
THE BANKING REGULATION REVIEW

SIXTH EDITION

EDITOR
JAN PUTNIS

LAW BUSINESS RESEARCH

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Chapter 27

KUWAIT

*Haifa Khunji and Basem Al Muthafer*¹

I INTRODUCTION

Kuwait has a stable banking system that is sizeable, well developed and enjoys the backing of a strong support system.² Besides commercial and specialised banks at the heart of the system, there is an increasing number of financial companies and investment funds, as well as insurance companies.³

The banking industry in Kuwait is characterised by high competition among domestic banks, with the National Bank of Kuwait (NBK) currently enjoying a dominant market share with an increasingly large local and regional client base. Other major banks include Gulf Bank, CBK, Burgan Bank and Al Ahli Bank.

The global financial crisis had a negative impact upon Kuwait's financial system, but the authorities succeeded in preserving financial stability.⁴ The banks had high credit exposures to more volatile sectors including investment companies and real estate.⁵ During the global financial crisis, the tighter liquidity conditions and falling asset prices adversely affected the quality of Kuwaiti banks' assets and resulted in large increases in banks' non-performing loans, particularly for the investment companies and real estate sectors.⁶

Following the crisis, the authorities introduced measures to uphold confidence in the banking system, including the extension of bank deposit guarantees, bank liquidity injections, reductions in interest rates and the adoption of a financial stability law,

1 Haifa Khunji and Basem Al Muthafer are partners at KBH Kaanuun.

2 Oxford Business Group: Intervention Ensured Stability For Banking Sector: 11 May 2010.

3 International Monetary Fund – Kuwait: Financial System Stability Assessment: May 2004.

4 International Monetary Fund – Kuwait: Financial System Stability Assessment Update: 1 July 2010.

5 www.ameinfo.com: Fitch says Kuwaiti banks to remain under pressure: 29 August 2011.

6 International Monetary Fund; see footnote 4.

Law Decree 2 of 2009 on Enhancing the State Economic Stability, which provides for several kinds of financial and economic stimuli intended to promote financial stability in Kuwait and improve economic conditions.⁷ Further, 2012 saw the CBK revamping its bank governance rules in a bid to bring them in line with international best practices.⁸

II THE YEAR IN REVIEW

Kuwaiti banks, both conventional and Islamic, continue to adopt a conservative approach, and Kuwait's banking sector remains on the path to recovery from the worldwide financial crisis with a significant improvement in bottom line figures.

However a by-product of the banks' conservative policies that helped to reignite growth is that they have also contributed to the low credit growth witnessed in Kuwait since 2010. That said, rating agency Moody's has stated that Kuwait is not likely to enter a negative credit situation. The banks' conservative approach to lending is said to have simply demonstrated their ability to maintain strong fundamentals as well as the ability to build up provisions in difficult times.

Kuwait's banks should therefore be able to maintain growth.

III THE REGULATORY REGIME APPLICABLE TO BANKS

The CBK (established by virtue of Law 32/1968 (CBK Law)) is responsible for the supervision, regulation and licensing of deposit and non-deposit taking of financial institutions and investment houses, operating in the Kuwaiti financial system. This authority extends to investment houses, some of which operate according to Islamic financial principles. Islamic banks have been subject to CBK supervision since 2003.⁹

The Supervision Sector at the CBK is responsible for implementing the provisions of Chapter III of the CBK Law, amended under Decree Law No. 130 of 1977 and all applicable regulations and instructions issued by the CBK. Chapter III of the CBK Law provides for the organisation of banking business in Kuwait.

Article 56 of the CBK Law provides that banking business may only be practised by institutions set up in the form of joint-stock companies, whose shares are placed for public subscription. Banks that are founded or co-founded by the government and branches of foreign banks licensed to operate in Kuwait may be exempted from the aforementioned provisions by a decision of the Council of Ministers. Funds allocated for opening a foreign bank's branch in the state of Kuwait should not be less than 15 million Kuwaiti dinars. This amount may be increased by a decision of the board of directors of the CBK.

The board of directors of the CBK stipulates the rules and regulations to be complied with in connection with the operation of branches of foreign banks in Kuwait. Before the incorporation process begins, the application to establish a bank in Kuwait

7 2010 International Monetary Fund – Kuwait: Financial Stability Assessment.

8 www.arabtimesonline.com/NewsDetails/tabid/96/smld/414/ArticleID/184701/t/Kuwait-cbank-issues-new-guidelines-on-banks-governance/Default.aspx

9 International Monetary Fund; see footnote 3.

should be presented to the CBK's board of directors to issue recommendations. No banking institution may commence operations until it has been registered in the Register of Banks at the CBK.

In accordance with Article 57 of the CBK Law, unless the prior authorisation of the CBK has been obtained, the direct or indirect ownership by any single natural person or legal entity in a Kuwaiti bank should not exceed 5 per cent of a bank's capital. However, there are some exceptions to these provisions (e.g., governmental bodies). Where single ownership does exceed the 5 per cent threshold, there is an obligation on the person or legal entity to dispose of the excess within the period defined by the CBK Law.

Article 86 of the CBK Law also regulates the activities of branches of foreign Islamic banks authorised to operate in Kuwait. In accordance with Article 89 of the CBK Law, Islamic banks should be registered in a special register for Islamic banks at the CBK.

IV PRUDENTIAL REGULATION

i Prudential supervision function

Under the current legal framework, the prudential regulation and supervision of the banking and investment companies sectors are conducted primarily by the CBK.

In February 2010, the Parliament passed Law No. 7 of 2010 (CMA Law), which, *inter alia*, established the Capital Markets Authority (CMA) in Kuwait and provided the CMA with the power to issue necessary by-laws and instructions to implement the CMA Law. Prior to the establishment of the CMA in 2010, the Kuwait Stock Exchange, a self-regulated authority, was charged with supervising brokerage firms, entities engaged in portfolio management and the Kuwait Clearing Company, as well as banks' and investment companies' activities related to securities trading and portfolio management on account of third parties. The supervision of the insurance industry, including brokers and agents, is the responsibility of the Ministry of Interior.

In essence, the CMA Law grants broad regulatory and monitoring powers over most investment companies' activities to the CMA, including licensing and issuing quantitative and qualitative regulation for securities businesses and prudential requirements for investment companies. There is, however, significant potential for regulatory and supervisory overlaps and gaps that need to be addressed to ensure effective oversight.¹⁰ In particular, the CMA Law is unclear on the respective responsibilities of the CBK and the CMA. The CMA should be tasked with regulating public and private offerings for Kuwaiti and non-Kuwaiti securities, the promotion of mutual funds and other collective investment schemes, and supervising and monitoring acquisitions and mergers of listed companies, with particular emphasis on protecting the rights of minority shareholders. However, the Law is not clear on whether the CBK or the CMA will take the lead on prudential regulation (solvency risk management, financial guarantees, capital and large exposure reporting limits) and general operational aspects (such as organisational structure, strategy, reporting lines and internal controls).

10 Kuwait: Financial System Stability Assessment – Update, International Monetary Fund, July 2010, IMF Country Report No. 10/239.

It can be observed from the recent financial crisis that there is a need for a major upgrade of the CBK's macro-prudential framework. To improve this framework, the CBK created a Financial Stability Unit (FSU), which plays a major role in addressing macro-prudential issues when they arise. The FSU can draw upon interdisciplinary expertise from the on-site and off-site supervision department and the foreign operations and economic research department.

Kuwait has shown progress towards achieving international standards. The CBK Law was amended in 2004 to enable the establishment of memoranda of understanding (MoUs) on information sharing and collaboration with foreign authorities for the purpose of consolidated supervision. It also gives the CBK the power to reject changes in significant ownership of a bank. A more gradual and comprehensive framework for remedial measures to deal with problem banks is now in place. This allows the CBK to impose fines, limit activities, remove senior management, and appoint a controller or a commissioner, or both, to manage the bank.

ii Other functions

Bank risk management

The CBK has issued comprehensive regulatory guidance to assist banks in better identifying and managing risks in the future and capturing them in the ICAAP.¹¹ The intent of the supervisory review process – which has yet to be implemented – is not only to ensure that banks have adequate capital to support all the risks in their business, but also to require banks to develop and use better risk-monitoring and management techniques.

The CBK has begun the important process of moving the supervisory process from a compliance-based to an enhanced risk-based approach. This involves a gradual but fundamental reshaping of the business process of banking supervision and its organisation, as well as adequate leadership and an appropriate change process. The CBK is also in the process of further developing an enhanced risk-based supervisory system and a more elaborate early warning system.

Banks' corporate governance

The CBK is slowly playing a more assertive role in enhancing corporate governance practices in banks. The CBK's board of directors agreed in 2012 to issue new directives regarding the governance rules and regulations of Kuwaiti banks. These directives generally aim to improve banks' governance standards by ensuring the board of the CBK actively takes part in the management of banks, as well as protecting shareholders' interests and the interests of all parties involved. The focus of the CBK and Kuwaiti banks also shifted to risk management and to the need to enhance internal supervision as well as putting into place systems for internal and external auditing.¹²

11 Internal Capital Adequacy Assessment Process: these guidelines, which supplement Basel II's second pillar (supervisory review process), are based on the Supplemental Pillar II Guidance issued by the Basel Committee in July 2009.

12 *Arab Times*; see footnote 8.

Investment companies

The CBK is in the process of strengthening its regulation and supervision of investment companies.¹³ The new regulatory initiatives encompass new prudential requirements, as well as improvements in corporate governance and risk management. In response to the global financial crisis and in line with international initiatives for improving financial sector resilience, the CBK is considering introducing a regulatory ceiling on investment companies' maximum leverage; liquidity ratios to prevent the build-up of excessive maturity mismatches between assets and liabilities; and a regulatory ceiling on foreign debt. Regulation must be complemented with effective supervision (including of investment companies' activities outside Kuwait) and enforcement.

Contingency planning and crisis management

Contingency planning and crisis management arrangements need to be strengthened. An MOU formalising inter-agency cooperation arrangements between the CBK, the Ministry of Finance, the Kuwait Investment Authority and the CMA, and the regular testing of these arrangements, would strengthen crisis preparedness. Inter-agency coordination and cooperation during financial crises occurs mostly on an informal basis,¹⁴ raising the risk of conflicts of interest, lack of preparation and inadequate information sharing among regulators. The MOU would provide an explicit description of responsibilities in the event of a financial crisis. The adequacy of inter-agency arrangements and the overall state of crisis preparedness could be tested regularly in crisis simulation exercises.

Resolution framework

Kuwait's bankruptcy framework needs to be amended to introduce a specific resolution regime for failing financial institutions beyond the corporate bankruptcy regime. Kuwait does not have a specific resolution regime setting out distinct bankruptcy procedures for financial institutions, particularly banks and investment companies, which would help reduce the impact of failures of financial institutions on the financial system and the real economy. Furthermore, the existing bankruptcy procedures can be cumbersome, with onerous court procedures. These issues are not addressed by the new Law No. 2 of 2009 or the Financial Stability Law (FSL).

Facilitating debt rescheduling for viable investment companies is a major challenge within the current legal and regulatory framework. In the absence of a special resolution regime, progress with debt rescheduling in the investment companies sector has been slow. Only one investment company has sought debt rescheduling under the FSL. Furthermore, only investment companies that seek to use the FSL's provisions undergo a mandatory assessment of their viability, which consists of an evaluation of the consulting companies, but is extensively commented upon by the CBK.

13 To address weaknesses in risk and asset management in the investment company sector, in June 2010 the CBK imposed new regulations on financial leverage, liquidity and international borrowing of investment companies.

14 The Ministry of Finance and the Ministry of Commerce and Industry are represented on the CBK board, while the CBK is also represented on the Kuwait Investment Authority board.

iii Management of banks

Central Banking Law 32/1968 (CBK Law)

Without prejudice to the provisions of the Law of Commercial Companies, wherever they are not in conflict with the provisions of the CBK Law, banking business may only be practised by institutions set up in the form of joint-stock companies, the shares of which are placed for public subscription.¹⁵ Funds allocated for opening a foreign bank's branch in Kuwait shall not be less than 15 million Kuwaiti dinars. This amount may be increased by a decision of the board of directors of the CBK.

The CBK's board of directors lays down the bases, rules and regulations to be complied with in regard to the operation of branches of foreign banks in Kuwait. Before the formalities of incorporation are processed, applications to establish banks should be presented to the board of directors of the CBK to issue the necessary recommendations.

The paid-up capital of any bank should not be less than 75 million Kuwaiti dinars.¹⁶ Unless by prior authorisation of the CBK, the direct or indirect ownership by any single natural person or legal entity in a Kuwaiti bank shall not exceed 5 per cent of the bank's capital. Governmental bodies and bodies with independent or attached budgets are exempted from these provisions. Where single ownership exceeds the above percentage for any reason whatsoever, the concerned natural person or legal entity shall dispose of the excess within the period defined by the CBK.

Violation of this provision results in the shareholder not availing itself of the excess equity in regard to voting rights in the bank's general assembly and directing the bank.

The board of directors of the CBK shall lay down the bases and rules defining the concept of indirect ownership.

According to Article 58 of the CBK Law, if the capital of a bank falls below the minimum limit referred to in Article 57 of the CBK Law, the bank shall cover the deficit within such period as may be fixed by the Central Bank, provided that the period shall not exceed one year from the date the bank concerned is notified.

Based on Article 68 of the CBK Law, the CBK applies to all banks under its supervision a set of minimum professional quality standards to be met by executives and members of the boards of directors, with regard to qualifications, experiences, leadership and initiative potential, along with the ability to deal appropriately with changes and developments. Banks in Kuwait strive to achieve all these through a high-quality management system that, in turn, provides the basis for value-added supervision.

iv Registration of banks

No banking institution is allowed to start operations until it has been registered in the Register of Banks at the CBK.¹⁷ Under Article 60 of the CBK Law, the registration or refusal of registration of banks shall be effected by a decision of the Minister of Finance on the recommendation of the board of directors of the CBK. The Minister of Finance shall, on the recommendation of the board of directors of the CBK, issue regulations

15 Article 56 of the CBK Law.

16 Article 57 of the CBK Law.

17 Article 59 of the CBK Law.

for the registration of banks, including the rules, procedures and dates for registration, amendments and publication of this registration.

Further to the above, registered banks shall notify the CBK of any amendments they intend to make to their MoUs or articles of association. If such amendments are approved in principle by the CBK, the formalities necessary for processing them may then be accomplished in accordance with the provisions of the Law of Commercial Companies.¹⁸

A bank may be deleted from the Register of Banks owing to the following reasons:

- a* at its own request;
- b* if it does not start business within one year from the date it is notified of the decision regarding its registration in the Register of Banks;
- c* if it is declared bankrupt;
- d* if it merges with another bank;
- e* if it ceases its operations, or if its liquidity or solvency are endangered; or
- f* if it commits any act in violation of the provisions of this Law.¹⁹

v Banking supervision

All the core regulatory principles advocated by the Basel Committee are adequately incorporated within the CBK supervisory system. Although the CBK's supervisory systems rely on a constant monitoring of the state of banking and monetary affairs in Kuwait, they are nonetheless in line with relevant worldwide developments.

For the sake of transparency, Kuwaiti banking units have been legally required to adhere to the International Accounting Standards in the preparation of their accounts since 1991.

In December 1993, the CBK issued its instructions on the minimum controls that should be adhered to by Kuwaiti banks in rationalising and regulating their credit policies, such as subjecting the extension, renewal and increase of credit to the receipt of a corresponding client's application; providing credit on the basis of a proper case study; and ensuring that the extended credit is used for the declared purpose.

In April 1995, the CBK set the maximum credit concentration limits for Kuwaiti banks at 15 per cent of a bank's broad capital for any single client, within the framework of the relevant Basel Committee recommendations.

In November 1996, the CBK issued general guidelines highlighting the requirements for the internal control systems of banks and the external auditors reports regarding the evaluation of these systems.

In April 2007, the required minimum capital adequacy standard for local banks was set at 12 per cent effective at the end of December 1997. This increased from the 8 per cent rate applied as of the end of 1992.

The adoption in September 1997 of a rating system for banks based on the 'CAMEL' approach was in addition to the ongoing enhancement of the early warning system currently applied.

18 Article 61 of the CBK Law.

19 Article 63 of the CBK Law.

Furthermore, a policy for the assessment and management of bank liquidity based on a maturity ladder approach was implemented thereafter.

V CONDUCT OF BUSINESS

i Confidentiality

Article 28 of the CBK Law provides that:

Unless otherwise permitted by law, no member of the board of directors, manager, officer or employee of the Central Bank shall disclose any information which relates to the affairs of the Bank or its customers, or the affairs of other banks subject to the control of the Central Bank, and to which he has access by reason of the duties of his office; except for cases where so permitted by the Law.

Thus, without prejudice to the application of any severer punishment under any other law, anyone who violates the prohibition provided for in Article 28 above shall be liable to imprisonment for a term not exceeding three months and to the payment of a fine not exceeding 225 dinars, or to either one of the said penalties, plus dismissal from service to all cases.

Article 80 of the CBK Law provides that:

Central Bank officials authorised to conduct inspections shall – during the term of their service and after quitting their jobs – maintain the confidentiality of accounts, books, and documents they review by virtue of their duty. They shall not disclose any information relating to the affairs of the banks or institutions inspected, or to the affairs of their customer, except in such cases where it is permissible to do so by law, and that without prejudice to any severer punishment under any other law, every person who violates the prohibition provided for in the preceding paragraph shall be liable to imprisonment for a period not exceeding three months and to the payment of a fine not exceeding 225 dinars, or to either of these two penalties, plus discharge from service.

These two provisions above are specifically addressed to CBK employees, yet are considered as the legal basis for the commitment of Kuwaiti bank employees in general to maintain confidentiality within the banking business.²⁰

Furthermore, Article 43 of Decree Law No. 39 of 1980, which was integrated into the Civil and Commercial Procedure Code, states that:

[...] the provision prohibiting lawyers, doctors, agents or others from disclosing any facts or information they become aware of, by reason of their profession or in their capacity thereof, even after the expiration of their service or capacity.

20 Instructions Regarding Banks to Maintain the Confidentiality of Information and Data Concerning their Customers, Circular Circulated to all Banks dated 2 December 1986.

The above-mentioned legal rules addressing the commitment of banks to maintain customer confidentiality are complemented by Article 30 of the Constitution of the State of Kuwait, which provides that ‘personal freedom is secured’, where personal freedom means everything relating to individual and financial persona.

Banks’ commitment to keeping the confidentiality of customers’ data and information is intended to create confidence in the country’s banking system and to provide assurance for people that their transactions with banks will not be exposed to the public or disclosed, except where so permitted by the law.

ii Consumer credit legislation

Although there is no separate legislation covering the confidentiality of bank accounts in Kuwait as is the case in some other countries, there are several strict laws protecting the right of customers not to disclose the secrecy of such accounts, including Law No. 32 of 1968 with respect to Currency, the Central Bank of Kuwait and the Organization of Banking Business. This Law prohibits any director, manager, officer or employee of a bank from disclosing any information in the course of his or her employment and after termination of service in connection with the bank’s affairs, customers or affairs of other banks that he or she may have had access to because of his or her employment, except in cases where the law authorises such action. The punishment in the case of unlawful disclosure takes place according to the provisions of Article 85-bis of the aforesaid Law.

The Law further states that anyone who violates the restriction provided for in Article 85-bis is liable to imprisonment for a term not exceeding three months or payment of a fine not exceeding 250 Kuwaiti dinars, or both, in addition to a court ruling for dismissal.

The Law Concerning the Capital Market Authority and Companies Listed on the Kuwait Stock Exchange also emphasises the necessity of observing the confidentiality of customers’ information and not disclosing such information, either intentionally or unintentionally.

iii Privacy

There are several constitutional and legal provisions that protect the right to privacy.

Article 30 of the Constitution states that personal liberty is guaranteed. There is no doubt that bank confidentiality is one of the fundamental aspects of such personal liberty, the protection of which is based upon political, economic and social considerations in addition to legal principles.

Article 43 of Legislative Decree No. 39 for 1980 with respect to Evidence in Civil and Commercial Matters states as follows: ‘Any lawyer, medical practitioner, attorney or other persons who may come to know through his occupation or capacity any information shall not disclose it even after the termination of his service or loss of his capacity.’

Article 41 of Law No. 6 of 2010 with respect to Labour in the Private Sector gives an employer the right to dismiss a worker without notice, compensation or indemnity if a worker discloses the secrets of the establishment so as to cause or be likely to cause a certain loss thereto.

Banks in general pay a great deal of attention to ensuring that banking business activities are conducted in compliance with international guidelines and practice. Banks in Kuwait tend to adopt all the effective measures and precautions to ensure the protection and confidentiality of their data and information related to their customers. The CBK has offered close supervision and has issued numerous principles and guidelines covering privacy. One of the main targets of the CBK's oversight has been the misuse of customers' information, for which it has established a unit that undertakes periodical inspection of banks for checking and testing their information systems, computers and their applications, and ensuring the availability of the regulatory restrictions for such systems to prevent any breach of information security. Each bank is instructed to take appropriate actions to deal with areas of negligence and omissions and to bridge gaps in their business systems to enhance the effectiveness of their regulatory guidelines.

In addition, the CBK has also issued instructions concerning the principles of sound management of financial institutions, which includes the necessity of the boards of directors' compliance with ensuring the confidentiality of information and compliance with professional conduct. Moreover, banks are required to comply with the instructions issued in November 1996 concerning rules of internal control, which ensure the prevention of direct and indirect access to assets and information except by the authorised personnel to avoid irresponsible uses of such information.

iv Anti-money laundering

The Kuwait Financial Intelligence Unit (KFIU) operates under the auspices of the CBK. The KFIU, in collaboration with the Office of the Public Prosecutor (OPP), works to process and exchange information about suspicious money laundering activity. In particular, the KFIU is responsible for the following:

- a* receiving reports of money laundering transactions from the OPP, analysing the reports and providing technical opinions to the OPP;
- b* maintaining a database and statistics with regard to these reports;
- c* contributing to training and awareness programmes regarding combating money laundering transactions in coordination with the National Committee of Fighting Money Laundering Transactions and Terrorism Finance and other relevant bodies; and
- d* coordinating with the OPP on the exchange of information and data at both the national and international level.

The current anti-money laundering law does not specifically cite terrorist financing as a crime; therefore, terrorist financing criminal cases are handled under 'crimes against the state' statutes.²¹ In 2010, the Minister of the Interior made a decision to transfer the responsibility for money laundering crimes from the General Directorate for Criminal Investigations at the Ministry of the Interior to Kuwait State Security.

21 International Monetary Fund Country Report No. 11/267, Kuwait: Report on Observance of Standards and Codes – FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism, September 2011.

Kuwait has had difficulty implementing the current anti-money laundering law due in part to structural inconsistencies within the law itself. Law No. 35 of 2002, the Law Regarding Combating Money Laundering Transactions, does not mandate that the KFIU act as the central or sole unit for the receipt, analysis and dissemination of suspicious transactions reporting requirements. This Law sets out the definition of money laundering, criminalises money-laundering operations and enlists the different penalties. The KFIU that is in place operates under the CBK, and is not an independent and autonomous competent authority. The vague delineations of the roles and responsibilities of the KFIU, the CBK and the OPP continue to hinder the overall effectiveness of Kuwait's anti-money laundering regime.

A major development in strengthening the anti-money laundering systems was the enactment of Law No. 35 of 2002 regarding Anti-Money Laundering Operations, supplemented by several CBK instructions. The Law is understood to order financial institutions to register their sources of money and impose other organisational measures and penalties. Any transaction giving rise to a 'reasonable belief' that it is connected to money laundering must be reported. Banks and credit and financial institutions have to identify and report clients for all cash transactions exceeding 3,000 Kuwaiti dinars. It is also now a criminal offence for anyone to fail to tell the authorities if they know about a laundering operation.

v Consumer protection

The CBK and the CMA are the authorities that undertake customer and trader protection. Financial institutions also have complaint units that deal with customer grievances.

A recent innovation has been the creation of ombudsmen, who are independently appointed by the banks to oversee grievance procedures on their behalf. Ombudsmen are independent from the banks and are known for acting impartially, with the sole mandate of investigating customer complaints and rectifying errors that cause grievance.

Kuwaiti customers still tend to turn to the more traditional internal grievance procedures described above, as the concept of ombudsmen is still new in Kuwait. The CBK is encouraging banks, and in particular investment banks, to appoint them.

VI FUNDING

To support their lending, Kuwait's banks primarily source their funds from customer deposits and domestic and international wholesale markets.

A crucial aspect of bank funding activities is the requirement for banks to maintain adequate liquidity. Article 72 of the CBK Law provides that the board of directors of the CBK may whenever necessary draw up rules and regulations to which all banks shall adhere to ensure their liquidity and solvency.

The global financial crisis weakened lending and investment banking, pushing up provisions for loan defaults and causing a decline in the value of banks' investments in the Middle East.

Kuwait was forced to guarantee all deposits at local banks in 2008 after Gulf Bank reported its loss and Global Investment House, the country's biggest investment bank,

defaulted on US\$2.8 billion of debt.²² Gulf Bank, one of Kuwait's largest lenders, made a loss on derivatives trades, prompting the authorities to suspend trading on the bank's shares and the CBK to appoint a supervisor to oversee the lender's activities.²³ In response to this, Law No. 30/2008 Concerning Guarantee of Deposits at Local Banks in the State of Kuwait came into effect on 3 November 2008. The Law consists of three articles, the first of which stipulates that:

The State hereby guarantees the deposits in local banks in the State of Kuwait. The guarantee of the principal amounts of deposits will apply to all types of deposits, including balances of savings accounts and current accounts.

Kuwaiti regulators also increased the amount of risk management that is required by banks in the region, as well as transparency. Gulf Bank continues to comply with the loans-to-deposits ratio introduced by the CBK in 2004, which requires Kuwaiti banks to maintain an average ratio for loans to deposits of 85 per cent.

VII CONTROL OF BANKS AND TRANSFERS OF BANKING BUSINESS

i Control regime

Foreign acquisitions

Ministerial Resolution No. 205 of 2000 regulates the participation of non-Kuwaitis in Kuwaiti shareholdings companies. In accordance with the provisions of Article 3 of this Resolution, a non-Kuwaiti investor is permitted to own and to trade in bank shares. The approval of the CBK is required if an investor wishes to own more than 5 per cent of the capital of any bank. It is prohibited for non-Kuwaiti investors to exceed the ownership of 49 per cent in the capital of any individual bank, unless the prior approval of the Council of Ministers has been obtained and following consultation with the CBK.

Acquisition of shares in Kuwaiti banks

Articles 71 to 75 of the CMA Law regulate share acquisitions in banks. The most important provision is Article 72, which states that a person who wishes to submit an acquisition offer must submit to the CMA a copy of the offer documents accompanied by its basic details and information. The CMA thereafter has a maximum of 10 business days to review the statement and offer documents and to issue its approval.

The procedure is further elaborated upon in Article 74, which states that a person has 30 days from the date of acquiring directly or indirectly the ownership of more than 30 per cent of the traded securities of a listed joint-stock company to submit a purchase offer for all the traded shares according to the conditions and guidelines outlined by the Implementing Regulation. The Article also states that the CMA may

22 Bloomberg: 'Gulf Bank Sees 'Slight' Improvement with every Quarter'; 26 October 2011.

23 Central Banking.com: 27 October 2008.

make exemptions to this rule if this is in the public interest or in the best interest of the remaining shareholders.

Finally, Article 75 states that an issuer whose securities are subject to an acquisition must submit to the CMA a reply expressing his or her opinion and recommendation to the shareholder within seven days of receiving the offer.

VIII OUTLOOK AND CONCLUSIONS

Kuwait's banks have undertaken substantial restructuring and recapitalisation programmes over the past couple of years, and have emerged from the world financial crisis arguably battered, but certainly stronger.

However, the lack of economic diversification of its economy (growth of the non-oil sector is the second lowest in the GCC) and a fractured political environment are some of the challenges Kuwait has to face to truly start the process of reform, upgrade its economic 'brand' and reap the benefits of the region's economic developments.

Reform in banking is only one among many important factors that will contribute to the overall maturation of Kuwait's economy.

Appendix 1

ABOUT THE AUTHORS

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Haifa Khunji has more than 12 years of experience in transactional work and litigation. She trained and subsequently worked with leading international law firms in Dubai, Doha and Kuwait prior to joining KBH Kaanuun at its inception and now manages the Bahrain operation. She advises on a range of contentious and non-contentious matters with an emphasis on corporate finance and banking. Ms Khunji acts for major local and international banks as well as leading international and regional companies both in arbitration and court proceedings taking place in Bahrain and Kuwait. In non-contentious matters she advises on corporate structures, corporate finance and activities such as acquisitions, mergers, demergers, joint ventures as well as both conventional and Islamic banking and finance.

BASEM AL MUTHAFER

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Basem Al Muthafer was called to the Kuwait Bar in 1992 and has extensive litigation experience in the areas of corporate finance and banking, arbitration, bankruptcy and debt recovery. He advises on project finance transactions, tax structures, acquisitions, private equity transactions (including acting for various funds and target companies), joint ventures, partnerships and shareholders' arrangements and capital management structures, acting for investment and commercial banks in Kuwait.

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