Introduction

Michael Kortbawi
Bin Shabib & Associates (BSA) LLP

1. Introduction

The Middle East and North Africa (MENA) has been a hub for trade and commerce throughout history, originally comprising an integral part of the spice trading routes and serving as a link to the West for the Silk Road. The overland routes through the MENA region were eventually exhausted due to the efficiency of water routes, and the region remained relatively quiet on the commercial front until the discovery of oil in the early 20th century. Over the past three decades the corporate market has re-emerged to become once again one of the most lucrative places to conduct business worldwide.

The MENA region's flourishing financial environment attracts a diverse customer base from every jurisdiction, providing businesses with expansive opportunities and profits unlikely to be achieved elsewhere in the world. The wide variety of corporate infrastructure options, the growing availability of business facilities and advantageous cost and tax structures have all made the MENA region desirable for multinational companies looking to expand into emerging markets.

The traditional structure of family businesses in the region is also evolving. Family businesses have begun expanding their infrastructure and goals to become sophisticated global players, where once they were only local entities surviving for just two or three generations. Family businesses are now attracting customers and business from around the world. Corporate governance standards in family businesses are also being developed and implemented at a feverish pace, boosting companies' profiles to compete with their international counterparts.

However, rapid regional growth also brings many challenges, particularly since legislation has not kept up with the fast-moving economic changes. Both foreign and local M&A practitioners have called for the implementation of stronger, more consistent corporate laws. There is also a need for the application of international best standards and practices in corporate transactions and corporate governance. From the outside, the MENA region appears to be rife with corruption and unpredictable regime changes. The perception is that the rule of law is applied inconsistently, and that there is little to no transparency. The region's growth has also created a steep learning curve for companies and practitioners who wish to enter and thrive in the emerging MENA marketplace. This book provides a comparative guide to M&A in 11 countries across the MENA region: Bahrain, Egypt, Jordan, Kuwait, Lebanon, Morocco, Oman, Qatar, Saudi Arabia, Tunisia and the United Arab Emirates. Each country must be viewed not only as a separate jurisdiction, but also as a dynamic part of the region as a whole.

This book is intended to be used as a comprehensive reference tool for both lawyers

http://www.pbookshop.com

and non-lawyers. It has been written to target seasoned M&A practitioners, as well as directors, shareholders and other parties who are approaching M&A transactions in the MENA region for the first time. It introduces readers to each jurisdiction's business practices and provides country-specific tips for navigating a variety of M&A options. An outline of each jurisdiction's legal system and laws ensures that both practitioners and parties to M&A transactions are made aware of compliance issues, due diligence practices and limitations on foreign ownership in every jurisdiction. The information contained herein will assist readers to make informed decisions and develop effective strategies regarding business deals in the region.

Each chapter focuses on a single jurisdiction's approach to M&A, including the legal and governmental limitations of merging or acquiring companies. The chapters are written by legal practitioners with local M&A knowledge in their respective jurisdictions. These experts have worked extensively in M&A transactions and bring a rich background that cannot be matched by practitioners who merely research local M&A transactions without having experienced the language, practical situations and cultural nuances of each jurisdiction.

The official language of each jurisdiction in this book is modern standard Arabic, which is also the official language of the regulatory and legal systems in each jurisdiction. The authors are well versed in civil law and have practised in the region for a number of years. The insider approach to each chapter allows for not only a comprehensive overview of M&A practices, but also invaluable experiences and case studies on how M&A activity is carried out in each jurisdiction. Readers can be confident that using this book will enable them to navigate the basics of each jurisdiction's specific systems in regards to M&A procedures.

The structure of each chapter includes a detailed evaluation of due diligence, merger agreements, pre-merger agreements, the scope of M&A agreements, important clauses in M&A agreements, choice-of-law clauses and dispute resolution clauses. Each chapter also includes an analysis of post-merger issues that may arise and individual case studies from past M&A transactions.

http://www.pbookshop.com

2. Legal structures in the region

Most countries in the MENA region operate under civil law systems. A civil law legal system is codified and is therefore somewhat easier to negotiate for outsiders than a common law legal system, which is based mainly on precedents. The civil law legal system in the MENA region is an amalgamation of the French legal tradition and Islamic *Sharia* laws derived from the *Quran* and the *Sunnah*. *Sharia* law is developed by Islamic scholars and leaders who make decisions by consensus regarding legal issues that are not directly addressed by the *Quran* or the *Sunnah*. The *Sharia* laws in the MENA jurisdictions are generally codified as part of the main legislative body.

This union of different judicial cultures is manifested as a dual legal structure of secular civil law courts and religious courts based on Islamic traditions. Naturally, there are nuances particular to each jurisdiction's legal system. For instance, Morocco's hybrid structure is also influenced by Jewish traditions. The legal system in Jordan contains some areas of law that still reflect the early Ottoman traditions in the region. Similarly, Bahrain's legal system also includes some traditional tribal laws

specific to that jurisdiction. Tunisia distinguishes itself in that *Sharia* law was abolished in 1956 – the *Sharia* courts were dismantled at that time, but *Sharia* law still influences some personal status areas of Tunisian law.

Saudi Arabia is the only country represented in this book that has a vastly different legal system from the others. *Sharia* law is used in Saudi Arabia, but it is not memorialised in any formal code. This can lead to uncertainty in the application and content of Saudi Arabian laws, and the lack of judicial precedent also makes legal interpretation problematic. Recognising these challenges, in 2010 the Saudi Arabian government announced its intention to codify *Sharia* law in order to provide more consistency and clarity to the rule of law.

The differences among the laws of the MENA countries make it imperative to consult with local legal advisers at all stages of a business transaction. Legal advisers should not advise on transactions in the overall region due to the specificities present in each jurisdiction.

3. Evolution of family businesses in the region

Much of the growth in the Gulf Cooperation Council (GCC) over the past 60 years has been thanks to family businesses. Today, family businesses comprise between 75% and 80% of the GCC market, fostering a healthy commercial environment.[1] Family-owned companies in the region have traditionally enjoyed limited international competition and access to vast amounts of capital and information from the surrounding area.[2] In particular, the cultural specificities of inheritance law within the GCC have allowed some companies to flourish and avoid succession disputes over the short to medium term. The typical structure of a family business allows it to circumvent many of the challenges posed by traditional models of corporate governance. However, without the continuing diligence of management, adaptation to generational changes and an adequate management succession model, many of these businesses fail to survive past the third generation.

The causes of the deterioration of a family business over time are not dependent on common factors. They are generally based on family dynamics, succession disputes, conflicting individual interests and a lack of corporate sophistication and financial planning. The two most frequent problems are the difficulties of balancing business objectives with family interests and working with the regulations in place within MENA jurisdictions.

Long-term management plans must be implemented by family businesses in order to move the company into the hands of third-generation owners. This involves not only a change in corporate governance, but also a change in the management's mindset. Most managers of family businesses are balancing business efficacy decisions against their underlying loyalty to the greater family goal. Often, these decision makers are in conflict and only a strong corporate governance model can help a business to overcome this disparity.

http://www.pbookshop.com

---

1 See www.arabianbusiness.com/family-business-focus-at-doha-conference-85044.html and www.pwc.com/m1/en/advisory/family-business.jhtml.

2 Booz&Company online report at www.booz.com/media/uploads/GCC_Family_Businesses_Face_New_Challenges.pdf.

The interaction between members of a family business is dominated by a loose relational model whereby employment contracts are vague, if they exist at all. This is completely different from the strict contractual models found in normal businesses and multinational corporations, which must be governed by such a model. Increasingly, family companies are finding that they must incorporate a hybrid model which uses elements of both relational and contractual models. This focuses on keeping the core aspects of relational interaction, but includes the safeguards of contractual relations to foster a more efficient means of dispute resolution.[3]

Despite the dominant presence of family businesses in the region, there is no legal platform that promotes the growth of such companies. Within the United Arab Emirates, the main legal framework relating to business activities is the Commercial Companies Law – a rigid body of law that lends no service to the specificities of family business. The law creates conflict for the management of family companies as they try to balance the rules of generational succession and the restrictions placed on company shareholders and owners.

4. Growth in the region

The investment of both capital and infrastructure within the MENA region has seen a significant increase over the past 50 years. With the region's population growing by almost 500% over this period, there has been a huge push for political, economic and social development. This development has primarily been fuelled by oil and has been incredibly successful at maintaining a significant level of mid-term expansion. Public spending by many jurisdictions within the region has been another driving force behind their prosperity. This level of capitalism creates an attractive climate for mergers and acquisitions.

Public sector-driven and protected industries can no longer sustain the economic growth or the job creation seen in recent years. This has led the more progressive governments, such as that of the United Arab Emirates, to stress the importance of diversifying public and private investment. The MENA governments are calling for trade and investment reforms, which historically have yielded higher growth rates than governmental funding, and moreover, trade and investment reforms also generate employment.

In order to foster investment, countries must focus on certain areas of regulation and authority, such as providing strong legal platforms, political stability, government transparency, reputable economic and financial institutions and favourable corporate tax structures. If these areas are weak, prospective investors will either demand higher returns on investment or refrain from investing entirely. Thus, it is crucial that governments cooperate with other federal institutions and business leaders to develop their economies to bring down the costs of foreign investment.

The region experienced a drop of around 35% in foreign investment in 2011, which was attributable largely to worldwide economic stagnation, but also to uncertainties created by political and social changes.

Over the past 50 years the region has seen considerable growth in infrastructure

3 Online report at www.nrf.ae/bulletin/january-2013-v1-iss4-en.pdf.

http://www.pbookshop.com

and real estate. Multinational corporations have swarmed to the region to take advantage of tax structures and, within some sectors, relaxed labour laws. Although there has been growth, there must be a continued effort to invest in areas that create jobs and to alert the rest of the world that the MENA region is an attractive investment.

5. Country particulars

5.1 Saudi Arabia

The kingdom of Saudi Arabia is an oil-rich country which attracts the business of multinational companies from all over the world.

Legal due diligence can be time consuming and difficult when conducting M&A transactions in Saudi Arabia. Little public information is available on corporate entities, and therefore the buyer must mostly rely on the seller's disclosure of corporate documents. The availability of information for due diligence depends on the target's standard of corporate governance, the management structure and the seller's willingness to cooperate with the due diligence exercise.

The typical forms of business merger in Saudi Arabia are:

- the private acquisition of shares in the target;
- the private acquisition of the target's assets and business; and
- the acquisition of shares in a joint stock company.

In Saudi Arabia, tax primarily consists of corporate income tax, withholding tax and *Zakat*, the religious levy. For local companies, tax is assessed on the share of profit of the foreign partner in the local company. Companies owned solely by Saudi and GCC nationals are subject to *Zakat*. A foreign acquirer should seek the advice of a chartered accountancy firm regarding the withholding tax implications of the payment of dividends to non-resident shareholders in a Saudi company.

Sharia is the fundamental law of Saudi Arabia and governs all contractual interactions between the parties. As stated above, the broad nature of *Sharia* law means that Saudi courts can apply broad discretionary powers in the review and interpretation of business documents. This makes the transaction process largely unpredictable in Saudi Arabia.

There is also a Saudisation policy in place which requires that in a business with 20 or more employees, at least 30% of those employees must be Saudi nationals. Foreign companies must comply with Saudisation practices in order to remain registered to conduct business in Saudi Arabia.

Foreign investment is allowed in every sector in Saudi Arabia except the following:

- exploration, drilling and production of oil and gas;
- manufacturing of military equipment;
- road transportation;
- real estate investment in Mecca and Medina;
- real estate brokerage;
- printing and publishing services;

http://www.pbookshop.com

- audiovisual and media services;
- recruitment services;
- commercial agencies and franchises; and
- fisheries.

Regarding alternative dispute resolution, Saudi Arabia has acceded to the United Nations Convention on Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention).

5.2 Egypt

The Egyptian courts and other government agencies do not use electronic or online databases and search capabilities. As a result, due diligence and information disclosure can be extremely time consuming. Certain searches require an application by the target itself or a party with power of attorney for the target. Under Egyptian banking law, the secrecy of a client's accounts and information may not be disclosed without the client's prior written approval.

Due to the leniencies of Egyptian law, the laws governing M&A agreements can be non-Egyptian if the parties so desire. However, this is valid only to the extent that such laws do not contravene Egyptian federal law or other moral and cultural rules. Usually, Egyptian law is chosen to govern such transactions to avoid any unnecessary difficulties that may arise during the proceedings.

Tax matters are generally handled by specialised tax accountants, rather than by lawyers. However, there is no capital gains tax or withholding tax on dividends for non-Egyptian tax-resident shareholders. The purchaser will not be liable for any previous unpaid taxes or tax evasion, but may be subject to the payment of sales tax.

In general, the purchaser will not be required to obtain new governmental permits, approvals or licences for the target to continue as a going concern or for the performance of its activities as conducted before the closing date. The seller will also generally continue to be responsible for all or part of the vast majority of the target's pre-closing liabilities.

There are generally no foreign ownership restrictions in Egypt, and companies can be up to 100% owned by foreigners. This allows many more avenues for foreign direct investment than other Gulf countries provide. This gives Egypt the potential to attract significant amounts of investment; however, to facilitate this, more political and economic stability will be needed.

Egyptian law regards the intentions of parties entering into contractual obligations as important in ascertaining the actions to which parties are bound. Memoranda of understanding are an integral part of the acquisition process in Egypt and are usually non-binding. That notwithstanding, there are obvious implications for engaging in activity that runs contrary to such documents. To make the process more efficient and avoid ambiguity over parties' obligations, such memoranda must specify the date on which each company is free to pursue other transactions.

The documentation involved in M&A transactions is fairly complex and will include regional and company specificities. According to general business practices, documents are usually prepared in English. However, if a government agency is in

http://www.pbookshop.com

any way involved, documents are submitted to this agency in Arabic and then translated into English. Due to the problems that arise during this process, many companies believe that a standardisation procedure should be incorporated into the M&A process. This would make Egypt more attractive for businesses wanting to engage in the process, but which are discouraged because of the lack of rigid procedural standards.

Share purchase agreements operate fairly efficiently within Egypt, with title to shares transferring automatically from the seller to the purchaser, if desired. The purchase price can be transferred to the seller in whichever currency it prefers, as there is no currency control in place.

M&A contracts will often include dispute resolution clauses. As a party to the New York Convention, Egypt recognises foreign arbitral awards as valid and binding. The only exception to a New York Convention award would be in cases where the Egyptian courts have exclusive jurisdiction. Documents that must accompany an application for enforcement of a foreign award include:

- original and authenticated copies of the agreement and the award;
- an Arabic translation of the award;
- a copy of the minutes of the issuing court; and
- a copy of notification of the award to the party against which the award was made.

The Egyptian courts also have non-exclusive jurisdiction in relation to entities or assets situated in Egypt and in respect of obligations that were, or were to be, performed within Egypt.

http://www.pbookshop.com

5.3 United Arab Emirates

The United Arab Emirates provides a unique option for companies seeking to do business within the region. All seven emirates are subject to UAE federal law, with each emirate having its own specific rules and regulations. Within Abu Dhabi and Dubai, a number of business areas are designated as free trade zones. These pockets of land are considered to be separate corporate states with respect to the laws that govern them. The free trade zones aim to provide special legal and economic platforms that the UAE federal law cannot offer at present.

With the advent of these free-trade zones, there has been an influx of multinational companies into the United Arab Emirates. Along with this influx, the legal system has had to adapt rapidly to the jurisdictional and contractual problems that have arisen.

The United Arab Emirates has developed objective market indicators which acquirers can use to value targets. This makes the valuation process efficient and helps companies through early stages of M&A deals, which often prove difficult. Confidentiality and non-disclosure agreements have also become standard practice in connection with M&A transactions.

Valuing a company can be difficult when both parties have to agree on the fair market price of the seller's goodwill. This has become more difficult in jurisdictions such as the United Arab Emirates, where there is no objective market price for the