

SIGNIFICANT AMENDMENTS TO THE UAE COMMERCIAL COMPANIES LAW

Federal Law by Decree No. 26 of 2020 (the Amendment Law), introduces a number of significant changes to the UAE Commercial Companies Law (CCL). The changes not only affect the foreign ownership regime (which has been the subject of much recent press speculation) but will also have an impact on transactional issues for UAE corporates. This briefing provides an overview of the key changes that will be implemented under the Amendment Law.

Foreign ownership

As anticipated, the Amendment Law has repealed the Foreign Direct Investment Law along with the repeal and/or replacement of the key provisions dealing with foreign ownership under the CCL. These include:

- Article 10, which established the 51% UAE ownership requirement for onshore companies
- Article 151, which sets out prescriptive requirements for participation of UAE nationals on the boards of joint stock companies (JSCs)
- Article 329, which established the requirement for a UAE national service agent for branches of foreign companies.

A new Article 10 provides for the establishment of a Committee, to be formed by way of a Cabinet Resolution, that will include representatives from the Emirate's economic departments. The Committee will determine which activities will have "strategic impact" on the UAE economy and a list of such activities will then be issued by way of a Cabinet Resolution, along with the licensing requirements for entities that carry out such activities. It is anticipated that the strategic impact list will act as a negative list, whereby UAE national participation is required at some level, including activities (such as commercial agency, for example) where 100% UAE national ownership is likely to remain necessary.

Subject to any powers set out for the Committee pursuant to the Cabinet Resolution mentioned above, the competent authorities (i.e. local economic departments) will have the powers to:

- determine the percentage of UAE national shareholding levels/board participation for companies
- approve applications and fees for establishing companies

Whilst the removal of the foreign ownership restrictions is encouraging, it remains to be seen how this change will play out in practice, including whether

Key areas affected by the Amendment Law:

- Foreign ownership
- Procedural matters
- Capital markets
- Transaction considerations
- Minority shareholder protections
- Directors' duties
- Bankruptcy provisions

Foreign ownership

- Removal of the 51% UAE ownership rule for onshore companies and repeal of the FDI Law
- Removal of the requirement for a UAE national service agent for branches of foreign company
- Cabinet to form a Committee to determine "strategic impact" list of activities and licensing requirements for those entities
- Local Economic Departments to determine UAE shareholder and board participation of other business activities

C L I F F O R D C H A N C E

a consistent approach will be adopted across the Emirates. We will be following developments closely in this regard.

Procedural matters

The following matters may give rise to a requirement to update company constitutional documents (see the paragraph entitled "*Action required*" at page 6 of this briefing).

Shareholder Meetings – LLCs and JSCs

Both LLCs and JSCs are affected by changes to the requirements for calling and holding shareholder meetings. In particular, the notice period for calling a shareholders' meeting has been re-increased from 15 days to 21 days (as was the position under the repealed 1984 version of the CCL). Additional requirements include: i) an obligation on the company to file a copy of the invitation of the meeting with the competent authority (i.e. the DED, SCA or MoE); and ii) the need to appoint proxies (other than board members) by way of a power of attorney. It remains to be seen whether the local economic departments will enforce this requirement on LLCs, as historically other company filings have not been accepted despite provisions to this effect in the CCL.

The new provisions also provide for flexibility with regards to holding and attending meetings via "modern technological means", subject to the controls issued by the relevant authorities. As a Covid-19 response measure, the SCA issued a decision to the Public JSCs that it regulates to permit the holding of virtual shareholder meetings and to vote via virtual methods, so this is not a new practical consideration for such entities.

Quorum requirements - LLCs

The quorum requirement for LLC AGMs has been reduced from shareholders owning 75% of the company's share capital to 50%. This is subject to anything higher prescribed in the company's articles.

In the event that a quorum is not met in the first instance, and a second meeting is required, then the quorum is reset such that (subject to the company's articles), it is valid "*no matter the number of attendees*". This has changed from the previous threshold of shareholders owning 50% of the company's share capital and removes the need for a third meeting (in the event that the second meeting would have otherwise been deemed inquorate).

In addition, the time period for calling the second meeting has been changed from 14 days following the first meeting date to "*within at least five (5) days (or a maximum of fifteen (15) days) from the date of the first meeting*".

Auditor rotation requirements – LLCs and JSCs

In a positive move the three year auditor rotation requirement has been increased to six fiscal years (although the "*partner*" in charge of the audit must be replaced after three years). An auditor may be reappointed two fiscal years from the expiry date of its original term of appointment. On a strict interpretation of the CCL, in lieu of provisions to the contrary, the auditor rotation requirements apply to both JSCs and LLCs.

Dispute resolution mechanisms – LLCs

LLCs are now required to include dispute resolution provisions in their constitutional documents that deal with "*settling disputes that arise from the*

Procedural changes

A number of procedural changes have been included under the Amendment Law, including:

- Notice periods for calling AGMs have been extended from 15 to 21 days
- Quorum requirements altered for LLCs
- LLCs required to include dispute resolution mechanisms in constitutional documents to deal with potential disputes between shareholders and shareholders and directors
- Auditor rotation requirements have been increased from three to six years
- Companies will need to review their constitutional documents in light of these changes

affairs of the company, whether between the company and any of its managers or among the shareholders in the company".

Capital markets

A number of provisions affecting the ease with which Public JSCs can raise capital and issue debt are welcome additions to the Amendment Law.

IPOs

The CCL currently imposes liability on third party advisors in respect of the accuracy of the company's prospectus. Under the Amendment Law this liability now rests only with the founding committee and/or board of directors, as applicable. Third party advisors, nevertheless, retain their obligation to perform their work with due skill, care and diligence.

In addition, the maximum free float requirement of 70% may be increased with the permission of the SCA, whilst the lock-up period for founding shareholders has been reduced from two years to six months.

It remains to be seen what will happen under Article 10 and the knock-on effects it will have for Article 151 and UAE national participation on boards (see paragraph entitled "*Foreign ownership*" at page 1 above), but a potential relaxation on the current board composition requirements in favour of foreign nationals would, no doubt, be welcomed by international investors.

Strategic Investors

Positive changes to the strategic investor regime (which allows the Public JSC to issue shares to the investor(s) on a pre-emptive basis under certain criteria) have also been included in the Amendment Law. In particular, the removal of certain criteria for strategic investors to provide two years financial reporting history and to operate in a similar business activity to the Public JSC that it wishes to invest in. The removal of this criteria opens up the strategic investor regime to a greater pool of investors and, potentially, individual investors as opposed to just corporates.

Bonds and Sukuk

The Amendment Law provides that pre-emption rights will not apply in respect of convertible bonds and sukuk. The SCA had previously applied this approach in practice but this addition to the CCL provides helpful clarification. In addition, a right to a pro-rated dividend in the financial year of the conversion of a bond or sukuk to shares is permissible subject to anything to the contrary in the prospectus or issuance terms of the bond or sukuk. Again, this provides clarification that the bond issuer can set out terms for the payment of any dividend in the issuance terms and conditions.

The Amendment Law also removes the one year time limit that exists under the CCL for the board to act on a Special Resolution of the shareholders approving the issue of a bond or sukuk. This is a helpful provision, as the time limit had created a requirement to have an annual shareholder meeting addressing the point (for issuers with wholesale funding programmes regularly accessing the capital markets this was arguably overly administrative). However, for the avoidance of doubt, the Amendment Law does not circumvent circumstances where a specific shareholder resolution is required to issue regulatory capital instruments as per UAE Central Bank guidance.

Positive changes impacting capital markets

- Removal of third party advisor liability in respect of the prospectus
- Potential for the maximum free float requirement to be increased above 70% with the SCA's approval
- Reduction of the lock-up period from two years to six months
- Strategic investor criteria relaxed
- Clarity on pre-emption and dividend rights in respect of issuance of convertible bonds
- Removal of one year time period for the board to act on the shareholders' resolution to issue a bond

Transaction considerations

Certain helpful clarifications and other amendments have been included in the Amendment Law, which impact considerations for transaction structuring. A summary of the key changes is set out below.

Capacity – LLCs and Private JSCs

Investment management has been removed from the list of business activities restricted to Public JSCs, opening up the possibility for both LLCs and Private JSCs to carry out this activity. Banking and insurance business may still only be carried out by Public JSCs.

See also our comments below in respect of potential capacity issues for failure to update constitutional documents at the paragraph entitled "*Action required*", from page 6 of this briefing.

Related party transactions (RPTs) – LLCs and JSCs

Currently LLCs are not subject to the RPT prohibition under the CCL. The Amendment Law, however, provides for the issuance of a Cabinet Resolution, upon a proposal of the Minister of Economy, setting out provisions to be applied to LLCs dealing with related party transactions. Therefore, a specific RPT regime is anticipated for LLCs.

The existing RPT regime applicable to JSCs has been expanded. Additional disclosure requirements have been included. The disclosure requirements include:

- Prior to entering into an RPT, the related party must disclose to the board of directors the nature and terms of the transaction and all essential information concerning its shareholding in the relevant companies/related parties, including the extent of its interest in, or benefit from, the transaction.
- A notification requirement, when entering into an RPT, for the chairman of the board of directors of the relevant JSC to notify the relevant authority (i.e. the SCA for Public JSCs and the MoE for Private JSCs) with a statement containing information about the relevant party, details of the transaction, and the nature and extent of the relevant party's benefit from the transaction.

Such disclosure requirements align with the SCA's existing RPT rules under its Corporate Governance Regulations, so this addition to the CCL does not present a practical change for Public JSCs.

In addition to the expansion of the RPT requirements, the definition of "Related Party" has been removed from the CCL. This provides the relevant authorities (i.e. the SCA and MoE) with an opportunity to redefine existing definitions of "Related Party" under their governance rules, which previously have been based on the CCL's existing definition.

Financial assistance - JSCs

The key changes to the financial assistance prohibition include the addition of two exemptions. The first relates to underwriters who, pursuant to the underwriting agreement, agree to purchase any unsubscribed shares to support UAE entities undertaking an IPO. This is a helpful clarification and supports prior market thinking that this activity fell outside the intended scope of the financial assistance prohibition. The second exemption relates to a carve out for entities licensed by the Central Bank that provide loans to "any

Transaction considerations

- Investment management activities may now be carried out by LLCs and Private JSCs
- RPT regime expanded and new prohibition anticipated for LLCs
- New financial assistance prohibition exemptions to include banks lending in the ordinary course of business and underwriters supporting IPOs
- Clarification on prohibition of loans to directors for entities regulated by the Central bank

person to enable them to hold any securities issued by such companies", provided such loans are given in the ordinary course of business and do not contain any preferential conditions. This is a potentially helpful exemption when considering structuring options that include UAE entities carrying out banking and lending activities.

Loans to Directors – JSCs

The Amendment Law formalises the exemption for loans to directors by entities regulated by the Central Bank. Shortly after the enactment of the CCL in 2015, the Central Bank issued a notice to banks providing for this exemption but there was a question mark over the Central Bank's authority to issue an exemption to what was a blanket prohibition under the CCL. This change is therefore helpful and clarifies the position.

Minority shareholder protections

Although there has been little precedent for minority shareholder action in the UAE, the Amendment Law sets out a number of provisions that increase minority shareholder protections. These include a lowered threshold of 10% by which a shareholder can request the board to hold a general meeting (from the previous 20% threshold for joint stock companies and 25% for LLCs). A further boost to minority shareholder protections includes the ability of shareholders owning 5% or more of the company's share capital (as opposed to a previous threshold of 10%) to add items to the agenda of a General Assembly meeting.

Directors' duties and board composition

Alongside the potential board composition changes under Article 151 (see further detail at the paragraph entitled "*Foreign Ownership*" at page 1 and the paragraph entitled "*Capital Markets*" at page 3 of this briefing), the Amendment Law removes the requirement for two-thirds of directors of JSCs to be shareholders of the company.

The Amendment Law also expands directors duties' to the company's "*Executive Management*". Executive Management is defined broadly and includes: "*the general manager, CEO or the executive chairman of the company, their deputies, everyone in high executive positions, executive management officers and those appointed to their positions personally by the board of directors*". This is a crystallisation of the concept of a de facto director, which was previously considered to be implied under the CCL but not provided for expressly.

The concept of striking-off a director has also been introduced under the Amendment Law, whereby an individual may be prohibited from acting as a director for a minimum of three years where there has been a court judgment finding that director to be in breach of his/her duties. There were no strike-off provisions under the CCL prior to these changes, although the UAE bankruptcy regime does include this concept.

Bankruptcy provisions

LLCs in financial distress

A new provision for LLCs is introduced under the Amendment Law, whereby if a company is facing liquidation/inability to pay its debts, a shareholder may, based on a report of the company's financial manager or their delegate, apply to the courts "*for an urgent judgement to increase the capital as necessary to save the company or settle the debts*".

Other matters

- Increased minority shareholder protections
- Expansion of directors' duties to "Executive Management"
- New provisions dealing with LLC's facing financial distress
- Expansion of existing provisions dealing with JSCs that face losses amounting to half of the company's share capital

JSCs losses

When a Joint Stock Company's losses reach 50% of its share capital, the board has an obligation (amongst others) to call a General Assembly so that the shareholders may decide, by way of special resolution, whether to continue or wind-up the company.

The Amendment Law sets out further procedural steps that the directors must follow upon calling the General Assembly, including:

- Providing the board with up to 30 days from the date of invitation to convene the general meeting (this is longer than the new 21 day time limit for convening a general meeting).
- Requiring the board, where the recommendation is to continue the company, to include a restructuring plan and auditor's report with the invitation to convene the meeting. The restructuring plan attached to the invitation must include a feasibility study, plan of debt settlement and a schedule for completing the restructuring.
- Requiring the board, where the recommendation is to liquidate the company, to include an auditor's report, company liquidation plan and schedule (to be approved by the board of directors of the company and its financial consultant) and nominate one or more liquidators as approved by the Authority.

In the event of the restructuring recommendation being implemented the Board must keep the Authority (i.e. the SCA in respect of Public JSCs and MoE in respect of Private JSCs) updated on the progress of any restructuring plan on a rolling 3 month basis. The relevant Authority must also approve the appointment of (and has the right to remove) the financial consultant that will assist with the preparation and implementation of the restructuring plan.

When will these changes take effect?

The majority of provisions enacted by the Amendment Law will take effect on 2 January 2021.

However, Article 10 (on the foreign ownership restriction), Article 151 (on UAE National participation on JSC boards) and Article 329 (on UAE service agents for branches of foreign companies) will come into effect six months from the date of the Amendment Law's publication in the Official Gazette. Despite a late notification to the market of the publication of the Amendment Law, it was gazetted on 30 September 2020, meaning that these provisions will take effect from 30 March 2021.

Action required

In light of the changes under the Amendment Law, companies will need to review their constitutional documents and consider what changes will be required and/or preferred. In particular, the increase of the notice period for calling an AGM to 21 days will likely need to be updated in both LLC and JSC constitutional documents, whereas LLCs will also need to give consideration to the amended quorum requirements and required dispute resolution mechanisms (see paragraph entitled "*Procedural matters*" at page 2 of this briefing for further information on these issues).

Failure to act

Companies must "*adjust their status*" (i.e. update their constitutional documents) before 2 January 2022 or, unless such transitional period is

Key dates

- Majority of Amendment Law to take effect from 2 January 2021
- Articles 10, 151, 329 in relation to foreign ownership restrictions and UAE national board participation to take effect from 30 March 2021
- Companies constitutional documents to be updated before 2 January 2022, unless this transitional period is extended by Cabinet Resolution
- Companies that fail to update their constitutional documents will be "deemed dissolved"

extended by way of Cabinet Resolution, face being "*deemed dissolved*". Given the implications for capacity should a company fail to update its constitutional documents by this deadline, companies are encouraged to act promptly and begin the review and update process on a timely basis.

Conclusion

The Amendment Law brings with it a number of helpful clarifications. The changes in respect of provisions relating to capital markets could be particularly beneficial for investors. However, the changes of most significance in terms of attracting investment into the UAE relate to the provisions for relaxing the foreign ownership restrictions and it waits to be seen how these provisions will be implemented by the local authorities in practice.

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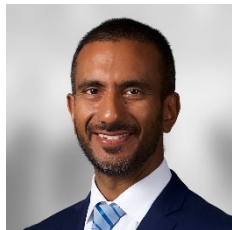
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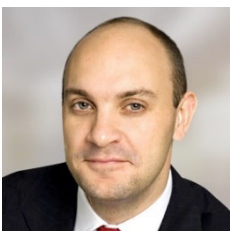
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