

**CONSULTATION PAPER
CP112**



TESTING FINTECH INNOVATIONS IN THE DIFC

6 March 2017

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Preface

During 2016, the DFSA announced¹ its willingness to engage with the rapidly evolving world of financial technology, or fintech.

Our efforts in this area are in conjunction with those of the DIFC Authority, who have recently launched The Hive accelerator², the first-of-its-kind in the Middle East, and with the broader innovation strategies of the Government of Dubai and of the UAE Government.

The DFSA is able to engage with fintech in a simple and straightforward manner, because our existing regime is flexible enough to accommodate many aspects of fintech without introducing new Rules or new types of financial service activities. In particular, we can accommodate the testing of fintech innovations within our regime.

The DFSA has been dealing with, and discussing opportunities with, a number of interested fintech innovators. We are now of the view, given interest received to date, that it would be helpful to current stakeholders and the wider public for us to set out more explicitly how we will deal with future enquiries from those interested in establishing a presence in the DIFC for a fintech business.

We do not propose introducing new Rules. Instead we set out, in Guidance, how we can make use of the flexibility in our regime to facilitate the testing of innovative fintech business models in the DIFC.

Who is this Consultation Paper aimed at?

This paper will be of interest to:

- Persons who are operating, or intend to set up, a fintech business and base themselves in the DIFC;
- Authorised Firms already providing Financial Services in the DIFC, who are developing, or intend to develop, a fintech business;
- Persons providing legal, accounting, audit, oversight of compliance services in the DIFC; and
- Potential investors in, or users of, fintech services.

¹ See, for example, the Welcome Note to our '[DFSA in Action](#)' Volume 13, September 2016

² <http://fintechhive.difc.ae/>

What are the next steps?

The DFSA invites interested parties to provide their views and comments on the issues outlined in the Consultation Paper (CP), using the table of comments provided, to consultation@dfsa.ae. Please mention the CP number (112) in the subject line.

The deadline for providing comments on this CP is **5 April 2017**.

Once we receive your comments, we shall consider if any further changes are required to these proposals. We shall then proceed to make the relevant changes to the DFSA's Rulebook. You should not act on these proposals until the relevant changes to the DFSA Rulebook are made. We shall issue a notice on our website telling you when this happens.

1. Introduction

Much has been written over the past two years, or more, about the subject of fintech. We do not propose to repeat here what has been written elsewhere, instead, for the purposes of this paper, and of the DFSA's work in this area, we consider fintech to be the use of technology to support or enable innovative financial services business models. We consider a defining characteristic of fintech to be that it can allow significant step changes in a way a financial services business model operates.

It is our view that fintech opens up possibilities to at least the following:

Improves interaction between financial services firms and customers, including bringing new players into the financial services arena

Improves the efficiency, structure and competitiveness of markets (including value chains)

Makes new financial services products available

Improves risk management by financial services firms

Reduces both the risks and the costs of many financial services back office processes

Improves efficiency and security in the provision of financial services

2. Proposal – Innovation Testing Licence

As noted above, we do not consider it necessary to create a standalone, or completely new, regime to facilitate a fintech business proposition. For any innovative fintech business proposition, we will find the appropriate combination of DFSA Rules from our existing regime that should apply to the financial service activity being tested. The same approach has been adopted in a number of other countries (such as the United Kingdom and Australia). It has also been the approach we have adopted with a number of fintech proposals received to date.

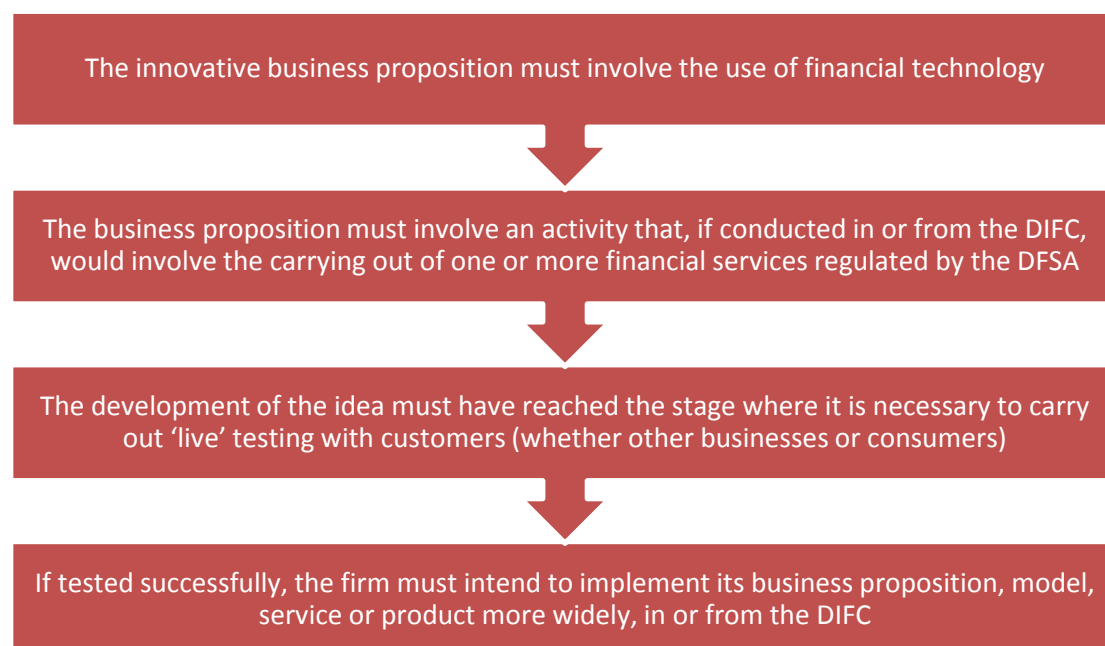
This approach consists of reviewing the DFSA Rules that would normally apply and considering if they need to be waived (i.e., completely disapplied) or modified (i.e., applied in a different form that is appropriate for the actual circumstances) for that fintech proposition.

We have set out below an explanation of this approach and the eligibility requirements for a fintech firm to benefit from this proposal.

The DFSA would welcome any comments or questions on its approach to the testing of innovative fintech business propositions, as set out in this paper.

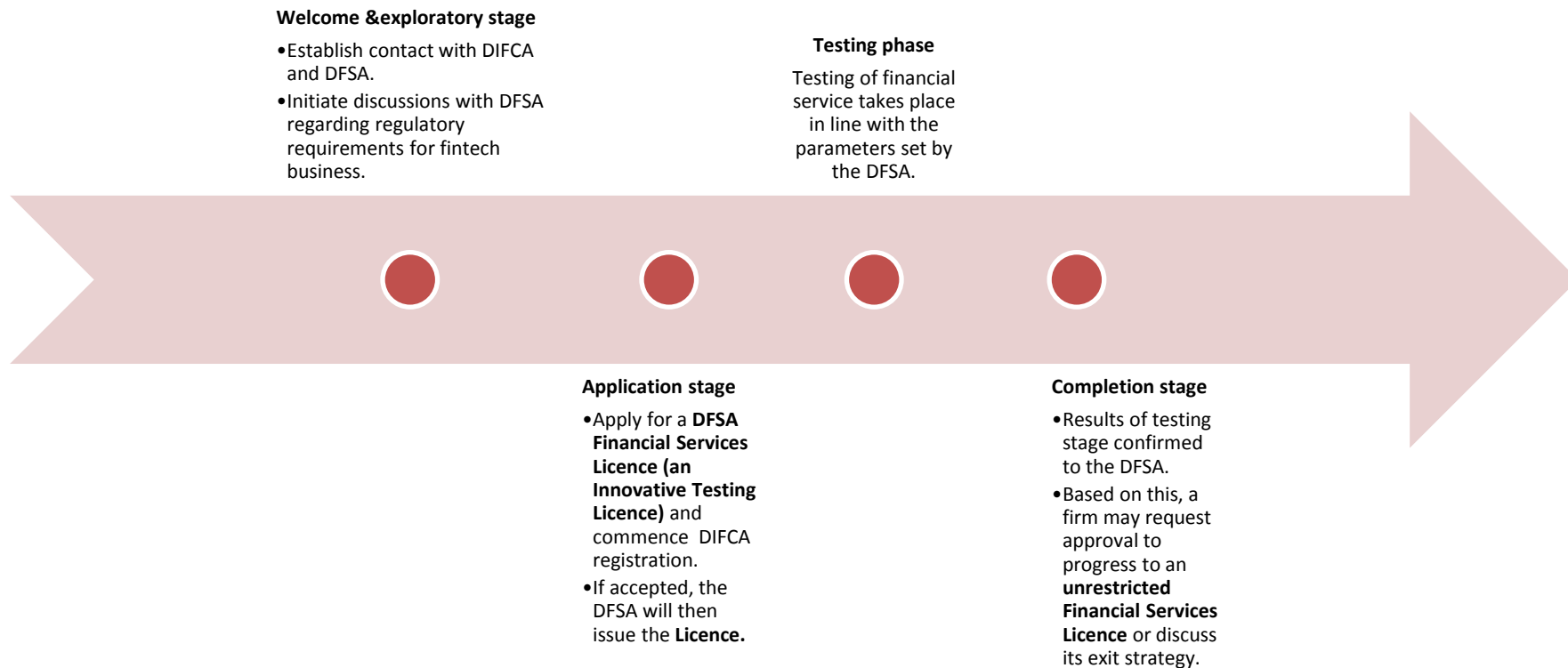
Qualifying criteria

We are proposing a number of qualifying criteria that a fintech proposal would need to meet. These cover:



Application process

The DFSA expects the overall application process would look something like the diagram below.



Step 1: Welcome & exploratory stage

Interested firms should engage with the DFSA at an early stage. The DFSA will work with the firm to establish what regulatory requirements should apply, and what requirements should be waived or modified.

While the DFSA will tailor appropriately the application of its regime to the particular circumstances of the fintech firm, and its business proposition, there are a number of requirements that the DFSA would expect to apply in all cases where regulation is needed. These include, but are not limited to:

- (a) the fitness and propriety of the applicant;
- (b) the need for the firm to act with integrity;
- (c) the need for the firm to act with due skill, care and diligence;
- (d) the firm to communicate information to customers in a way that is fair, clear and not misleading;
- (e) being open and co-operative with the DFSA;
- (f) having an office in the DIFC; and
- (g) complying with all UAE Federal Law prohibitions.

Step 2: Application stage

Upon confirmation that the proposal is in line with the criteria described above, the firm would apply for and, if it meets the requirements for authorisation, receive a Financial Services Licence from the DFSA referred to as an **Innovation Testing Licence (ITL)**. This Licence will reflect the nature of activities conducted during the testing phase under the firm's ITL Test Plan. This will include a number of restriction and conditions regarding the activities that a fintech firm can carry out, to ensure that the testing of the business proposition, service or product is appropriately controlled. Some of the restrictions and conditions that may be included in the Licence would be:

- (a) restricting the business that may be carried out under the Licence to testing its product or service;
- (b) a requirement to include prominently on all its communications that it is 'Regulated by the DFSA for innovation testing only;'
- (c) limiting the number and type of customers involved in testing of its product or service;
- (d) a defined timeline for testing, including clear milestones;

- (e) how the firm intends to ensure that customers (and other key market stakeholders) understand the nature of the testing of the model, product or service and its risks;
- (f) the safeguards the firm intends to put in place to ensure customers (and other key market stakeholders) are adequately protected, in the event of a problem arising from the use of the technology or failure of the business proposition; and
- (g) the firm's exit strategy for an orderly wind-down in the event that its innovative business proposition and fintech activity is not successful.

The DFSA will also publish the waivers and modifications that apply to the firm's activities during this testing phase.

Step 3: Testing phase

As the purpose of our approach is to allow the firm to test and develop its fintech proposition (but not to carry on a fully operational fintech business) the DFSA would expect the firm to use the simplified regulatory framework under the ITL for a limited period of time only. The period will be generally six to twelve months, and in exceptional cases, the DFSA may consider extending that to a period of no longer than two years.

Step 4: Completion phase and progression to business as usual

Both during, and at the end of, the testing period the fintech firm would be expected to notify the DFSA of its results during the testing phase and also whether it wants to carry on its fintech business on a broader scale or cease carrying on activities in the DIFC.

Based on its decision, the DFSA would discuss with the fintech firm the process for obtaining approval to remove the restrictions, so it has a full Financial Services Licence or, alternatively, to exit. If the firm does become fully operational, it would ordinarily be expected to comply with all relevant regulatory requirements. However, in appropriate cases, the DFSA may consider whether further waivers or modifications are required to specific Rules.

Fees

The main objective of the proposals set out in this consultation paper is to facilitate the testing of fintech innovations in the DIFC. As such we are proposing to apply a fee that would be proportionate to the scope of the limited licence and discussions with the fintech firm during the application stage.

Issues for consideration:

Q1: Do you have any comments or questions on our proposed approach to the testing of innovative fintech business propositions?

Q2: Do you agree with our proposal to apply a fee that would be proportionate to the scope of the limited Licence?

Annex 1: Table of Comments

Name of commentator:		
Name of entity (if applicable)		
Is your response confidential?	<input type="checkbox"/> Yes	<input type="checkbox"/> No

Notes:

- The DFSA reserves the right to publish, including on its website, any comments you provide. However, if you wish your comments to be kept anonymous, you must expressly request at the time of making comments that this should be the case.
- Your answers may require explanations. Please include those in the second column.
- If you do not wish to comment on any issue, please select the “no comments” box.

Ref.	Response	Comments on proposal
Q1:	Do you have any comments or questions on our proposed approach to the testing of innovative fintech business propositions?	
	<input type="checkbox"/> Yes	
	<input type="checkbox"/> No	
	<input type="checkbox"/> No comments	
Q2:	Do you agree with our proposal to apply a fee that would be proportionate to the scope of the limited Licence?	
	<input type="checkbox"/> Yes	
	<input type="checkbox"/> No	
	<input type="checkbox"/> No comments	