

Why is Due Diligence a necessity in the Middle East?

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If a company has ever been involved in the purchase of a business interest or if it has ever been the subject of a sale or if it has engaged in a public offering of securities, then it will likely be familiar with the due diligence process.

Typically, due diligence is undertaken to assist a potential buyer in determining whether it is worth investing in a particular business.

There are several types of due diligence processes carried out in an acquisition scenario (depending on the size of the transaction) and these are:

1. **Business Due Diligence:** this involves reviewing the operational aspects of the target's business. This type of due diligence is undertaken by industry experts retained by the buyer;
2. **Financial Due Diligence:** this process enables the buyer to assess all financial aspects (i.e. indicators such as cash flows, balance sheets etc. of the target) of a potential acquisition to determine the benefits, liabilities, risks and opportunities. This type of due diligence is undertaken by financial experts usually also retained by the buyer or any lenders involved in the acquisition; and
3. **Legal Due Diligence:** this entails a review of the target's business to identify potential legal exposure and non compliance issues that could be inherited by the buyer as a result of its purchase of a stake in the business. This type of due diligence includes a review of the company's:
 - constitutional documents;
 - employee benefits and labour arrangements;
 - material contracts;
 - real estate assets;
 - intellectual property owned and used by the company;
 - financings;
 - insurance policies;
 - regulatory compliance (i.e., environmental and health and safety);
 - tax compliance; and
 - any litigation involving the company.

Legal due diligence is undertaken by legal practitioners retained by the buyer.

Why is Due Diligence indispensable in the Middle East?

Undertaking a legal due diligence process assists the buyer in evaluating the target's business to determine a suitable purchase price for procuring a stake in the said business. Doing a due diligence is also helpful for the buyer to understand the nature of the target's business and to assess where this

business fits in with its own growth strategy and enterprise.

Increasingly, international clients question the need to commence the legal due diligence process when contemplating a potential acquisition. Whilst it is tempting to skip the due diligence process (which can be time consuming and costly if not managed efficiently) and go straight to the preparation of the transaction contract, this is not advisable, particularly in the Middle East.

Some clients argue that they can rely on publicly available information on the target's business. In the case of any potential exposure (not identified due to the absence of a due diligence), these can be protected against by the inclusion of broad representations and warranties by the seller's and/or the target, as well as the inclusion of broad indemnities in favour of the buyer in the transaction documents. This approach is not recommended because enforcement of these protections in a court of law, particularly local courts where proceedings are conducted in Arabic, can be time consuming, with very different processes and rules for assessing financial damages. Resolution could take years.

Furthermore, in the Middle East there are almost no corporate records publicly available. In the case of the Dubai International Financial Centre ('DIFC') there is some limited information available on the public register. In other jurisdictions, the names of directors of a company, its shareholders and the solvency status of a company is publicly available information; however, this is not the case in the Middle East. This information must be specifically requested from and supplied by the sellers or the target.

With respect to litigation, no definitive public searches can be done on target entities in the Middle East courts. While it is possible to do an unofficial search in the courts of Dubai, the results are not detailed or always accurate. Usually a valid and formally notarised power of attorney from the sellers or the target permitting the buyer or its counsel to do a litigation search on the target is required.

Moreover, when acquiring real estate or verifying ownership, a title search would need to be carried out. However, public title searches are not possible in the Middle East as these records are not publicly available. It will not be possible for the buyer to do this search without a valid power of attorney from the sellers or the target authorising the buyer to carry out the investigation.

Similarly, if the business you are seeking to acquire has properties located in master communities, a buyer would be advised to confirm that all service charges and community fees have been paid to date. However, such investigation will not be possible without presenting a valid power of attorney to the master developer from the seller or the target authorising the buyer to carry out the investigation. This is also important because without the master developer's no objection certificate (which will only be provided once all dues owed to the developer are cleared) the resale will not be able to be completed.

Depending on the type of business forming the subject of the potential acquisition, investigations with special government authorities may be required. For example, if the acquisition involves the purchase of a regulated business (e.g. a clinic or a school), investigations need to be carried out with the regulatory authorities to ensure that the requisite approvals for the operation of the clinic or school premises are in place. To make such inquiries the consent and support of the sellers and/or the target will be required as this information is not publicly available.

Conclusion

Conducting legal due diligence enables the buyer to make an informed decision to proceed with a prospective acquisition. It also enables the buyer to identify and mitigate risks by including tailored protections in the transaction documents. The two reasons which make due diligence indispensable in the Middle East are:

1. the almost complete unavailability of useful information about the target from public sources; and
2. the problem of relying on an unfamiliar litigation system not geared towards resolving commercial cases quickly.

If a buyer does not do due diligence in this region, that buyer flies blind and flies towards risk.

Al Tamimi & Company's [corporate commercial team](#) regularly undertakes legal due diligences and prepares/advises on the transaction documents in the context of M&As in the region and internationally. For further information, please contact [Alyzeh Zahid Vana](#) (a.zahid@tamimi.com).