The new UAE Commercial Companies Law 2015 (the CCL) has now been in force for some 9 months. We thought it an appropriate time to review the key changes under the new law and to summarise our experience to date of its implementation in practice.

What does it do?

Status?

- Regulates certain anti-competitive practices and merger activity
- But various matters crucial to its practical application remain outstanding

In force since February 2013

Implementing Regulations October 2014

More regulations awaited

The Competition Law

According to press reports, the draft includes:

- flexible new strategies to bail out businesses in financial distress
- provisions to decriminalise bounced cheques

Draft approved by Council of Ministers

With Federal National Council for approval

The Insolvency Law

Seeks to:

- modernise the UAE’s arbitration legislation
- ensure the UAE is fully compliant with its obligations under the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards

Latest draft released by Ministry of Economy in 2013

The Arbitration Law

Minister of Economy has announced drafting is at advanced stage

May allow greater foreign-ownership in certain sectors of the economy

Unclear which sectors may be opened up

The Foreign Investment Law

Since the CCL came into force, we have been busy advising our clients on its implications for their businesses and corporate structures. We are assisting many LLCs with updating their memoranda of association to reflect the new law and we expect this to continue as the deadline for compliance approaches on 30 June. We are analysing several single-member company structures. We have also registered a pledge over shares in a LLC, under one of the most notable new provisions of the CCL.

At this early stage, however, various aspects of the CCL remain to be fully understood. Article 104 is a prime example. This Article carries over to LLCs the provisions relating to public joint stock companies. How this is intended to work in practical terms is unclear and is generating much market debate, as clearly not every provision which applies to a PJSC is relevant or appropriate for a LLC.

In the sections below, we discuss the key points arising under the new law and how we are dealing with them in practice. We also give our views on some of the more controversial issues.

Looking ahead to future developments, although the sharp drop in oil price has resulted in a deceleration of growth and domestic demand in 2016, the UAE continues to diversify in terms of investment beyond oil. Dubai in particular looks forward to Expo2020 and the opening up of the Iranian market presents new opportunities. From a legal perspective, the CCL is just one part of a suite of new laws at the federal level seeking to modernise the UAE’s business environment (see Table 1). The introduction of VAT across the GCC and a UAE federal corporate tax are also anticipated in the near term. There is every reason to retain a positive outlook in terms of growth and development for the UAE going forward.

We hope that you find this special edition a useful and informative read. If you have any feedback or comments please do not hesitate to contact us.

Niall O’Toole
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The CCL came into force 1 July 2015, repealing in its entirety the former UAE Commercial Companies Law (No. 8 of 1984) (the Old CCL).

- Broadly similar to the Old CCL in terms of structure and company types
- No change to the foreign ownership restrictions
- Introduction of single member companies, holding companies and common investment funds
- Amended provisions on general meetings for LLCs
- Introduction of new statutory process for pledges of LLC shares
- Increased emphasis on corporate governance
- Mandatory adoption of international accounting standards by UAE companies
- Provisions aimed to encourage IPOs and to facilitate the listing process
- Relies heavily on future secondary regulation in several areas

**Single member companies**

We are advising several clients on establishing and converting existing LLCs into single member companies and have recently successfully completed such a conversion. The authorities across the UAE are working to put in place the requisite systems and processes and are demonstrating an encouraging willingness to work with businesses and their advisers to facilitate this. The naming convention for single member companies is still rather awkward and we await to see how this will evolve.

*Niall O’Toole, Partner*

The CCL has introduced modernising changes in certain areas of corporate structuring, while preserving the status quo in others.

**Foreign ownership**

The structuring of investments and corporate transactions in the UAE is strongly influenced, in particular, by the restrictions on foreign ownership under which at least 51% of the capital of a company established onshore in the UAE must be owned by a UAE national.

These restrictions have remained unchanged under the CCL. The UAE Minister of Economy has made clear that foreign ownership will instead be covered in a new Foreign Investment Law.

**New company types**

The CCL contains the following potentially helpful new concepts:

- **Single member companies**: single member companies are now permitted, subject to the UAE’s foreign ownership restrictions. This will facilitate investments and acquisitions by UAE (and potentially GCC) nationals, who will now be able to incorporate wholly-owned companies. It is hoped this change will encourage sole establishments to incorporate in order to benefit from limited liability and separate legal personality from their owners. This change could also potentially be useful in the restructuring of a large group, e.g. to facilitate the separation of different business lines into a series of wholly-owned subsidiaries beneath a single holding company parent. However, the full range of set-up options for single member companies is still to be fully understood, whilst working within the foreign ownership restrictions.

- **Holding companies**: a limited liability company (LLC) or a joint stock company (JSC) may now be established with the sole object of holding “subsidiaries” incorporated in the UAE or overseas. A holding company may undertake ancillary activities to that primary object, including management of its subsidiaries, but will not be entitled to trade or undertake any other activities. The holding company concept adds greater transaction structuring flexibility as compared to the Old CCL, under which acquisition vehicles in the UAE had to find an appropriate licence category (and there was not a category for a pure “holding company”). However the practical requirements, such as the need for, and space requirements of, commercial premises of a holding company, are yet to be clarified.

- **Common investment funds**: the CCL introduced the concept of common investment funds with separate legal personality. However further regulation from the Securities and Commodities Authority (SCA) is awaited for the detail.
Muhassa companies

As well as adding new concepts, the CCL has also removed certain company types. Most notably, one type of entity which was referred to in the Old CCL which no longer appears in the CCL is the muhassa (otherwise known as a joint participation or an “Article 56 joint venture”).

The muhassa no longer exists as a type of entity which may be established in the UAE under the CCL. This is, presumably, because the entity did not in reality exist outside of a private arrangement between the partners. It is still possible to enter into a joint venture or partnering arrangement on a contractual basis, but such an arrangement is not subject to the CCL.

Under Article 9, any type of company which is not expressly provided for in the CCL is null and void and persons concluding contracts in its name will be individually and jointly liable for its obligations. In other words, any one of the partners in a muhassa company may be held liable to third parties under the new CCL for the liabilities arising out of that arrangement (rather than the company itself). The partner which received the claim would then need to pursue the other partners under the terms of the joint venture agreement.

Impact on LLCs

Certain important modernising changes have been introduced for LLCs in particular, for example:

- **Share pledges**: under the Old CCL, there was considerable debate as to whether a shareholder in a LLC was able to pledge its shares. This debate focused on both the legal technicalities as to whether a pledge of LLC shares was possible, and the practicalities of registering and enforcing the security. The CCL now expressly permits shareholders to pledge their LLC shares. However, several issues remain outstanding, in particular with regard to enforcement.

- **Management**: under the Old CCL, a LLC was allowed a maximum of 5 directors (also called “managers”). This cap has been removed, allowing for the creation of more flexible board structures.

- **General meetings**: provisions have been included to allow for meetings to be held on short notice and for notices to be given by electronic means.

**Muhassa companies**

It is not uncommon in the UAE, particularly under long term partnering agreements for example in the construction industry, for the arrangements between the partners to be by way of a muhassa. Any such arrangements should be looked at closely to see whether they should be restructured under a different corporate form, going forward. The provisions in the CCL in relation to liability of partners of null and void forms of company may be disadvantageous to overseas contractors. They may be more likely to receive third party claims on an individual basis in relation to any liabilities of a previous muhassa company in which they were a partner, if they have accessible assets overseas, or reputational concerns.

Mark Blanksby, Partner

**LLC share pledges**

We recently concluded the registration of a pledge over the shares in an onshore LLC, which was granted in favour of a UAE financial institution. The process was very similar to that required for a pledge over shares in a JAFZA or DMCC freezone company. The document needed to be executed in front of a notary and then registered with the authority. On registration, the DED issued a formal notice confirming that details of the pledge were recorded on the commercial register of the company in question. Unlike a commercial mortgage there was no need to advertise the security before it was registered.

Adrian Low, Partner

**Changes to LLC Memoranda of Association**

We are assisting many of our clients with updating their LLC memoranda of association to reflect the provisions of the new CCL. These amendments fall into 2 categories: changes which are mandatory under the new CCL and amendments which are desirable to make the operation of an LLC more efficient.

For example, the basis on which the quorum and voting at general meetings is calculated has been amended under the CCL. The relevant provisions in a memorandum may need to be changed to ensure they continue to provide the same level of voting control for the shareholders, in particular those holding a minority of shares.

Optional changes include provisions allowing for notices to be given by way of electronic communication.

Jonathan Silver, Partner
Directors’ duties

Directors’ duties and liabilities are integral to any corporate governance regime by upholding minimum standards and providing rights of redress for management failures. The CCL has introduced some significant changes in this area, for example:

- **A positive statement of duties:** any person authorised to manage the company must protect its rights and exercise the diligence of a prudent person and must act in accordance with the objects of the company and the powers granted to him.

- **Provisions specifically in relation to LLCs:** addressing conflicts of interest and the liability of LLC directors.

- **A restriction on companies exempting officers (current and former) from liability:** any provision of the company’s memorandum of association authorising such an exemption of liability is void.

- **Loans to directors:** the Old CCL prohibited JSCs from making or guaranteeing loans to their directors, but the CCL has widened this prohibition significantly. It now extends to a director’s family members (spouse, children and any other relative to the second degree) and there is a new prohibition on loans to companies in which the director and/or such family members hold over 20% of the share capital. The Old CCL also included an express exemption for banks and credit companies which does not appear in the CCL; however, this exemption has been reapplied by virtue of a Central Bank circular. Breach of the prohibition is a criminal offence.

Corporate governance rules for joint stock companies

Article 6 of the CCL provides for the Minister of Economy to issue corporate governance regulations for private JSCs (PJSCs) (other than banks and finance companies) where the number of shareholders exceeds 75. For public JSCs (PJSCs), the Securities and Commodities Authority (SCA) continues to be responsible for such regulations.

The SCA has not as yet issued any new regulations for PJSCs pursuant to the CCL. The most recent SCA regulation in this regard - requiring PJSC boards to nominate at least one female for appointment to the board (Ministerial Resolution No. 225 of 2015) - referenced the Old CCL.

In relation to governance of PJSCs, Ministerial Resolution No. 228 of 2015 came into force on 1 May 2015. Companies have 12 months within which to comply. The Resolution includes provisions requiring at least one independent director, the appointment of directors by cumulative secret ballot, the chairman to be a non-executive, the appointment of nomination and remuneration and audit committees and the implementation of internal systems and controls to manage risk. Although the Resolution does not expressly state that it only extends to PJSCs with more than 75 shareholders, given that its legislative authority stems from Article 6, this is presumably the case.

Unfair prejudice

Shareholder(s) of a JSC holding at least 5% of the share capital may lodge a complaint with the SCA that the affairs of the company are being conducted in a manner which is prejudicial to the interests of all or any of the shareholders, or that the company intends to do, or omit to do, an act which may cause loss to a shareholder.

The cause of such an action could include, for example, proposals voted into force by a majority shareholder against the interests of the minority. The SCA will consider any such complaint and take court action on
the shareholders’ behalf if it believes that it is well founded. If the SCA takes no action, the shareholder may nevertheless initiate court proceedings on its own behalf.

**Related Party Transactions**

A JSC is now restricted from entering into transactions with its related parties. Where the value of the transaction is equal to or less than 5% of the company’s share capital, board approval is required; where this is exceeded, shareholder consent is required. In addition, the value of such transactions must be independently assessed by an SCA - approved assessor. The term “related parties” is defined widely as the chairman, the directors and senior executive management (and any companies in which such persons hold at least 30% of the share capital, and the subsidiaries, associated companies and sister companies of those companies). In a Circular to PJSCs in February, the SCA widened the definition even further to include significant shareholders and those with effective control over the company.

**Powers of the Board**

The Old CCL provided that the board of directors of a JSC could not enter into loans for a term of more than 3 years, sell the company’s real property or business premises or create mortgages over such property write-off debt due to the company or submit the company to arbitration unless the power to do so was set out in the articles of association or such matter constituted one of the objects of the company; otherwise, specific shareholder approval was required. The new CCL maintains this restriction but also extends it to cover mortgages/pledges of movable property.

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**Financial assistance**

One of the most talked about provisions of the new CCL is Article 222, which prohibits a JSC or any of its subsidiaries from providing financial assistance to any shareholder to enable the shareholder to hold any shares, bonds or sukuk issued by the company. Financial assistance includes providing loans, gifts or donations, security and guarantees.

A prohibition on financial assistance is designed to protect creditors and shareholders from a depletion in, or misuse of, the company’s assets and may therefore be viewed as a tool to support good corporate governance.

Unlike other jurisdictions, there are no specific exemptions to the CCL prohibition and there is no process which can be followed to permit (“whitewash”) the assistance.

The extra-territorial reach of Article 222 is unclear. We think it is unlikely to extend to a UAE company providing financial assistance in respect of the acquisition of a foreign parent company. It is not clear, however, whether a UAE company which permits a foreign subsidiary to provide such assistance would be caught.

There is market discussion as to whether the prohibition extends to acquisitions of interests in LLCs in light of Article 104 of the CCL (see commentary).

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**Article 104**

Article 104 of the CCL seeks to apply all of the provisions relating to PJSCs to LLCs unless the law provides otherwise, with references to the SCA to be replaced by references to the DED for this purpose.

It is not clear how this will be applied in practice given there is a significant difference in the nature of LLCs and JSCs respectively. The Ministry of Economy has not as yet issued any guidance in this regard. Article 104 therefore continues to cause debate in the legal community. The provisions on related party transactions, financial assistance and director loans, for example, could have significant implications for corporate transactions in the UAE if they extend to LLCs.

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**Financial assistance**

We consider that Article 222 by its own terms covers “upstream” financial assistance provided by a LLC subsidiary in respect of a JSC parent company. However, we do not agree that the prohibition necessarily extends to financial assistance in respect of acquisitions of interests in LLCs by virtue of Article 104. The Arabic term for “shares” used in Article 222 does not cover LLC “interests”. The general public policy reasons behind Article 104 are not certain, but this seems to be a stretch in the application. There are also strong public policy arguments against such an extension: creditors of LLCs are already protected by other provisions of the CCL and such an extension has the potential to hinder the local UAE M&A market to a significant extent in light of the likely territorial reach of the provision.

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Although the Old CCL required the production of audited accounts by a LLC, in practice the authorities have not required or registered the filing of such accounts, and no particular accounting standard was imposed. While accountants in the UAE have broadly followed international accounting standards (IAS), other less stringent standards have also been adopted.

The CCL has taken some initial steps towards alleviating these problems:

**New Companies’ Registrar:** a Companies’ Registrar is to be formed, initially to supervise the Trade Names Register. More detailed regulations are to be published in due course setting out its additional activities and duties (see commentary). It is envisaged that companies will be able to file documents electronically with the Registrar. Concerned parties may request copies of particulars as set out in the records kept by the Registrar; and

**Company Accounts:** UAE companies are now required to prepare their accounts in accordance with IAS. The CCL also includes specific financial record keeping obligations and a requirement to keep such records at the company’s head office for at least 5 years.

In terms of publicity, JSCs are now required to publish their annual accounts in two daily local newspapers and to provide copies of such accounts to the authorities. However, it is unclear whether, and if so the extent to which, equivalent publication and filing requirements will be applied in respect of LLCs by virtue of Article 104. There is no longer any separate requirement for the audited accounts of a LLC to be filed with the local DED, as was the case under the Old CCL. Of course, if and when VAT and corporate income tax are introduced in the UAE, the authorities may apply a more rigorous approach to the preparation and filing of LLC company accounts than is currently the case.

It is also unclear at this stage the extent to which the existence of a LLC share pledge will be made public. As noted above, in our experience there is no need to advertise the pledge - although it seems to be possible for the pledge to be noted on the commercial register if requested by the LLC in question.

**Due diligence & accounts**

To date, those seeking to conduct due diligence in relation to a UAE LLC have had to rely heavily on cooperation from the target company and its management, as publicly accessible information is very restricted. This problem is often exacerbated by a lack of reliable company accounts.

We await the detailed regulations before we can fully assess the impact of the new Companies Registrar. It is to be hoped that, at a minimum, key corporate documents such as a company’s memorandum of association and commercial licence will be registered. However, the term “concerned parties” is not defined. It is therefore unclear who will be able to access the relevant documents once filed; for example, does the term include third parties who can prove a relevant interest, such as a prospective buyer or creditor of the company?

As regards accounts, while the formal adoption of IAS and the introduction of financial record keeping obligations are each helpful developments, independent audit regulation and public access to such accounts when produced are important next steps to achieving reliability and transparency in respect of UAE company accounts.

**Phil O’Riordan, Partner**
There have been some important changes to the way in which auditors are appointed, removed and their duties in relation to UAE companies. As was the case under the Old CCL, there is no difference in the role of an auditor for a JSC and of a LLC (other than the auditor specifications).

- **Specifications**: auditors of JSCs must meet certain criteria specified in more detail by SCA regulation (see Board of Directors' Decision No. 25 of 2015 concerning the registration of auditors of public shareholding companies and mutual funds). In particular, such auditors must have at least 5 years’ experience of auditing JSCs.

- **Appointment and renewal**: as under the Old CCL, the general assembly may appoint one or more auditors annually; however there is a new maximum term of three successive years of appointment.

- **Removal and resignation**: There are new provisions relating to the removal and resignation of auditors. The general assembly may dismiss the auditor by ordinary resolution and the relevant authority must be informed of the reasons for such dismissal. The auditor may resign by written notice to the company and the relevant authority, citing the reasons for such resignation. A general assembly of the company must be convened within ten days of such resignation to consider the reasons and to appoint another auditor.

- **Fees**: the auditor’s fees must be specifically reflected in the company accounts.

- **Auditor’s Report**: there are some additional content requirements for auditor’s reports, such as the inclusion of statements as to whether the company has purchased any shares or stocks during the fiscal year and regarding transactions involving conflicts of interest and/or related parties.

- **Joint Reports**: as under the Old CCL, where there is more than one auditor, each must prepare a separate report and each auditor shall be “liable for his own fault”. However, there is a new requirement that such auditors shall, in addition, prepare a “common report” for which they shall be “jointly liable”. Joint auditors preparing a common report would therefore be well advised to put in place contractual contribution arrangements as between themselves in respect of such potential joint liability.

- **Trading and consultancy**: there is a new prohibition on auditors trading in company securities or “providing any consultancies to any person in connection with such securities”. (Note that Article 20 of Federal Law No. 12 of 2014 concerning regulation of the audit profession which came into force in March 2015 already prohibits such behaviour.)

- **Whistle-blowing**: there is a new requirement imposed upon auditors to notify the relevant authority of any violations of the law or of any criminal behaviour of which he becomes aware during performance of his duties within ten days’ of detection. Any auditor who contravenes this provision may be suspended, struck off or referred for prosecution.
Capital markets

The CCL has introduced a raft of changes to facilitate capital markets transactions. Further SCA regulation will flesh out the detail of the CCL provisions. Some of the key changes in this area include:

- Reduction in the mandatory minimum free float for listed PJSCs: the CCL requires between 30% and 70% of the shares to be publicly offered, compared with 55% to 80% under the Old CCL.
- Secondary offers (offers for sale) now permitted: Article 279 of the CCL now permits shareholders of a company converting into a PJSC to sell a maximum of 30% of the company’s capital in the IPO.
- Provisions permitting and facilitating book-building, underwriting and trading in nil-paid rights on a rights issue (the SCA has recently published draft regulations in relation to IPOs for public consultation).
- Issuances to strategic investors: shares may be issued to “strategic investors” outside of the pre-emption regime.

Provisions encouraging IPOs

The fact that the founders can now retain up to 70% - and therefore control - of their companies may encourage more local businesses to consider an IPO. The sell-down provision is also helpful, in that it provides a partial exit route for the founders at the time of listing. The 30% cap, together with the retention of the 2-year lock-up period, are understandable protections in a UAE context: in a market with a large, less sophisticated retail investor base, it is not unreasonable to require the founders to stand behind their company for a period of time post-listing.

Prarthna Chaddha, Partner