



Digital Bank Licensing Principles

The National Bank of Georgia strives to promote development of new technologies and innovative approaches in the financial sector to increase financial stability and financial inclusion. To this end, the National Bank of Georgia is introducing a technologically neutral risk supervision approach and open regulation principles. These principles represent a part of the [National Bank's supervisory strategy for 2020-2022](#). It is noteworthy that within the framework of this approach, the National Bank has already launched the [Financial Innovation Office](#) and a [Regulatory Laboratory](#).

Currently, the NBG is considering the issue of digital bank licensing in Georgia. By facilitating the development of the digital banking model, the National Bank aims to: promote the development of innovative business models and diversity of financial products; make better use of big data; develop a customized, convenient, fast and affordable digital financial ecosystem utilizing the technological infrastructure around the customer; use effectively the cloud services; simplify integration with technology companies and develop a banking as a service business model; facilitate entry of new technological players and increase competition in the financial sector. At the same time, the supervisory goals of the National Bank of Georgia are: implementation of new risk mitigation mechanisms in the process of developing a new digital bank model, development of modern reliable standards for personal data security in cyberspace and improvement of systemic and financial stability risk management. It should be noted that under systemic risks the National Bank also means shortcomings in protection of consumer rights and interests, which may potentially have a negative impact on financial system development and financial stability.

Digital Bank Business Model

The National Bank of Georgia considers digital bank as a business model that has a potential to increase access to finance, reduce the cost of financial intermediation and, at the same time, meet the following technological criteria (inter alia, combination of only few from the below listed can be acceptable):

- ✓ Provide banking services mainly through digital channels;
- ✓ Use materially new technologies and / or innovative technological business models for the local market when providing banking services;
- ✓ Focus on developing open banking and wholesale banking as a service business model;
- ✓ Both external and internal banking modules are based on the API interface and the technological infrastructure relies on a modular arrangement (e.g. according to the principles of [BIAN Standard](#));
- ✓ Have digital technological means for user identification, authentication and can provide this service to the third parties.

The definition of digital bank does not imply such new financial products that do not contain a technological component, nor does it imply efficient implementation of existing business models in the market, where efficiency and competitive advantage come from non-technological components.

Requirements for obtaining a license

An applicant can be any legal entity that shall meet the following requirements:

- ✓ Meet the technological criteria of digital bank;
- ✓ Be able to demonstrate that it has a sustainable business model of digital banking that is not just a general concept. This implies the presence of a detailed and reliable business plan, which also includes:
 - Details on how the applicant intends to conduct its business and progressively meet the requirements for obtaining a full banking license;
 - Financial and operational goals, relevant quantitative and qualitative benchmarks and deadlines that will be used to assess the success of the activity.
- ✓ Have a business termination plan and deal appropriately with technology-related risks. The termination plan must include:
 - The list of triggers upon which the termination plan will take effect;
 - The organizational unit and persons responsible for triggering and smooth implementation of termination plan;
 - Identification and mitigation of material risks that could hinder the execution of the plan;
 - Mechanisms for minimizing risks for consumers and the financial system;
 - Channels and resources that will be used to make settlements with customers;

- ✓ Analyze the risks of money laundering and terrorism financing during the process of providing services through electronic channels and their mitigation measures.
- ✓ Meet the requirements for obtaining a banking license defined under the legislation of Georgia.

The business plan as well as business termination plan submitted by the applicant shall be subject to periodical review and development in parallel with the digital bank licensing process.

Licensing Process

The purpose of the digital bank licensing process is to identify potential systemic risks in the business model through testing in a trial and real environment and, if any, to effectively and timely mitigate them. If this is not possible, the process shall ensure prompt suspension of banking activities. It should be noted that the test results based on the new business model can become the basis for further development and refinement of the National Bank's supervisory framework. When issuing a license to digital bank, the National Bank, in order to minimize systemic risks, will use a step-by-step transition approach towards a full banking license, which, like the principles set out in the [Statute on the Regulatory Laboratory Framework and its Application](#), involves three stages:

I. At the initial stage, the National Bank will assess:

- ✓ Innovativeness of the presented business model and compliance with the concept of digital banking.
- ✓ Compliance with the requirements established under the legislation of Georgia for obtaining a banking license.

As a result of the assessment, the National Bank will issue a banking license and set a deadline for the operation of the digital bank. A digital bank license is issued with a number of conditions and restrictions, including:

- ✓ Alleviating the minimum regulatory capital requirement - 10% [of the minimum regulatory capital defined for commercial banks](#);
- ✓ Alternative liquidity requirements; instead of computing the LCR-NSFR, the simple liquidity coverage ratio is calculated in proportion to the attracted funds; the initial limit is 100%.
- ✓ Restrictions on banking operations. Banking transactions are allowed only for insiders participating in the test.

- ✓ Terms, conditions and benchmarks to limit systemic risk, and test the potential of a proposed business model. Certain terms may include direct or modified operational goals and respective quantitative and qualitative benchmarks stemming from the business plan.

Following the license issuance, the digital bank has the opportunity to seek additional qualified investors for the gradual replenishment of the remaining capital, taking into account the eligibility requirements set by law.

The National Bank of Georgia will consider the issue of relieving the listed requirements based on the individual needs of the presented business model.

II. At the next stage, the license holder should pass a proof of concept test, which involves examining the business model in a test environment. In addition, the bank must submit:

- ✓ The penetration test on the full operating environment of the bank, security systems assessment and network audit reports conducted by independent third party.
- ✓ Audit and risk assessment for the outsourced third party systems and cloud service providers.

III. Upon successful completion of the second stage, the entity should be allowed to conduct banking operations in the real environment within the limits set by the National Bank. These limits may include:

- ✓ Attracting deposits and equivalent credits;
- ✓ Liquidity;
- ✓ Use of complex financial products (e.g. complex derivative and structured products). This does not imply restrictions on the use of technologically complex products.
- ✓ International operations.

A full audit of the information systems conducted by an independent third party shall be submitted to the National Bank within 6 months following the commencement of operations in the real environment.

The National Bank will revisit the above limits and requirements periodically, according to individually defined deadlines and test monitoring results, and in case of satisfactory outcome, remove the restrictions set for the bank, after which the latter will continue to operate under the full banking license.

This process can go on for no more than 3 years. Digital Bank may additionally request the extension of this process for not more than 1 year.

At any stage, in the event of detecting significant systemic risks and / or operational challenges, the National Bank of Georgia may require activation of the business termination plan and revoke the banking license.

Consulting and discussions for interested parties

Those interested in obtaining a digital bank license and/or developing a digital bank framework can contact the National Bank's [Financial Innovation Office](#).