

INSURANCE REGULATION IN THE ADGM AND THE DIFC: A COMPARATIVE GUIDE



The Abu Dhabi Global Market (ADGM), located on Al Maryah Island, Abu Dhabi, was established in 2013 as Abu Dhabi's financial services free trade zone. The ADGM ultimately intends to be a broad financial services hub for local, regional and international entities seeking to do business in the Gulf and the wider region. Its initial focus is on the private banking, wealth management and asset management sectors, reflecting Abu Dhabi's particular economic strengths.

In June 2015, ADGM issued its first set of commercial regulations and rules, including regulations relating to the legal framework to be applied in ADGM and regulations in relation to companies, commercial licensing, insolvency, employment, property and strata title. The approach of the ADGM is to mirror the United Kingdom's legislation, thus incorporating common law principles within the ADGM legal framework.

Potential investors have been eagerly awaiting the second round of regulations, particularly those in relation to the regulated financial services that can be undertaken in and from ADGM. On 20 and 21 October 2015, the Board of Directors of ADGM issued regulations regarding the rules governing the provision of financial services in and from ADGM, including rules in relation to conduct of business, the management and marketing of funds, anti-money laundering and sanctions and prudential rules.

These regulations and rules are broadly based on the United Kingdom's Financial Services and Markets Act 2000 (FSMA).

This article considers the key features of the new regulations and compares them to those currently in place in Dubai's financial services free trade zone, the Dubai International Financial Centre (DIFC). We have not addressed in this article the regulations and rules in relation to other financial services, limited liability partnerships or data protection.



Financial services – overall framework

The range of financial services that can be undertaken in and from ADGM are set out in the core Financial Services and Markets Regulations 2015 (Financial Services Regulations), with subsidiary requirements being set out in separate rulebooks which are administered by an independent financial services regulator, the ADGM Financial Services Regulatory Authority (FSRA). The FSRA will also have the power to issue indicative, non-binding guidance in relation to the rules.

This is similar to the DIFC's financial services regulatory framework, pursuant to which the DIFC Regulatory Law¹ sets out the range of financial services that can be undertaken in and from the DIFC, with supplementary details being set out in separate rulebook modules which are issued and administered by the Dubai Financial Services Authority (DFSA). The DFSA also issues indicative, non-binding guidance within its Rulebook modules.

Similar to the DIFC, entities providing financial services, referred to in ADGM as "regulated activities", in and from ADGM will need to obtain two licences:

- A commercial licence from the registration authority – the Registration Authority in ADGM and the DIFC Registrar of Companies in the DIFC.
- A regulated activity permission/ financial services licence from the

financial services regulator - the FSRA in ADGM and the DFSA in the DIFC.

Regulated activities and insurance related activities

ADGM's Financial Services Regulations effectively provide the following two restrictions, which are aligned with those under FSMA and the DIFC Regulatory Law:

- Carrying out a "regulated activity" by way of business without the necessary authorisation or exemption, referred to as the "General Prohibition" in ADGM and the "Financial Services Prohibition" in the DIFC².
- In the course of business, communicating an invitation or inducement to engage in investment activity unless authorised or unless the content has been approved by an Authorised Person, the "Financial Promotion Restriction" in ADGM and the "Financial Promotions Prohibition" in the DIFC³.

Schedule 1 of the Financial Services Regulations sets out what will be a "regulated activity" in ADGM and provides for the following types of insurance-related regulated activities:

- Carrying out contracts of insurance as Principal.
- Effecting contracts of insurance as Principal.

- Insurance intermediation⁴.
- Insurance management⁵.

The definitions of each of the above activities and the applicable exclusions in the Financial Services Regulations are very similar to those provided for in the DFSA Rulebook's General Module (GEN). The only material difference between the ADGM's and the DIFC's insurance related activities is that the ADGM's Financial Services Regulations provide an additional exclusion from the activity of Insurance Management. The Financial Services Regulations provide that an exclusion to the activity of Insurance Management is any activity which:

- (a) "is carried on in the course of carrying on any profession or business which does not otherwise consist of the carrying on of Regulated Activities in the Abu Dhabi Global Market; and
- (b) may reasonably be regarded as a necessary part of other services provided in the course of that profession or business.

(2) But the exclusion in sub-paragraph (1) does not apply if the activity in question is remunerated separately from the other services."⁶

Part 4 of Schedule 1 of the Financial Services Regulations provides a definition of a "Contract of Insurance" and divides these into 7 classes of life insurance and 9 classes of non-life insurance. The definition is the same as that provided in Appendix 4 of the DFSA Rulebook's GEN.

1 DIFC Law No. 1 of 2004.

2 ADGM: Article 16 of the Financial Services Regulations. DIFC: Article 41 of the DIFC Regulatory Law.

3 ADGM: Article 18 of the Financial Services Regulations. DIFC: Article 41A of the DIFC Regulatory Law.

4 Defined in the Financial Services Regulations as follows: "Insurance Intermediation means –

(a) advising on Contracts of Insurance;

(b) acting as agent for another person in relation to the Buying or Selling of Contracts of Insurance for that other person; or

(c) making arrangements with a view to another person, whether as principal or agent, Buying Contracts of Insurance."

5 Defined in the Financial Services Regulations as follows: "Insurance Management means providing management services or exercising managerial functions for an Insurer". Management services and managerial functions include administration and underwriting.

6 ADGM Financial Services Regulations, Schedule 1, paragraphs 37(3) and 75.



ADGM General Rulebook (GEN)

ADGM's GEN applies to all persons to whom the Financial Services Regulations apply and sets out:

- Core principles such as integrity, due skill, care and diligence, resources etc.) with which Authorised Persons and Approved Persons must comply.
- The requirements upon senior management to implement effective systems and controls, including best practice relating to corporate governance and remuneration.
- The FSRA's authorisation requirements to become an Authorised Person and requirements relating to Approved Persons.
- A requirement for Authorised Persons to appoint auditors and ensure their production of regulatory returns.
- Complaints handling and dispute resolution procedures.
- The FSRA's supervisory standards.
- The requirements for representative offices operating in ADGM.

Chapters 2, 3, 4, 5, 6, 7 and 8 of ADGM's GEN are very similar to Chapters 4, 5, 6, 7, 8, 9 and 11 respectively of the DFSA Rulebook's GEN. The material differences between the ADGM's GEN and that of the DFSA are:

■ Conflicts of interest and information barriers:

The management of conflicts of interests are one of the core principles to be upheld by authorised firms within both ADGM and the DIFC. However, ADGM's GEN Chapter 5 further elaborates on the systems and controls to be put in place by firms to ensure prevention and management of conflicts and necessary disclosures in the event of a conflict. ADGM's GEN Chapter 5 also provides further detail in relation to information barriers or "Chinese walls" between different sections of its business where necessary which are similar to those adopted in the UK FCA Handbook. While the DFSA Rulebook's Conduct of Business Module (COB) and the DIFC Markets Law⁷ contain several references to and a brief definition of the concept of "Chinese Walls", ADGM's GEN Rules 3.3.25 to 3.3.30 provide much more clarity in this respect.

■ Registered auditors:

The DFSA requires that authorised firms which are incorporated in the DIFC ensure that their auditor, at the time of appointment and for the duration of the engagement, is registered with the DFSA.⁸ ADGM's equivalent, GEN Rule 6.4.1, contains no such requirement. However, as the FSRA will not register auditors, ADGM's GEN Rules 6.6.4 to 6.6.9 provide detailed requirements in relation to the contents of auditor's reports and requires Authorised Persons to

procure that their auditors ensure their auditor's reports comply with these requirements.

■ Disregarded holdings and controllers:

ADGM's regime relating to notifications to, and approvals from, the FSRA in respect of changes in control over Authorised Persons is modelled on Part XII of FSMA and there are therefore subtle differences with the regime applicable in the DIFC. Both the DFSA and ADGM provide that a controller is a Person who either alone or with any Associate:

- (a) Holds 10% or more of the shares in either the Authorised Person or a Holding Company of that Authorised Person.
- (b) Is entitled to exercise, or controls the exercise of, 10% or more of the voting rights in either the Authorised Person or a Holding Company of that Authorised Person.
- (c) Is able to exercise significant influence over the management of the Authorised Person as a result of Holding shares or being able to exercise voting rights in the Authorised Person or a Holding Company of that Authorised Person or having a current exercisable right to acquire such shares or voting rights.⁹

ADGM's rules in relation to disregarded holdings when considering whether a person is a

⁷ DIFC Law No. 1 of 2012.

⁸ DFSA GEN Rule 8.4.1(c).

⁹ ADGM GEN Rule 8.8.2.



Controller includes a carve-out in relation to shares representing no more than 5% of the total voting power which are held by an Authorised Person with a Financial Services Permission to deal as principal who:

1. Holds the shares in the capacity of a market maker.
2. Neither intervenes in the management of the Authorised Person in which it holds the shares, nor exerts any influence on that Authorised Person to buy the shares or back the share price.¹⁰

The above carve-out is not provided for in the DFSA's regime. ADGM also requires:

- The prior approval of the FSRA before a person can become a Controller of an Authorised Firm – this is similar to the DFSA's requirements.¹¹
- The prior written approval of the FSRA for any increase of control from below 20% to 20% or more.¹² This is in addition to approval requirements for similar thresholds as those of the DFSA from below 30% to 30% or more and from below 50% to 50% or more.¹³
- Notification to the FSRA if a person proposes to decrease that person's holding from the 50%, 30% and 20% thresholds.¹⁴ In contrast, the DFSA only

requires a notification for a decrease from above 50% to 50% or less.¹⁵

- **Major acquisitions:** The DFSA requires Authorised Firms to notify the DFSA of any proposed "Major Acquisition" by the Authorised Firm of another body corporate and to not proceed with the acquisition, unless it obtains the DFSA's no objection or the DFSA does not object within 45 days of the notification.¹⁶ ADGM does not have an equivalent to this process, although there is a general obligation on Authorised Persons to notify the FSRA of "*any proposed restructuring, merger, acquisition, reorganisation or business expansion which could have a significant impact on the Authorised Person's or Recognised Body's risk profile or resources*".¹⁷

- **Representative offices:** ADGM's GEN Chapter 9 contains the requirements in relation to Representative Offices. Such rules are contained in a separate Representative Office Module of the DFSA Rulebook (REP), however, the requirements in the DFSA Rulebook's REP and Chapter 9 of ADGM's GEN are broadly similar.

ADGM Conduct of Business Rulebook (COBS)

ADGM's COBS sets out the rules of conduct applicable to any firm carrying on any Regulated Activity in ADGM. The rules reflect international standards

and are substantially similar to those in the DFSA Rulebook's Conduct of Business (COB) module. Notably, ADGM's proposed client classification regime in Chapter 2 of COBS is in line with the DIFC's client classification regime which was introduced in April 2015 and provides for the following categories and sub-categories of clients:

1. Retail clients.
2. Professional clients which consists of:
 - "Deemed" professional clients.
 - "Service-based" professional clients.
 - "Assessed" professional clients, although the net asset threshold is stated in ADGM's COBS as US\$500,000; the DFSA's net asset threshold is increasing to US\$1 million from 1 April 2016.
3. Market counterparties.

ADGM's COBS also includes similar provisions in relation to reliance on client classifications made elsewhere and group client classifications as those implemented by the DFSA in April 2015.

Importantly for the insurance industry, ADGM's COBS Rule 7.2.2 contains the same restriction as in the DFSA's COB Rule 7.2.2 which effectively restricts insurance business, insurance intermediation and insurance management activities in relation to

¹⁰ ADGM GEN Rule 8.8.3(c).

¹¹ ADGM GEN Rule 8.8.4(1)(a) and DFSA GEN Rule 11.8.4(1)(a).

¹² ADGM GEN Rule 8.8.4(2)(a).

¹³ ADGM GEN Rule 8.8.4(b) and (c) and DFSA Rule 11.8.4(a) and (b).

¹⁴ ADGM GEN Rule 8.8.9(b).

¹⁵ DFSA GEN Rule 11.8.9(b).

¹⁶ DFSA GEN Rules 11.10.8 to 11.10.12.

¹⁷ ADGM GEN Rule 8.10.6.



any risks situated in the UAE which are outside the ADGM/DIFC geographical boundaries to reinsurance business. Therefore, like the DIFC, it is likely that ADGM will operate primarily as a wholesale reinsurance hub.

ADGM Prudential – Investment, Insurance Intermediation and Banking Rules (PRU)

ADGS's PRU applies to all Authorised Persons in ADGM other than insurers, representative offices, and credit rating agencies. Similar to the DFSA Rulebook's Prudential – Investment, Insurance Intermediation and Banking (PIB) module, Authorised Persons in ADGM are allocated to five categories based on their activities, with firms undertaking Insurance Intermediation and Insurance Management falling into Category 4.

Also similar to the requirements in the DFSA's PIB module, ADGM's PRU requires Category 4 firms to hold capital which is the higher of:

- US\$10,000.
- If the firm will not hold Insurance Money, 6/52 of Annual Audited Expenditure or if the firm will hold Insurance Money, 18/52 of Annual Audited Expenditure.¹⁸

ADGM Prudential – Insurance Business Rules (PIN)

ADGS's PIN applies to all Insurers¹⁹ in ADGM unless certain provisions specify a narrower application, the key exception being Insurance Special

Purpose Vehicles (ISPVs)²⁰. ADGM's PIN is substantially similar to the DFSA Rulebook's Prudential – Insurance Business Module (PIN) and does not reflect the pending EU Solvency II Directives, which are due to come into force on 1 January 2016. We understand that both the DFSA and ADGM are waiting until Solvency II has been implemented in Europe before considering the appropriateness of similar rules in the DIFC/ADGM.

Both ADGM's PIN and the DFSA's PIN require an Insurer to have capital resources that are, in the opinion of its directors, formed on reasonable assumptions, adequate for the conduct of its business, taking into consideration the size of the Insurer and the mix and complexity of its business.²¹ Further, ADGM's PIN and the DFSA's PIN require that an Insurer that is not a Protected Cell Company must have Adjusted Capital Resources, which are calculated in accordance with Appendix 3 of PIN, equal to or higher than the amount of its Minimum Capital Requirement, which is calculated in accordance with Appendix 4 of PIN.²² However, an important difference between ADGM's PIN Appendix 4 and the DFSA's equivalent is the requirement in the DFSA's PIN that an Insurer's Minimum Capital Requirement must always be equal to or higher than:

- Class 1 Captive Insurer: US\$150,000.
- Class 2 Captive Insurer: US\$250,000.

- Class 3 Captive Insurer: US\$1,000,000.
- All other Insurers: US\$10,000,000.²³

ADGM's PIN does not specify any such minimum requirement for insurers that are not captives. The minimum capital requirements in relation to captives are discussed further below.

Captive Insurance Business Rules (CIB)

ADGS's CIB sets out specific rules in relation to captive insurers. This distinguishes ADGM from the DIFC, which does not contain a specific rulebook in relation to captives, but rather provides rules relating to captives in several different modules of the DFSA's Rulebook. The ADGM's CIB sets out four categories of captive insurer for the purpose of determining applicable capital rules:

- **Class 1 Captive Insurer:** effects or carries out contracts of insurance only for risks related to or arising out of the business or operations of the group to which the insurer belongs.
- **Class 2 Captive Insurer:** obtains no more than 20% of its gross written premium from third party risks arising from business or operations that are closely linked to the business or operations of the group to which the insurer belongs.
- **Class 3 Captive Insurer:** effects or carries out contracts of insurance

18 ADGM's PRU Rules 3.6.2 and 3.7.2 and DFSA GEN Rules 3.6.2 and 3.7.2.

19 That is, Authorised Persons in ADGM who are authorised under their Financial Services Permission to carry on the activities of Carrying Out Contracts of Insurance as Principal and/or Effecting Contracts of Insurance as Principal.

20 An ISPV is defined in both the ADGM Rulebook's Glossary Module and the DFSA Rulebook's Glossary Module as an insurer which:

(a) assumes risks by way of reinsurance; and
(b) is required to fully fund its exposures to those risks through the proceeds of a debt issuance or some other financing arrangement where the repayment obligations under those arrangements are subordinated to the insurer's reinsurance obligations.

As ISPVs fully fund their exposures, ISPVs are not required to comply with the following requirements in ADGM's PIN and the DFSA's PIN: Chapter 2: management and control of risk; Chapter 3: long-term insurance business; Chapter 4: capital adequacy; Chapter 6: financial reporting; Chapter 7: actuaries; and Chapter 9: insurers in "run-off".

21 ADGM PIN Rule 4.2.2 and DFSA PIN Rule 4.2.2.

22 ADGM PIN Rule 4.3.2 and DFSA PIN Rule 4.3.2.

23 DFSA PIN A4.2.3.



only for risks related to or arising out of the business or operations of persons who engage in similar, related or common businesses, activities, trade, services, or operations and is owned by these persons or by a body corporate of which all such persons are members.

■ **Class 4 Captive Insurer:** a captive insurer which the FSRA decides does not meet the requirements for a Class 1, 2 or 3 Captive Insurer.

While the DFSA's captive insurer regime is similar to that in ADGM's CIB, the key distinction is that unlike the FSRA, the DFSA does not have a discretion to allow the establishment

of a captive which does not meet the requirements for a Class 1, 2 or 3 Captive Insurer, that is, the DIFC does not have a Class 4 Captive Insurer.

As noted above, the DFSA's PIB rules specify certain minimum capital requirements for captives. By way of comparison, the ADGM's minimum capital requirements for captives are²⁴:

TABLE 1

ACTIVITY	ADGM (US\$)	DFSA (US\$)
Class 1 Captive Insurer	150,000	100,000
Class 2 Captive Insurer	250,000 (unless the FRSA sets a different amount)	250,000
Class 3 Captive Insurer	500,000	1,000,000
Class 4 Captive Insurer	1,000,000 (unless the FRSA sets a different amount)	N/A

HFW comment

Over the last 10 years, the DIFC has established itself, and the UAE, as a leading international financial centre and has served as a hub for regional and international insurance operations, including most recently for the Corporation of Lloyd's and several Lloyd's underwriting agencies. Although it is likely that ADGM will further strengthen the UAE's position as a leading international financial centre there is, at this stage, some uncertainty as to the relationship between the DIFC and ADGM. Both ADGM and the DIFC offer foreign investors:

- The opportunity to establish a 100% foreign owned entity.
- 0% tax rate.
- Ability to repatriate profits and capital.
- An English language, common law jurisdiction, with entities operating in ADGM/DIFC being exempt from the application of UAE Federal and Emirate-level laws on civil and commercial matters (UAE criminal laws will continue to apply).

- An independent court system, financial services regulator and registrar.

Therefore, it is not immediately clear how ADGM will compete with the DIFC, particularly in light of the DIFC's 10 year "head start". It currently appears that ADGM offers the following advantages over the DIFC:

ADGM provides lower licence fees (see Table 1 for a comparison of the financial services licence fees in ADGM and the DFSA's equivalent licence fees).

TABLE 2: ADGM REGULATED ACTIVITY PERMISSION AND DFSA FINANCIAL SERVICES LICENCE FEES

ACTIVITY	ADGM FEE (US\$)	DFSA FEE (US\$)
Insurance Intermediation and/or Insurance Management	3,000 for one activity or 8,000 for both	15,000 for one or both activities
Effecting Contracts of Insurance and/or Carrying Out Contracts of Insurance	30,000	40,000
Approved Person/Authorised Individual approval	500	500 (other than in conjunction with an initial application for a licence)

²⁴ ADGM's CIB Rule 2.2.2 and DFSA's PIN A4.2.3.



ADGM may have an advantage because the underlying legal framework for ADGM is English common law as it stands from time to time, subject to specific ADGM regulations and UAE laws applicable to ADGM²⁵. Therefore, English common law in relation to areas such as contracts, torts, trusts, equity will apply directly to those operating in and from ADGM. This is in contrast to the DIFC, which rather than directly applying English common law, codifies certain aspects of English law into specific DIFC laws and regulations, for example DIFC specific Contract Law and Law on Damages and Remedies. ADGM's model is similar to the models adopted in Hong Kong and Singapore and is a new model in the Middle East.

As a result of ADGM's direct application of English common law, English court judgments authority on ADGM's courts. ADGM's Court of First Instance and Court of Appeal will have jurisdiction over all civil and commercial disputes within ADGM. Recently it was announced that The Right Honourable Lord David Hope of Craighead would be Chief Justice of the ADGM Courts and Linda Fitz-Alan would be the ADGM Courts Registrar. Lord Hope is one of the most respected and experienced senior judges in the United Kingdom. Ms Fitz-Alan has more than 30 years' legal experience, including over four years' as CEO and Principal Registrar of the Supreme Court of New South Wales, Australia. The appointment of Lord Hope and Ms Fitz-Alan, both from common law backgrounds, will ensure that ADGM offers a sophisticated and certain legal and regulatory regime, similar to financial centres such as Singapore, Hong Kong and London.

As discussed above, ADGM's CIB Rulebook provides a more flexible captive insurer regime than that of the DFSA and comparable and at times

lower minimum capital requirements for captive insurers. We expect that this added flexibility will encourage the establishment of new captives in ADGM.

Another possible draw-card for ADGM, albeit of a non-regulatory nature, is the vision for Al Maryah Island's development as a 114 hectare business, leisure and entertainment hub compared to the DIFC which is 110 acres (approximately 44.5 hectares). Al Maryah Island offers exclusive shopping and dining venues as well as the Cleveland Clinic, part of Mubadala's network of world-class healthcare facilities, to serve the needs of the free zone's residents, workers and visitors.

There is a general expectation that many financial institutions will establish their operations in ADGM in order to gain access to the Abu Dhabi financial markets. Abu Dhabi is a large market with several large local banks and powerful sovereign wealth funds, including the world's second-largest sovereign wealth fund, Abu Dhabi Investment Authority. Generally, in order to cater to the Abu Dhabi market, an entity must establish operations in Abu Dhabi.

Having said that, the DIFC offers potential investors the legal and regulatory certainty of a financial centre that has been in operation for over 10 years and has therefore overcome many of the initial teething problems that ADGM is likely to face in the coming months, if not years. The DIFC also provides its own very successful arbitration centre, the DIFC-LCIA Arbitration Centre, which is founded on a strategic partnership between the DIFC and the London Court of International Arbitration, one of the longest-established international institutions for commercial dispute resolution. At this stage, ADGM does

not have an equivalent arbitration centre, although we understand that an ADGM arbitration centre will be established in the future.

One thing is for certain, we will all be monitoring the progress of the ADGM and its competition with the DIFC over the next few years!

25 ADGM Application of English Law Regulations 2015.



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