UAE Supreme Court Rules on Unclear Arbitration Clause

March 21, 2021

When drafting an arbitration clause, it is vital to make sure that the clauses are simple and clear in order to avoid uncertainty and disputes over their semantics and effect. This is the first step to ensuring the time and cost-effectiveness of a potential dispute as it will minimize the risk of possible disagreements regarding the jurisdiction of the tribunal or the process of appointing the arbitrators. At the very outset of drafting the arbitration clause, it must be explicit that the parties wish to have their disputes resolved via arbitration and to waive the original jurisdiction of the courts. If this intention cannot be inferred, it means that the 'medium' used has missed its target.

The repercussions of the failure to express clarity and intention of the parties to refer to arbitration in case of a dispute manifested in a case leading to a Federal Supreme Court judgment issued recently.

The Case in Question

The case in question revolves around an agreement that was executed in March of 2013, relating to the non-payment of medical supplies.

The language used in the arbitration clause was in English and the issue arose out of whether or not the clause was explicit in commanding the parties to refer to arbitration as the dispute resolution mechanism.

The arbitration clause stated in case the parties could not reach an amicable settlement in relation to any dispute within 30 days, either party may trigger arbitration dispute

proceedings to be seated in Abu Dhabi, conducted in English and subject to the rules of the Abu Dhabi Commercial Conciliation & Arbitration Centre.

When the dispute arose for non-payment over the sale of the medical supplies, one of the parties filed the dispute before the Primary Court. The Primary Court found it had no jurisdiction to hear the case due to the arbitration clause.

The Primary Court judgement was appealed with the argument that the original language used in the arbitration clause did not obligate the parties to refer to arbitration, but rather, was an optional method for dispute resolution. The Appeals Court accepted the appeal argument and remanded the case to the Primary Court to apply its jurisdiction and rule on the merits of the dispute.

The party arguing that the arbitration clause was obligatory challenged the ruling of the Appeals Court before the Federal Supreme Court on the basis that it had submitted a translation of the arbitration clause from English to Arabic, provided by a judicially certified legal translator, to the court which evidenced that the arbitration clause was obligatory.

The Federal Supreme Court ruled that the judgement of the Appeals Court was unfounded as it did not debunk the translation presented by the party advocating for the obligatory language of the arbitration clause.

The Federal Supreme Court found that the Appeals Court could have ordered the appointment of a language expert from the respective expert registry, or the party advocating for the courts' jurisdiction could have submitted a counter-translation evidencing that the arbitration clause was indeed optional. Neither of these potential procedures had occurred.

The Federal Supreme Court overturned the Appeals Court judgement.

But what if the Appeals Court of its own accord or by litigant’s request ruled for the requirement of a court-appointed language expert to opine on the English text of the arbitration clause?

Or what if the party advocating for litigation had submitted a translation by a judicially certified translator that arbitration clause was optional?

In both hypotheticals; the result would have been an even further prolongation of the dispute and an increase in costs.

The moral of the case is the importance of clear and effective arbitration clauses (or agreements); that include the seat of arbitration, number and selection of arbitrators, institutional or ad hoc, governing law of the subject matter in dispute and possibly governing law of the arbitration agreement (if different), capacity to agree to arbitration, the authority to sign arbitration agreements, multiple party arbitration, enforcement, opt-in and opt-out provisions (although they may be problematic), sovereign immunity if a party to the transaction is a State, scopes of disputes covered, and other matters.

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UAE Supreme Court ruled tender committee liable for

contractor’s rejected bids of 65 million Dirhams

March 21, 2021

In the late nineties, a contractor sued a government tender committee for AED 65,467,250 in compensation for losses and lost earnings as a result of not being awarded five tenders related to construction and maintenance works that the contractor had bid for.

The contractor argued that its five bids contained the lowest prices and fulfilled all the conditions of the tenders. Both the primary court and the appeals court rejected the claim.

The Federal Supreme Court, however, overturned the lower court judgments and found the tender committee to be administratively liable towards the contractor for the five rejected bids.

The case was brought forth on grounds of contravening Abu Dhabi Law No. 4/1977 On Tenders, Auctions and Warehouses in the Emirate of Abu Dhabi – particularly on the basis that Article 21 of the said law states that:

“The preference between the tenderers shall be according to the selection of the tenderer presenting the lowest total price, should the bid thereof be consistent with the tender conditions. However, the tenderer presenting a higher price may be chosen should the lower prices be unreasonably low and not assuring proper work progress.”

The Federal Supreme Court ruled that it was evident from the statutes regulating contracting by way of tender, that the legislator has subjected public tenders to basic principles of

openness, equality, freedom of competition and the mechanism for awarding the tender, and obligates the administrative authority (i.e. the tender committee) to disclose the reasons for rejection of a bid.

The Court’s rationale was that this is to ensure that the administrative authority follows a decreed path in order to reach the appointment of the best bidders in accordance with the law. The contracting procedures are organized by way of tender, so that it takes place in two stages, the first of which includes preliminary work and the second in which the contract is concluded.

Continuing, the Court stated that the preliminary tender processes consist of setting the conditions for the tender, announcing it, receiving bids, fulfilling the conditions of the tender, and then separating between the bids. These were considered by the Court to be internal organizational rules that are the prerogative of the tender committee. Nonetheless, the Court opined that the provisions that are set by the legislator are for the benefit of the administrative authority (i.e. the tender committee) and private persons alike, with the aim of ensuring the impartiality of the bidding processes and respecting the principle of equality among all bidders.

In interpreting the law, the Federal Supreme Court noted that the bidder with the lowest price is originally the owner of the right to the award whenever the bid is consistent with the terms of the tender, and with the exception of this principle, the administrative authority may award the tender that was submitted at a higher price if the lower price was unreasonably reduced, as there may be concerns regarding good performance, and this exception was a violation of the basic principle that governs public tendering procedures, which is the mechanism for awarding the tender.

In its judgment, the Federal Supreme Court found the tender committee to be administratively liable.

The significance of this case is not only that a contractor had succeeded in an action against an administrative decision issued by an administrative authority (i.e. the tender committee), but that the Federal Supreme Court found the committee to be liable for its decision.

In other words, the Court did not only invalidate the decision, but also found that liability arose against the contractor's claim of AED 65,467,250.

One of the rarely commented upon competencies under Emirati law is administrative law and administrative decisions; the law that governs the relations between government agencies, and government agencies and the private sector, and the decision taken by government agencies.

There is no single administrative legislative text in the UAE, rather, the corpus of administrative law is comprised of scattered provisions in various pieces of legislation – but mainly the Constitution and Article 84 (bis) of the Civil Procedures Law – and also scholarly works and jurisprudence.

As a matter of fact, Article 84 (bis) was only added to the Civil Procedures Law in 2014.

In 2019, there were almost 1,130 administrative cases filed before the various stages of the Federal Courts. Not to mention the myriad other administrative cases that are domestic respective of domestic administrative authorities in Emirates that have independent judicial authorities (i.e. Abu Dhabi, Dubai, RAKI, DIFC, and ADGM).

Most administrative disputes revolve around invalidating an administrative decision – in other words – cancelling the administrative decision and its consequence. The discussion surrounding forms and procedures of administrative disputes is quite broad and has its own respective nuances such as the effects of administrative decision *in rem* and those *in personam*, and whether effects can be retrospective, or whether

there can be a monetary value attached to an administrative decision and its invalidation.

However, with all that said, it is extremely rare for a Court to find an administrative authority liable for an administrative decision – particularly where the plaintiff is claiming compensation for losses and lost earnings.

Generally, the Courts either uphold the administrative decision, or invalidate it, or invalidate it *and* replace it with a quasi-judicial/administrative decision – but rarely does a Court find the administrative authority liable.

This particular case in this article is what one may refer to as an 'orphan' case. It occurred in an exceptional instance, and it is unclear if there are other similar judgments, or whether the Federal Supreme Court may repeat such a judgment.

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Supreme Court Ruling: Defamation via Snapchat (Parody and the DIFC IP Law)

March 21, 2021

Case facts, arguments, and Federal Supreme Court ruling

In late 2018, a complaint was filed before the public prosecution alleging the editing and alteration of an advert

video on Snapchat by the accused for purposes of mocking and defaming the advertiser (the complainant/victim).

The complaint was filed pursuant to Article 21 of the Cybercrime Law for using “an electronic information system or any information technology means for amending or processing a record, photo or scene for the purpose of defamation of or offending another person or for attacking or invading his privacy”, punishable with imprisonment of a minimum of one year and/or a fine of AED 250,000 to AED 500,000.

The defendant challenged the accusation on two grounds;

1. That the complainant/victim had withdrawn the complaint.
2. That the purported crime lacked financial or moral causation on the part of the defendant.

The criminal courts rejected the first argument on the grounds that withdrawal of criminal complaints pursuant to Article 16 of the Criminal Procedures Law is limited to the crimes laid out in Article 10 of the Criminal Procedures Law; theft, breach of trust, insult, slander, and other crimes, but does not include the Cybercrime Law provision subject of the complaint.

As for the second argument, the defendant argued that the accusation lacked financial or moral causation, arguing that the advertisement by the victim published via Snapchat was not edited by the defendant in malice.

The defendant argued that he had discovered a grammatical error in the advert which he commented on in an edited reproduction of the original video, with no intent to defame or insult the advertiser. This argument was also rejected by all levels of courts.

The Federal Supreme Court upheld the lower courts ruling in finding the defendant guilty of violating Article 21 of the Cybercrime Law.

In its judgment, the Federal Supreme Court reasoned that the reproduction of the victim's original video that had been published via Snapchat and the defendant proceeding to publish the edited version via Snapchat was punishable as the act was for the purposes of creating parody out of the original content.

Fair use, parody, the DIFC IP law, and what this means for businesses

The Federal Supreme Court's judgment raises questions towards the liability of parties in what could generally be considered as fair use for a limited and transformative purpose, to comment upon, criticize, or parody works (such as multimedia/social media).

Between 2006 and 2009, Mac (Apple) ran 66 television spots that parodied Microsoft. In 2014, IKEA published an advert on YouTube that parodies Apple's iPhone. In 2019, BMW published an advert that parodies the retirement of Mercedes-Benz's CEO, Dieter Zetsche, showing an actor playing Zetsche substituting a Mercedes-Benz for a BMW.

Business generally employ parody and satire for numerous reasons – sometimes targeted against other businesses for market exposure, at other times to sell content (such as satirical magazines).

Various jurisdictions generally allow for the reproduction of works for commentary and criticism, or parody, unless actual malice is proven, and in which case the threshold to evidence actual malice is generally high.

Recently, on 21 November 2019, DIFC Law No. 4 of 2019 on Intellectual Property was promulgated, and interestingly, the new law explicitly permits the use of a trademark registered in the UAE, or a well-known trademark, for parody purposes so long as the parody is conducted within the jurisdiction Dubai International Financial Center.

This is the first explicit statute on parody in the UAE.

Notwithstanding, the Federal Cybercrime Law is federal criminal legislation, which would essentially supersede the DIFC jurisdiction.

As for social media businesses, internal curator policies, geotagging, end-user license agreements, and other considerations must be addressed in light of these substantial novel developments.

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Federal Appeals Court Reverses Tax Penalties (UAE)

March 21, 2021

Client Alert

Recently, the Federal Appeals Court (UAE) reversed late payment penalties applied by the Federal Tax Authority on voluntary disclosures in two separate tax disputes for two separate taxpayers assisted by Wasel & Wasel.

The Federal Appeals Court has ruled on nearly six tax disputes between 2019 and June 2020, almost three of which have been successful in reversing penalties imposed on taxpayers by the Federal Tax Authority.

Wasel & Wasel has been counsel on two of the three successful

judgements before the Federal Appeals Court reversing multi-million Dirham tax penalties.

The penalties reversed were late payment penalties imposed on voluntary disclosure submissions.

These latest judgements by the Federal Appeals Court continue the success record of Wasel & Wasel on tax disputes before the tax disputes resolution committees and the Federal courts.

Moreover, Wasel & Wasel was able to obtain these successful judgements without the Federal Courts ordering the appointment of a court expert, which lead to an increased speed of the court proceedings.

The two companies had filed objections before the Dubai Tax Dispute Resolution Committee in 2019 against the late penalties on voluntary disclosures.

In mid-2019, the Dubai TDRC ruled in favour of the taxpayers and reversed late penalties imposed on voluntary disclosures.

The TDRC rulings were subsequently challenged before the Federal Primary Court in late 2019.

The Federal Primary Court upheld the TDRC rulings in early 2020, maintaining the reversal of late penalties on the voluntary disclosures.

The Federal Appeals Court judgements follow a significant number of TDRC and Federal Court rulings and judgements since 2019 that Wasel & Wasel has assisted taxpayers with, in addition to various other issues taxpayers face; such as private clarification tax disputes, out-of-State taxpayer disputes; tax disputes arising out of audits by the Federal Tax Authority; tax disputes arising out of supply to Government entities; and more.

To access the Getting The Deal Through publication on tax disputes in the UAE; click here.

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New Tax Evasion Court (UAE)

March 21, 2021

New court

On 10 November 2020, His Highness Sheikh Mansour bin Zayed Al Nahyan, Deputy Prime Minister and Minister of Presidential Affairs, and Chairman of the Abu Dhabi Judicial Department issued Resolution No. 35 of 2020 (the "Resolution").

Article 1 of the Resolution states that:

"A Court is to be established in the city of Abu Dhabi and shall be dedicated to hearing Money Laundering and Tax Evasion Crimes. The Court shall be under the Abu Dhabi Criminal Court."

So far, there have not been reported tax evasion crimes in the UAE.

In December 2019, however, news was issued that the Federal Tax Authority and the Federal Public Prosecution had begun coordination and cooperation on regulatory measures to address cases of tax evasion, to develop training courses in the field of tax evasion and means of confronting it, and to form a joint team to work on identifying the legal documents and requirements to be dealt with for tax evasion issues and to manage the witness and victim protection program.

Tax evasion was addressed by a court for the first time during civil proceedings on 14 October 2020 when the Federal Supreme Court addressed tax evasion in a judgment related to voluntary disclosures.

The Federal Supreme Court took the position that where a person discovers an error, they must disclose and correct the error (within twenty weekdays) – or be found to have committed tax evasion.

Tax evasion

Tax evasion is defined in the law as:

"The use of illegal means resulting in the reduction of the amount of the due tax, nonpayment thereof, or a refund of a tax that a person does not have the right to have refunded under any tax law."

The criminal penalty for tax evasion is a prison sentence and/or a monetary penalty up to five times the amount of evaded tax.

The tax legislation does not limit the prison sentence term, but Article 69 of the Penal Code states that:

"The minimum period of imprisonment may not be less than a month nor exceed three years, unless the law provides otherwise."

Because the tax legislation does not state otherwise, one can draw from the Penal Code that prison sentences for tax evasion crimes can be a minimum of a month and a maximum of three years.

As opposed to the self-declaratory tax regime for tax returns and so on, where the burden of proving the accuracy of the tax return falls upon the taxable person, in tax evasion issues, the burden of proving tax evasion falls on the Federal Tax Authority. – As is the case between civil and criminal cases.

It is to be noted that the Penal Code explicitly states that ignorance of the law is not to be considered an excuse – hence knowledge and application of the tax legislation is expected of all taxpayers, failure of which may lead to finding a tax evasion offense.

Procedure

As for the court procedure, Article 2 of the Resolution states that:

"Appeals to the judgements rendered by the specialized Court…shall be heard by one of the specialized circuits of Appeal of the Abu Dhabi Criminal Court."

The specialized court will thus – seemingly – comprise of three stages of trial; a primary level, an appeals level, and final the Abu Dhabi Court of Cassation (criminal).

Prior, it was expected that tax evasion crimes would come under the ambit and jurisdiction of the Federal Primary Court (criminal circuit), given that tax evasion is a federal crime.

However, with the Abu Dhabi Judicial Department establishing an Abu Dhabi dedicated criminal court for tax evasion crimes, it is expected that the Emirates with independent judicial systems will have jurisdiction over tax evasion crimes that occur within their Emirate (or fall within their jurisdiction for other reasons).

The Emirates with independent judicial systems are Abu Dhabi, Dubai, and Ras Al-Khaimah (RAK). The remaining Emirates utilize the Federal court systems.

This will ultimately lead to potential diversity in judgments and reasonings, as there will expectedly be separate judgments over similar issues by the Abu Dhabi Cassation Court, the Dubai Cassation Court, the RAK Cassation Court, and the Federal Supreme Court.

Liability

As a general matter, a tax evasion accusation would be levied against the taxpayer (as the original debtor) and against the legal representative of the taxpayer company (i.e. the listed authorized signatory on the commercial registration of the company, or the listed representative with the FTA).

However, both the tax legislation and the Penal Code address complicity – i.e. where others are involved in the potential tax evasion crime.

This is extremely important for employees of the taxpayer and external advisors to the taxpayer alike to take note of, as any could be deemed an accomplice to a tax evasion crime.

For example, if the finance director of a company discovers an error but does not take action on that error within the requisite time period to avoid tax penalties, the company (taxpayer) may be found to have committed tax evasion, and the finance director to be a direct accomplice to that action.

In another hypothetical, if a tax agent advises their client not to disclose a particular tax error to avoid facing tax penalties, the tax agent could be found to be an accomplice by causation.

Article 26 of the Tax Procedures Law addresses complicity as follows:

“The competent court shall impose tax evasion penalties against any person who is proven to have been directly involved or instrumental in tax evasion…[and] any person who is proven to have been directly involved or instrumental in tax evasion shall be jointly and severally liable with the person whom he has assisted, to pay the payable tax and administrative penalties pursuant to this law or any other tax law.”

There are two types of criminal complicity; direct and by causation.

Direct complicity is defined in the Penal Code as one of three categories:

1. A person who perpetrates the crime with another person.
2. A person who participates in its perpetration when it consists of several acts and deliberately commits one of its constituent acts.
3. If a person sub-serves another person by any means to execute the criminal act and the latter is not criminally responsible for this act for any reason whatsoever.

Complicity by causation is also defined in the Penal Code under three categories:

1. If the person instigates to commit a crime that was perpetrated as a result of this instigation.
2. If the person conspires with others to perpetrate a crime that occurred as a result of this conspiracy.
3. If the person gives the doer a weapon, tools or anything else used in the perpetration of the crime of which he had knowledge; or willfully assists the perpetrator, by any other means, in the preparatory acts or those facilitating or completing the perpetration of the crime.

FTA powers

Article 50 of the Tax Procedures Law grants the Director-General, and tax auditors appointed by a decision of the Minister of Justice, the capacity of judicial officers for tax violations.

Under Article 30 of the Criminal Procedures Law, judicial officers have the power to inquire about crimes, search for their perpetrators and collect the necessary information and

evidence for investigation and indictment.

Article 45 of the Criminal Procedures Law grants judicial officers the power order the arrest of the accused, present and against whom there is enough evidence that they committed a crime.

Nonetheless, criminal trial proceedings would be conducted by the respective public prosecution.

As such, the initiation of a criminal case may only be via an application of the FTA's Director-General pursuant to Article 17 of the Tax Procedures Law.

Ultimately, the Director-General and certain FTA tax auditors can act as judicial officers with the powers to search, investigation, question, and indict a person for tax evasion.

Subsequently, the complaint is submitted to the public prosecution by the Director-General in order for the new Tax Evasion Court to adjudicate the case.

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Constitutional Circuit of the UAE Federal Supreme Court Re-Opens Avenues for Appealing

Against Court Seizure Orders / Garnishments

March 21, 2021

Background

The Executive Regulations to the UAE Civil Procedures Law that came into effect in early 2019 amended the right of persons to appeal to seizure orders limiting the right to only the distrainee (the debtor whom the order is issued against).

Prior to this amendment, the distrainee, the judgment creditor, and any concerned person had the right to appeal against a seizure order.

In May of 2019, a creditor applied to the Dubai Courts to seize a performance bond held by the debtor.

The application was rejected.

The creditor appealed the rejection and in July 2019 the Dubai Courts turned down the appeal on the basis that Article 114(3) of the Executive Regulations to the Civil Procedures Law limits appeals against seizure orders to the distrainee (the debtor) only.

The creditor argued that Article 114(3) is unconstitutional pursuant to Articles 14, 25 and 41 of the UAE Federal Constitution and requested the Dubai Court of Appeals to grant leave to file a constitutional case before the Constitutional Circuit of the Federal Supreme Court for review of the constitutionality of Article 114(3).

The Dubai Court of Appeals found merit in the request and granted the creditor leave to file a constitutional lawsuit before the Constitutional Circuit of the Federal Supreme

Court, which the creditor proceeded to do so in September of 2019.

Defense arguing the constitutionality of Article 114(3) was submitted by the Cabinet of Ministers and the Minister of Justice, represented by the State Disputes Department of the Ministry of Justice, and the Dubai Legal Affairs Department on behalf of the President of the Dubai Primary Court.

Decision

The Constitutional Circuit of the Federal Supreme Court rejected the argument that Article 114(3) is unconstitutional but stated that creditors and any concerned persons may rely on Article 60(1) of the Executive Regulations to the Civil Procedures Law to appeal against seizure orders.

Article 60(1) states that a petitioner whose request has been rejected, the person against whom the order has been issued, and any concerned persons, have the right to file a grievance against said order unless the law or the Executive Regulations stipulate otherwise.

Prior to this ruling by the Constitutional Circuit, it was understood that Article 114(3) was a carve-out provision that applied the restriction provided for in Article 60(1); "*…unless the law or the Executive Regulations stipulate otherwise*…".

The Constitutional Circuit, however, ruled that Article 114(3) is not a carve-out provision and creditors and concerned persons may rely on Article 60(1) to file appeals against seizure orders.

Constitutional Litigation (Brief)

In the UAE, filing a constitutional case directly before the Constitutional Circuit of the Federal Supreme Court is a right restricted to the federal and local government agencies only.

Private litigants may only file a constitutional case with the Constitutional Circuit if granted leave by a subject matter trial court in an on-going substantive case.

The basic principle is that a constitutional lawsuit is filed based on an existing substantive case before the trial court. In which a litigant argues the unconstitutionality of legislative text against the substantive dispute. If the trial court accepts the argument it authorizes the litigant to file a constitutional lawsuit. Alternatively, the trial court may of its own accord find that the text is unconstitutional and refer it to the Constitutional Circuit of the Federal Supreme Court for review.

However, this does not make the constitutional lawsuit a subordinate lawsuit, but rather a case that is separate from the subject matter dispute because it – the constitutional lawsuit – deals with a subject that differs from the merits of the substantive case.

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Dubai Judges Rule Employment Termination is Force Majeure in Rent Dispute

March 21, 2021

Amongst the flurry of expectations and predictions on the

application of force majeure arguments in light of the employment terminations currently occurring globally, whether related or unrelated to COVID-19, a panel of judges in the Primary Circuit of the Rental Disputes Center of Dubai ruled that termination of employment fulfills the requirements of a force majeure event and can be relied on as grounds to terminate a lease agreement.

Case

A lessee failed to pay rent from 1 January 2019 till 23 October 2019.

The landlord issued the requisite formal notice for payment to the lessee on 19 February 2020.

Upon expiry of thirty days past the formal notice, the landlord commenced trial procedures.

In early 2020, the landlord filed a case before the Primary Circuit of the Rental Disputes Center requesting; eviction, payment of outstanding rents, payment of maintenance charges, penalties, amongst other reliefs.

The lessee filed a counterclaim on the basis that they had been terminated from their employment and hence a force majeure event had manifested preventing them from complying with their obligations of paying rent and requested; return of the rent deposit, termination of the lease agreement, and costs.

In arguing force majeure in the counterclaim, the lessee relied on two real estate rulings of the Dubai Courts:

No. 238/2012: “Force majeure is understood to render compliance with obligations impossible pursuant to Article 273(1) of the Civil Procedures Law…”

No. 415/2011: “Hardship and force majeure events must be respected in ending or limiting the performance of an

obligation…if the underlying event is in a general sense exceptional and unusual, and was not foreseen at the time of entering into the agreement…”

The lessee argued that the force majeure event was that they had been terminated from their employment on 29 December 2019.

The landlord did not counter the force majeure argument with any defenses on the non-application of a force majeure event.

Notwithstanding the fact that termination of employment had occurred after the debt had accrued, the panel of judges accepted the argument that termination of employment is an unexpected event fulfilling the conditions of a force majeure event and that the continuance of the obligations under the lease agreement would cause hardship to a level of the impossibility of performance and ordered the termination of the lease agreement as of the date of the final ruling.

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Hostile LLC takeovers under the new 100% UAE ownership laws

March 21, 2021

An announcement took place on 23 November 2020 that foreign

investors can have complete ownership of Emirati companies that are governed by the Federal Commercial Companies Law ("CCL") otherwise known as "on-shore" companies.

The concession is limited to limited liability companies and private joint stock companies, including those owned by a single shareholder.

The most common form of corporate formulation is generally a limited liability company, with 49% of the shares of the company owned by a foreign investor (or investors), and 51% owned by a national shareholder (or shareholders).

It goes without saying that this development grants substantial flexibility to new foreign investors.

But here we consider certain implications for currently existing companies.

Minority shareholders who currently own 49% or less of a business will look to expand their ownership.

Amicable negotiations to buy-out the shares of the majority shareholder may not succeed for various reasons, such as the majority shareholder leveraging their position to sell their shares at exorbitant valuations.

And majority shareholders who currently own 51% or more of a business will look to protect their ownership.

What ensues from these machinations will be attempts at hostile takeovers.

What is a hostile takeover?

In a general sense, a hostile takeover is in reference to forcible buyouts of a publicly listed company when the board of the public company is rejecting the sale.

Different strategies are employed such as "bear hugs" where

the acquirer would issue a tender offer to the public stockholders to buy the publicly traded shares at a value higher than the publicly traded value.

Or “dawn raids” where the acquirer would purchase all the publicly traded shares as soon as the stock exchange is open for business.

Or a “proxy fight” which is basically an attempt to reform the board of the public company for a new board to approve the acquisition.

Notwithstanding, hostile takeovers are in essence an attempt by a person/company to forcefully – and with hostile tactics – acquire all or controlling interest in a business.

In this article, we detail hostile takeovers in the manner between a minority and a majority shareholder of a limited liability company (“LLC”) – where the minority shareholder (the “predator”) may attempt to forcibly takeover all of the target shares of the majority shareholder in the LLC, or enough shares to grant the predator controlling interest.

Although there are many strategies, here we discuss examples of five offense strategies that a predator may employ, and five defense strategies that a majority shareholder could trigger, in a hostile takeover attempt.

Offense strategy: interlocking takeover

An interlocking takeover would occur where there are more than two shareholders, and the predator and another shareholder (the “interlocking shareholder”) jointly own over 50% of the share capital and use their combined controlling interest to remove the third shareholder target and obtain its target shares.

Article 677 of the Federal Civil Transactions Law (“CTL”) grants the shareholding majority the right to apply to the

court for removal of any shareholder if the request is based on sound grounds.

Sound grounds could include where a shareholder is engaged in competing business or is convicted of a felony (such as money laundering), and so on, but this would ultimately be up to the judge's discretion.

As to continuity in the business, a lawsuit aimed at removing a shareholder would not generally prejudice the continuing operations of the LLC.

"That when the decision is made to remove a shareholder from the company, the company continues among the rest of the shareholders, and the separated shareholder in this case deserves his share and this share is estimated according to its value on the date of filing the lawsuit." (Federal Supreme Court Judgment No. 933/2019)

The interlocking shareholder may subsequently sell its shares to the predator, granting the predator complete share ownership of the LLC.

Offense strategy: grey knight takeover

A grey knight takeover is where the predator engages another person/company (known as a "grey knight") to acquire the target shares of the majority shareholder which would result in the predator and the grey knight jointly owning simple majority (over 50%) or a supermajority (75% and above) of the LLC's share capital.

A grey knight is generally an offeror who purchases shares without expressing any hostility and represents itself as a neutral share purchaser.

If the share ownership of the predator and the grey knight jointly grants a supermajority of 75% that would fulfil the quorum for convening a general assembly (Article 96 of the

CCL), and voting on matters that require extraordinary general assembly consent such as amendment of the articles of association of the LLC (101 of the CCL).

The predator and the grey knight could also trigger Article 677 of the CTL to obtain the target shares.

Offense strategy: creeping parent takeover

A creeping parent takeover occurs where the majority shareholder is a company rather than a natural person, and the predator gradually and interceptively acquires controlling interest of the majority shareholder company.

At times, the majority shareholder parent company is a non-active, invaluable entity and any offers to purchase shares of the majority shareholding company at above-market values would be too attractive to refuse.

Article 77 of the CCL establishes the principle of non-divisibility of shares owned by a company. This means that the target shares would be owned indivisibly by that company (not divisibly by its parent level shareholders), hence once the predator has controlling interest at the parent level of the majority shareholder, the predator may *de facto* control the target shares, and ultimately the LLC.

The predator may also engage a grey knight for takeover of the controlling interest of the majority shareholder parent company.

Formulation:

Company A (the predator) owns 49% of Company X.

Company B owns 51% of Company X (the target shares).

Company X is the valuable entity.

Company A (or the grey knight) offers to purchase minor or all

shares of Company B at a premium price.

Company A eventually owns controlling interest of Company B.

Offense strategy: toehold takeover

A toehold takeover is the acquisition by the predator of minimal additional shareholding (usually 5% or less) to gain a toehold into majority shareholding as precursor to a hostile takeover action.

For example, if the predator owns only 49%, they may purchase 1.1% at minimal to own a total of 50.1% of the share capital of the LLC.

Subsequently, the predator may trigger Article 677 of the CTL as described above.

Offense strategy: black knight takeover

A black knight takeover occurs where the majority shareholder is in debt to a third-party creditor, and the creditor triggers Article 20 of the CCL to enforce its debt against the target shares of the majority shareholder.

The shares would then be sold at court auction, granting the predator the opportunity to purchase the shares at the auction.

The black knight may also be the predator itself, if the predator has proven debt against the majority shareholder.

Defense strategy: safe harbor

A safe harbor defense would occur where the majority shareholder, facing a hostile takeover, would add a commercial activity to the LLC which falls outside Cabinet Resolution No. 16 of 2020 (Concerning the Determination of the Positive List of Economic Sectors and Activities Eligible for Foreign Direct Investment and Percentage of their Ownership).

By adding an activity that falls outside Cabinet Resolution No. 16 of 2020, the predator would no longer be able to comply with the complete foreign ownership requirements and be prevented from owning more than 49% of the LLC by the regulators.

Defense strategy: backward integration

A backward integration defense involves the majority shareholder acquiring the source of the LLC's business; such as the producer of raw materials that the LLC uses for its commercial activities, or the ancillaries which are necessary to the LLC.

By controlling the source of the LLCs commercial activity, the majority shareholder would have leverage to prevent hostile takeover action by the predator.

Defense strategy: golden parachute

A golden parachute defense occurs when the majority shareholder has, or obtains, a managerial role in the LLC with extensive benefits and end of service gratuity that would render the removal of the majority shareholder financially detrimental to the LLC that the predator is dissuaded from a hostile takeover action.

Defense strategy: show-stopper

A show-stopper defense essentially involves the majority shareholder commencing trial proceedings to prevent hostile takeover action.

Defense strategy: forward integration

A forward integration defense mirrors a backward integration defense except the majority shareholder would purchase the businesses that make use of the LLC's services or products to control the market of the LLC.

Using deal counsel as raiders or killer bees

Predators looking to engage in hostile takeover action would engage a raider as a takeover artist to lead the hostile takeover action. This is generally the law firm / counsel in charge of the hostile takeover.

Majority shareholders looking to defend against hostile takeover action would engage a killer bee to fend off the action. A killer bee would generally be the law firm / counsel in charge of defending against a hostile takeover.

Both predators and majority shareholders need to consider whether their deal counsel (i.e. their law firm / counsel that assisted in establishing the relationship / the LLC) should also act as their raider or killer bee, respectively, in hostile takeovers.

An initial thought may be that the deal counsel who had assisted in advising on the deal and setting up the LLC should also be the raider or killer bee because they are already familiar with the corporate structure and nuances that took place during the incorporation process.

But before this initial thought is acted upon, a predator should ask whether the deal counsel had advised on including provisions in the articles of association of the LLC that require the majority shareholder to sell to the minority shareholder where there is a change of law.

If not, then the deal counsel may face “confirmation bias” which reflects a strong view favoring a position during the deal, which may be difficult to alter for the deal counsel to act as the raider.

Another concern is that deal counsel may be subject to discovery proceedings if trial takes place.

For example, if an expert is appointed during trial

proceedings pursuant to Federal Law 10/1992 on Evidence in Civil and Commercial Transactions, the expert may be granted powers to investigate correspondences, documents, or any other potential evidence that took place at the time of the deal/corporate establishment, including those prepared by the deal counsel.

Hence, trial proceedings may be negatively affected if the raider or killer bee is the same as the deal counsel.

Another conflict of interest may occur if the deal counsel had been jointly engaged by all the shareholders to conclude the deal / establishment process, rendering the deal counsel incapable of being engaged by the predator or the majority shareholder, as a raider or killer bee, due to direct conflict of interest.

Ultimately, it may be appealing to revert to deal counsel to act as the raider or the killer bee, but the risks may outweigh the presumed benefit, which results in favoring new counsel to effectively manage the hostile takeover.

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Demystifying Disputes in Country-by-Country Reporting

Compliance

March 21, 2021

Country-by-Country Reporting (CbCR) compliance obligations for multinational entity groups (MNCs or multinational companies) were introduced in the UAE in mid-2019 via Cabinet Resolution No. 32 of 2019, where the first notification and reporting deadline was set for 31 December 2019.

There is no shortage of industry experts in the UAE to have assisted MNCs with the technical elements of the submissions with respect to contents of the report, identification of constituent entities, tax residency parameters, and so.

In this article, we look at the penalties that could be imposed on an MNC for violation the CbCR compliance obligations, and how to dispute those penalties before the competent authorities.

Penalties

The Ministry of Finance, which oversees CbCR compliance, has the authority to implement penalties of various proportions on the reporting entity (e.g. the MNC);

- Failure to retain CbCR compliance documents/data for a minimum period of five years after the date of reporting to the Ministry of Finance: AED 100,000;
- Failure to provide the Ministry of Finance with any information requested: AED 100,000;
- Failure to report information in a complete and accurate manner: AED 50,000 to AED 500,000; and
- Failure to submit on the reporting date or failing to notify the Ministry of Finance on or before the reporting date of the intention to file for a certain

accounting period: AED 1,000,000 and AED 10,000 daily until the failure is resolved, or the daily amount reaches ED 250,000.

The Ministry of Finance must notify the reporting entity in writing if the reporting entity violates any CbCR compliance requirements and should provide a grace period of fourteen business days for the reporting entity to rectify the contravention.

If the reporting entity fails to rectify, the penalties would apply, and the reporting entity must be notified of the penalties within six months of the date the penalty liability arises, or the violation comes to the attention of the Ministry of Finance.

Insufficiency of funds or lack of access to information are not cause for excuse against the imposition of a penalty.

Any penalty applied must be settled by the reporting entity within 30 business days from the notification date of the penalty, or the date of which a grievance against the penalty has been denied.

Grievance

If the reporting entity may submit a grievance if it has grounds to believe that; (i) it did not commit a violation that warrants the imposition of a penalty; or (ii) disagrees with the amount of the penalty imposed on it.

The grievance must be submitted to the Ministry of Finance within 30 business days from the date of notification of the penalty.

The Ministry of Finance must notify the reporting entity of its decision within 60 business days. If no decision is provided to the reporting entity within 60 business days, then the grievance is deemed accepted, and the penalty imposed

shall be canceled.

Litigation

Cabinet Resolution No. 32 of 2019 on the CbCR compliance regulations is silent on what occurs if the Ministry of Finance decides to reject the grievance.

In this case, the reporting entity may turn to the Civil Procedures Law which provides the reporting entity with an avenue to apply for the annulment of the Ministry of Finance's rejection of the grievance in its nature as an administrative decision.

The appeal would be lodged before the administrative circuit of the federal courts and must be lodged with 60 calendar days from the date the reporting entity is notified of the Ministry of Finance's rejection of the grievance, or the date on which the reporting entity is otherwise proved to have admittedly been informed of the rejection.

Grounds for Appeal

As a general matter, Emirati jurisprudence provides that administrative decisions by government bodies (or civil servants) may be appealed on five grounds;

- if a decision is outside the administrative powers of the government body;
- procedural issues in that the government body does not issue its decision pursuant to the steps and procedures provided for by law (e.g. Supreme Court Case No. 146/1985);
- lack of jurisdiction whereby the government body is not the competent body to issue the decision in dispute (e.g. Supreme Court Case No. 258/1993);
- lack of reasoning whereby the decision issued does not

provide the legal or factual grounds to support its action (e.g. Supreme Court Case No. 772/2004); and

- abuse of power in cases where an administrative decision is issued in an arbitrary manner, or in a manner that deviates from public benefit (e.g. Supreme Court Case No. 89/2001).

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UAE Tax Judges: Textualism or Original Intent? (and private clarification disputes)

March 21, 2021

In comparison with general dispute practices, tax disputes are subject to a limited number of judges; three judges at the tax dispute resolution committees (TDRCs), one judge at the Tax Disputes Circuit of the Federal Primary Court, one judge at the Tax Disputes Circuit of the Federal Appeals Court, and the Chief Justice at the Federal Supreme Court.

The three judges at the TDRCs are appointed pursuant to Ministerial Decrees and serve a term of one to three years, that may be extended.

Each TDRC has an alternate judge that adjudicates disputes in place of the primary judge in case the latter is unavailable.

Each of the tax disputes circuits of the Federal Primary and Appeals Courts is headed by a judge appointed pursuant to Ministerial Decree – the first appointment having had occurred pursuant to Decisions No. 237 and 238 of 2019.

Finally, tax disputes that reach the Federal Supreme Court would be adjudicated by a panel of five judges; the Chief Justice and four judges.

What does this mean?

Other disputes in the UAE, such as construction, banking and finance, personal affairs, criminal matters, and so on may be adjudicated over by one of a plethora of judges, depending on the Emirate or court system that has jurisdiction over the dispute, the respective circuit, stages of litigation, amongst other variables.

With such a significant number and variety of judges reasoning and issuing rational over interpretations of the same provisions of law, it is relatively difficult to hone in on a particular stance that the judiciary is taking with respect to a particular law or provision.

On the other hand, because tax disputes have only begun in 2018, and due to tax disputes being heard by a limited number of judges, a tax dispute litigant (or their counsel) can develop better foresight to the persuasions of each of the TDRCs or Federal Court tax dispute circuits.

Textualism or original intent?

Tax judges have taken differing positions on readings of certain tax law provisions. The difference in rationale generally boils down to whether the interpretative approach is an explicit application of the text, or whether the judge expands the reading of the law to grant more weight to the intent of the legislator* at the time the law/provision was drafted and ratified.

*The ‘legislator’ essentially means their Highnesses the seven Rulers of each Emirate who approve Federal law, supported of course by the Ministry of Justice and the technical and legislative lawmaking committees.

A practical example for this discussion would be disputes over decisions by the Federal Tax Authority that do not have an immediate monetary value; such as a dispute over a private or public clarification as opposed to a dispute over an incorrect tax return or a voluntary disclosure.

There is a level of procedural ambiguity with respect to disputes over private or public clarifications. The Tax Procedures Law and the Cabinet Decision forming the TDRCs requires that a tax dispute litigant settle any taxes and/or penalties in dispute prior to objecting before the competent TDRC. The question becomes; what if a clarification dispute does not have an immediate monetary value (i.e. tax or penalty liability) as is generally the case?

We have seen so far different judicial interpretations amongst judges on this particular issue as to whether a dispute that has no immediate monetary value (such as a private or public clarification dispute) can be adjudicated upon.

Of the various methods of judicial interpretation; two common approaches are textualism and original intent. A textualist would look at the structure and text of the law and apply the explicit reading of a provision. Original intent applies where the judicial interpretation of a law or provision broadens the analysis into what the authors of the text intended to achieve.

Of course, the spectrum of whether an interpretation falls within either approach is extensive, but the example provided with respect to tax disputes that carry no monetary value provides a useful empiricist view within the following cases.

In one private clarification dispute in 2019, a textualist

judicial interpretation resulted in a tax judge finding that no immediate monetary value in dispute renders non-fulfillment of the requirement of settling the taxes and penalties prior to objecting and serves as grounds for rejection of a private clarification dispute on a procedural basis.

In another private clarification dispute also in 2019, an original intent judicial interpretation resulted in the finding that dispute procedures in tax laws were intended to grant avenue for adjudication of disputes vis-a-vis the Federal Tax Authority notwithstanding the lack of an immediate tax or penalty liability, also as the subject matter in dispute may ultimately manifest a tax or penalty liability in the future or in retrospect based on the tax treatment in dispute.

The difference in the method of judicial interpretation applied in these two cases draws a very practical example of how different judicial interpretation approaches could bear significantly different results, and how tax dispute litigants would benefit from understanding the nuances of tax dispute procedures and prior interpretive approaches taken by the UAE tax judiciary.

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