

Foreign securities: the differing regimes

Stuart Walker of Afridi & Angell highlights the differences between the regimes of the UAE Central Bank and of the Dubai Financial Services Authority

Regional super-liquidity, and the sizable number of investors who base themselves in the United Arab Emirates, mean that questions as to the sale and structuring of financial products in the UAE commonly arise in the region. Historically, many products have been structured as offshore offerings. Increasingly sophisticated regulation within the UAE is encouraging the onshore marketing and sale of these products.

The UAE Central Bank regulates the offering, marketing and sale in the UAE of non-listed foreign securities, other than any offering, marketing and sale of financial products in or from the Dubai International Financial Centre (DIFC). Financial services in the DIFC are subject to the regulatory attention of the Dubai Financial Services Authority (DFSA). The Central Bank and the DFSA differ in many respects.

The Central Bank-DFSA regulatory overlap is experienced most acutely by those institutions that have had a long-standing presence in the UAE and have now also opened offices in the DIFC. These institutions, being both licensed by the Central Bank and authorized by the DFSA, are subject to two quite different regimes. The DIFC is a wholesale environment and the provision of financial services to retail customers is prohibited. This means that full-service financial institutions (that is, those providing retail, commercial and investment banking services) frequently find it necessary to have a UAE presence, both inside and outside of the DIFC.

To the extent that foreign securities (both equity and debt securities) are issued, transferred and traded outside the UAE, limited responses to specific requests from customers in the UAE for information and other low-profile activi-

ties have traditionally been tolerated by the Central Bank as falling below the threshold for requiring a licensed presence in the UAE. However, marketing, sale and advisory activities relating to unlisted foreign securities in the UAE may be conducted only by a party holding an appropriate licence. So as a matter of regulatory convenience, the offer and sale of foreign securities to UAE residents have traditionally been structured to occur outside the UAE.

UAE laws do not prohibit persons in the UAE from owning or holding foreign securities and there are no UAE reporting requirements with regard to owning or holding these securities.

However, if an offering in the UAE to a limited group of potential investors of foreign securities (not listed on a securities market licensed in the UAE) is effected in a manner that renders the offering subject to UAE regulatory requirements, several sets of separate licensing requirements are potentially relevant.

If the sale of a security (or multiple parts of the sale transaction) occurs in the UAE, three potential regulatory issues must be considered: compliance with Central Bank regulations, compliance with the DFSA regime, or both.

Central Bank issues

The provision of offering documents, advice to prospective purchasers of securities, execution of subscription agreements and the offer and sale of securities in the UAE are subject to regulation by the Central Bank.

Regulated investment

Article 5(1) of Resolution 164/8/94 of the Board of Directors of the Central Bank

Concerning the System of Financial Investment Companies and Institutions and Companies for the Banking, Financial and Investment Consultations reads:

"The person licensed to practice the banking, financial and investment consultations in consideration of fees shall carry on one or more of the following activities:

- C. To provide an advice or opinion to any natural or juridical person directly in writing or through printed materials in connection with the value of securities or any other financial instruments or any banking services available in the state or likely to be introduced in future.
- D. To recommend to any natural or juridical person, directly, in writing or through printed materials, to carry out the banking activities or make use of the banking services made available by the banking organizations or in investment or dealing in securities or any other financial instruments or by the purchase or sale thereof."

The investment consultation services for which a licence is required under Article 5(1) of Resolution 164 would extend to consultation services relating to the securities offered to investors in the UAE. If the relevant securities are offered in the UAE, provision of any offering documents to prospective shareholders in the UAE would be subject to the licensing requirement of Article 5(1) of Resolution 164.

Article 6 of Resolution 164 states:

"It shall not be permitted for any natural or juridical person to carry on the financial investment activities or activities of the banking, finance and investment consultations in the UAE unless he is licensed thereto in writing by the Governor of the Central Bank on the ground of this resolution or if he were one of the persons exempted hereunder."

So any services relating to the securities described in any offering documents that would fall under the definition of "financial investment activities or activities of the banking, finance and investment consultations" conducted in the UAE would be subject to the foregoing licensing requirement, in addition to other regulatory requirements imposed under UAE law.

Regulated brokerage activity

Article 2 of Resolution 126/5/95 of the Board of Directors of the Central Bank

Author biography



Stuart Walker
Afridi & Angell

Stuart Walker practises in the areas of banking, capital markets and financial services regulation. Before joining the firm, Walker was an associate with Lovells and specialized in private equity acquisition finance, leveraged buyouts, syndicated lending and debt restructurings. Walker also has experience of the London reinsurance market and property development financing. Advising clients on the application of Dubai

International Financial Centre law and Dubai Financial Services Authority regulation forms a core part of Walker's current practice.

Concerning Regulations of Financial and Currency Brokers provides:

"The business carried on by the broker shall be limited to brokerage in sale and purchase of local and foreign stock and bonds, currencies and commodities, and brokerage in stock exchange operations."

Article 3 of Resolution 126 proceeds to clarify as follows:

"No natural or juristic person may carry on brokerage business in the United Arab Emirates except after obtaining a licence for that from the Central Bank under a decision of the Board of Directors."

The transmission of any offering documents to any prospective purchaser of securities in the UAE and execution of any agreement and any other transaction document from within the UAE would appear to constitute brokerage activity for which the involvement of a licensed broker would be required under Articles 2

and 3 of Resolution 126.

Regulated offering of foreign securities

Article 4(6) of Resolution 164 provides as follows:

"The Central Bank shall be entitled to approve the sale of units/shares of the Funds and the shares of the foreign companies and other securities in the UAE, if the applicants adhere to the conditions of the Central Bank for sale."

If foreign securities relating to investment funds are sold to persons in the UAE, the regulatory requirements set out in Article 4(6) of Resolution 164 would also appear to apply to the securities. The application for approval may be made by a commercial or investment bank licensed in the UAE and the services of an appropriately licensed UAE entity would have to be obtained for this purpose.

Resolution 164 does not offer any guidance on whether a particular offer or sale of foreign securities would be deemed to be in the UAE or abroad.

Public offer of a foreign security

The public offer of a foreign security that is not listed in the UAE is regulated by the Central Bank under Circular 444 of 1987, as amended. The Central Bank does not have jurisdiction over foreign securities listed on one of the exchanges in the UAE that is regulated by the UAE Securities and Commodities Authority.

Offers in or from the DIFC

The DIFC has, in the short time it has been operational, introduced a regulatory regime that is more familiar to international institutions.

Article 41(1) of DIFC Law 1 of 2004 (the Regulatory Law), subject to certain exceptions, prohibits any person from carrying out a financial service in or from the DIFC. This is known as the Financial Services Prohibition, as per Article 41(3) of the Regulatory Law.

The DFSA is empowered to make rules as to the kinds of financial services that may be carried out by authorized firms and by authorized market institutions (Article 42(1) of the Regulatory Law).

Rule 2.2.1 of the GEN Module of the DFSA Rulebook states that an activity is a financial service if it is an activity listed in Rule 2.2.2 and it is carried on by way of business in the manner described in Rule 2.3.

Types of securities marketing activities

Low-profile activities likely to be tolerated by the Central Bank

- Responding to requests for information received from potential investors.
- Short visits with potential institutional investors known or introduced to the offeror's representatives at the investor's invitation.
- Passing information to the UAE resident through their existing financial adviser, who is located abroad.
- Advertisements in newspapers published abroad that circulate in the UAE, provided that no references are made to specific presentations or meetings that will be held in the country,

and provided that any specific address to which potential investors are referred for inquiries is outside the UAE.

- Inviting journalists from the UAE press to news conferences and road shows held outside the UAE.

Activities that might attract the Central Bank's regulatory attention

- Publicly advertising specific securities in the general media.
- Cold calling, mailshots, or other aggressive and high-profile marketing to potential investors with whom there is no prior connection or introduction.
- Sponsoring public events or publica-

tions in a manner that calls attention to the offeror's activities in the country.

- Announcing through general advertisement that the public may meet offeror's representatives at a specific place within the UAE.
- Advertisements or announcement regarding the financial products on local TV or radio or in newspapers or magazines.
- Holding or conducting publicly advertised conferences on general subjects of interest to investors at a time when marketing or securities has commenced or is about to commence, for the purpose of assisting this marketing.

FOREIGN SECURITIES

Not all offers of securities will involve the provision of a financial service but consideration of the Financial Services Prohibition should be given by all parties involved in any offer that touches upon the DIFC in any way. The financial service of "arranging and advising upon credit or deals in investments" is broad enough to potentially catch many of those involved in any securities transaction with any connection to the DIFC.

Article 13(2) of the Markets Law 2004 sets out the prohibition on offering securities in the DIFC as follows:

"A person shall not make an offer of Securities in the DIFC unless the offer of Securities is made by way of an Exempt Offer or Prospectus Offer in accordance with this Part and the Offered Securities Rules."

Exempt offers attract a lighter (but not insignificant) regulatory burden than that associated with prospectus offers. A prospectus offer effectively requires DFSA clearance before any offer is made. This is because of the filing requirements with the DFSA coupled with the prohibition upon the distribution of any prospectus before the offeror has confirmed that the DFSA "has not notified the Person proposing to make the Offer that he must not publish the filed Prospectus".

The Markets Law and the Offered Securities Rules (the OSR Module of the DFSA Rulebook) govern the offer of securities and other financial instruments other than units in collective investment funds. (The regulatory framework for the DIFC funds regime is found in the Collective Investment Law 2006.)

Whether an offer is being made in the DIFC is a factual matter and one on which the analysis will vary from transaction to transaction. Guidance issued to date by the DFSA suggests that the regulator intends to cast its net widely. Of particular interest has been the DFSA guidance issued in connection with on-line offers. This reads:

"Many cross-border offers with a DIFC element will be caught by these Rules ... Cross-border offers of Securities made to Persons in the DIFC fall within the Rules. Any Person who makes such an Offer is required to comply with the obligations of an Offer under the Rules regardless of whether he is established in the DIFC or elsewhere ... The scope of the regime applies without differentiat-

ing the media by which Offers take place. In the context of internet-based offerings, this means that an operator of a website on which Securities are Offered to Persons within the DIFC will be subject to these Rules regardless of whether the operator is established in the DIFC or elsewhere."

The DFSA has a wide range of powers, and widely drafted objectives. Article 16 of the Markets Law gives the DFSA absolute discretion to issue, with immediate effect, a stop order if the DFSA believes that an offer has or would contravene either the Markets Law or the OSR Module of the DFSA Rulebook. The DFSA also has the power to apply to either the DIFC Court or the DIFC Financial Markets Tribunal for any one of a variety of orders, including orders that fines be imposed. To date the only regulatory enforcement actions taken by the DFSA have been in connection with organizations fraudulently holding themselves as having been authorized by the DFSA. The UAE's civil and commercial laws do not apply within the DIFC. The criminal laws apply and the Dubai police have authority to act in the DIFC.

Offers from, but not in, the DIFC

An entity intending to make an offer of securities from the DIFC must: (a) advise the DFSA in writing of the nature of the offer (including the jurisdiction in which the offer is to be made); and (b) comply with any initial and ongoing obligations that apply in that jurisdiction in relation to the offer of securities. The requirement that this notification be made before the event, coupled with the ease by which the DFSA can issue stop orders, means that offers from the DIFC are effectively subject to DFSA consent.

Central Bank-DFSAs MoU awaited

The differences in the Central Bank and the DFSA regimes, and the regulatory overlap being experienced by some institutions in the region, has led to calls for a joint statement to be issued by the regulators. A public statement has been expected for some time. In its absence, many market participants must remain mindful of the need to comply with two different regimes.

Company profile

Afridi & Angell Legal Consultants

Afridi & Angell is a law firm with offices in Dubai, Abu Dhabi and Sharjah, United Arab Emirates. The firm conducts a general corporate and financial legal practice and an international practice specializing in the Middle East.

Clients of the firm are multinational corporations, businesses, entrepreneurs, financial institutions and governments who seek advice in respect of their domestic and international affairs, including cross-border transactions, and inward and outward investment activities.

Lawyers of the firm combine the professional training and experience necessary to handle complex matters with regional knowledge and proficiency, including linguistic capabilities.

Total Partners: 7

Total lawyers: 20

Areas of practice

Corporate and commercial
Banking and financial services
Maritime and shipping
Project finance
Capital markets and privatization

International commerce
Insurance
Intellectual property
Arbitration and litigation support
Real estate and construction

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