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## Urgent Deadline for LLC Side Agreements

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06 October 2007

November 15, the ban of Company Formation Side Agreements starts

Dubai - For decades, UAE-based companies with international partners are governed by a dangerous mix of official contracts in combination with so called "side agreements" as a long-standing business practice. This practice was established to accompany Article 22 of the UAE Company Law, stating "it is a requirement for the establishment of a company to have one or more national partners whose share in the company's capital is not less than 51%." Under existing laws for most of the commercial sector, foreign investors can own a maximum of 49 %.

"Legislative changes now are making domestic and international investors with holdings in the country very nervous," states Kirsten Kraeter, GM of KLP Group Emirates, a local provider for innovative company formations and domiciliation models. "Effective November 15, an amendment to the Commercial Company Law is set to ban all kinds of side agreements and side letters between foreign and local co-owners of UAE-based firms."

The push to abolish these side agreements was passed already in 2004. "But the date for implementation was deferred for three years, to give the Ministry of Economy time to better protect business investments, for example by issuing a new release of the UAE Company Law," states Martin Kraeter, Principal at KLP. "The problem now is: Three years passed without getting major changes in company legislation - and now furthermore "side agreements" are banned. This means, all legal handshakes in the past between foreign and domestic investors will be made null and void. It will be as if these agreements never existed!"

Major downside of the ban is that it could discourage international investors who may be hesitant to sink money into the UAE without any legal protection, due to the existing 49:51% regulations. The risk is high, that the country will lose a lot of potential investment from around the world. But the ban concerns also all existing companies and might lead to reconsideration of UAE activities in many cases.

Kirsten Kraeter: "Till now only a handful of investors were aware about the worst fact that "side agreements" were not seen as real contract base in case of court disputes." This, because their content mostly contradicts the notarized, and by this official, articles of association. "Only a few consultants and advisors cared already in the past for state-of-the-art company contract systems without the need for such 'side agreements' ", she continues, "Most of the advisors we know just do what ever they did: Using contract templates with lowest withstood from the notary public and pushing all essential regulations aside in the 'drawer'. To deploy a suitable contract system which really protects all partners and investors is of course more effort, and maybe promised 'days for getting a license' might be revised - but in our experience it is worth it".

Summarizing - and to be calm foreign investors - there are still ways to protect investments in a legal and notarized way. It depends, how so often, from the quality and engagement of the business & legal advisor, if and how a company is set up in the suitable manner.

- Ends -

#### About KLP Group Emirates

*KLP is an international active Management & Consulting Group, specialized in Business Development, Domiciliation and Business Setup handling. The KLP team consists of entrepreneurs with practical and legal backgrounds as well as profound experience in developing companies and protecting investor interest. With own offices in UAE, Germany and the U.S., KLP is focused on the business environments in the entire GCC (Gulf Cooperation Council) region in a combination with onshore and offshore knowledge for the benefit of clients from high-taxed economies all over the world.*

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