

Revamp of the UAE Federal Companies Law: 100% Foreign Ownership and Enhancements to Ease of Doing Business

December 7, 2020

In what represents a major legislative move, the UAE has taken another step towards attracting foreign direct investments and enhancing the ease of doing business. Decree Law No. 26 of 2020 (Decree-Law), which was adopted at the end of September but only published at the end of November 2020, amends 51 articles of the Commercial Companies Law of 2015 (CCL) and introduces three new articles. The key changes are summarized in the table starting on page 3.

The amendments include the abolition of the rule requiring 51% of the capital of companies established “onshore” in the UAE (i.e., outside of the UAE’s free zones) to be held by UAE nationals. The new amendments also cover other important aspects relating to the management, financing and control of UAE companies, which are aimed at increasing flexibility and improving corporate governance. This is the most substantial change to the UAE companies law regime since 2015.

The Decree-Law will enter into force starting January 2, 2021 except for the provisions abolishing minimum Emirati ownership levels, the nationality requirements for directors of public and private joint stock companies, and the removal of the local service agent requirement for branches and representative offices of foreign companies. These will become effective six months following publication in the Official Gazette.¹ We also note that several of the new amendments provide for additional regulations and rules to be adopted. As such, while companies and investors are encouraged to start scoping out how to capitalize on the recent changes, it might be wise to wait until the full picture comes into view before moving into implementation mode.

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¹ While the Decree-Law was included in the Official Gazette released on November 30, 2020, the issue was dated as of September 30, 2020.
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Impact on Free Zones: Attraction is likely to remain

While at first glance the ability to own 100% of “onshore” UAE companies calls into question the relevance of the dozens of free zones in the UAE, including the Dubai International Financial Centre and the Abu Dhabi Global Market, the Decree-Law will not necessarily diminish the appeal of financial and other free zones. 100% foreign ownership was one of the main attractions of these free zones, but was counteracted by the relatively high real estate costs and difficulty conducting business outside the free zones. However, international financial services firms, asset managers, investment firms, holding companies and professional services providers may still seek to invest in financial free zones because of their familiar legal and regulatory regimes, and because they are now the location of ecosystems of similarly situated firms and provide a 50-year no tax commitment. The Decree-Law also removes the requirement for local service agents, which will make it easier for free zone companies to conduct business “onshore”.

Historical Context: Prevalence of mitigation structures and gradual erosion of foreign ownership restrictions

Foreign investors wishing to beneficially own more than 49% of “onshore” UAE companies have traditionally relied on a number of structures, including trust-based structures and sponsorship arrangements, in order to get around the now-abolished rules on Emirati ownership. Such trust, sponsorship and other arrangements will not be automatically unwound following the entry into force of the Decree-Law, unless the sponsor agrees or the arrangements contain stipulations to this effect.

In an effort to boost foreign direct investments, the UAE issued the Foreign Direct Investment Law in September 2018 (**FDI Law**) which opened the way to 100% foreign ownership in certain sectors. The “positive list” of sectors was set out by the UAE Council of Ministers in a decision adopted in March 2020. The FDI Law was a significant step towards the

liberalization of the UAE foreign ownership regime, but required companies wishing to benefit from it to complete certain procedural steps and abide by certain rules not applicable to CCL companies generally. The new Decree-Law, which was announced only a few weeks after the issuance of the first FDI Law licenses in major emirates, repeals the FDI Law and introduces a paradigm shift in the UAE national policy towards investment – 100% foreign ownership is from now on the rule rather than the exception. Some “strategic impact” activities, yet to be defined, may remain subject to restrictions on foreign ownership.

Impact on In-bound Mergers and Acquisitions and International Listings: Amendments remove impediments to deal-making

In the past, the 49% foreign ownership has complicated in-bound merger and acquisition transactions. While the sponsorship and trust arrangements referred to above allowed foreign companies to have full or majority beneficial ownership and control of CCL companies, many international investors—in particular, those managing third party funds, such as private equity firms—were uncomfortable with the separation of the beneficial and legal ownership and the uncertainty that prevailed around the enforceability of the sponsorship and trust arrangements. This impediment is now removed.

In addition, sponsorship and trust arrangements were irritants in international listings of “onshore” UAE businesses with non-UAE holding companies. Such listings required extensive risk factor disclosure about the sponsorship and trust arrangements used to hold their onshore UAE businesses and invited the scrutiny of regulators, underwriters and auditors. While such listings were ultimately able to proceed, the new CCL amendments will be a welcome simplification of the listing and disclosure process.

The table below summarizes the key changes enacted by the Decree-Law.

Key Changes	Description
100% foreign ownership	<p><i>Businesses in the UAE are now open to full foreign ownership, except “strategic impact” activities</i></p> <ul style="list-style-type: none"> — The long-standing requirement for a UAE “onshore” company to have one or more UAE shareholders holding a 51% minimum participation in the capital of the company has been removed. The general rule, henceforth, is that all businesses (except those involved in “strategic impact” activities) are open for full direct foreign ownership. — Activities with “strategic impact” will be determined by the Council of Ministers, upon recommendation of a special committee that will include representatives of the Department of Economic Development (DED) in each emirate. It is unclear whether the list will continue to cover all activities appearing under the “negative list” of the FDI Law, which the latest Decree-Law repeals.² While it is reasonable to expect that sectors such as oil and gas exploration and production, military and defense, air transport and telecommunications services would continue to be “restricted”, it is unclear whether the same will apply to activities such as banking and finance, insurance and commercial agencies. — Companies engaged in “strategic impact” activities may be subject to minimum UAE shareholding and board participation requirements, which will be determined by the DED of each emirate. Different restrictions may thus apply to companies operating in the same sector, depending on the emirate in which they choose to establish their business.
Directors	<p><i>Requirements relating to board composition have been relaxed</i></p> <ul style="list-style-type: none"> — The new amendments remove the requirement that the majority of the directors of a public or private joint stock company, including the Chair, be UAE nationals. This may not extend to companies involved in “strategic impact” activities, which must observe any specific requirements set out by the Council of Ministers or the DED of each emirate. — Prior to the new amendments, only one third of the board of directors of a joint stock company could be composed of directors having expertise who are not shareholders. This upper limit is now removed.
No local agent requirement	<p><i>A local service agent is no longer needed to establish a branch or representative office of a foreign company in the UAE</i></p> <ul style="list-style-type: none"> — Foreign companies desiring to establish a branch or representative office “onshore” in the UAE were previously required to appoint a local service agent, whose mission consisted primarily of dealing with the UAE governmental and administrative authorities on behalf of the company, and assisting with the license renewal process. This is no longer a requirement under the recent amendments.
Additional flexibility for certain types of companies	<p><i>Further flexibility for various other companies</i></p> <ul style="list-style-type: none"> — The Decree-Law creates the possibility for entities other than public joint stock companies to carry out banking and insurance activities if the specific legislation regulating those sectors allow it. This amendment is to be read in conjunction with another recent change made to Law No. 14 of 2018 regarding the Central Bank and the Organization of Financial Institutions and Activities, which now allows financial institutions other than banks to take the form of a private joint stock company or a limited liability company (LLC). — The maximum number of shareholders in private joint stock companies was previously capped at 200. This is no longer the case.

² See our [April](#) and [November](#) alert memos which contain a description of the negative and positive lists under the now-abolished FDI regime.

Key Changes	Description
Corporate transactions	<p><i>Balancing flexibility and the protection of corporate interests</i></p> <ul style="list-style-type: none"> — New provisions have been introduced allowing emergency capital raises at the request of a partner for any LLC facing the risk of insolvency or default on its debt. Shareholders that do not participate in the emergency capital raise will be diluted. — The concept of pre-approved, authorized capital has been removed. All capital increases must be approved by a special shareholder resolution. Shareholder resolutions to increase capital can be valid for three years. Capital increases must be carried out in accordance with the rules and requirements adopted by the Emirates Securities and Commodities Authority (ESCA). — ESCA had issued a decision Concerning the Rules of Acquisition and Merger of Public Shareholding Companies (Decision No 18/RM of 2017) containing provisions for squeezing out minority shareholders in public tender offers, as well as provisions entitling minority shareholders to request that they be bought out. The Decree-Law grants a statutory basis for these procedures. Furthermore, it includes a provision permitting a company to issue new shares (without offering preferential subscription rights to shareholders) in support of an exchange offer. — The new amendments offer more flexibility for the admission of strategic partners into a joint stock company. The previous requirements under which a strategic partner must conduct an activity similar or complementary to the one conducted by the company, and that the strategic partner should have issued financial statements for at least two financial years, have been removed. The issuance of shares to a strategic partner must comply with any other conditions imposed by ESCA. — The Decree-Law offers a company more flexibility to acquire and dispose of its own shares (i.e., treasury shares), provided it observes any requirements set out by ESCA.
New rules for public offerings and bond and sukuk issuances	<p><i>Possibility to offer up to 70% of shares in an IPO upon conversion; 6-month lock-up on founders; new duty of care</i></p> <ul style="list-style-type: none"> — Where an existing company is converted into a public joint stock company, it can sell up to 70% of its shares in the related public offering, up from the current 30%. A converting company may also carry out a primary share offering via a capital increase. In addition, a lock-up now applies to shares held by founders in case of conversion, ending six months after listing of the public joint stock company. — In the case of the establishment of a new public joint stock company, the founders committee is liable for the accuracy, sufficiency and completeness of any document, studies or reports submitted to the relevant authorities. The founders committee and the board of directors (where there is one) co-sign the offering memorandum and are responsible for the accuracy of information contained therein. A duty of care applies to professional advisors and other persons involved in the offering process. They must conduct their work diligently and must each be responsible for its functions. <p><i>More flexibility for bond and sukuk issuances and vis-à-vis convertible bonds</i></p> <ul style="list-style-type: none"> — The requirements for the issuance of negotiable bonds and sukuks (whether or not convertible into shares) will be determined by ESCA only (the reference to the UAE Central Bank has been removed). The previous conditions requiring the capital to be fully paid up and the company to have issued financial statements for at least one fiscal year before it could issue debt or sukuk have been removed. — A new provision has been added authorizing a company to increase its capital by issuing bonds or sukuks and converting them into equity. Further, the new amendments allow companies more flexibility in defining the terms and conditions of their convertible bonds.

Key Changes	Description
Improved governance	<p><i>Further improvements to corporate governance</i></p> <ul style="list-style-type: none"> — All non-listed CCL companies will need to comply with requirements for corporate governance established by the Minister of Economy. Previously, the Minister of Economy had authority to adopt governance standards for private joint stock companies with more than 75 shareholders. — Additional disclosure requirements have been introduced in connection with related party transactions (which now follow the definition in the ESCA Corporate Governance Guide). — More specific rules have been introduced where the cumulative losses of a company reach 50% of its share capital. They include enhanced disclosure obligations of the board of directors towards the shareholders (auditor’s report and, depending on the circumstances, either a clear restructuring plan with a timeline, or a clear liquidation plan with proposed names of ESCA-approved liquidators). In the case of a restructuring, the board must oversee the implementation of the plan and must provide ESCA with regular updates. — The prohibition on financial assistance to any person desiring to acquire securities issued by the company or any of its affiliates has been expanded. The company cannot use its reserves, cash or profits to satisfy any obligation of any such person. An exception, however, has been added authorizing the provision of loans (subject to these not including preferential terms) to enable persons to acquire securities of entities licensed and regulated by the UAE Central Bank. The amendments clarify that undertakings and indemnities to underwriters are not deemed to be financial assistance.
Expanded bases for liability	<p><i>Liability of directors and management</i></p> <ul style="list-style-type: none"> — Directors continue to be liable for any act of fraud, abuse of power, or breach of the law or the company’s constitutional documents. The recent amendments extend this liability to all members of executive and senior management. — The base for shareholder lawsuits is expanded significantly to include claims against the company and its management, claims against the board of directors without being required to first notify the company, as well as claims exercised on behalf of the company by holders of 10% interest. Shareholders are entitled to reimbursement of their legal expenses, including attorneys’ fees. — With respect to LLCs, the memorandum of association must set out the mechanics for resolving disputes between the company and its management, or between partners of the company.
Auditor Rotation	<p><i>Auditor rotation</i></p> <ul style="list-style-type: none"> — New rules regarding the appointment and rotation of auditors have been introduced. Public joint stock companies must be audited by an audit firm, which cannot continue its mandate beyond six consecutive years (during which the partner in charge must be changed after 3 years). The firm can be reappointed only after two years have lapsed since the termination of its appointment.
New rules for shareholder meetings	<p><i>Shareholder meetings</i></p> <ul style="list-style-type: none"> — The general meeting must be called upon a request of shareholders or partners holding 10% of the capital of the company (down from 25% for LLCs and 20% for joint stock companies). The quorum for a general meeting of an LLC has been reduced to 50% on first call (down from 75%). New rules have been introduced with respect to notice requirements. The minimum notice period has been extended from 15 days to 21 days for both LLCs and joint stock companies, and a copy of such notice must be communicated to the DED in the relevant emirate (for LLCs) or to ESCA (for public joint stock companies). — One or more shareholders holding 5% of the share capital of a joint stock company can request items to be added to the agenda of a general meeting. The previous minimum threshold was 10%. — Several amendments provide for the use of modern technologies, allowing remote meeting and electronic voting and deliberations (subject to any specific requirements set out by the Minister of Economy or ESCA).

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