



ABU DHABI GLOBAL MARKET
سوق أبوظبي العالمي

FINANCIAL SERVICES REGULATORY AUTHORITY
سلطة تنظيم الخدمات المالية

A Financial Services Regulatory Authority Guide -
Authorisation of Digital Banks in Abu Dhabi Global Market

Introduction

This Guide is issued under the Financial Services and Markets Regulations 2015 (**FSMR**) by the Financial Services Regulatory Authority (**FSRA**), the independent financial services regulator of Abu Dhabi Global Market (**ADGM**). Its aim is to define the FSRA's key considerations in assessing an application to establish a digital bank in ADGM, including accepting deposits, providing credit, and transactional bank accounts, as well as money transfer and payments services.

Recognising recent financial technology developments in the banking industry, and within the context of its existing rules and regulations pertaining to the business of banking, the FSRA **encourages the establishment of digital banks**, believing that ADGM provides the ideal jurisdiction and environment for their operation and success. The FSRA considers that digital banks can provide innovative customer solutions and contribute to the development of the overall financial ecosystem, by promoting inclusion, particularly in the SME sector, thereby enhancing the growth and reach of the financial services sector in ADGM and more widely.

General

Establishing and operating a digital bank is a complex undertaking, and the regulatory requirements are extensive. This Guide therefore seeks to identify overall regulatory requirements, but also to highlight particular additional considerations in relation to the authorisation of digital banks.

A digital bank is one that accepts deposits, and carries on other related financial services activities, primarily through online, digital or electronic means rather than through interaction with customers in physical premises. The FSRA considers that, in addition to specific risks such as information technology, cyber security, and heightened operational risks, a digital bank remains exposed to all of the usual risks that face a conventional financial institution accepting deposits under an FSRA prudential Category 1 licence, such as credit, market, interest rate, and liquidity risks. Therefore, an application for a digital bank must evidence an ability to comply with similar authorisation criteria and regulatory obligations incumbent upon conventional banks in ADGM.

Threshold Conditions

In considering an application to establish a digital bank in ADGM, the FSRA will be mindful of threshold conditions set out in FSMR and Chapter 5 of the FSRA's General Rules (**GEN**). These include the need for adequate and appropriate resources, including financial; fitness and propriety; whether the entity can be supervised effectively; and proposed compliance arrangements, including policies and procedures.

Rationale and Business Plan

At the core of a successful application to establish a digital bank must be a credible and comprehensive regulatory business plan that sufficiently articulates the rationale for the proposal, and which presents a viable and sustainable model. The FSRA's application form contains a template business plan, which if completed correctly, should encourage a comprehensive submission. The FSRA is an activities-based regulator, and the business plan should highlight all activities proposed, including those in addition to banking business such as accepting deposits.

The regulatory business plan should demonstrate a clear link between the target markets and customers, the proposed services to be offered, and financial projections, which should take a realistic view of likely revenues (and their timing) and expenses.

Legal Structure

The FSRA encourages and welcomes applications to establish digital banks in the ADGM, and anticipates three particular sources of interest: from conventional banks seeking to establish digital banks or branches of digital banks; from firms with innovative value propositions; and from partnerships between technology companies and financial institutions.

The FSRA digital banking regime is able to accommodate both branches of existing regulated banks, and ADGM companies. A branch is not subject to the FSRA's prudential capital requirements, and therefore the agreement of the applicant's home state regulator will be required. A subsidiary would be classified as a domestic firm in ADGM, a distinct legal entity with its own governing body and capital resources.

The FSRA's legal framework, namely its Prudential — Investment, Insurance Intermediation and Banking Rules (**PRU**), would require a digital bank applicant to be majority owned by an existing, regulated deposit-taking institution. However, the FSRA will consider modification of the PRU Rules to allow for proposals by start-up digital banks that do not meet this requirement. The consideration of such an application relies on adequate resources, including the financial soundness and credibility of any shareholders offering financial support, robust systems and controls, and management, including board members and a senior executive management that have suitable experience in running a regulated financial institution.

The FSRA would also expect an applicant for a digital banking licence to have understood, and have processes to observe, Federal restrictions on accepting deposits in the UAE dirham or from the State's markets, and on dealing in the UAE dirham set out in Federal Law No. (8) of 2004. This will mean that a digital bank in ADGM will need to secure correspondent banking facilities in the UAE or overseas.

To be authorised and regulated by the FSRA, a digital bank must have premises in ADGM, and be registered or incorporated under ADGM's Registration Authority.

Ownership and Control

The FSRA will require information about the digital bank's ultimate beneficial owners, and corporate and natural person controllers holding more than 10% of the applicant or any holding entity. Allied to this, the FSRA will review any close links or connected parties within the overall organisation structure.

Staffing

The FSRA would expect the digital bank application to explain proposed human resources, which should be proportionate in number and experience to the scale of the activities to be conducted. The FSRA does not mandate the size of a board, but in addition to its assessment of individual board members, will take a holistic view of the board's overall composition, and would anticipate a balance of banking, financial technology, and governance experience, as well as a significant proportion of independent, non-executive directors.

Leading the executive management team, the Senior Executive Officer should be based in the UAE and bring a balance of technical banking and senior management experience commensurate with the digital bank's proposed activities.

Other mandatory positions cover compliance, anti-money laundering, and finance, which should be exercised by suitably experienced individuals, with demonstrable segregation of their roles from the business functions.

While not mandatory appointments under the regulations, the FSRA would expect a digital bank to appoint senior individuals to oversee risk and information technology.

Governance – Management, Systems and Controls

An applicant for a digital banking licence should demonstrate an operational structure which apportions significant responsibilities between the members of its board and senior management in such a way as to meet the corporate governance requirements of GEN. The digital bank's board and senior management must comprise an adequate mix of individuals who have between them relevant knowledge, skills, expertise, and time commitment to carry out their duties effectively. Roles and responsibilities must be clearly defined, with clear reporting lines, and segregation between business and control functions.

The digital bank must have systems and controls in place to address issues including risk management, compliance, conduct, conflicts of interest, internal audit and business continuity.

Outsourcing

The FSRA does not object to the use of outsourcing, but a digital bank needs to be aware that it remains responsible for any functions carried out by third parties, whether or not they are part of the same group. A digital bank will need to explain any material outsourcing

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Abu Dhabi Global Market Square Al Maryah Island PO Box 111999 Abu Dhabi United Arab Emirates T +971 2 333 8888
مربعة سوق أبوظبي العالمي جزيرة الماربه ص ب 111999 ابوظبي الإمارات العربية المتحدة هاتف 971 2 333 8888

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arrangements as part of its application, and provide policies and processes to comply with requirements in GEN. The FSRA will be interested in understanding the resource allocation that has been agreed, as well as the experience and capacity of the outsourced service provider.

Risk Management

Consistent with a traditional financial institution, a digital bank must be cognisant of the risks to which it is exposed, and implement appropriate processes, controls and oversight systems to identify, measure, monitor and manage them. A digital bank should also realise that some risks, such as operational risk, will be amplified by its business model.

A digital bank will need to consider, at least, credit risk and all the components of market risk, as well as operational risk. A digital bank applicant should consolidate its approach to risk in an Internal Risk Assessment Process (**IRAP**) document, and submit this as part of its application. The FSRA will further expect the digital bank to reassess and update its risk models on a regular basis.

Information Technology Risk and Cyber Security

Given the nature of a digital bank, technology-related risk is a key concern, encompassing information security, systems connectivity and soundness, and business continuity. The FSRA will expect a digital bank applicant to put in place robust information technology structures, and to test these for any vulnerabilities before commencing business. Further, the FSRA will expect a digital bank to have measures in place to address cyber security, and that these be tested prior to commencing business.

An applicant for a digital banking licence should not underestimate the time it will take to implement robust information technology systems, which may involve liaison and agreement with third party providers. The FSRA accepts cloud-based solutions to data management.

Prior to final licensing, the FSRA will require the digital bank to have its information technology systems connectivity and security tested by an independent third party specialist, which should form the basis for a board attestation of operational readiness.

Financial Crime

The FSRA considers an assessment of financial crime, money laundering and terrorist financing, and fraud risks to be key considerations in the conduct of banking business, and this applies equally to a digital bank. Therefore, the FSRA expects a digital bank applicant to have policies and procedures in place to address the requirements of the Anti-Money Laundering and Sanctions Rules and Guidance (**AML**) Rules.

Capital and Prudential Requirements

The base capital requirement applying to digital banks that accept deposits under prudential Category 1 is USD10 million. It is more likely, however, that the Risk-Based Capital Minimum will apply as the higher requirement. This is calculated on the basis of the totality of risks the digital bank will face in the course of its business and operations, and includes core Tier 1 (CET1) and Tier 1 capital adequacy ratios of 6% and 8% respectively, with a Capital Conservation Buffer of 2.5%, along with a minimum leverage ratio of 3%.

The FSRA expects a digital bank applicant to assess its capital coverage, liquidity, and contingency funding provisions as part of a substantive and comprehensive Internal Capital Adequacy Assessment Process (**ICAAP**), and submit this document as part of the application.

Payment Services

In addition to digital bank proposals to be licensed under Category 1, the ADGM regime can accommodate applicants seeking to establish innovative solutions in relation to payments accounts and transactions, such as e-wallets, tokens, and stored value cards. Depending on the specific services to be offered, these can attract a lower regulatory and capital burden than a full digital banking licence, usually falling under Category 3C.

Application Process

The FSRA is pleased to speak to potential applicants in relation to digital banking and payments proposals. Please contact the FSRA at: authorisation@adgm.com.

The usual process is to have an initial meeting to explore the proposition, followed by submission of a draft regulatory business plan completed in advance of a full application, upon which the FSRA will provide feedback in around two weeks. Once a full application is submitted, the FSRA, depending upon the complexity of the business plan and completeness of the application, will endeavour to provide its decision concerning the issuance of an approval in principle within 10 to 12 weeks. The delivery of an in-principle approval will provide the applicant with the certainty of final authorisation to allow the securing of premises, hiring of staff, and systems and infrastructure build-out necessary to commence business.

The FSRA would expect digital bank applicants to take some time to fulfil their in-principle approval conditions, and will work with them closely during this period.

Digital Banks in ADGM: Summary of Requirements

Threshold Conditions	<ul style="list-style-type: none"> • Adequate and appropriate resources, including financial • Fitness and propriety • Capable of being supervised effectively • Compliance and risk management arrangements
Business Plan	<ul style="list-style-type: none"> • Must be credible and comprehensive • Effectively describes the proposal's rationale • Viable and sustainable • Regulated Activities to be conducted
Legal Structure	<ul style="list-style-type: none"> • Branch or ADGM company – ADGM premises • Parent bank, or • Satisfactory ownership, governance and senior management
Controllers	<ul style="list-style-type: none"> • Natural persons or entities holding more than 10%
Staffing	<ul style="list-style-type: none"> • Controlled Functions: <ul style="list-style-type: none"> ○ Licensed Directors – the FSRA will take a holistic view of the Board's composition ○ Senior Executive Officer – must be resident in the UAE • Recognised Functions: <ul style="list-style-type: none"> ○ Compliance Officer (must be UAE resident) ○ MLRO (Must be UAE resident) ○ Finance Officer • Senior management positions such as business heads, Chief Risk Officer and Chief Technology Officer should be addressed
Management, Systems and Controls	<ul style="list-style-type: none"> • Operational structure should apportion significant responsibilities between the board and senior management • Adequate mix of individuals with relevant knowledge, skills, expertise and capacity • Clearly defined roles
Outsourcing	<ul style="list-style-type: none"> • Responsibility cannot be outsourced • Clearly defined role allocations • Experience and capacity of the outsourced provider
Risk Management	<ul style="list-style-type: none"> • Evidence awareness of relevant risks • Controls in place to identify, measure, monitor and manage • Some risks, such as IT and operational, may be enhanced • IRAP
IT Risk and Cyber Security	<ul style="list-style-type: none"> • Systems must be robust, and tested prior to launch • Policies and procedures in relation to cyber security • Independent review and testing
Financial Crime	<ul style="list-style-type: none"> • Financial crime, AML, CFT and fraud are key risks, requiring comprehensive policies and procedures

Capital	<ul style="list-style-type: none"> • No requirements for branches, only liquidity • Requirement for ADGM incorporated companies is higher of: <ul style="list-style-type: none"> ○ Base Capital Requirement: USD10 million ○ Risk-based capital minimum based on the totality of risks <ul style="list-style-type: none"> ▪ CET1, 6%; Tier 1, 8% • ICAAP
In-principle approval	<ul style="list-style-type: none"> • All conditions to be satisfied prior to launch

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