

# Promoting foreign investment funds in the UAE just got a bit harder

The UAE Securities and Commodities Authority's (SCA) recent Board Decision No.9 of 2016 on the regulation of investment funds (the IFRs) came into force on 1 August. It repeals SCA Board Decision No.37 of 2012 on the same subject (the Old IFRs) and, in doing so, makes some important changes to the UAE investment funds regime.

The IFRs make considerable improvement to the Old IFRs, particularly in respect of the licensing requirements for UAE investment funds. However, for promoters of foreign funds in the UAE, the IFRs are now more restrictive and impose additional costs and hurdles for registering foreign funds with the SCA.

## The new licensing scheme

**The domestic UAE funds industry will welcome the easing of the SCA's licensing requirements.**

### Broader range of applicants

Licence applicants may either be:

1. an SCA-licensed company dealing in securities;
2. a company incorporated under the UAE Commercial Companies Law whose main business activity is to establish and manage funds. The Old IFRs restricted this to Public Joint Stock Companies;
3. a local bank or a branch of a foreign bank which is licensed by the Central Bank of the UAE (CBUAE) to establish and manage funds; or
4. a branch of a foreign company whose head office is licensed by its home regulator to establish and manage funds, and is subject to "a regulatory authority that is similar to the [SCA]".

### Lower capital requirement

Under the Old IFRs, the minimum capital requirement was AED10 million. This has now been reduced to AED5 million. However, banks and financial institutions are no longer permitted to submit a bank guarantee to the CBUAE in lieu of a capital.

### No minimum fund contribution

Previously, fund managers were required to subscribe to a minimum of 3% of the funds units. This is no longer the case under the IFRs.

### New systems and controls requirements

The IFRs have expanded on the applicant fund managers' systems and controls requirements to now include:

1. appointing adequate technical and managerial staff in accordance with SCA's requirements;
2. providing adequate technical and IT systems in accordance with SCA's requirements;
3. providing internal controls for compliance with the applicable rules and legislation;
4. providing a risk management manual which highlights

## What you should know

- new licensing standards
- private placement exemption removed
- foreign promoters must now rely on reverse solicitation
- foreign fund promoter must now register fund, not local placement agent
- adoption of Key Investor Information Document
- significant increase in fees

the potential risks and sets out the proposed mitigation. The SCA may agree to defer the above requirements for a specified time after the granting of the licence, if the applicant undertakes to comply within that specified time.

## Extending the fund starting period

**Funds now have more time to set up and begin their activities.**

The previous regulations required a fund to begin its activities within 3 months of the registration date or have its registration revoked. This has been increased to 12 months.

Notwithstanding this, the new starting grace period may not be extended.

## Foreign funds – loss of several exemptions

**The "Reverse Solicitation" exemption is now the main 'safe-harbour' for offering foreign funds in the UAE.**

Under the IFRs, a foreign fund may now only be promoted in the UAE where:

1. it has been approved for promotion by the SCA and distributed through a local licensed placement agent;
2. the promotion is to a UAE Federal or local Government authority or a company wholly-owned by such an authority; or
3. it is promoted on a reverse solicitation basis.

Under the Old IFRs, exempt private placements of foreign funds were permitted and did not require SCA approval. Private placements were exempt (and therefore not subject to the approval/licensing requirements) where the placement was targeted at, inter alia:

1. financial portfolios owned by federal or local government entities;
2. companies, institutions or entities if one of their purposes is to invest in securities, provided that dealing with such entities shall be restricted only to their private financial portfolios and not extended to their Clients'/Prospects' customers' portfolios; or
3. Investment Managers, where the decision making power regarding the investment lies solely with the Investment Manager.

Under the old IFRs, foreign funds could also be offered to existing clients of the foreign firm, provided that the client became a client by legitimate means i.e. without breaching the IFRs. We understand that this "exemption", as well as the private placement exemption, no longer exist.

Regarding the reverse solicitation exemption, Article 2(3)(b) of the IFRs states that the following scenario is excluded from its scope:

"when an investor located in the State initiates an offer or the purchase of specified units in foreign funds located outside the State, that is not made as a result of promotional activities by the foreign fund, its promoters or the distributors of its units, subject to this being proven by the relevant party."

Note that for a foreign fund promoter to rely on the reverse solicitation exemption, it would need to keep proper records demonstrating that the approach was unsolicited and initiated by the UAE investor.

## Introducing the "Qualified Investor"

**The IFRs introduce the concept of a Qualified Investor to whom private funds may be offered. Such private funds require registration with the SCA.**

The IFRs introduce two types of Qualified Investors:

1. "Self-reliant" investors, which consist of:
  - (a) Government bodies (Federal and local) and entities owned by them;
  - (b) International organisations;
  - (c) persons who are licensed to carry out commercial activities in the UAE, provided that investing is one such activity;
  - (d) individuals whose annual income is no less than AED1 million, or their gross net worth (excluding their primary place of residence) is at least AED5 million and who acknowledge that they have sufficient knowledge and experience (either by themselves or with the assistance of a financial advisor) to assess the risks involved in subscribing to funds units.
2. Investors that are represented by an SCA-licensed investment manager.

Interestingly, the IFRs do not provide for a lighter disclosure regime or other regulatory exemptions when funds are

offered to Qualified Investors. One would have thought that the SCA would have permitted foreign funds to be offered directly to Qualified Investors by way of private placement without being subject to the registration requirement (and without the need to rely on the reverse solicitation exemption). Instead, the concept of Qualified Investors is only used in the definition of a private fund, which is a UAE domestic fund which is offered to "a Qualified Investor and for his own account".

## Adopting the Key Investor Information Document (KIID)

**The introduction of the KIID is an investor-friendly enhancement which helps align the UAE regime with the European Union (EU) standards.**

The KIID is essentially a simplified prospectus. The fund "incorporator" or the manager is required to draft the KIID in Arabic and follow the SCA's template. The KIID has to be regularly updated.

The IFRs require a KIID to be produced for all UAE domestic funds in the UAE, including private funds.

It is notable that a number of EU simplified prospectus elements are not required, such as:

- the identity of the authority responsible for the fund (relevant for registered foreign funds);
- a warning that the fund's home jurisdiction tax regime might impact investors in other countries (relevant for registered foreign funds);
- overview of the fund's past performance;
- the date of the preparation of the KIID; and
- the extent of the provider's legal liability for the KIID.

Note that the Old IFRs explicitly allowed a prospectus to be drafted in the English language, although the Arabic copy would prevail in the event of discrepancy. There is no equivalent provision under the IFRs.

## New fees

### SCA updated its funds fees in conjunction with the new regime

There has been a sharp increase in fees under the IFRs. For example, the SCA fee for licensing a fund manager has increased from US\$4,000 to US\$13,700. The annual renewal fee for the fund manager's licence, which used to be US\$1,300, is now at US\$6,800.

Fee description	Amount (US\$)
Fund registration fee (public & private)	2,700
Fund annual registration fee (public & private)	800
Foreign fund registration fee	9,500
Foreign fund annual registration fee	2,000
Fund manager registration fee	13,600
Fund manager annual registration fee	6,800

For the registration of a foreign fund, the SCA fee, which was US\$4,000 under the Old IFRs, is now US\$9,500 per fund and, additionally, the SCA now levies a new annual renewal fee of US\$2,000 per fund.

## Conclusion

The IFRs create additional hurdles for persons promoting foreign funds in the UAE and will no doubt have an impact on foreign firms selling their funds to UAE investors on a cross-border basis, as well as to financial institutions in the UAE financial free zones which promote both foreign and free zone funds to investors in the UAE. For many such financial institutions, the registration of their funds with the SCA (and cost of annual renewal) may involve a cost/benefit analysis.

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