

Crowdfunding in Bahrain

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Conventional Financing Based Crowdfunding Business (“CFC”) Person to Business (P2B) is a lending e-platform which takes place on an online portal, through which people lend money to businesses, for the purpose of gaining a financial return in the form of interest payment and a repayment of the principal sum (loan amount) over a pre-specified period of time. CFC Platforms may raise funds for borrowers based in Bahrain or abroad, subject to regulation.

Regulations and licensing

The new Crowdfunding regulations issued by the Central Bank of Bahrain (“CBB”) create a legal framework for loan crowdfunding (both conventional and Sharia compliant) while providing governance for financial technology or FinTech businesses and protection for their customers. The regulations are aimed at helping small and medium size enterprises and start-ups to get access to alternative forms of funding when more traditional funding options are not available.

Firms operating an electronic platform in relation to lending must be licensed in Bahrain, as ‘operators of P2B Conventional Financing-based Crowdfunding Platforms’, under the CBB Rulebook Volume 5 – Financing Based Crowdfunding Platform Operator. The minimum capital requirement for these CFC Platform Operators is Bahraini Dinars (“BD”) 50,000 to be maintained on an on-going basis. This is new type of license. A CFC Platform Operator is not permitted to engage in Business to Business (B2B), Business to Person (B2P) or Person to Person (P2P) lending.

Category of investors and borrowers

Retail investors are not permitted to participate in finance-based crowdfunding given its high-risk nature. Only expert and accredited investors are allowed to provide loans through these platforms while the borrowers must be small or medium sized business with paid-up capital not exceeding BD 250,000.

Under a CFC agreement (entered into between the CFC Platform Operator and the lenders), lenders are restricted to lending not more than 10% of their net assets to any single borrower. All lenders intending to participate in a CFC Platform must fill out the ‘Self Declaration Form’ declaring that they meet this requirement.

Under a CFC agreement, the amount of capital provided must be less than or equal to BD 100,000 in aggregate, per borrower, within a 12 month period. Additionally, the term of loans must not exceed five years.

The minimum subscription to be received in a CFC offer must not be less than 80% of the crowdfunding offer size. In the event that the borrower is unable to raise the minimum required loan subscription, all subscription monies received must be returned to the lenders no later than 7 calendar days of the closing date of the crowdfunding offer. In case of over-subscription, CFC Platform Operator must ensure that no funding shall be made to the borrower in excess of the original offer size. Also, the lenders must get proportionate share of the Crowdfunding offer size.

The CFC Platform Operator

The role of CFC Platform Operators is restricted to arranging deals, bringing together borrowers and lenders. CFC Platform Operators are strictly prohibited to provide any advice on deals. A CFC Platform Operator itself may lend money to borrowers, who use the platform subject to:

1. Obtaining the required license from the CBB for carrying financial services of providing credit; and
2. Adequate disclosure of the conflicts of interest which will arise for each transaction on their website.

CFC Platform Operators must make arrangements with a local retail bank (which holds the appropriate CBB license) to facilitate transactions. Also:

1. Lenders must prefund the full committed amount by depositing it at the designated licensed retail bank in Bahrain. The name of the retail bank must be disclosed to the CBB.
2. The CFC Platform Operator must designate an escrow account as an aggregate account for all borrowers. The CFC Platform Operator must maintain within its records separate sub-accounts for each borrower. The name of the designated bank must be provided to the lenders.

Disclosure of information

CFC Platform Operators must ensure that sufficient information is available to lenders on the profiles of the borrowers. CFC Platform Operators will publish information disclosed by the borrowers to them in the 'Standard Forms for Borrowers' and the related required documents submitted by the borrowers, thus allowing lenders to make informed lending decisions. Moreover, the documentation must state the governing law for the financing transaction.

The disclosure of such information shall be on standard CBB prescribed templates. Additionally, such information must be provided to potential lenders before they agree to commit to lending. In cases where the borrower is not based in Bahrain, adequate disclosure on cross-border risk must be provided to the potential lenders. It is the responsibility of the lenders to perform their own creditworthiness assessments on the borrowers and other related due diligence before making any commitment to lend.

The general regulations are the same for both conventional and Sharia-compliant crowdfunding platforms. For the latter, an additional requirement is that the financing structure should be Sharia-compliant, for which Sharia advisory services will be needed.

The CBB have said regulations for equity-based crowdfunding will be announced soon.

Crowdfunding had been popular in the UK and USA, for example Kickstarter is an American public benefit corporation based in New York that maintains a global crowdfunding platform focused on creativity. The introduction of crowdfunding in Bahrain is likely to enhance Bahrain's reputation and competitiveness in the financial services sector by allowing access to funds for small to medium businesses. This is also good news for entrepreneurs in the region seeking to develop ventures which may otherwise have been restricted due to access to finance.

These Crowdfunding regulations are another step that the Central Bank of Bahrain has taken towards consolidating Bahrain's position as a regional financial hub.

Al Tamimi & Company's Banking & Finance team regularly advises on matters relating to licensing and regulatory advice. For further information please contact Natalia Kumar (n.kumar@tamimi.com).