

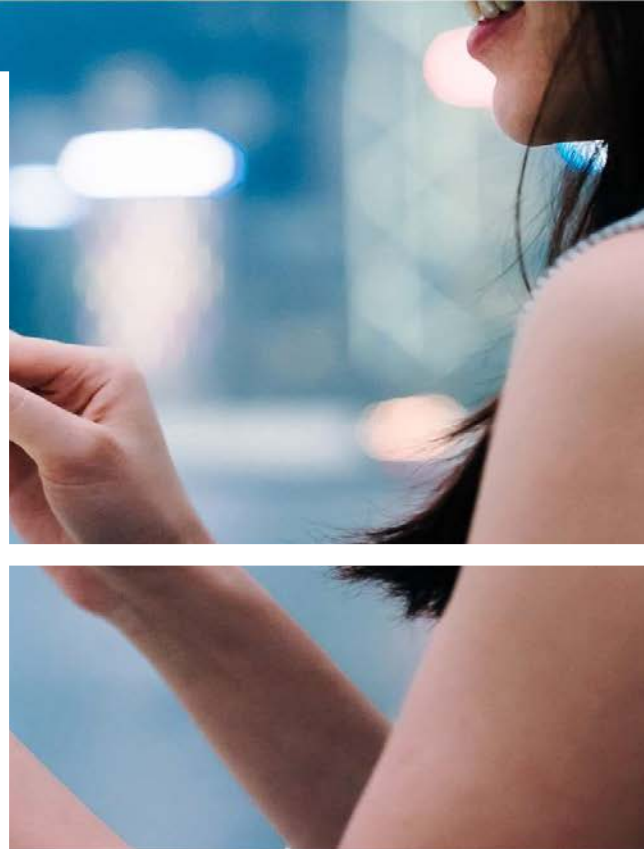
Loan-based Crowdfunding Activities Regulation

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Loan-based Crowdfunding Activities Regulation



On 14 October 2020, the UAE Central Bank (“**UAECB**”) issued the Loan-based Crowdfunding Activities Regulation (the “**Regulation**”) that stipulates the minimum standards required to conduct Loan-based Crowdfunding Activities (“**LCA**”). Notably, the UAECB stated that they encourage Loan-based Crowdfunding Companies to exceed the minimum requirements outlined in the Regulation, as the goal of the Regulation is to safeguard the financial system from the risks posed by LCA and safeguard the interests of consumers in the UAE.

The Regulation was published in the official gazette on 28 October 2020 and was stated to come into force one month from publication. Therefore, the Regulation has been in effect since 28 November 2020. It only applies to the loan-based crowdfunding model and does not apply to donation-based, reward-based, or crowdsourced equity based crowdfunding models.

LCA involve the solicitation of funds, in the form of loans, from lenders through a platform for specific projects. The Regulation defines Loan-based Crowdfunding Companies (“**LCCs**”) as companies duly incorporated under the Companies Law (excluding Partnership and Limited Partnership companies) with business objectives that include electronic finance or similar activities, that carry out such activities through a platform which interposes between lenders and borrowers engaging in LCA and operate using only a pricing business model. A pricing business model allows lenders to select investment opportunities and the price of the loans are decided by the LCC’s platform.

The Regulation has far reaching jurisdiction. Under the Regulation, companies will be regarded as engaging in LCA within the UAE, if they meet one of the following criteria:

1. the company, carrying out LCA, is either incorporated in the UAE, or the crowdfunding platform is hosted in the UAE;
2. the crowdfunding platform utilizes a company address situated in the UAE for correspondence; or/and
3. the company provides LCA to clientele residing in the UAE.

Based on the expansive reach of the Regulation, its conditions and requirements should be examined by regional and international LCCs with ties to the UAE.



The Loan-based Crowdfunding Activities Regulation - *key takeaways*

The Regulation has divided LCCs into two categories based on their lending volume. Category 1 (Large) will consist of large LCCs that facilitated cumulative loans of AED 5,000,000 and above in a calendar year and Category 2 (Small) will consist of smaller LCCs that facilitated cumulative loans of below AED 5,000,000 in a calendar year.

Licensing Requirements

All companies that elect to undertake LCA within the UAE and are governed by the Regulation must apply to the UAECB for a LCA license. The license will be issued either as a Category 1 or a Category 2 license.

Applications to obtain a LCA license must be made in the manner prescribed by the UAECB's licensing manual. Any foreign Loan-based Crowdfunding Company that is regulated in another jurisdiction who wishes to apply for a license to set-up a subsidiary in the UAE must obtain a No-Objection from the regulator of its home-jurisdiction prior to submitting an application for a LCA license.

The LCA licence will be valid for a period of twelve months and can be renewed, subject to the UAECB's approval.



Capital Requirements

The Regulation prescribes the following minimum capital requirements for LCCs based on their categorisation. The minimum capital requirements for Category 1 companies is AED 1,000,000 and for Category 2 companies is AED 300,000. Further, under the Regulation, LCCs must hold the higher of, the capital as stated above; or capital equivalent to 5% of the outstanding lending volume.

Once the LCA license application is approved by the UAECB, the LCC must provide a bank guarantee issued by a locally incorporated UAE bank that evidences value equal to the required capital. The UAECB may cancel or modify a LCA licence if a LCC does not commence operations within one year of a LCA licence being granted.

Lender Requirements

Once an LCC is duly licensed and functioning, they must ensure that they only receive loans, via their platform, from lenders that meet the requirements prescribed in the Regulation. The Regulation stipulates that only the following two categories of lenders may participate in LCA:

1. market counterparties, which are lenders that can evidence net assets of over AED 2,000,000 (outside of their primary residence) and self-attest to their classification as a Market Counterparty; and
2. retail lenders, who are lenders that are not market counterparties.



The Loan-based Crowdfunding Activities Regulation - *key takeaways*



Governance

Once a LCC begins operations, the Regulation requires the appointment of the following critical personnel, who must obtain authorisation by the UAECB:

- Members of the Board of Directors;
- Chief Executive Officer / General Manager;
- Chief Financial Officer;
- Chief Risk Officer;
- Head of Compliance;
- Money Laundering Reporting Officer (MLRO); and
- Sharia Advisor (as appropriate when offering Islamic products).

Risk Governance Framework

Additionally, LCCs must have an appropriate risk governance framework in place to identify all material risks, inclusive of policies, processes, procedures, systems and controls to identify, measure, evaluate, monitor, report and control or mitigate material risk on a timely basis. The key risks that the risk governance framework should address include but are not limited to:

1. Operational Risk;
2. Conduct Risk;
3. Fraud by Employees;
4. Cybercrime;
5. Money Laundering and Terrorist Financing; and
6. Mis-Selling Risk.



Outsourcing

Prior approval is required from the UAECB whenever an LCC proposes to enter into a material outsourcing arrangement with other parties. The LCC must ensure that it will meet the UAECB's requirements as set out in the Regulation.

The Loan-Based Crowdfunding Activities Regulation - *requirements*

Conduct of Business

In its efforts to safeguard the financial system from the risks posed by LCA and safeguard the interests of consumers in the UAE, the Regulation has outlined clear guidelines to govern the conduct of LCCs. The Regulation dictates that LCCs shall ensure that they are compliant with the following requirements dictated in the Regulation.



1. Lender Selection and Suitability

LCCs must take reasonable care when on-boarding lenders and should assess the suitability of lenders and ensure that lenders have a clear understanding of the risks that they are undertaking when participating in LCA. The onboarding process must be documented, and appropriate training must be provided to all associated employees.

2. Lending Structure

LCCs must ensure that, when a loan is provided using their platform, that there is a written loan agreement in place between the borrower and lender that is legally enforceable. The loan agreement should stipulate sufficient details regarding the loan, the terms of repayment, and the rights and obligations of the borrower and lender.



3. Borrower Risk Assessment

LCCs should ensure that they have a sufficient and transparent risk scoring system in place. The basis and methodology of risk scoring, and due diligence should be made publically available. Further, LCCs should ensure to review the financial situation of borrowers on an annual basis, at minimum. In the event of any material change, LCCs should communicate their assessment to their clients.

LCCs must require borrowers to declare their current and intended borrowing from other LCCs and other sources per calendar year. LCCs should take reasonable steps to monitor whether borrowers are accessing loans through any other sources, including through regular checks with Al Etihad Credit Bureau.



4. Ceiling on Lending

In each calendar year, LCCs should impose a limit on lending per person, per project to AED 20,000 for retail clients and AED 50,000 to market counterparties. Additionally, in each calendar year, LCCs should impose a limit on total lending per lender to AED 200,000 for retail clients and AED 500,000 for market counterparties.

5. Ceiling on Borrowing

In each calendar year, LCCs must impose a borrowing limit on borrowers of AED 10,000,000. Further, LCCs must only allow borrowers to list themselves on one crowdfunding platform, per project. As part of its due diligence, LCCs will be responsible for ensuring that borrowers do not listed on any other crowdfunding platform for the same project.



The Loan-based Crowdfunding Activities Regulation - *requirements*

6. Loan Release

LCCs should implement measures to prevent borrowers from gaining access to any amounts raised until the borrower has raised 100% of their funding goal and prevent borrowers from accessing any amount exceeding their funding goal.

7. Client Money

LCCs should not accept, take, or receive the transfer of full ownership of money from clients. LCCs must maintain segregated escrow accounts holding clients' money that must be externally audited on a monthly basis for Category 1 companies and on a quarterly basis for Category 2 companies. Further, client funds shall only be held with local retail banks who are licensed and regulated by the UAECB.

8. Disclosure to Lenders

LCCs must disclose comprehensive information about the borrowers linked to a specific project directly to lenders.

9. Reporting and Record Keeping

LCCs must submit reports to the UAECB in the prescribed form within thirty days of the period specified below, based on their category:

Category 1: quarterly (as of the end of March, June, September and December); and

Category 2: Semi-annually (as of the end of June and December).

LCCs must report the following minimum information to the UAECB within their reports; financial position, client money held, complaints and its resolution, details of loans arranged each quarter, and details of defaults and near-defaults. Additionally, records of client money and completed transactions should be retained for a minimum period of ten years by the LCC.

10. Contingency Portfolio Administration Arrangements

In the event that an LCC should fail or be wound-up (either voluntarily or involuntarily), the LCC must have documented arrangements in place to ensure that the loan portfolio continues to be administered. The Board of the LCC bears ultimate responsibility for ensuring that contingency portfolio administration arrangements are in place.





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An abstract background image featuring a dense field of blue fiber optic cables. The cables are illuminated from the bottom right, creating a bright, glowing effect with many small, out-of-focus light points and streaks of light extending towards the top left.

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