Major Revamp of DIFC Companies Law

Izabella Szadkowska - Partner - Corporate Structuring / Corporate Services / Corporate / Mergers and Acquisitions / Capital Markets / Family Business
i.szadkowska@tamimi.com - Dubai International Financial Centre

Although the Proposed Law may undergo changes before enactment, we highlight in this article the key changes that the DIFC has proposed.

These key changes are:

- a new scheme for corporate classification of DIFC companies by removing limited liability companies and introduction of division into private and public companies;
- enhanced directors’ duties;
- new mergers and scheme of arrangement provisions;
- ‘whistle-blower’ protection provisions;
- expanded powers for the Registrar of Companies (‘Registrar’); and
- enhancements to company accounting and audit requirements.

New Classification of DIFC Companies

The DIFC Companies Law presently envisages two types of companies: companies limited by shares and limited liability companies (‘LLCs’). The Proposed Law would no longer have the LLC regime and would instead divide companies limited by shares into two new classifications.

The Proposed Law would establish a distinction between public and private companies. Under the Proposed Law, a public company could offer its shares to the public, could have any number of shareholders and must operate with at least two directors and a company secretary.

A private company, on the other hand, would be prohibited from offering its shares to the public and could seek subscriptions only through a private placement of shares. Further, private companies could have a maximum of fifty shareholders and operate with only one director under the Proposed Law.

Regulatory requirements concerning private companies (e.g. accounting and general reporting requirements) would be significantly lighter than those applying to public companies. This distinction is designated to allow smaller businesses to operate in the DIFC with lower capitalisation levels and without facing onerous compliance burdens.

A significant change proposed is the replacement of the current minimum share capital requirement of USD 50,000 with tailored capital requirements for public and private companies. A public company would be required to have a minimum capital of USD 100,000, of which at least 25 per cent must be paid up. However, a private company would not be required to have a minimum share capital.

We understand that there will be some new provisions introduced under DIFC Companies Regulations (COR) concerning a transition process for already incorporated LLCs, facilitating their conversion to public or private companies limited by shares.

Directors’ Duties

Under the current law, DIFC directors are required to act honestly, in good faith and lawfully, with a view to the best interests of the company, and to exercise the care, diligence and skill which a reasonably prudent person would exercise in comparable circumstances. The other important duty of any DIFC director is to disclose interests in a transaction entered into, or proposed to be entered into, by the company that conflicts or may conflict with the interests of the company.

The Proposed Law would expand the current regime of directors' duties by providing more prescriptive duties applicable to directors, including duties to: (a) act within powers conferred by the company's constituent documents; (b) promote the success of the company; (c) exercise independent judgment, reasonable care, skill, and diligence; (d) avoid conflicts of interest; (e) decline to accept gifts from third parties capable of creating a conflict of interest; and (f) declare any personal interest in a proposed or existing transaction or arrangement.

The Proposed Law would also introduce a requirement for the board of directors of a public company to submit a report for each financial year setting out, amongst other things, the performance of the company during the year, which must be included in the company's annual report. This requirement would not be applicable to private companies.

Mergers and Schemes of Arrangements

Under the current law, no merger or scheme of arrangement provisions exists. The only comparable provision addresses the protection of minorities in a takeover.

However, the Proposed Law would introduce a new merger regime that applies to public companies established in the DIFC wishing to merge with other companies, including those established in jurisdictions outside the DIFC.

A major initiative added under the Proposed Law is the addition of new provisions that allow companies to conclude compromises or arrangements with creditors and/or shareholders, with final approval by the DIFC Court. These provisions will give much greater flexibility to companies in implementing both solvent and insolvent restructurings. The provisions for compromises and arrangements apply to both public and private companies.

Registrar's Powers

Under the current law, the objectives that the Registrar is to pursue in exercising its powers and discretions are not expressly stated. The amendments under the Proposed Law contain significant new provisions relating to the Registrar's powers. These include:

- defining the objectives for the exercise of the Registrar's powers;
- introduction of 'due process requirements' ;
- extension of the Registrar's enforcement powers;
- addition of investigative powers under other legislation administered by the Registrar; and
- expanded document inspection powers.

The Proposed Law creates a new power for the Registrar to inspect premises of and obtain information and documents from, a DIFC company and to dissolve a company that has undergone a voluntary winding-up process.

In addition, the amendments under the Proposed Law:

- extend the Registrar's powers in respect of recognised foreign companies;
- enable the Registrar to take action against the company or any officer of the company (both existing and former) for a period of three years from the date the Registrar becomes aware of an alleged contravention of DIFC law based on the information found by an inspector;
- strengthen the powers of the Registrar relating to inspection and investigations; and
- enable the Registrar to apply to the DIFC Court to disqualify a director from being involved in the management of a company.

Accounting and Audit

Whilst retaining the current regime relating to company accounts, reporting, and audit requirements in substantially the same form, the Proposed Law would introduce directors' reporting requirement for public companies.

Small private companies would be exempted from the requirements to have the company's annual accounts audited and filed with the Registry, to alleviate unnecessary regulatory burdens on such companies. To qualify for this exemption, a private company must have not more than 20 shareholders and its annual turnover cannot exceed USD 4 million.

'Whistle-Blower' Protection

Neither the current DIFC Companies Law nor the DIFC Employment Law provide any specific protections for 'whistle-blowers'.

The new proposals under the Proposed Law would introduce new 'whistle-blower' protection provisions in the DIFC Companies Law that shield any person who discloses to the Registrar, or a company's auditor or director, any information relating to a reasonable suspicion that the company has, or may have, contravened DIFC law. Such a discloser would be shielded from civil or contractual liability, unfair dismissal, and other actions prejudicial to the interests of that person – provided the disclosing person acted in good faith.

Although the UAE Penal Code applies in the DIFC and generally prohibits disclosure of confidential information, should DIFC law allow such disclosure, the whistle-blower is arguably also exempt from such liability under onshore UAE law because the UAE Penal Code provides an exception if the disclosure is 'allowed by law'.

Other Changes

The amendments under the Proposed Law also include the following new provisions:

- the requirement to file special resolutions with the Registrar, so that such information is available to the DIFC;
- introducing more formal pre-emption rights for existing shareholders of companies, to guard against undue dilution of existing shareholders' rights, with appropriate exclusions for arrangements such as employee share schemes, but retaining flexibility for private companies to remove or restrict pre-emption rights through express provisions in their articles of association; and
- providing companies with the flexibility to hold, as treasury shares, those shares redeemed by the company (including redeemable shares), provided certain conditions are met.

The amendments under the Proposed Law evidence the fact that the DIFC is working hard to make its offering more attractive to businesses and high net worth families. The proposed changes confer greater flexibility to companies to do business, with the option to select the level of regulation applying to their business. Investors and creditors of public companies will derive extra comfort from the higher levels of transparency and accountability of their corporate directors.

The DIFC Authority should be applauded for sharing the Proposed Law with the business, financial, and legal community, permitting wide discussions, comment and meaningful consultation.

Al Tamimi & Company's Corporate Commercial team regularly advises on matters of corporate commercial nature to corporate clients operating in the DIFC and UAE on-shore and public and private companies registered and operating in the UAE, particularly family businesses as well as incorporation / transfer of incorporation of entities in/to the Dubai International Financial Centre. For further information please contact i.szadkowska@tamimi.com.