

# The introduction of a new licence by the SCA

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## Background and Introduction

When the Securities and Commodities Authority (“SCA”) introduced Decision No. 1 of 2014 concerning Investment Management (the “Investment Management Regulations”), asset managers in the UAE that were historically licensed by the Central Bank were encouraged to obtain a new investment management licence from the SCA under the Investment Management Regulations (the “Investment Management Licence”). This new licence was meant to be the successor to the financial investment license previously granted by the Central Bank to conduct asset management services.

The term ‘Investment Management’ is defined in the Investment Management Regulations as the “management of Securities Portfolios for the account of third parties or the management of Mutual Funds in accordance with investment objectives and policy defined in the investment management agreement signed between the Investment Manager and its clients including individuals, establishments or Mutual Funds.”

In 2016, the SCA issued new fund regulations pursuant to Decision No. 9 RM of 2016 (the “Fund Regulations”). The Fund Regulations created a new licence category known as the “Management Company” licence (the “Management Company Licence”). The Management Company Licence permits the licensed entity to establish and manage mutual funds.

## Comparison

An initial impression of these two seemingly similar licences may illicit confusion as to why there is a need for both. However, the Fund Regulations have clarified the differences between the two licences and the following is a summary of the scope of each licence:

**Establishment of funds:** The Management Company License allows for the Management Company to establish funds, provide administrative services, and promote and supervise such funds. In contrast, the Investment Management Company License does not permit the establishment of funds.

**Management of funds:** The Management Company Licence also permits the Management Company to manage funds it has established, but does not permit the management of funds that it has not established. The Investment Management Company Licence permits the licensee to manage funds that are established by others, without permitting the establishment of funds.

**Security Portfolios:** The Investment Management License allows for the management of securities portfolios, but the Management Company License does not.

## Licensing Conditions

The following are the conditions to obtain a Management Company Licence under the Fund Regulations:

1. The applicant must be:
  - a company operating in the area of securities and licensed by the SCA;
  - a company incorporated to undertake the establishment and management of Mutual Funds;
  - a local bank or a branch of foreign bank licensed by the Central Bank; or
  - a branch of a foreign company licensed in the jurisdiction of its head office to establish and manage mutual funds and subject to a regulator similar to the SCA.
2. The share capital must not be less than AED 5 million.
3. The memorandum of association of the company must be authenticated before the official authorities and must be in Arabic or translated into Arabic.
4. The licensing fee must be paid.
5. Technical and administrative staff required to practice the business as per the rules issued by the SCA must be appointed.
6. Appropriate office, software and technical systems required to practice the business in accordance with the requirements of SCA must be procured.
7. The establishment of an internal control system that ensures the integrity of applying the law, regulations, decisions and circulars issued, as well as the bylaws applicable in the markets.
8. The creation of an operational manual for risk management that identifies and defines the potential risks, including the regulatory risks, which may face the company, how to handle them if they occur, and the monitoring and reporting of such risks in a manner that enables the company to continue in business and comply with the Fund Regulations.

Generally, most of the requirements to set up a Management Company are similar to those required to set up an Investment Management Company. Therefore, a licensed Investment Management Company may also apply for the Management Company Licence as it will already have met many of the Management Company License's requirements. This makes the Management Company License application much easier and faster for entities already holding an Investment Management Licence.

### **Obligations of the Management Company**

The Management Company has a number of obligations and restrictions prescribed by the Fund Regulations. The Management Company must:

1. Assume the tasks of the management of the investment of the fund it establishes, including the administration, promotion and supervision of the fund. The unit holders may not interfere in the management of the fund in any way, except in the matters set forth in the prospectus or the matters which the Management Company decides must be submitted to the unit holders for voting.
2. Act as the legal representative for any mutual fund in dealings with third parties.
3. Refrain from the management of security portfolios or mutual funds established by third parties without obtaining a Investment Management Licence.
4. In the case of the company also being licensed as an investment manager, refrain from investing the money of security portfolios it manages in any mutual funds it establishes or manages without the prior consent of the unit holders.
5. Ensure its capital is at least 0.02% of the net value of the assets of the funds established or managed by the company where the value of assets of the Mutual Funds established or managed by the company exceeds one billion Emirati Dirhams, provided that the additional capital does not exceed 40 million Emirati Dirhams.
6. Manage risks and conflicts of interest with the security portfolios managed by the company with any mutual funds which the company establishes or manages.
7. Ensure the assets of the fund are maintained separately from the money and assets of the

Management Company and from the assets of any other fund established or managed by the Management Company.

8. Refrain from promoting or providing administrative services to third parties without obtaining the approval or licence to practice that activity from the SCA.
9. Appoint a custodian for the fund and not change the custodian without the consent of the SCA and refrain from acting as the custodian for the mutual funds established or managed by the Management Company.
10. Ensure that the Management Company, its parent company, affiliates, related or sister companies do not hold 30% or more of the capital of the entities in which the mutual funds established or managed by the Management Company invest.
11. Refrain from collecting subscription or redemption fees in cases where the investment is in the units of funds or shares of investment companies established or managed by the Management Company by itself or through associated or related management companies.
12. Assess the assets, calculate the net asset value of the unit, and distribute or maintain the profits.
13. Disclose all the information related to the fund and any other disclosures in relation to the fund's activities, reports and prospectus to the unit holders.
14. Ensure that the management fees conform to the risks and interests of the fund and with the interests of its unit holders. The management fees shall be defined and reviewed as per the applicable procedures in the Management Company. The fees shall be defined and be at a fixed rate, and additional incentive fees shall be disclosed in the prospectus.
15. Ensure that employee salaries are not associated with the performance of the fund.
16. Ensure that the fund units shall be sold and redeemed at the announced price of the units' net asset value and as per the mechanism set forth in the prospectus, provided that announcement is made at least twice a month.
17. Inform the unit holders of the dividends and the cases of suspending the redemption operations using the notification method set forth in the prospectus. All the procedures shall be documented and they shall be handled fairly.
18. Set an effective investment policy to manage the liquidity and suspension of the redemption operations that ensure an amount of liquidity that conforms to the nature of the fund to face the risks related to the fund's investments. Such liquidity may be represented in investment instruments with low risks and can be transferred into cash upon request.
19. Perform the sale and purchase operations in the markets while achieving "best execution" and not be biased so as to achieve special gains or compromise the rights of unit holders. The Management Company may not fabricate transactions to increase the commissions, fees or expenses of other entities.
20. Not allow the Management Company or any of its employees to obtain special gains or privileges from the fund except the agreed management fees.
21. Study the financial position of the companies and the assets in which the assets of the fund established or managed by the company are invested.
22. Constantly maintain the solvency required to practice the business to ensure its ability to meet its obligations as per the relevant criteria issued by SCA.
23. Set a written bylaw within a month from the date of receiving the license and provide the SCA with a copy of such bylaws while considering amending the provisions of such bylaws in conformity with the amendments made to the law, regulations, decisions or circulars issued under such law and inform the SCA of the same.
24. Conduct regular reviews of the internal control system and the operational manual of risk management and update them continuously in line with the nature of the company's business and as applicable in this field.
25. Set the professional ethical rules for its employees, supervise its employees, and regulate and control their personal transactions in securities to ensure they strictly abide by the provisions of the law and the regulations, decisions and circulars issued by SCA, especially those related to honesty, integrity and conflict of interests.
26. Cooperate and coordinate with the internal auditor and enable it to practice its tasks. Inform the SCA

of any violation of the law or the regulations, decisions, circulars, or rules issued under such law or the bylaws applicable in the markets.

27. Exercise due care in the performance of its tasks.

The introduction of the Management Company License will have several vital implications on the funds market in the UAE. This will especially affect existing Investment Management companies, as they will now have to apply for an additional license to be able to set up new funds, which will involve additional cost and time. As far as we are aware, no Management Company License's have yet been issued by the SCA, despite the Fund Regulations having been in place for several months. As the Fund Regulations will likely affect the way in which existing Investment Management companies operate and how new entrants will assess market conditions, it is important for such entities to carefully consider the implications of the Fund Regulations.