

The top portion of the page features a dark green background with a complex, glowing circuit board pattern. The lines and nodes of the circuit are rendered in a lighter green, creating a sense of depth and technology.

InFocus

Digital Financial Advice Module Summary

A summary of digital financial advice regulations
issued by the Central Bank of Bahrain

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INTRODUCTION

On January 21st 2019, the Central Bank of Bahrain (CBB) issued draft regulations (14 pages) on the provision of digital financial advice (also referred to as robo-advisory). The document is directed towards digital financial advice providers alongside banks and investment firm licensees that are looking to offer such advice digitally. This module is available under the CBB Rulebook Volume 1 (Conventional Banks), Volume 2 (Islamic Banks), and Volume 4 (Investment Businesses). The CBB will be accepting feedback for Volume 1 and 2 modules until February 20, 2019; whereas Volume 4 module's deadline for feedback is February 21, 2019.

DEFINITIONS

Algorithms

A set of mathematical rules that translates the data entered into a system through financial modelling techniques to generate financial advice.

Digital Financial Advice

The provision of financial advice through the use of technology (also commonly known as robo-advice or automated advice). Digital financial advice is subjected to a comprehensive governance and controls framework as the technology is based on algorithms and assumptions that translate consumer inputs into financial advice.

Key Themes

Governance of digital financial advice process

Licensees providing digital financial advice must have detailed and effective oversight of the digital financial advice process and the client-facing tool. Governance of the digital financial advice process involves the identification of system design defining purpose, scope, and algorithms. In regard to algorithms, a testing strategy should be implemented to detect errors, biases, or unauthorized access.

Additionally, the algorithms need to be regularly updated based on changes in the market or regulations. Finally, the algorithms should be prepared for the suspension of digital financial advice in key scenarios such as when there are two or more conflicting answers to risk profiling or an error is detected that could likely result in a breach or consumer loss.

While licensees are obligated to oversee client-facing tools, the CBB also highlighted that the licensees are not allowed to outsource key processes and management of client-facing tools.

Technology supporting the digital financial advice tool

The algorithms need to be able to identify clients who would be classified as unsuitable investors. Licensees are required to maintain a regularly updated security policy document that includes details on the IT system supporting the digital financial advice tool, implemented security measures, location of licensee data centers, policies on system monitoring, and external technology partners authorization.

Digital financial advice control framework evaluation

The control framework of the digital financial advice tool needs to be tested and evaluated by an external consultant once a licensee initially sets up its system, if any changes have been made to the system, and also every three years.

Licensee obligations to client

Licensees of digital financial advice are obligated to inform clients during the on-boarding process of the following:

- Full scope of digital financial advice including the methodologies, assumptions, limitations, and risks of the algorithms
- Specific circumstances in which licensees can replace digital advice with human judgement or discontinuation of the service
- Disclaimer regarding the digital financial advice that does not consider client's personal circumstances
- Changes to key input parameters and algorithms

Consumer protection

To safeguard the interest of the consumer, licensees should be able to protect the clients from unsuitable advice. It is important for the licensee to protect client data and licensees are required to adhere to Bahrain's Personal Data Protection Law (PDPL) issued on 12 July, 2018 to ensure client data protection.

CONCLUSION

This summary highlights key requirements and recommendations by the CBB for future digital advice providers. Alongside the brief, we highly recommend reading the draft regulations which can be found in Volume 1, Volume 2, and Volume 4.