Explanatory Note

to the Ministerial Resolution regarding the Central Bank of Kuwait's Supervision over Investment Companies

In accordance with the provisions of Article (55) of the Law No. 32 of 1968 regarding Currency, the Central Bank of Kuwait and the Regulation of Banking, amended by the Law Decree No. 130 of 1977, some investment companies in Kuwait have become subject to certain provisions of Chapter Three of the said law, as stipulated in the resolutions promulgated by the Minister of Finance. This is provided that the Central Bank of Kuwait (CBK) Board of Directors' approval is obtained for each company.

Considering the challenging conditions impacting investment companies and the circumstances the local economy is experiencing, developing a supervision framework for investment companies has become imperative. This includes designating a registry for investment companies with the CBK, and laying down additional rules and provisions in addition to those stated in the ministerial resolutions issued with respect to CBK's supervision.

The additional rules and provisions mentioned in the attached draft ministerial resolution aim to strengthen CBK's oversight over investment companies with regards to solvency and ability to address risks arising from deterioration of their investment portfolios and increase of non-performing loans extended by them.

To elaborate, **Article (1)** of the attached draft ministerial resolution explains the nature and activities of investment companies.

Article (2) states that investment companies may not carry out banking activities, which, under the CBK law, are solely practiced by banks. The last paragraph exempts existing investment companies whose mandates include certain banking activities due to being established before the CBK law came into force, as they have been practicing these activities for a long time.

Article (3) states that investment companies may not carry out foreign exchange activities for third parties, except for existing investment companies whose mandates include foreign exchange.

The purpose is to ensure that investment companies will not crowd out exchange companies, and to assign specializations under the activities of financial institutions of the same nature so that the CBK will be able to lay down regulations for supervising each type of these financial institutions.

Article (4) states that investment companies may not represent foreign banks or foreign banking institutions in the State of Kuwait, and carry out banking activities inside Kuwait on their behalf, nor enter into management contracts with them.

Management contracts authorize a contracted entity to make decisions for running a company, and practicing influence. Such contracts do not include those between a Kuwaiti investment company and a foreign entity to provide technical services.

Article (5) provides for the CBK supervision over the establishment of new investment companies, ensuring a need for their establishment, and that their capital is adequate and mandates are sound.

Articles (6) to (11) stipulate the rules and provisions relating to the preparation of the investment companies' registry with the CBK. This includes registration guidelines, required information, amendments to that information, elimination from the registry and dissolution of eliminated companies.

Article (12) states that the CBK Board of Directors shall lay down the rules and regulations the investment companies must comply with to ensure their creditworthiness, in particular the minimum ratio of a company's own funds to its obligations.

Article (13) states that the CBK Board of Directors may lay down rules for bonds issued by investment companies for its own account including the maximum limit and interest rate. This article also states that rules and regulations may be dictated to govern issuance, or contribution to issuance, of bonds in the domestic market on behalf of third parties.

Article (14) stipulates that the CBK Board of Directors may set for investment companies the maximum limit of finance to a single customer, and special conditions for loans, covering the loan term and collateral.

It also stipulates that a "Center of Risks System" for the loans granted by investment companies to others may be established.

Article (15) states that the CBK Board of Directors may adopt a scheme for the provisions the investment companies must make against nonperforming loans and potential risks in their investment portfolios, in order to safeguard investment companies.

Articles (16) to (19) highlight the CBK's mandate to provide investment companies with regulations to realize the targets of the credit or cash policy. In addition, the CBK may inspect investment companies to ensure the soundness of their activities and financial positions, and monitor them through provided information, statements and statistical data. The CBK approves investment companies' balance sheets and profit & loss accounts before presenting them to the general assemblies to ensure the soundness of financial positions and requiring adequate provisions and reserves.

The CBK may ask investment companies' auditors to conduct an objective evaluation of those companies' assets and obligations, and sign any statements or information sent by those companies to the CBK.

Article (20) provides for the actions the CBK Board of Directors may take in case an investment company encounters severe financial difficulties that jeopardize the soundness of its financial positions.

Article (21) stipulates that the CBK may impose penalties as stipulated under Article (85) of the CBK law on any investment company that violates the provisions of its memorandum or articles of association or CBK-issued instructions/resolutions, or did not submit the required information and statements, or submitted inaccurate statements.