PM Securities Sdn Bhd, when in fact he was never licensed by the SC. KOPRO is a c-ooperative society established for the employees of Proton Holdings Bhd, a PLC. In February 2018, Ismail pleaded guilty and was sentenced to one year imprisonment and fined RM1 million (in default six months imprisonment, for each charge).

In February 2018, the Executive Chairman of Three-A Resources Bhd (3A), Dato' Mohd Nor Abdul Wahid (Mohd Nor), was charged for insider trading of 3A shares. Mohd Nor is alleged to have acquired the 3A shares through the account of one Azuzay Zamani. Azuzay was charged for allowing Mohd Nor to effect the acquisition of the 3A shares in his account.

In another case, the SC also charged two individuals, A.F.M. Shafiqul Hafiz and Dato' Harjit Singh Gurdev Singh, in February 2018 with insider trading involving the shares of Johor Land Bhd (JLand). At the material time, A.F.M Shafiqul Hafiz was the former Managing Director of Jland.

In March 2018, two former senior investment bankers, Tan Giap How and Ng Ee Fang were charged for insider trading of Hirotako Holdings Bhd (Hirotako) shares. At the material time, Tan was the Regional Head of Equity Markets at AmInvestment Bank while Ng was the bank's Head of Equity Derivatives. The SC also charged Ng's husband, Daniel Yong Chen-I, for allowing Ng to effect the acquisition of the Hirotako shares through his CIMB Investment Bank Bhd account.

Outcomes of Criminal Prosecutions and Appeals

From January to June 2018, the SC was able to secure convictions against three individuals for various capital market offences.

In April 2018, a former investment banker who held the position of Head of Equity Markets at Aseambankers Malaysia Bhd (now known as Maybank Investment Bank Bhd), was convicted and sentenced to six months imprisonment and was fined RM1 million (in default of six months imprisonment) for insider trading in the shares of Road Builder Holdings Sdn Bhd. Goh Keng Huat was charged in 2017 with 10 counts of insider trading in the said shares.

In April 2018, Alan Rajendram Jeya Rajendram (Alan), a former executive director of LFE Corporation Bhd (LFE) pleaded guilty to committing criminal breach of trust in respect of the company's funds amounting to RM18.99 million. The plea was made following a full trial involving 35 witnesses for the prosecution and three witnesses for the defence. He was sentenced to three years imprisonment. Alan's conviction at the Sessions Court followed an earlier notable outcome for the SC in March 2018 when the Court of Appeal dismissed Alan's appeal against his conviction for four charges of knowingly permitting the furnishing of false statements to Bursa Malaysia under section 122b(bb) of the *Securities Industry Act 1983* and section 369(B)(b) of the *Capital Market and Services Act 2007* respectively. The false statements were in relation to fictitious purchases made by a subsidiary of LFE in all four quarters of the company's unaudited financial results for its financial year ended 31 December 2007. In this case, the Court of Appeal affirmed the sentence of one year jail and fine totalling RM1.2 million which was ordered to take effect immediately.

A detailed excerpt of the above cases can be found at: https://www.sc.com.my/post_archive/updates-on-criminal-prosecution-in-2018/

Civil Enforcement and Regulatory Settlements

In January 2018, the High Court held in favour of the SC against Chan Soon Huat (Chan Soon), for insider trading breaches in the shares of WCT Bhd. Chan, who was one of the founders of WCT. Chan Soon was also ordered to pay the sum of RM3,238,760.55 claimed by the SC and a civil penalty of RM500,000 to the SC. The decision has been reported as:

Suruhanjaya Sekuriti Malaysia v. Chan Soon Huat [2018] 9 MLJ 782.

In March 2018, seven defendants whom the SC had earlier sued for market manipulation had agreed to admit to the claim brought by the SC.

Kenneth Vun @ Vun Yun Liun, Teng Choo Teik, Simon Ling Siang Hock, Lye Pei Ling, Chuah Hock Soon, Choong Lay Ti and Gui Boon Huat were sued by the SC in 2014 for their involvement in false trading and market rigging transactions in relation to DVM Technology Bhd (DVM Tecnology) shares. DVM Technology, a company listed on the ACE Market was involved in the business of providing IT solutions.

In addition to agreeing to pay a sum of RM3,823,231.92, which constituted three times the profits made by them as a result of their manipulative trading in DVM shares, and a civil penalty of RM750,000, the seven individuals also agreed:

- not to hold office as directors in any public-listed company for a period of five years; and
- to not trade in any securities on Bursa Malaysia for a period of five years either directly or through any of their agents.

In the same month, seven defendants whom the SC had earlier sued in 2017 for market manipulation had agreed to admit to the claim brought by the SC. Ng Wai Hong, Lo Ga Lung, Toh Pik Chai, Ling Pik Ngieh, Ng Soo Tian, Chan Kok and Chai Shou Wei were sued by the SC for their involvement in false trading and market rigging in relation to APL Industries Bhd (APLI) shares. APLI, a company listed on Bursa Malaysia's Main Market at the time, was primarily involved in the business of manufacturing and retailing of latex examination gloves.

The defendants agreed to pay a sum of RM2,354,672.13 which constitutes the profits as a result of their manipulative trading in APLI shares and a civil penalty of RM200,000.

A detailed excerpt of the above cases can be found at: https://www.sc.com.my/post_archive/details-of-civil-action-taken-in-2018/

For the period between January to June 2018, one individual entered into a regulatory settlement with the SC amounting to RM56,900.00 over insider trading breaches.

The details of the regulatory settlement can be found at: https://www.sc.com.my/post_archive/regulatory-settlements-in-2018/.

FOR MORE INFORMATION

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