

Central Bank of Bahrain (CBB) launch regulatory sandbox for fintech firms

Rad El Treki - Partner, Head of Office - Bahrain - Corporate Structuring / Corporate / Mergers and Acquisitions / Capital Markets / Commercial / Corporate Services
r.eltreki@tamimi.com - Manama

June 2017 witnessed the introduction by the Central Bank of Bahrain (“CBB”) of a regulatory sandbox aimed at enabling firms to test and develop their products in a virtual space. The introduction of the regime positions the Kingdom of Bahrain (“Bahrain”) as only the second state within the Gulf Cooperation Council to implement such a framework. This article provides an overview of the new framework, including eligibility requirements and the application procedure and timelines.

A regulatory sandbox can be considered to be a framework and process that facilitates and encourages the development of the financial technology (“FinTech”) sector in a safe, measured and pragmatic manner. The virtual space created by such a framework provides a safe area in which FinTech businesses (both established and start-ups) can test and refine their technology based innovative products, services and platforms without being immediately burdened by the usual regulatory and financial requirements which would otherwise apply to their activities. The effect is that FinTech firms are able to experiment with their products and services for a specified timeframe within a partially deregulated environment where the firms are able to offer their products and services to customers, but where risks to customers (and to the wider financial system as a whole) are mitigated none the less.

Key characteristics of the Bahrain Regulatory Sandbox

Some of the particularly notable features of the Bahrain regulatory sandbox include the following:-

- The regulatory sandbox is open to existing CBB licensees as well as to entities or firms which are not currently licensed by the CBB (both Bahraini and foreign). Such non-licensed firms or entities may include financial sector companies as well as technology and telecom companies; professional services firms which partner with or service financial institutions; and any other type of applicant working within the financial services industry and deemed acceptable by the CBB.
- The regulatory sandbox is open both to existing FinTech solutions which have been tested within a lab environment, as well as to ideas and solutions which are yet to be fully developed and/or tested.
- The timeframe for any applicant to remain within the regulatory sandbox is a maximum of nine months (with the possibility of an entirely discretionary extension of three months).
- The testing of the product or service by the applicant may be limited by the CBB in terms of the number of volunteer customers and/or the amounts involved.

Eligibility Criteria

The key eligibility criteria to be satisfied by applicants include the following, all of which must be evidentially demonstrated to the satisfaction of the CBB:

- Innovation. The applicant’s product or service (or its use) must be shown to be truly innovative or be significantly different to existing solutions within the Bahrain market.
- Customer Benefits. The applicant’s product or service (or its use) should offer tangible direct or indirect benefits to customers, supported by quantifiable estimates or demonstrations.

- Technical Testing (for existing solutions). Where the applicant's product or service involves an existing solution, the solution needs to have undergone technical testing with the results to be provided to the CBB. In the alternative, external validation of the technical soundness of the solution from a reputable third party may be accepted.
- Regulatory testing readiness. Applicants are required to show evidence of a well developed regulatory testing plan, to include highlighting of the key risks the solution poses; details of how these will be mitigated; and details of adequate safeguards to protect customers.
- Post-testing deployment in Bahrain. The applicant should demonstrate both its intention and ability to deploy the proposed solution in Bahrain by way of submission of a Sandbox exit strategy (to include specific details of proposed scale-up and future deployment).

Application Procedure

Applicants are required to submit their application in writing to the CBB using the template CBB application form, attaching all relevant supporting documentation. The application form includes sections in which applicants must provide details of the following:

- A description of the applicant's organisation including its corporate structure, key business lines and centres, and its financial standing and technical expertise;
- The proposed innovative financial solution, and how it satisfies the eligibility criteria discussed above;
- The information as to the type (and number) of volunteer customers to be included in the applicants sandbox testing; how these will be sourced, and proposals to protect the volunteer customers and their confidentiality;
- Key performance indicators and targets which will be used to determine the success of the testing whilst in the regulatory sandbox;
- The cyber security and other relevant measures to be taken by the applicant to maintain security of the solution service or product; and
- The applicant's exit plan, plans for scale up and deployment strategy, together with a timeline of steps to be taken to meet the additional legal and regulatory requirements to be satisfied after exiting the regulatory sandbox.

The CBB has the right to relax certain requirements on a case by case basis.

Upon receipt of the completed application and all accompanying documentation together with the application fee (current set at one hundred Bahraini Dinars) the CBB will review the application and endeavour to respond to the applicant within fifteen days, either approving or rejecting the applicant's application.

Where approved, the applicant is then able to enter the regulatory sandbox in accordance with the terms and conditions of the framework and the applicant's application and commence the testing of its product or service based solution. The CBB have indicated that arrangements have been put in place with the other relevant Bahraini government authorities (for example, the Ministry of Industry Commerce and Tourism and the Labour Market Regulatory Authority) to enable applicants to, for example, employ and sponsor (for visa purposes) employees in Bahrain during the testing phase. Full details of these arrangements and how they operate are awaited.

Whilst in the regulatory sandbox, applicants are required to adhere to the relevant CBB regulations with regards to Know Your Customer (KYC), Anti-Money Laundering (AML) and Countering Financing of Terrorism (CFT). Additionally, in so far as the applicant will as part of its sandbox testing be receiving any money from the volunteer customers, the applicant is required to entrust the handling of these funds to CBB licensed retail banks.

At the end of the designated sandbox period (which as mentioned, is a maximum of nine months with the

possibility of an entirely discretionary extension of three months) the applicant exits the regulatory sandbox, and may apply for the relevant CBB licence depending on the precise activities of the applicant.

Since the launch of the new framework, six entrants have so far been welcomed into the regulatory sandbox, including London based Tramonex (a forex start-up focused on facilitating conversion and settlement services to automate cross border transaction); Dubai firm Now Money (one of the first FinTech companies in the Gulf to use mobile banking technology to provide accounts, financial inclusion and a range of low cost money remittance options to low-income workers); and Belfrics Global (a Malaysian based Bitcoin technology provider).

The CBB has also established a dedicated FinTech Unit within the CBB with the mandate of ensuring the provision of the best services to individual and corporate licensees in the financial sector. The FinTech Unit is responsible for the approval process to participate in the regulatory sandbox, as well as supervision of licensed companies' activities and operations, including cloud computing, payment and settlement systems, and monitoring technical and regulatory developments in the FinTech field.

The introduction of the new framework and the creation of a dedicated FinTech Unit within the CBB is consistent with Bahrain's continued focus on further developing the Kingdom as the emerging FinTech and financial services hub of the Middle East region, promoting increased competitiveness and the encouraging the embracing of new technologies. At the same time, the safeguards built into the scheme will assist to maintain the required level of consumer protection and regulatory oversight which have long established Bahrain as one of key financial sector hubs in the region.