

A NEW BUILDING BLOCK TO ADGM’S FINANCIAL ECOSYSTEM ADGM LAUNCHES NEW REGULATORY FRAMEWORK FOR PRIVATE FINANCING PLATFORM

On 10th September 2018, Abu Dhabi Global Market (“ADGM”), the International Financial Centre in Abu Dhabi, United Arab Emirates, launched a new framework to regulate the operators of Private Financing Platforms (“PFPs”) serving equity investment, debt financing and trade receivables funding needs of private enterprises including start-ups and SMEs (the “Framework”).

The Framework provides a tailored and well calibrated regulatory support system for transactions facilitated through a PFP in the UAE.

This regulatory development constitutes a breakthrough in developing a safer marketplace for investors/lenders and a pathway to borrowers/investee, providing a sound alternative to the traditional form of funding route too often not catered to private enterprises.

Why the Need for Alternative Source of Financing?

Private enterprises including start-ups and SMEs play an important role in UAE’s economic growth and diversification. SMEs contribute nearly 60 per cent of the UAE’s GDP and this is estimated to grow to 70 per cent by 2021¹. In 2017, the Dubai Financial Services Authority (“DFSA”) regulating the Dubai International Financial Centre (“DIFC”) launched a regulatory framework for loan and investment-based crowdfunding platforms.

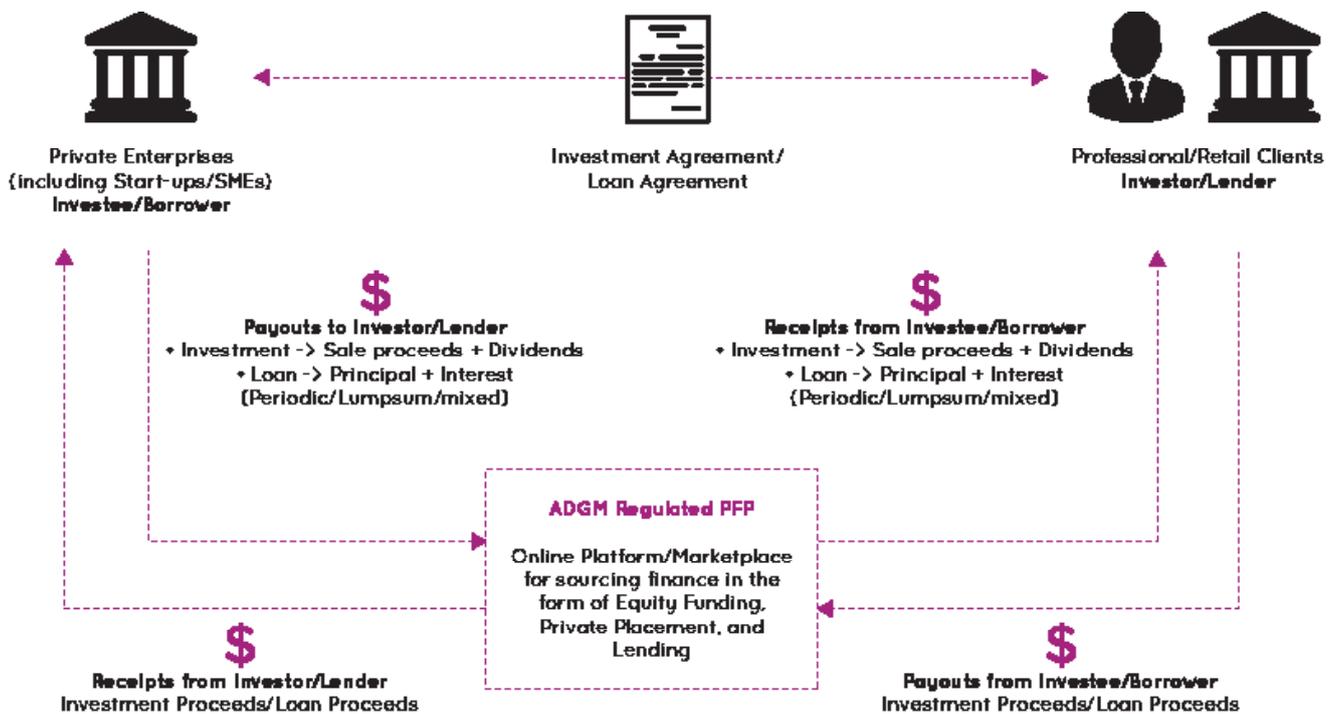
Alternative sources of financing beyond bank lending and other traditional forms of funding are key enablers for private enterprises growth fostering overall economic growth.

The PFP Framework has specific distinctive features catering to those needs and is a welcome addition to the UAE regulatory landscape.

In laymen’s term – What is a PFP and How Does It Work?

The PFP is an online platform that allow private companies including start-ups and SMEs to source funding from private and institutional investors to launch and scale their businesses. Such PFPs allow innovative business models that serve different businesses and client segments.

Under the Framework, a proposed PFP player is free to develop innovative business models based on the business objective to be achieved and remain compliant.



1. Source: <https://government.ae/en/information-and-services/business/crowdfunding>

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Regulatory Highlights of PFP Framework

Some of the key aspects of the Framework is provided below:

- The Activity of Operating a PFP is regulated by this Framework and requires Financial Services Permission ("FSP") from the Financial Services Regulatory Authority (FSRA) by a prospective market player proposing to operate a PFP.
- The lenders/investors (clients) could be Professional as well as Retail clients.
- PFP operators may not provide any financial advisory services to its client.
- The borrower/investee must be a body corporate seeking finance for the business venture.
- A financing proposal to be published on a PFP should qualify "Exempt Offer" criteria.
- PFP operator has an option to appoint a custodian or deal with client money and client assets themselves.
- Capital requirements differ substantially depending on whether the PFP operator proposes to hold or control client assets.
- The PFP Operator is required to undertake appropriate and proportionate due diligence on borrower/investee proposing to list their financing proposal on the PFP.
- The PFP Operator could offer an incidental Exit facility to permit lenders/investors to exit their PFP transaction. However, if it exhibits the characteristics of a trading facility, the PFP Operator may require a separate FSP for Operating a Multilateral Trading Facility or Operating an Organized Trading Facility.

Associated risks

While there are many advantages of a PFP framework to the overall economic ecosystem, there are risks associated with the transactions undertaken through a PFP model.

The risk includes and are not limited to the following:

- Loss of capital – Owing to the borrower/investee having no or limited established track record
- Lack of liquidity – Risk of investor/lender not being able to exit the transaction or exiting at a significant discount
- Lack of information – Not having sufficient information on the investee/borrower to enable fully informed investment decision making.
- Platform failure – Risk of not able to recover the assets where PFP Operator handling Client Assets fails and becomes insolvent.
- Conflicts of interest – Remuneration model of a PFP Operator is typically linked to the amount of funds raised. Hence, the interests of a PFP Operator may be more aligned with businesses raising finance than those of its client providing financing.

Conclusion

The Framework is an outcome of the continuing initiatives and efforts of ADGM's FSRA to develop and update the overall financial ecosystem and to bolster the growth of UAE's economy at large. It represents one of the milestones of ADGM's dedication and continual efforts in providing business-friendly, customized solutions that aim to enhance financial services experiences and the ease of doing business in ADGM.

Given the risk and rewards associated with alternative sources of funding, it is an important financing decision for the investors as well as the investee. It is important to have an appropriate governance framework on the ground for the PFP Operator and relevant education for the prospective investors, investees and market intermediaries to make it a "success" story.

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Who we are

Re/think is a boutique accounting, audit, advisory, regulatory compliance and tax advisory firm with offices in Dubai and Abu Dhabi (ADGM), focused on providing businesses of varying sizes with timely, proactive, and customized business solutions from start-up and early development to the latest stages of a business lifecycle.

We offer tailored regulatory expertise and focus on guiding clients to reduce the risk of non-compliance across a wide range of compliance services and regulatory advice. While we focus on compliance consultancy services including advisory, training and process improvement, we do not just tell you what to do, we give you practical ways to make things work for your business.

For further information and assistance, please write to us at ask@rethink-hq.com

Who will assist you



Sofia Mota, Director and Head of Regulatory and Compliance Services

Extensive experience in the financial services sector and consulting across Europe, Middle East and Africa. Sofia has a track record of successful regulatory projects including banking institutions set ups. Her strong knowledge of financial products and regulatory frameworks adds to her extensive work experience in top tier financial institutions. Sofia holds and L. LM in Banking and Finance from the University of London and is a member of the Chartered Institute for Securities and Investments. Sofia is also experienced in designing and implementing operational risk management and governance frameworks across retail and wholesale markets. She currently acts as a compliance mentor for the ADGM Fintech RegLab and has completed the Oxford/Saïd Business School Fintech Programme.



Gail Goring, Director - Regulatory and Compliance Services

Experienced corporate lawyer with over 15 years' experience in regulatory and compliance services spanning across the Caribbean, Cayman Islands and in the UAE as the former Head of Regulations and Operations for RAKICC (IBC Offshore & Free zone Registry) with a strong knowledge of international business companies' regulatory frameworks, financial services (including FinTech) and financial products (particularly Funds) as well as specialized expertise as a certified Anti-Money Laundering Specialist and FATF trained Legal expert examiner and certified in FATCA & CRS reporting.