

INSIGHTS

## The UAE Securities and Commodities Authority Issues Investment Fund Regulations Adopting a "Twin Peaks" Regulatory Approach

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Following an extensive consultation period, the UAE Securities and Commodities Authority (SCA) has issued its regulations for investment funds pursuant to [Board Decision No. \(37\) of 2012 Concerning the Regulations as to Mutual Funds](#) (Regulations).

The Regulations are significant because, among other things, they:

- identify the pathway for all fund transactions, as the same relate to local funds and foreign funds active in the UAE;
- establish the SCA as the body with regulatory authority over several categories of service providers to investment funds, as well as over local funds and transactions in all funds (whether local or foreign), which in turn, identifies opportunities for financial services providers to qualify for and provide such services; and
- bring about the implementation of a "twin peaks" approach towards financial sector regulation by placing business conduct and investor protection functions with the SCA and prudential, safety and soundness functions with the UAE Central Bank.

### **Pathway for Local and Foreign Investment Funds**

The general framework of the Regulations begins by broadly defining mutual funds, a term used throughout the Regulations, as "a financial vehicle practicing the activity of investors' money formation for the purposes of investment [...]". The Regulations do not apply to joint bank accounts, group insurance contracts, employee motivation programs and to other matters/persons listed in Article 2(3) of the Regulations.

Regulated investment funds are then divided into "Local Funds" (those "established in the UAE, excluding the free zones, and licensed by the SCA.") and "Foreign Funds" (those "established outside the UAE under the laws and regulations in force in a foreign countries [sic]"). By way of example, investment funds established in the Dubai International Financial Centre are treated as Foreign Funds under the Regulations.

### **Local Funds**

The Regulations "apply to all matters pertinent" to Local Funds. Local Funds may be established by either a joint stock company organized under *UAE Federal Law No. (8) of 1984, the Companies Law* or a UAE branch of a foreign entity. In either instance, a joint stock company (Sponsor) must have a minimum share capital of AED 10 million and contribute 3% of the capital of each Local Fund established.

The AED 10 million requirement may be satisfied by giving an unconditional guarantee up to this amount in favor of the SCA where the Sponsor is an entity licensed by the UAE Central Bank, a bank, a branch of a foreign bank or a financial investment company. The SCA may call upon the guarantee at any time to cover any financial liabilities owing to investors, as determined by the SCA. Local Funds include both "Open-End Funds" (including Exchange Traded Funds) and "Closed-End Funds." After approval by the SCA, units of these Local Funds may be listed and traded in the market.

To establish a Local Fund, a Sponsor applies to the SCA using the SCA's standard application forms. The Sponsor submits these forms to the SCA along with all other required documents and data. The SCA will subsequently approve or reject the application within 30 business days and, as the case may be, notify the UAE Central Bank of the licensing of the Local Fund.

The Offer Document (prospectus or offering memorandum) is central to the establishment, governance and marketing of a Local Fund. The Regulations set out the basic requirements for:

- the Offer Document and its amendment;
- the investment policy;
- the restrictions and limits on tradable securities (when applicable);
- the methods of subscription, issuance, listing and trading of units;
- the evaluation of assets and pricing of the Local Fund;
- the distribution and redemption of units;
- the treatment of Local Fund assets;
- the leveraging of the Local Fund;
- the financial reporting requirements applicable to the Local Fund;
- the conduct of the general assembly of unit holders;
- the organization, governance, conflicts of interest, and function of the fund board of directors;
- the disclosure requirements and availability of Local Fund information for investors; and
- the termination of Local Funds.

Article 29 of the Regulations divides the oversight of Local Funds between the UAE Central Bank on prudential supervision matters and the SCA on investor protection matters.

### **Foreign Funds**

The Regulations also "apply to the promotion of" Foreign Funds within the UAE. Foreign Funds may be promoted in the UAE upon approval by the SCA of an application submitted by the "Local Promoter" (as described below). The SCA approval is required for private offerings of Foreign Funds. Foreign Funds promoted in a public offering must be subject to the oversight of a regulator similar to the SCA and duly licensed to promote public offerings in their home jurisdiction. With respect to both private and public offerings of Foreign Funds, the SCA has the authority to add conditions or grant exemptions for approval as it deems fit.

Foreign Funds may only be promoted in the UAE by a "Local Promoter" that is either: (1) a bank licensed by the UAE Central Bank; (2) an investment company licensed by the UAE Central Bank; or (3) an entity licensed as a Local Promoter by the SCA, unless promoted in a private offering through a local representative of the Foreign Fund company subject to a minimum subscription of AED 10 million. The Regulations require that the Local Promoter or local representative of the Foreign Fund company provide all mechanisms to enable the promoted fund to meet its obligations and duties to its investors. Specific additional requirements are placed upon Local Promoters under Article 39 of the Regulations, including the exercise of due diligence in selecting the promoted fund and post promotion follow-up "to safeguard the assets of investors."

Additional requirements for private placement of Foreign Funds include the limitation of contact for promotion to predetermined investors and minimum denominations of AED 1 million for funds established in a free zone located outside mainland UAE and of AED 500,000 for other Foreign Funds.

### **Service Providers**

The Regulations establish obligations for, and require the licensing of, specific service providers, including "Investment Managers," "Management Service Companies," and "Safe Custodians," as well as the Local Promoter described above. In many instances, the duties of a service provider are held to a "best efforts" and "exert due diligence" threshold. Among such requirements, the service provider must ensure "best execution" in the distribution and sale of units through brokers.

### **Twin Peaks**

As described above, the Regulations divide responsibility for the oversight and inspection of Mutual Funds between the UAE Central Bank for prudential supervision matters and the SCA for investor protection matters. As such, the Regulations constitute the first step in the implementation of a "twin peaks" approach to financial market regulation in the UAE.