

# FIDIC Middle East Contract Users' Conference

Dubai,  
24-27 February 2020

**Asel El Housan**

CEO, Head of Contracts and Commercial  
*AEH Consultancy*

**New regulations from the  
UAE Central Bank and  
Its Effect on the  
Construction Field**



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## IFRS 9 & 15 and Basel III effect on the Demand Guarantees and the Construction Field





## Definitions and Introduction

IFRS: International Finance Reporting Standards

A set of accounting standards developed by IASB (International accounting Standards Board).

The goal of the IFRS is to provide a global framework on how public companies prepare and disclose their financial statements





## IFRS 15 – Update in 2017

The objective of IFRS 15 is to establish the principals that an entity shall apply to report useful information to users of their financial statement which will include:

- Nature
- Amount
- Timing
- Uncertainties of revenue
- Cash flow

Which will arise from a Contract with a customer.





## IFRS 9 – Update in 2017

Take into account of Future Expected Credit Losses (ECL)  
Before 2017 Banks were obliged to take provisions of the losses and not the expected losses.

To Estimate ECL:

1. Probability of Default (PD)
2. Loss Given Default (LGD)
3. Exposure at Default (EAD)





## Basel 1988 – 2010

Basel is a set of international banking regulations put forth by the Basel Committee on Bank Supervision (BCBS) that sets out the minimum capital requirements of financial institutions with the goal of minimizing credit risk.

Basel had introduced new capital and liquidity standards to strengthen the regulation, supervision, and risk management of the world banking and finance sector.

**Introduce requirements on liquid asset holdings and funding stability**





## Basel III - 2010

Basel III aim is to strengthen bank capital requirement by increasing bank liquidity and decreasing bank leverage.

Two ratios were introduced

1. Liquidity Coverage Ratio (LCR): Ensure that sufficient level of high-quality liquid assets are available for one-month survival in a severe stress scenario (one-month cash outflow)
2. Net Stable Funding Ration (NSFR): Promotes resilience over long-term time horizon by creating more incentives for financial institutions to fund their activities with more stable sources of funding.



## Basel III - 2010

- **Tier 1 capital:** The most perfect form of bank's capital to keep it functioning through all the risky transactions. (liquidity, assets, etc) 8% to be reserved
- **Tier 2 capital:** the secondary component of the bank's capital, it is considered less secured. (loans, facilities) 2% to be reserved
- **Tier 3 capital** will be eliminated. It is the capital most banks hold to support their market risk, commodities risk, and foreign currencies risks. 0.16% to be reserved





## Consequences

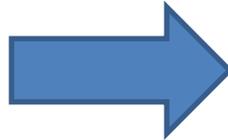
IFRS 9



Basel III



Open End Guarantees



Increasing Bank Provisions



Increasing The Margin and the Security

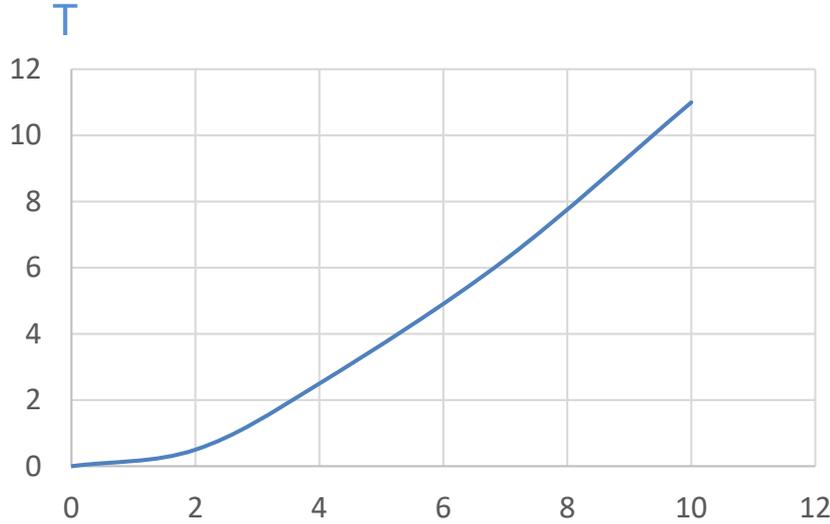


Increasing The Guarantee Price



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T Time

PD Probability of Default

PD

The Longest term of the Demand Guarantee = The higher the provision the bank should take

Unlimited Warrantee = Maximum Provision = More security from the customer + Higher price

1 Year Guarantee

1%

Open Ended Guarantee

2.5-5%





## New Regulations

UAE Bank had approached the UAE Central Bank with three requirements to be regulated

- Open Ended Guarantees.
- Conditional Guarantee.
- Guaranteed shouldn't be on first demand.

A decree from the UAE Central Bank is expected with a unified Guarantee template to be used across the market.

The Guarantee format is expected to have an expiry date.



## New Regulations

- Qatar Central Bank in October 2019 had issued a circular obliging the banks to follow a specific standard format (under URDG 758) which mandate an expiry date.
- All the new Demand Guarantees should follow the standard format.
- The renewal of the existing Demand Guarantees should follow the standard format if the Guarantee conditions allows that and such amendment will not impose any legal or financial obligations on the bank.





## Demand Guarantee

- It is a substitute of a cash deposit.
- The beneficiary is entitled to demand payment without asserting or providing evidence that the applicant is in breach. The fact that beneficiary has presented a demand payment, it implies that a breach has actually occurred and the claimed amount corresponds to the loss suffered.



## Demand Guarantee

- If no breach occurred, the applicant can claim repayment from the beneficiary without the guarantor being compelled to take part in it because the guarantor is not a party to the relationship between the beneficiary and the applicant.
- The Demand Guarantee is independent of the underlying relationship between the beneficiary and the applicant or any contract between them.
- The Demand Guarantee is subject only to its terms.





## URDG 758

### Independent bank guarantees

- At the outset it should be noted that guarantees are independent from the underlying relationship and the guarantee application. A guarantor will not go beyond the documents to check if the information contained therein is correct.
- A reference in the guarantee to the underlying relationship for the purpose of identifying it does not change the independent nature of the guarantee.



## URDG 758

### Independent bank guarantees

- When a demand is made to the guarantor, the guarantor is obligated to pay regardless of the underlying relationship. The obligation is based solely on the guarantee and the demand.
- The undertaking of the guarantor to pay under the guarantee is not subject to claims or defenses arising from any relationship other than the relationship between the guarantor and the beneficiary as described in the form of the guarantee.





## New Regulations

- Construction Think Tank.
- White Paper is under preparation.
- It contained 23 recommendation
  - Responsibilities of the parties and stakeholders.
  - Collaboration.
  - Standard conditions and amendments.
  - Legislation
  - Technology
  - Welfare
  - Disputes





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**Thank You**

**Asel El Housan**

B.Sc., MBA, Dipl PM, AClarb,

FIDIC Accredited Trainer

FIDIC Affiliate member

[Asel.Housan@aeiconsultancy.com](mailto:Asel.Housan@aeiconsultancy.com)

**AEH Consultancy**

+971 50 446 8548

