Appendix 7

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

The DFSA Rulebook

Conduct of Business Module

(COB)

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11 CROWDFUNDING

11.1 Overview

Guidance

1. This chapter applies to an Authorised Firm that Operates a Crowdfunding Platform (an 'operator').

2. A Crowdfunding Platform may be a Loan Crowdfunding Platform or an Investment Crowdfunding Platform. The key distinction is whether the Person providing funding on the platform enters into a loan agreement with the Person to whom it is providing funding or purchases an Investment (such as a Share, Debenture or Sukuk) issued by that Person.

3. The terminology used in this chapter varies according to the type of Crowdfunding:

   (a) 'borrower', 'lender' and 'loan' for Loan Crowdfunding; and

   (b) 'Issuer', 'investor' and 'Investment' for Investment Crowdfunding.

4. In this chapter, sections 1, 2 and 3 apply to all Crowdfunding Platforms (unless specified otherwise); section 4 sets out additional requirements for Loan Crowdfunding; and section 5 sets out additional requirements for Investment Crowdfunding.

5. In addition to the Rules in this section, an operator is required to comply with other parts of COB such as chapters 1, 2 and 3 and, if it holds or controls Client Assets, sections 6.11 to 6.14.

6. Both borrowers and lenders (in the case of Loan Crowdfunding) and Issuers and investors (in the case of Investment Crowdfunding) will be Clients of the operator. COB requirements will apply in relation to both types of Clients. Under section 3.3 and App 2, additional terms are required to be included in Client Agreements between a Crowdfunding Operator and its Clients (see Rules A2.1.5 and A2.1.6).

7. An operator will need to comply with relevant AML requirements, such as carrying out customer due diligence on Clients who are borrowers or lenders or Issuers or investors.

8. In the case of Investment Crowdfunding, the issue of Investments may result in the application of requirements under the Markets Law such as Market Abuse provisions or, if an offer is not an Exempt Offer, Prospectus requirements.

[*Note: the above Guidance is not being amended but is included for information only*]

11.2 Application and interpretation

Application

11.2.1 This chapter applies to an Authorised Firm with respect to the Operation of a Crowdfunding Platform.

Interpretation

11.2.2 In this chapter:

(a) "borrower" means a Person that has borrowed or is seeking to borrow money using a Loan Crowdfunding Platform;

(b) "commitment period" means the period specified by the operator during which lenders may commit to lending money to a particular borrower or investors may commit to investing with a particular Issuer;

(c) "cooling-off period", for Investment Crowdfunding, means the period referred to in Rule 11.5.2 when an investor may withdraw his commitment to invest with an Issuer;

(d) "investor" means an investor or potential investor using an Investment Crowdfunding Platform;

(e) "lender" means a Person who:

(i) lends money under a loan agreement; or

(ii) by assignment has assumed the rights and obligations of a Person who has lent money under a loan agreement;

(f) "loan agreement" means a loan agreement between a borrower and lender referred to in Rule 11.4.1;

(g) "operator" means a Crowdfunding Operator;

(h) "platform" means the website or other electronic media used to provide the service;

(i) "service" means Operating a Crowdfunding Platform; and

(j) "transfer", in relation to a loan agreement, means the assignment by the lender of his rights and obligations under the agreement to another Person.

[*Note: the above section is not being amended but is included for information only*]

11.3 Requirements for Crowdfunding Platforms

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11.3.6 (1) An operator must conduct due diligence on each borrower or Issuer before allowing it to use its service.

(2) The due diligence under (1) must include, as a minimum, taking reasonable steps to verify in relation to the borrower or Issuer:

(a) its identity, including details of its incorporation and business registration;

(b) the identity and place of domicile of each of its directors, officers and controllers;

(c) its fitness and propriety and that of each of the Persons referred to in (b);

(d) its financial strength, including checking financial statements;

(e) its financial history and past performance and its credit history, including checking with external credit agencies;

(f) any credentials or expertise it claims to have;

(g) the valuation of its business, current borrowing or funding levels (if any) and the source of any existing borrowing or funding;

(h) its business proposal;

(i) its commitment and that of its directors, officers and controllers to the business, including how much capital they have provided and any potential flight risk; and

(j) that its business is being carried on in accordance with applicable laws in the jurisdiction where it is based.

Guidance

1. The type of background checks the DFSA expects an operator to conduct under Rule 11.3.6(2)(c) include, for example, whether the Person has been:

a. found guilty of a criminal offence;

b. the subject of any finding in a civil proceeding of fraud, misfeasance or other misconduct;

c. the subject of a judgment or agreed settlement in a civil proceeding exceeding $10,000;

d. disqualified from acting as a director or taking part in the management of a company; or

e. bankrupt or the director, or a person concerned in the management, of a company which has gone into liquidation or administration.

2. The purpose of the due diligence under Rule 11.3.6(2)(j) is to check that the business itself is lawful in the place in which it is being carried on i.e. that the owner has the necessary permits and that the activity is lawful. The borrower or Issuer should certify these matters and provide relevant documents where appropriate.

Disclosure of information about the borrower or Issuer

11.3.7 An operator must disclose prominently on its website relevant information about each borrower or Issuer, including as a minimum:

(a) the name of the borrower or Issuer, the full name and position of each of its directors and officers and the full name of each controller;

(b) the place of incorporation of the borrower or Issuer and the place of domicile of each director, officer and controller;

(c) a description of the borrower's or Issuer's business;

(d) except as provided in Rule 11.3.7A, the most recent financial statements, if any, of the borrower or Issuer and a warning that the operator gives no assurances about their accuracy;

(e) the valuation of the ~~borrower's or~~ Issuer's business~~,~~ and, for a borrower and an Issuer, ~~its~~ their current borrowing or funding levels and the source of ~~its~~ their borrowing and ~~its~~ liquidity;

(f) a detailed description of the proposal for which it is seeking funding including:

(i) the total funding sought;

(ii) how the funds will be used; and

(iii) the target level of funding sought and what will happen if that level is not met or is exceeded;

(g) the results of the due diligence carried out by the operator on the borrower or Issuer and any limits on the due diligence that could be carried out;

(h) any grading or rating by the operator of the borrower's or Issuer's creditworthiness, including:

(i) how the grading or rating has been assessed;

(ii) an explanation of what the different grading or rating levels mean; and

(iii) a clear statement that this should not be taken as advice about whether money should be lent to the borrower or invested with the Issuer;

(i) for a loan or Debenture, the duration of the loan or Debenture, details of interest payable and any other rights attaching to the loan or Debenture;

(j) for a Share issue, any rights attaching to the Share, such as dividend, voting or pre-emption rights;

(k) whether any security is being provided and, if so, the circumstances in which it might be exercised and any limitations on its use;

(l) if applicable, any other reward or benefit attaching to the loan or Investment and the terms on which it is available;

(m) for a Share issue, whether investors have any protection from their shareholding being diluted by the issue of further Shares; and

(n) that the borrower or Issuer, and information provided about the borrower or Issuer, are not checked or approved by the DFSA.

11.3.7A (1) An operator who, but for this Rule, would be obliged to disclose the financial statements of a borrower under Rule 11.3.7(d), may instead disclose on its website financial ratios relating to the borrower in accordance with this Rule.

(2) The operator must disclose the following financial ratios relating to the borrower:

(a) current assets ratio: consisting of the current assets of the borrower divided by the total current liabilities of the borrower;

(b) quick assets ratio: consisting of the cash and current receivables of the borrower (liquid assets) divided by the total current liabilities of the borrower;

(c) debt ratio: consisting of the total debt of the borrower divided by the total assets of the borrower;

(d) debt to equity ratio: consisting of the total liabilities of the borrower divided by the total equity of the borrower;

(e) return on assets ratio: consisting of the total net income of the borrower divided by the average total assets of the borrower;

(f) profit margin: consisting of subtracting the total expenses of the borrower from the total revenue of the borrower; and

(g) operating cash flow: consisting of cash flows from operations of the borrower divided by current liabilities of the borrower.

(3) An operator must ensure that the financial ratios:

(a) cover at least the two most recently ended fiscal years or, if the business has operated only for a shorter period, that period;

(b) are disclosed in a clear and easily understandable way that:

(i) includes an explanation of what the ratios mean and how they are calculated; and

(ii) allows comparison between borrowers; and

(c) specify whether the information on which the ratios are based has been audited.

(4) An operator must:

(a) verify, either itself or by using a suitably qualified third party, that the financial ratios are correct; and

(b) disclose with the financial ratios:

(i) that it has verified that the ratios are correct; or

(ii) if it has used a third party to verify the accuracy of the ratios, the identity and relevant qualifications of the third party that has verified that the ratios are correct.

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Business cessation plan

11.3.18 The operator must:

(a) maintain a business cessation plan that sets out appropriate contingency arrangements to ensure the orderly administration of loan agreements or Investments in the event that it ceases to carry on its business; and

(b) ensure, as far as reasonably practicable, that the contingency arrangements can be implemented if necessary.

11.3.19 The operator must review its business cessation plan at least annually and must update the plan as necessary to take into account any changes to its business model or to the risks to which it is exposed.

Guidance

~~The business cessation plan may, for example, set out arrangements for another appropriately regulated third party to take over the administration of existing loans or Investments.~~

1. The business cessation plan should contain enough information that, in the event of a wind down of the business, it will assist in the orderly administration of loan agreements or Investments. It should as a minimum include:

    a. a business overview i.e. a factual description of how the platform conducts its activities;

    b. analysis of the critical functions of the business;

    c. trigger events that might cause a wind down of its business (these events should be specific to the particular business, rather than generic);

    d. analysis of what functions are required and need to be undertaken for an orderly wind down of the business; and

    e. how communications with Clients, business partners and creditors will be undertaken during the wind down period.

2. The operator should put in place measures that, as far as reasonably practicable, ensure that the contingency arrangements can be implemented if necessary e.g. by entering into an agreement with a third party to provide certain services. The

operator should consider the need to obtain professional advice about the likelihood of the arrangements being effectively implemented. The operator will need to disclose the contingency arrangements it has in place (see Rule 11.3.3 (r)).

Credit cards not to be used

11.3.20 The operator must take reasonable steps to ensure that a Retail Client does not use a credit card to lend or invest using the platform.

Guidance

An operator may permit an investor to use a debit card to fund a loan or investment provided it has adequate systems in place to distinguish between a debit and a credit card.