

M&A FOR UAE BANKS AND FINANCIAL INSTITUTIONS - REGULATORY UPDATE

There has been significant M&A activity in the financial institutions industry across the Middle East in recent years. The COVID-19 crisis will prompt further consolidation, acquisitions and restructurings and recent regulatory changes (outlined in this paper) could facilitate such activity in the UAE.

Additional clarity from the Central Bank of the UAE in relation to approval requirements and process will be welcomed by the industry.

The regulations now envisage prescriptive and often detailed requirements, which will necessitate even greater planning and regulatory engagement as well as a well thought through (and properly documented) impact analysis early on.

OVERVIEW

There have been several regulations in recent years in the financial services sector covering M&A in the UAE. Most recently, the CBUAE has published two circulars in respect of oversight and approvals for changes in control of banks and acquisitions by banks (Circular 2 of 2020 and Circular 5 of 2020). Both regulations implement the relevant parts of the Central Bank Law of 2018.

Prior to this, the UAE Security and Commodities Authority (SCA) and the UAE Insurance Authority have each published guidelines in respect of approvals for M&As within their remits.

The rules remain subject to the permitted thresholds for foreign ownership of financial services firms, which have not been amended in the recent changes.

Bank M&A Implications

- Carefully assess the requirements in the regulations and prepare for detailed regulatory engagement as part of the process.
- Early and well thought through engagement will be key, along with understanding the specific issues the CBUAE is likely to be concerned with, especially in the current climate. This will include: classification of the acquisition, approach to due diligence and the scope of any required internal assessments.
- Acquisition and change of control rules apply also to international banks with branches in the UAE, triggering local notification requirements.

CBUAE REGULATIONS

Circular 2 of 2020 and Circular 5 of 2020

Background and common principles

The Central Bank Law requires approvals for changes in controlling interest, mergers with and acquisitions of other institutions and transfers of liabilities. The recent circulars set out a detailed framework around this and the relevant thresholds.

The rules will apply to both locally incorporated and international banks with branches in the UAE (although for branches, it is expected to be largely a notifications regime for changes in its controllers and non-UAE transactions).

Prior to these rules, parties have typically been advised to take early steps to engage with the CBUAE and seek comfort on proposed transactions. This is now essential and transactions in the banking sector will need to be well prepared for more extensive oversight and formalised application processes with the CBUAE. Both circulars set out that the CBUAE will seek to ensure the standards imposed for transactions protect the soundness of banks,

financial stability and retail customers. These will be key aspects to cover in regulatory engagement.

An additional feature of the regulations is that they expressly place the onus on the boards of banks to take a "comprehensive approach" to assessing M&A and banks are encouraged to adopt leading practices.

CBUAE Major Acquisitions Regulations

Scope and Application

These regulations extend to both bank-specific M&A and other types of bank acquisitions, including for example, technology assets.

The definition of a major acquisition includes any asset over 5% of total regulatory capital (Tier 1, AT1 and Tier 2) (not total assets) thus capturing a relatively low threshold before prior approvals are triggered. Smaller acquisitions could be deemed as major by the CBUAE in advance – thus underlining the importance of early regulatory engagement.

There is a notification requirement for acquisitions over 1% of reg cap amount and this is expressly to be required within 30 days "after the transaction". However, in practice, we would expect there would be pre-discussions with CBUAE to ensure the transaction would not be deemed material.

Acquisitions of debts are excluded – this is helpful as loans are transferred in the ordinary course of business. However, it is not clear how larger banking portfolios transfers are captured by the rules. It is prudent to assume they are covered and debts included to calculate deal size.

Major acquisitions being undertaken by UAE banks outside of the UAE will also be subject to enhanced consideration and due diligence, which includes detailing of the political, economic and legal risks of the overseas jurisdiction in question.

M&A Diligence

The regulations prescribe that applications for CBUAE approval should include the due diligence report used for the comprehensive internal assessment of the acquisition, with guidance to seek no objection from the CBUAE ahead of commencing due diligence. This is likely to require a thorough process of identifying the relevant risks and benefits, and internally allocating what will be prepared for CBUAE approvals.

Detailed Approval Requirements and Approach

Following the 2018 Central Bank Law, banks must not acquire any institution, or transfer any of their liabilities without first obtaining CBUAE approval. The 2020 Major Acquisitions Regulations add that banks must obtain approval from the CBUAE prior to completing a major acquisition. There remains some uncertainty around the acquisition of an institution which is not a "major

Change of Control Requirements

- The change of control requirements in the CBUAE rules require CBUAE approval for 5%+ acquisitions of UAE banks and finance companies. This is a relatively low threshold. There is a notification requirement for bank acquisitions of 1% - 5% and changes in control for branches of non-UAE banks.
- For UAE insurers, approval requirements apply for 10%+ acquisitions, with a notification for acquisitions of 5% - 10%. For branches of non-UAE insurers, it is likely to be a notification requirement.
- As the SCA regulates a wide variety of different businesses, its change of control approval requirements differ from requiring approval to making notifications depending on the type of firm.
- As the regulator of public companies, the SCA also oversees major acquisitions of listed entities and various approval requirements kick in on acquiring public stakes, most notably the mandatory take-over rules in the SCA's M&A regulations for public companies.

acquisition" – underlining the requirement to seek initial discussions with the CBUAE.

In addition to the diligence report noted above, applications will require detailed information, including: key terms, price, funding and the impact on financials, governance and internal risk functions, HR and IT, along with the impact on the market generally and customers. Applications will also have to demonstrate compliance with the assessment criteria of the CBUAE, including customer protection, effective regulatory oversight, the recovery and resolution of the institution and that there will be no undue risks to customer protection or prudential requirements.

Board and Internal Duties

The rules also prescribe detailed internal governance requirements to be followed. These include that the board of a bank making a major acquisition carefully scrutinises and mitigates risks for the proposed acquisition, including the need for additional internal resource to assess and manage the risks.

Persons within banks who provide incorrect information to the CBUAE may be barred from being senior managers from a fit and proper perspective. These requirements may present challenges for sensitive M&A projects to be kept confidential within institutions.

CBUAE Change of Control Regulations

The change of control requirements for banks and finance companies impose a low threshold for where approval is required (5%) and detailed information on proposed controllers may be required, including historic financials. The change of control regime further emphasises the extensive oversight of the CBUAE in M&A going forward.

International banks with bank branches in the UAE will be obligated to comply with CBUAE disclosure obligations in respect of controllers, and events affecting their controllers in certain circumstances.

Article 95 of the Central Bank Law requires prior approval for persons seeking to acquire controlling interests in UAE banks. This has been set at 5% in the regulations, which state that a person may not obtain or divest shareholding over 5% without prior written approval. Approval of the CBUAE is also required in order to increase shareholding over 5%. The approval requirement covers direct and indirect changes in control (approvals for intra-group transfers may also be needed).

Branches of international banks must notify the CBUAE of changes in its control over 5%. UAE Banks must notify the CBUAE for 1% acquisitions or more. Prior written notice is also required where there is an intention to obtain or divest significant or controlling shareholdings.

The CBUAE will consider shareholders acting in concert as one group for the purposes of the ownership tests.

Banks are required to provide information to the CBUAE to identify who its controllers are from time to time, with immediate notification of a 5% change in control and upon becoming aware of any material information which may negatively affect the suitability of a controller.

Applications for approval for a change in control must include a questionnaire in a form prescribed by the CBUAE, including a detailed explanation of the shareholding structure, financial information of the applicant for the last three years, and other information reasonably necessary for the CBUAE. Applications must be made by the ultimate beneficial owner.

The CBUAE will require each proposed controller to be fit and proper and, similar to assessments in respect of acquisitions, ensure the transaction will not impact its effective supervision and the safety and soundness of the institution.

UAE Insurance Authority

Prior to the CBUAE Major Acquisitions Regulations, the UAE Insurance Authority public rules specific to changes in control of insurers in 2019. Insurance Authority approval is required for acquisitions of more than 10% of a UAE insurer, with a notification requirement for 5% acquisitions.

For a UAE branch of a non-UAE insurer, a notification is required to the Insurance Authority on changes in control. It would be advisable to check on the specific requirements in these cases.

These rules set out a similarly detailed application process for approvals, detailed information on financial resources. We expect extensive scrutiny from the Insurance Authority on capital requirements, following the overall of prudential requirements for insurers over recent years. We have

covered such financial regulations in our detailed briefing set out [HERE](#).

The rules do not yet extend to brokers, with firms generally engaging with the Insurance Authority to understand its requirements specific to the transaction.

We expect further consolidation in this sector in the future and we understand there is a positive desire for further mergers from the Insurance Authority. COVID-19 has had a varying effect on the industry, further covered in our international insurance toolkit [HERE](#), with some capital relief for brokers and an extension of the implementation of rules on the sales and commissions of life insurance set to add further pressures to brokers in this area.

Securities and Commodities Authority

The SCA regulates public companies and licenses many types of financial services firms conducting securities, commodities and markets business.

As set out in our briefing [HERE](#), the SCA has detailed guidelines and requirements for public company take-overs and acquisitions, including the requirements for a mandatory take-over offer applying to acquisitions of over 30%.

The SCA has different requirements in respect of changes in control depending on the type of financial services firm (which may not be public companies). Rules for investment managers and brokers require SCA approval in respect of certain changes in control, with rules covering financial advisers and promoters requiring notifications. However, most firms have a number of licenses and approvals from the SCA and will generally be advised to engage with the SCA on its requirements in M&A transactions.

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