

Appendix 10

In this Appendix underlining indicates new text and striking through indicates deleted text.

Some text that is not being amended is included for information only.



The DFSA Rulebook

Islamic Finance Rules

(IFR)

....

1. INTRODUCTION

1.1 Application

1.1.1 This module (IFR) applies to:

- (a) every Person who carries on, or holds itself out as carrying on, a Financial Service in or from the DIFC as in accordance with Shari'a;
- (b) a Domestic Fund which is operated or held out as being operated as an Islamic Fund;
- (c) a Person making an Offer in or from the DIFC relating to an Investment or Crypto Token which is held out as Islamic or Shari'a compliant.

Guidance

- 1. Most of the requirements that apply to Persons conducting Financial Services or distributing Securities as Islamic or Shari'a compliant are included in this module. There are other more generic requirements relating to such Financial Services or activities that are included in other modules of the DFSA Rulebook.
- 2. To enable Persons carrying on or proposing to carry on Islamic finance activities to easily access the Islamic finance related requirements applicable to their activities, the DFSA has created a web-based Islamic Finance Handbook. This handbook allows electronic navigation to reach the relevant provisions in the IFR and other DFSA Rulebook modules where Islamic finance related requirements applicable to specific Islamic finance activities are located. The handbook is accessible from the DFSA web-site.
- 3. Investment Tokens are Investments defined in GEN A2.1.1(3). An Investment Token is likely to be held out as being Islamic or Shari'a compliant when it is referred to using terms such as 'Islamic investment token', 'Islamic security token', 'sukuk token', 'Islamic fund token' or any other name that suggests or implies it is Islamic or Shari'a compliant.
- 4. Crypto Tokens are digital representations of value, rights or obligations and are defined in GEN A2.5. A Crypto Token is likely to be held out as being Islamic or Shari'a compliant when it is referred to using terms such as 'Islamic Digital Token', 'Islamic Token' or 'Islamic Digital Asset' or any other name that suggests or implies it is Islamic or Shari'a compliant.

....

2 ISLAMIC FINANCE

2.1 Application

- 2.1.1** This chapter applies to every Person to whom this module applies in accordance with Section 1.1.

2.2 Activities that constitute Islamic Financial Business

Guidance

1. Article 10 of the Law Regulating Islamic Financial Business 2004 prescribes what constitutes Islamic Financial Business. In essence, where a Person engages in any activity that constitutes a Financial Service and carries on or holds out the activity as being conducted in accordance with Shari'a, that activity constitutes Islamic Financial Business.
2. GEN section 2.2 sets out the activities that constitute a Financial Service.

2.3 Conducting Islamic Financial Business

Guidance

1. Article 9 of the Law Regulating Islamic Financial Business 2004 provides that in order to conduct Islamic Financial Business, the Authorised Person must have an endorsed Licence authorising it to conduct such business:
 - a. as an Islamic Financial Institution; or
 - b. by operating an Islamic Window.
2. Article 11 of the Law Regulating Islamic Financial Business 2004 governs the making of an application for an endorsement to conduct Islamic Financial Business.
3. Article 11(5) of the Law Regulating Islamic Financial Business 2004 governs the grant of an endorsement to conduct Islamic Financial Business as either an Islamic Financial Institution or by operating an Islamic Window. A Person must obtain the relevant endorsement before carrying on Islamic Finance Business as an Islamic Financial Institution or through an Islamic Window.
4. An Authorised Person with an endorsement to operate an Islamic Window may conduct some of its activities as a conventional Financial Service while conducting its Islamic Financial Business through the Islamic Window.
5. If Islamic Financial Business (whether through an Islamic Financial Institution or Islamic Window) is provided to Retail Clients, the Authorised Person must also have a Retail Endorsement on its Licence.
6. A Person may, subject to any restrictions in the DFSA Rules, carry on more than one Financial Service, provided that Person has the relevant authorisations or endorsements on its Licence as are applicable.

2.4 Islamic financial instruments and products

Guidance

1. The DFSA regulatory regime applies to a Person carrying on any Islamic financial activities in or from the DIFC if the activity:
 - a. relates to a financial instrument or product of the kind described in Guidance Notes 3 (Profit Sharing Investment Accounts), 5 (Investments), ~~and~~ 7 (Takaful insurance) and 10 (Crypto Tokens) below; and
 - b. is conducted by way of business and not expressly excluded from regulation as a Financial Service. Note there are a number of such exclusions in GEN chapter 2.
2. The DFSA will, when considering the treatment of Islamic Financial Business arrangements, take a “substance over form” approach.
3. The issue of financial products which are Securities such as Shares, Debentures or Units as defined in GEN A2.1.2 (which are a subset of the definition of Investments – see Guidance Note 5), attracts product specific disclosure requirements such as Prospectus or Exempt Disclosure Statements. Where such products are included on an Official List of Securities or made available to the public in the DIFC, there are initial and ongoing disclosure and other obligations that apply to the Reporting Entity (generally the issuer) under the MKT module. These MKT obligations are quite distinct from the obligations that apply to Persons carrying on Financial Services in respect of such financial products.

Profit Sharing Investment Accounts (PSIAs)

4. PSIAs do not fall within the GEN definitions of Investments. They are contractual arrangements under which Authorised Firms invest clients’ funds, often (though not always) on a pooled basis, and are generally treated by the firm as off balance sheet. They are sometimes structured under Mudaraba, so that the investor in principle bears the full investment risk. Although PSIAs have the characteristics of a Collective Investment Fund, under an express exclusion provided under CIR Rule 2.1.13, they are not treated as such. Instead, Managing a PSIA is a distinct Financial Service as defined in GEN Rules 2.2.2(r) and 2.21.
5. As Managing a PSIA is a Financial Service, the DFSA regulatory regime that applies to Persons carrying on Financial Services in or from the DIFC applies to Authorised Firms that manage PSIAs. As PSIAs are not Investments, the offer of PSIAs does not attract prospectus like disclosure. Instead, it attracts a tailored regulatory regime that applies to the entity, i.e. an Authorised Firm that manages the PSIAs (see IFR chapter 5 for these Rules). The Financial Service of Advising on Financial Products will apply to a Person giving advice on the merits of investing in a PSIA (as a PSIA is defined as a ‘financial product’ for the purposes of that activity). However, other activities such as dealing and arranging and COB requirements relating to those activities do not apply to a PSIA (as it is not an Investment as defined in GEN).

Investments

6. Investments comprise two types of products: Securities and Derivatives. These products are defined in GEN App2. Most of the conventional Investments defined in GEN App2 can be offered as Islamic financial products, provided the relevant requirements including Shari’a principles are adhered to and in accordance with any Shari’a Supervisory Board rulings as applicable. While not an exhaustive list, conventional Investments that are commonly used as Islamic financial products

include Shares, Sukuks, Units of Islamic Funds and also Structured Products. Increasingly, Derivatives are also being developed in accordance with Shari'a, such as a contract where the rights and liabilities of the parties are determined by reference to an underlying factor such as property of any description, currency rate or index, provided that the underlying factor in itself is Shari'a compliant and the contract does not involve any fundamental uncertainty (Gharar).

7. The DFSA regulatory regime applies to Persons who carry on in or from the DIFC any Financial Services activity in relation to any Islamic financial products that fall within the definition of Investments. However, particular products or instruments such as Profit Sharing Investment Accounts (PSIAs), Takaful and Islamic Funds attract product/instrument specific additional conduct and other requirements, which are included in this module.

Takaful insurance

8. Takaful insurance generally refers to an arrangement where an insurer establishes a Shari'a compliant fund, predicated for mutual protection, where participants donate a part of their contributions to the common fund which will be used to meet claims payments and any participation rights. The Takaful insurer's role is generally confined to managing the insurance activities and investing the fund assets in accordance with Shari'a.
9. Persons conducting Takaful insurance are conducting Insurance Business. There are two types of Financial Services that comprise Insurance Business, ie, Effecting Contracts of Insurance or Carrying out Contracts of Insurance. Accordingly, any Person carrying on these Financial Services activities is subject to the DFSA regime for regulating Financial Services. Where such activities are carried out as Takaful insurance, there are additional Takaful specific requirements that apply to such an insurer, which are set out in this module (see IFR chapter 8). In addition, there are certain activities relating to insurance, such as advising and arranging, which are regulated as Insurance Intermediation (see GEN section 2.19). Persons conducting those activities in relation to Takaful insurance are regulated in the same way as Persons conducting such activities in relation to conventional insurance.

Crypto Tokens

10. The DFSA regulatory regime for Crypto Tokens applies to Persons who carry on certain Financial Services related to Crypto Tokens, for example, operating a trading venue for Crypto Tokens or arranging, advising upon, or executing transactions relating to Crypto Tokens. It also applies to Persons who offer or promote Crypto Tokens in or from the DIFC.
11. A Person may be able to offer Financial Services relating to Crypto Tokens either as an Islamic Financial Institution or through an Islamic Window, subject to the views of their Shari'a Supervisory Board.