RISK MITIGATION PACKAGE:
FREQUENTLY ASKED QUESTIONS

Foreign shareholding into UAE mainland LLCs is limited to 49% versus 51% for the mandatory UAE shareholder*. Sharia law compliant tailor-made mechanisms can nonetheless mitigate – to the point of elimination – risks associated with having a local partner in the mainland structure and ensure that the foreign investor retains full control over management and profits. Below is a high-level overview of the key mechanisms that – in the firm's opinion – a comprehensive "mitigation package" should contain.

1. Can I allocate the 51% mandatory shareholding to two different local partners?

Yes. It is possible to divide the 51% mandatory local shareholding and engage more than one local partner to hold the shares of the local LLC. Each local partner will trigger separate sponsorship fees and require a separate documentation to mitigate the risks related to the mandatory local partnership.

2. Can I allocate the 51% mandatory shareholding to a GCC national other than a UAE national?

No. The local commercial code states that where 49% of the shares of an LLC are held by a foreigner, at least 51% of the total shareholding must be held by one or more UAE national(s).

3. My current local partner is not willing to execute the risk mitigation package; what can I do?

You may want to insist on the fact that the mitigation package secure; both the local and the foreign partners' positions. Local partners may question the added value of a global "mitigation package" and may favour the so-called "side agreement". Whilst the latter can still hold (some) value, it is the aggregate of all the mechanisms composing a mitigation package which:

i. addresses the risk related to local partner but also

ii. protects the local partner from the mandatory 51% holding of the shares into the company.

4. My local partner and I just signed the risk mitigation package. What's next?

Such documents require maintenance on an ongoing basis. It is particularly important that a track record is created as to the involvement of the local partner. E.g. we typically recommend that the local partner countersigns minutes of shareholders' meeting once a year. We similarly recommend for the local partner to execute on an annual basis an acknowledgment receipt for fees received along with a renunciation to any claims for the past year – notably dividends. On the other hand, obtaining a proxy from him and documenting all decisions *in absentia* is not best practice as it may be an indication of an artificial relationship which, in turn, may be challenged.

5. Can you tell me more about this mudharaba agreement my local partner and I will have to sign?

Via the implementation of the mudharaba agreement, the foreign partner finances the initial subscription in the LLC's capital by the local partner. The document will enable the foreign partner to claim the initial funding plus, above and beyond such initial funding, up to 99% of the value of the assets acquired through such funding. The duties created by the mudharaba agreement fall into Local Partner's probate procedure. In the event that Local Partner passes away, his heirs are bound by the mudharaba's terms and conditions.

6. How and when do I pay the local partner fee?

His/her remuneration, referred to as the "sponsorship fee", will often consist of a pre-agreed fixed fee paid on an annual basis. The local partner will in turn renounce to any claims above and beyond such fixed fee.

7. Can the mandatory 51% local shareholding be allocated to a corporate partner?

Yes. The mandatory 51% local shareholding can be allocated to a corporate partner subject for the latter to be owned 100% by UAE national(s).

8. What are the benefits of having the mandatory 51% shareholding held by a corporate local partner?

One key advantage is that the exit strategy is facilitated. When the local partner is a corporate entity, this entity will have full POA to transfer the shares away as and when requested without delay or penalty. An individual partner may be exempted to request a severance fee, triggering a potential delay on transferring the shares.

9. Is that all?

No. Although the corporate structure is owned ultimately by a UAE national, it is structured in a way in which it is managed by a management company, usually a western corporate service provider with multiple signatories, ensuring someone is always available as and when required by the foreign investor.

10. What else?

A corporate entity will have no 'emotional connection' (unlike an individual person). The relationship is less likely to break down over a disagreement. This is purely a business transaction between two companies.

11. What happens if my local partner, a UAE individual, passes away?

If you have an individual 51% shareholder and he/she passes away for a few months, restrictions will apply on what the business can do relating to trading, hiring of staff, moving money around in bank accounts.

12. Would I face the same difficulties with my corporate local partner

A corporate entity will smoothen the succession process. If the shareholder is a corporate entity and the UAE nationals behind that entity pass away then your business is less likely to be affected. It will be able to continue trading as usual. The term used in the market is "perpetual succession".

13. What type of licence should a corporate partner carry?

One should ensure that the corporate partner does not have a general trading type of license or any license that allows trading. It is good practice that this firm holds a license allowing "investment in commercial enterprise". The corporate partner should also have zero assets and no employees or bank account; this mitigates as much risk as possible for the 49% partner. Additionally, banks have small appetite for local LLCs which 51% shareholding is held by a general trading entity.

* Pursuant to Article 10 of the UAE Federal Law No.(2) of 2015 concerning Commercial Companies ("**New CCL**"):
"... any other company that is incorporated in the state shall have one partner or more of nationals whose share may not be less than 51% of the company capital."

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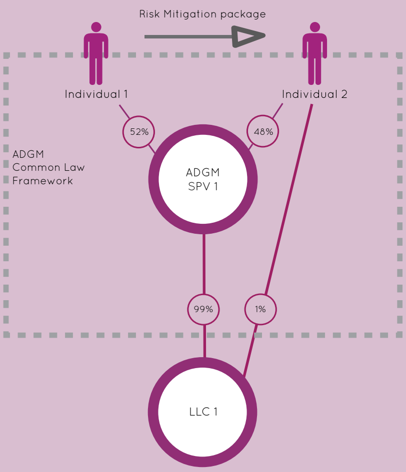
Case Study: Use of ADGM SPV for additional investor protection

Stakes in UAE mainland entities are often held through foreign registered SPVs. While traditional offshore centers like the BVI, Cayman Islands or Channel Islands have advantages – e.g. robust common law framework, substantial track record – they are not without downsides: e.g. delay in implementation of decisions (even if the SPV is effectively managed in the UAE), important costs related to legalization/super-legalisation of documents.



What's new?

By combining an LLC and an ADGM SPV, the shareholding is "lifted" from UAE mainland to ADGM – thus from a civil law to a common law framework.

The mandatory ultimate local ownership of 51% into the underlying LLC is maintained, in compliance with federal law.

What improves?

- split between operational vehicle and holding structure
- shareholders' relationship fenced within a common law framework
- increased investor protection
- access to a sophisticated regulatory regime and corporate tools
- less red tape: local notary public are not involved for transfer of shares (occurring at ADGM SPV level)
- faster implementation of decisions (single jurisdiction)
- important savings (no legalization/super-legalisation of documents unlike where a foreign holding co – e.g. BVI, Seychelles or Mauritius – is used)

Who we are

We are a multi-services platform catering to a broad spectrum of clients – from individual entrepreneurs and local SMEs to wealthy international families, to established blue-chip companies and multinationals. Our one-stop-shop offering is unique in the Middle East: a holistic and cross-disciplinary combination of a market-leading corporate services firm, a law firm's specialist expertise and a regulatory & compliance services practice, all through one single platform.

We have broad experience in implementing risk mitigation packages between foreign entrepreneurs and local partners, and are regularly instructed to draft such documentation or review and suggest improvements to the existing sets of documents.

Headquartered in the UAE, we are an entrepreneurial firm for entrepreneurial clients.

Who will assist you

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