

Banking in Singapore

12.1 Introduction

Switzerland currently manages approximately US\$2.2 trillion of offshore assets¹⁸⁵ due to its historic stable financial and political environment, which translates into a safe haven for investing money. Further, it also has long-standing expertise in multi-currency investments, with pro-investor banking secrecy laws, and discrete and well regarded personalised services. To many, Switzerland is a politically neutral, tax-efficient and trustworthy financial centre.

But Switzerland's position as an offshore financial centre is set to weaken with the possibility of significant fund outflows to Asia and elsewhere. Switzerland will soon lose some of its tax competitiveness which is one of the main benefits for its past success in attracting offshore funds.

In June 2003, under pressure from G8 countries, Switzerland has agreed to repatriate income taxes on accounts held by citizens of the European Union, due to start in July 2005, but which may be delayed further until 2006. The tax

¹⁸⁵Cohn, Laura and Fairlamb, David, "Singapore and its growing effect on private banking. Swiss banks: Paradise lost" (2003), *eBrain Hosting* (<http://www.ebrainhosting.biz/english/news/news-Singapore-private.html>), 29 February 2004.

rate will start at 15 per cent and increase to 35 per cent by 2011.¹⁸⁶

Other EU countries have also adopted or will adopt the EU's Savings Tax Directive, which requires financial institutions to report financial information on their non-resident investors. This means that account holders will have to pay taxes on their investment income to their respective governments, which previously was not done.

In the light of these developments, it is likely that the wealthy may decide to place their wealth away from Switzerland, and the other wealth management centres in Europe. The wealth management industry in Asia, especially Singapore, is poised to benefit from these recent developments in Europe over and above the growing amount of indigenous wealth in Asia.

Similar to Switzerland, Singapore has strong fundamentals. First, it has a good record of creating and maintaining sound economic policies and is politically stable. Its financial industry is regulated to the highest international standards. Second, it is the world's fourth largest foreign exchange centre with a large presence of public equity, private equity, and fixed income and hedge fund managers.¹⁸⁷

Third, Singapore has an extremely favourable regulatory environment for the placement and investment of offshore funds. Its tax system allows offshore funds to compound tax free, as no taxes on interest and capital gains are imposed on non-residents. There are also no barriers to the entry and repatriation of funds.

¹⁸⁶"EU tax deal leaves Swiss banking secrecy intact" (2003), *Swiss Info* (<http://www.swissinfo.org/sen/Swissinfo.html?siteSect=105&sid=3900237>), 24 October 2003.

¹⁸⁷Koh, Francis, Lee, Choon Li and Jindai, Parthasarthi, "Singapore as an emerging hub for wealth management", *Pulses, A monthly publication of Singapore Exchange Limited*, November 2003.

Fourth, the Singapore Government plays an active role at increasing transparency and minimising bureaucratic practices. Finally, it has stringent client confidentiality laws, comparable to those of Switzerland. With these advantageous factors measuring to those offered by Switzerland, Singapore has positioned itself to being the benefiting party to the movement of offshore funds out of Europe.¹⁸⁸

It can be seen that Singapore's development as an international financial centre began in the late 1960s. Since then, Singapore has implemented an economic blueprint that has encouraged inward investments of multinational corporations to Singapore. The inflows of foreign direct investment from the UK, USA and Japan provided an impetus to the development of the financial sector. By the 1980s, many of the world's leading financial institutions had set up operations in Singapore.¹⁸⁹

Over the years, its sound economic and financial fundamentals, conducive regulatory and business environment, strategic location, skilled and educated workforce, excellent telecommunications and infrastructure, and high living standards have attracted many reputable international financial institutions to set up operations in Singapore. On the back of growing prosperity in the region and support from the authorities, Singapore has developed into a regional, and subsequently, global foreign exchange trading centre. Today, only London, New York and Tokyo record higher foreign exchange trading volumes than Singapore. The Singapore International Monetary Exchange (SIMEX),¹⁹⁰ the first derivative exchange

¹⁸⁸Ibid.

¹⁸⁹Economic Review Committee, Sub-Committee on Services Industries, Financial Services Working Group, "Positioning Singapore as a pre-eminent financial centre in Asia" (2002), *Channel News Asia* (<http://www.channelnewsasia.com>), 9 November 2003, p. 1.

¹⁹⁰SIMEX and the Stock Exchange of Singapore (SES) have since merged to become the Singapore Exchange (SGX).

in Asia, also grew in stature to become a key Asian financial hub in the global chain of leading future markets. Today, financial services account for 11 per cent of Singapore's GDP.¹⁹¹

There is a large and diversified group of local and foreign financial institutions, numbering about 700, located in Singapore and offering a wide range of financial products and services. These include trade financing, foreign exchange, derivatives products, capital market activities, loan syndication, underwriting, mergers and acquisitions, asset management, securities trading, financial advisory services and specialised insurance services. The presence of these leading institutions has contributed to the vibrancy and sophistication of Singapore's financial industry.¹⁹²

Fund management companies in Singapore have expanded in terms of size, regional responsibility and capabilities, with 70 per cent of funds under management sourced from the USA, Europe and Asia.¹⁹³

Singapore's asset management industry has managed good growth since 1994. Assets under management (AUM) by Singapore-based financial institutions have grown steadily from S\$66 billion in 1994 prior to the implementation of developmental measures to S\$307 billion as at the end of 2001. Singapore has evolved into a major regional asset management centre, hosting more than 200 asset management outfits, which employed 1114 professionals as at the end of 2001.

¹⁹¹*Monetary Authority of Singapore* (<http://www.mas.gov.sg>), 3 November 2003.

¹⁹²*Ibid.*

¹⁹³Economic Review Committee, Sub-Committee on Services Industries, Financial Services Working Group, p. 3. The major Swiss and European private banks such as USB, Credit Suisse and ABN-Amro all have regional headquarters in Singapore.

Almost three-quarters of discretionary AUM are sourced from overseas.¹⁹⁴

Singapore's developmental objective is to become a centre for (a) managing the Asian investment portfolios of both Asian and Western clients and (b) managing global investments of clients in Asia. Today, 43 per cent of assets managed in Singapore were sourced from Europe and North America, with 30 per cent of assets invested in Singapore, 9 per cent in Japan and 18 per cent in the rest of the Asia Pacific. However, Singapore remains a predominantly Asian mandate centre, with funds mostly invested in Asia, although the amount of investment in the USA and Europe carried out from Singapore has increased in recent years.¹⁹⁵

The offshore-banking business is now under pressure around the world. But as offshore participants (particularly the many institutions with businesses in Switzerland) review their business in the light of unfavourable regulatory charges, they will find they have several options that will help them remain competitive.

One of the options is to grow beyond their home market. They can do so by building onshore presences in selected locations or by intensifying their efforts to grow in other key offshore locations such as Singapore. Thus there is the increasing need for Singapore to cement herself, in the minds of the offshore players, as the next best alternative.¹⁹⁶

Singapore has responded accordingly to the directives and recommendations of the international bodies such as the OECD, FATF and IMF in terms of (a) harmful tax practices, (b) money laundering, (c) confidentiality and (d) exchange of

¹⁹⁴Ibid.

¹⁹⁵Ibid.

¹⁹⁶"Winning in a challenging market: Global wealth 2003", *The Boston Consulting Group*, July 2003.

information. The following analysis of Singapore's legal and regulatory systems will demonstrate how it has responded to these issues and why in totality this regional financial centre will continue to develop ahead of the other Offshore Financial Centres (OFCs), and in doing so, will become the new jurisdiction of choice for those seeking to use an OFC for future wealth management.

12.2 Legal Framework: Legislation Enacted by the Parliament of Singapore

Singapore, which is a republic, was a colony of the United Kingdom and briefly part of the Federation of Malaya. She has a unicameral parliament and a government patterned after the Westminster model, in which Parliament enacts laws and confers executive powers thereunder upon ministers,¹⁹⁷ who form a cabinet headed by the Prime Minister.

The President is the constitutional Head of State. Although the President does not have executive powers, his assent is required before any legislation can have the force of law.¹⁹⁸ Local legislation comprises acts passed by Parliament and assented to by the President, and subsidiary legislation promulgated thereunder by ministers exercising their delegated authority.

Singapore's judicial system comprises three tiers of courts:

- (i) The Subordinate Courts, consisting of the Coroners' Courts, the Juvenile Courts, the Magistrates' Courts, and the Small Claims Tribunal.

¹⁹⁷The Ministers usually are empowered under their respective Acts to promulgate such subsidiary legislation as in necessary for the implementation of Acts.

¹⁹⁸Article 58 of the Singapore Constitution provides that "the power of Legislature to make laws shall be exercised by Bills passed by Parliament and assented to by the President".

- (ii) The Supreme Court, which comprises the High Court, the Court of Appeal, and the Criminal Court of Appeal.
- (iii) The Judicial Committee of the Privy Council, which traditionally has been the highest court of appeal for Britain's former colonies.

12.3 English Common Law and Statutes

The reception of English Common Law in Singapore was effected by the Letters Patent issued on 27 November 1826, more commonly referred to as the Second Charter of Justice, which established the Court of Judicature of Prince of Wales Island, Singapore, and Malacca and required the court "to give and pass Judgement and Sentence according to Justice and Right". This phrase traditionally has been interpreted to mean that the English law and equity, as it stood in England in 1826, was part of the law of the Straits Settlements.¹⁹⁹

As a result of the foregoing, matters which have not been legislated upon by the Singapore Parliament are governed by English Common Law, embodied in decided cases of the English courts, with such adaptation as are required by local circumstances.²⁰⁰

The Common Law enjoys continuous reception in Singapore as "the Common Law was traditionally conceived of as having existed from time immemorial and was merely

¹⁹⁹*Regina v. Williams* (1858) 3 Kyshe 16; *Fatimah v. Logan* (1871) Kyshe 225.

²⁰⁰See Woon, Walter (ed.), *The Singapore Legal System*, 1989, p. 119, where he states modifications to "suit the customs, manners, usages and religions of the native inhabitants." An example, he cites, the relaxation, in colonial days, of the common law concept of monogamous marriage in the case of the Chinese.

declared by the judges from time to time . . . ”.²⁰¹ According to this interpretation of the Common Law, the courts in England deciding a case today simply would be declaring the law as it has always been (and, hence, as it was at the date of the Second Charter of Justice), and applying it to the facts before them.

12.4 Singapore: An Alternative to Switzerland

In June 2003, the EU agreement with Switzerland to claw back some tax revenue from income earned on assets of EU citizens that are held by Swiss banks opened the gates for the capital outflow of assets under management by its private banking industry.

Under the deal, in 2005, EU-based clients of Swiss banks will face a 15 per cent tax on income and/or dividends from assets — such as bonds — purchased from their Swiss bank accounts. The taxes will be passed on directly by the Swiss banks to the governments of the clients’ home countries, without the clients’ names being revealed. The deal allows Switzerland to maintain its banking secrecy laws, whilst permitting the governments of EU countries to collect tax revenue that has, thus far, eluded them. Over time, the tax rates will be raised, in stages, to a maximum of 35 per cent.

After 2005, therefore, private banking clients who keep assets in Switzerland will be faced with the prospect of lower — and progressively declining — post-tax rates of return on their holdings.

Many of them have already been induced to move their money elsewhere. Hence, many Swiss banks consider Singapore the best alternative, and are gearing up for the shift, since the regulatory and legal systems are in place, these global

²⁰¹See Bartholomew, G.W., “English Law in Partibus Orientalium”. In A.J. Harding (ed.), *The Common Law in Singapore and Malaysia* (1985), p. 15.

investors are voting with their feet; a clear vote of confidence in Singapore's compliance with the supranational directives.²⁰²

12.5 Singapore: Financial System Stability Assessment

Singapore has evolved into a major regional asset management centre over the past few years in response to the government's efforts to develop this industry and now hosts more than 200 asset management firms. Total assets managed by Singapore-based financial institutions increased from S\$151 billion in 1998 to S\$344 billion in 2002. This increase can be attributed to transfers of regional portfolios to Singapore for management and continued expansion of management and advisory activities for the pan-Asian region in the light of Singapore's sound legal and tax environment and highly developed infrastructure. Some asset managers also centralised their regional trading and back office functions in Singapore. Of the S\$183 billion of discretionary assets as of end-2002, 30 per cent came from Singapore and the rest from abroad — mainly Europe and the United States.

Although the regulatory systems and supervisory practices exhibit a high degree of observance of international standards and codes, the IMF in 2004 made some specific recommendations to further enhance the risk-based regulatory and supervisory framework, to strengthen the accountability and independence on the Monetary Authority of Singapore (MAS), and improve monetary and financial policy transparency.²⁰³

²⁰²Khanna, Vikram, "S'pore an alternative to Switzerland?", *The Business Times* (Singapore), 5 November 2003.

²⁰³*Singapore: Financial System Stability Assessment, including Reports on the Observance of Standards and Codes on the Following Topics: Banking Supervision, Insurance Regulation, Securities Regulation, Payment and Settlement Systems, Monetary and Financial Policy Transparency, and Anti-Money Laundering*, International Monetary Fund, 2004, p. 36.

12.6 Singapore's Role as a Financial Centre

Singapore's sophisticated banking system, the transparent regulatory and the credible English Common Law system have aided Singapore's development as a pre-eminent regional financial centre in Asia which is also underpinned by the existence of an attractive business environment for financial institutions and a desirable quality of life for professionals. Effective promotion to communicate Singapore's value proposition and financial sector opportunities has attracted financial institutions and talent to Singapore. A deep pool of financial sector expertise and pro-physical infrastructure are key components of an attractive business environment. This attractive business environment has been created by focusing on the promotion of Singapore's financial centre, education and training, taxation policies and business infrastructure.²⁰⁴

It has been noted that "Singapore is politically stable, it has the world's most competitive economy, the best rated legal system and is a leader in information technology. There are stringent client confidentiality laws, no taxation for non-residents, and robust anti money laundering laws. Like Switzerland, Singapore is neutral and has an international reputation as a safe and secure environment."²⁰⁵

Since Switzerland has fallen in line with the EU's Savings Tax Directive, and as previously noted, with an estimated \$2 trillion in offshore assets held by EU citizens to be affected, it is not surprising that many of Europe's wealthy are reviewing other places to transfer their cash and the likely recipient of the outflow, it is now confirmed, is Singapore, which is not party to the EU directive.

²⁰⁴Economic Review Committee, Sub-Committee on Services Industries, Financial Services Working Group, p. 28.

²⁰⁵Ibid.

Competition is limited. The global crackdown on terrorism financing means tax havens in the Caribbean and the South Pacific were previously blacklisted or otherwise seen as tainted. Singapore is among the few still passing the “sniff test”. Hong Kong, suffers “sovereignty risk” due to mainland China’s increasing interference in the territory’s affairs.

With these basic pillars in place, the city-state has now positioned itself to emerge as the major beneficiary of the flight of funds from Europe.

To date, Singapore has enjoyed only modest success as an offshore banking centre. Offshore assets are estimated at \$120 billion, a tenth that of Switzerland’s, and most of that is held by overseas Chinese from South-east Asia. Assets held by EU citizens are easily under 5 per cent. That means there is room for growth.

Over the past five years, Singapore has stepped up its campaign to market the country as a financial centre, with bureaucrats on official trips to Europe holding meetings with private bankers to tout the charms of the South-east Asian nation.²⁰⁶ This is further demonstrated by the number of major banks and financial institutions that have established a presence in Singapore and the subsequent flow of funds under wealth management in Singapore.

12.7 Islamic Banking in Singapore

Islamic Banking has become a priority for Singapore’s central bank. As the MAS’s new chairman, Senior Minister Goh Chok Tong has pledged to boost Singapore’s status as a centre for Islamic financial services. Despite being a regional

²⁰⁶ “Swiss tax decision could see Singapore shine as a haven”, *Offshore Red: An OFC News Update*, Vol. 8, 2003, p. 175.

financial centre, Singapore is lagging behind Malaysia, now a key Islamic financial hub after it fast-tracked the liberalisation of this sector to attract rich Saudis following the 9/11 attacks.

According to Dr Zeti Akhtar, Malaysia's central bank governor, the Islamic banking sector remains largely untapped by South-east Asia, other than Malaysia and the market out there is very large and greater activity will contribute to the development of Islamic banking and finance on a global basis.

Compared to Malaysia, Islamic banking is at its infancy in Singapore, due largely to a lack of awareness and a small domestic market that has not attracted the major bankers. OCBC is the only active player in the banking sector, offering two Islamic deposit accounts in the consumer market. But it has failed to replicate here the success it has had in Malaysia, where it is the second foreign player in the field with some RM457 million (S\$204 million) in Islamic banking loans.²⁰⁷ HSBC Insurance is also offering takaful products as an acceptable avenue for financial planning in accordance with Islamic principles for the local Muslim community.

Singapore's efforts to develop Islamic finance should not be constrained by the fact that it is not a Muslim state as Islamic finance is already taking off in many non-Muslim countries. The first Islamic retail bank opened for business in the United Kingdom in September 2004. In July 2004, the former East German state of Saxony-Anhalt sold Europe's first Islamic sovereign bond. The Muslim Community Co-operative Australia (MCCA) was established in February 1989 to conduct financial dealings and transactions based on Islamic finance principles. The MCCA manages the Murabaha, Musharaka, Mudaraba, Qard-el-Hassan and Zakat funds.

²⁰⁷Chua, Val, "Wooing the Islamic Billion\$", *Today* (Singapore), 24 September 2004.

The Singapore Government intends to promote Islamic banking products to expand its reputation as a regional financial hub, and will collaborate with countries such as Malaysia and Brunei in this area.²⁰⁸ Whilst only 15 per cent of Singapore's population are Muslims, experience in other retail markets, such as Malaysia, shows that in excess of 70 per cent of that customer base are non-Muslims.

In its February 2005 budget, the government announced new measures to further support this sector by including the removal of the double imposition of stamp duties on Islamic transactions involving real estate, and that it would also accord payouts from Shari'ah bonds the same concessionary tax treatment granted to interest arising from conventional finance. Both measures are intended to put Islamic Banking on the same footing as conventional financing. In addition, the Government has commenced a series of signing of free trade agreements with a number of Middle Eastern and Gulf State countries.

Singapore's efforts to become an international financial centre for Islamic services will not be threatened by Malaysia's ambitions in the same field. BNM's governor, Tan Sri Zeti Akhtar Aziz, believes that Singapore's plans will instead hasten global development of Islamic banking and finance.

12.8 Conclusion

From the above, it can be seen that Singapore has established a highly credible brand name which is of the utmost importance in the global banking and financial world, and is now positioning itself to be the nexus for the convergence of both the conventional and Islamic banking and finance sectors in Asia,

²⁰⁸Siow, Li Sen, "S'pore can add value in developing Islamic finance", *The Business Times* (Singapore), 25 September 2004.

whilst Islamic banking is still in its infancy in Singapore. As former Prime Minister Goh has stated, its full development will complete Singapore's image as a true international financial centre, thanks to the stewardship of the government and the current generation of young mandarins.