THE PRIVATE EQUITY REVIEW

EIGHTH EDITION

Editor
Stephen L Ritchie

THE LAWREVIEWS

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This article was first published in June 2019
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Published in the United Kingdom
by Law Business Research Ltd, London
87 Lancaster Road, London, W11 1QQ, UK
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Enquiries concerning editorial content should be directed
to the Publisher – tom.barnes@lbresearch.com

ISBN 978-1-83862-013-4

Printed in Great Britain by
Encompass Print Solutions, Derbyshire
Tel: 0844 2480 112

ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following for their assistance throughout the preparation of this book:

A&L GOODBODY

ALLEN & OVERY

BAHR

CAMPOS MELLO ADVOGADOS
IN COOPERATION WITH DLA PIPER

CUATRECASAS

FASKEN

J&A GARRIGUES, SLP

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PREFACE

The eighth edition of *The Private Equity Review* follows an extremely active 2018. While the number of global private equity deals completed declined from 2017, the total value of such deals was the highest since 2007, and the third-highest of all time. Deal activity was weighted towards the upper end of the market, and included several large take-private transactions. Fundraising activity was also strong, as institutional investors remained extremely interested in private equity as an asset class because of its strong performance relative to public markets. As a result, private equity funds have significant amounts of available capital, leading to very competitive transactions being completed at increasing purchase price multiples. This has caused private equity firms to become even more creative as they seek opportunities in less competitive markets or in industries where they have unique expertise. Given all of this, we expect private equity will continue to play an important role in global financial markets, not only in North America and western Europe, but also in developing and emerging markets in Asia, South America, the Middle East and Africa. In addition, we expect the trend of incumbent private equity firms and new players expanding into new and less established geographical markets to continue.

While there are potential headwinds – including trade tensions, a slowing Chinese economy, Brexit and an eventual end to one of the longest-running recoveries in US history – on the horizon for 2019 and beyond, we are confident that private equity will continue to play an important role in the global economy, and is likely to further expand its reach and influence.

Private equity professionals need practical and informed guidance from local practitioners about how to raise money and close deals in multiple jurisdictions. This review has been prepared with this need in mind. It contains contributions from leading private equity practitioners in 25 different countries, with observations and advice on private equity deal-making and fundraising in their respective jurisdictions.

As private equity has grown, it has also faced increasing regulatory scrutiny throughout the world. Adding to this complexity, regulation of private equity is not uniform from country to country. As a result, the following chapters also include a brief discussion of these various regulatory regimes.

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I want to thank everyone who contributed their time and labour to making this eighth edition of *The Private Equity Review* possible. Each of these contributors is a leader in their respective markets, so I appreciate that they have used their valuable and scarce time to share their expertise.

Stephen L Ritchie
Kirkland & Ellis LLP
Chicago, Illinois
April 2019

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Part I

FUNDRAISING

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Chapter 21

UNITED ARAB EMIRATES

James Stull, Macky O'Sullivan and Sayf Shuqair[1]

I GENERAL OVERVIEW

Despite the financial downturn and the decline in oil prices that has recently characterised the United Arab Emirates (UAE), the country has weathered the storm and maintained its position as the centre for private equity in the Middle East and North Africa (MENA) region. It is projected that the partial recovery in oil prices in 2018, coupled with the ongoing all-out diversification drive and the recent tax reforms, will help the UAE economy to gain increased momentum in 2019. Over the past couple of years, the UAE has emerged and maintained its status as the preferred investment destination for most private equity and venture capital participants in the MENA region. This positive sentiment may in part be explained by the UAE's relatively diversified economy, and also be connected to increased concerns over economic and political factors in other leading MENA countries in the private equity arena such as Saudi Arabia and Qatar.

During the global financial crisis, Dubai, with a focus on real estate and financial transactions, was particularly hard hit, resulting in a near default on its debt payments and a subsequent bailout from Abu Dhabi. Many predicted the financial crisis would be the end of Dubai and would result in a transformative change to Dubai's free-spending and 'casino-like' culture. However, following certain significant restructurings and policy changes, Dubai has entered a period of sustainable growth, with significant projects in the tourism and real estate sectors announced in anticipation of the World Expo in 2020 – although the real estate sector has experienced sluggish growth over the past year. Abu Dhabi weathered the financial crisis by implementing a patient economic vision, buoyed by high oil prices. This approach resulted in four straight years of double-digit fiscal surpluses in the lead-up to 2015, which in turn led to massive budgets for the government to invest in mega projects, and to focus on important sectors of the economy such as healthcare and education. With an economy predominantly based on oil and related hydrocarbon revenues, the recent slump in oil prices has drastically reduced revenues for Abu Dhabi, which appears to be entering a stage of economic transition toward a more sustainable and diversified economy highlighted in the Abu Dhabi Vision 2030.

Considering the characteristics of the current landscape, governments and regulators in the wider GCC region are taking serious steps towards diversifying their economies and encouraging market competition and focusing on synergies and efficiencies. The most prominent examples have been the consolidation of several high-profile Abu Dhabi sovereign

1 James Stull is a partner, Macky O'Sullivan is a senior associate and Sayf Shuqair is an associate at King & Spalding LLP.

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entities (e.g., Mubadala Investment Company's recent acquisitions of International Petroleum Investment Company (IPIC) and Abu Dhabi Investment Counsel (ADIC)). Additionally, the financial services sector has been deemed to be overserviced in the UAE (and wider Gulf Cooperation Council countries) with 73 listed banks in the UAE and Saudi Arabia serving a population just above 50 million. This has resulted in some recent major changes in this sector, with both mergers (e.g., the recently completed merger of First Gulf Bank and National Bank of Abu Dhabi to create First Abu Dhabi Bank and the proposed merger of Al Hilal Bank, Union National Bank and Abu Dhabi Commercial Bank) and consolidations of banks (e.g., Saudi British Bank and Alawwal Bank), as well as proposed mergers of other financial institutions and insurance companies.

Investor sentiment in the venture capital and technology space has remained strong as the UAE government recently announced incentives for entrepreneurs and tech companies and it has encouraged developments in the fintech space. The most notable venture capital deals in 2018 include a US$200 million investment in car-booking service Careem by Saudi Telecom Ventures, Al Tayyar Travel Group, Kingdom Holding and Rakuten, a US$120 million investment in Property Finder by General Atlantic with participation from Endeavor Catalyst and a US$30 million investment in Wadi.com by Majid Al Futtaim Ventures. While the UAE witnessed a number of venture capital deals, neighbouring Saudi Arabia hosted the largest tech transaction: the acquisition of a minority stake in Saudi Arabian electronic payment services firm Geidea by UAE-based private equity powerhouse Gulf Capital for US$266.67 million.

Fundraising activity in the region, particularly the UAE, was hit hard by the downfall of Abraaj, which started when some of its investors, including the Bill & Melinda Gates Foundation and World Bank Group's International Finance Corporation, accused Abraaj of misusing investor money. The Abraaj situation further stifled what was already a difficult fundraising environment. Given the challenges, fund managers have had to become more creative when offering, and there have been bespoke fee structures and an increase in the popularity of the deal-by-deal approach to fundraising. This approach provides investors with more transparency and predictability and generally can be completed in a shorter time frame. Additionally, the deal-by-deal model generally features lower fees and expenses than would be featured in a larger blind-pool fund. While this method may be more labour-intensive from the perspective of a general partner, it generally results in a shorter fundraising period (as the amount being raised is smaller) and a shorter time frame for exit and payment of carry.

The slump in oil prices has taken a considerable bite out of the total market capitalisation as many of the companies listed on the stock exchanges in the UAE (NASDAQ Dubai, the Dubai Financial Market (DFM) and the Abu Dhabi Securities Exchange (ADX)) derive substantial revenues from oil production and related-energy industries. Stock exchanges in the UAE have recorded lower net profits over the past few years. In response to the new reality of decreasing oil revenues, the UAE has reformed its budget by cutting spending through a reduction in fuel subsidies and electricity subsidies. In Abu Dhabi, for example, electricity subsidies have been scaled back and water tariffs increased. To create additional income to cover the decrease in oil revenues, the government is imposing corporate taxes on onshore companies and implementing value added tax (VAT). The International Monetary Fund has hailed this decision, which it believes will strengthen the country's fiscal position. It is not expected that taxes would be imposed on companies operating in a free zone in the UAE,

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where most funds and investment managers are domiciled. Accordingly, it is not expected that the proposed taxes will have a substantial negative impact on the asset management industry in the UAE.

II LEGAL FRAMEWORK FOR FUNDRAISING

To be marketed onshore in the UAE, foreign funds (including funds established in the Dubai International Financial Centre (DIFC) and the Abu Dhabi Global Market (ADGM)) must be registered with the Securities and Commodities Authority (SCA) and offered by a licensed distributor unless the offer to an onshore investor is made on the basis of a reverse solicitation or the offer is made to certain sovereign-related entities or international bodies and organisations. Reliance on the reverse solicitation exemption is common place in the context of private equity fundraising in the UAE. In February 2017, Chairman Decision No. 3/RM of 2017 concerning Promoting and Introducing Regulations (PIRs) came into effect. Importantly, the PIRs expressly provide an exemption in relation to the promotion of foreign securities (including fund interests) onshore in the UAE based on a documented reverse solicitation. Foreign fund interests are otherwise generally not permitted to be promoted onshore in the UAE unless the promotion is to a qualified investor or the securities are registered with the SCA and an agreement with a locally licensed promoter is concluded.

On the other hand, in the DIFC and ADGM, there are no exemptions under the applicable securities laws that allow the marketing or offering of fund interests on a reverse solicitation basis. In the DIFC, a unit of a 'foreign fund' (i.e., a fund that does not meet the following criteria: (1) a fund established or domiciled in the DIFC or (2) a fund established or domiciled in a jurisdiction other than the DIFC and is managed by a fund manager who is licensed by the Dubai Financial Services Authority (DFSA)) may only be offered or sold in or from the DIFC by a firm duly authorised by the DFSA to carry out those activities. Similarly, in the ADGM there is no reverse solicitation exemption and the marketing or offering of fund interests to investors in the ADGM may only be carried out by an entity licensed by the Financial Services Regulatory Authority (FSRA) to carry out that activity. Given the flexibility provided by the reverse solicitation exemption onshore in the UAE and the preponderance of investors being located onshore, it is commonplace for most fundraising to be carried out physically onshore in the UAE as opposed to in the DIFC or the ADGM.

There are few private equity investment funds that are domiciled onshore in the UAE. This is primarily due to an onerous licensing process (for both the manager and the fund) some concerns regarding the clarity and predictability of the legal regime, and the costs (relative to the DIFC and the ADGM). The ADGM was launched in 2015 to encourage foreign investment by offering foreign businesses attractive concessions and a number of investment incentives, including a zero per cent tax rate and the ability to own a 100 per cent subsidiary (foreign ownership restrictions apply outside the free zones). The ADGM is still in its infancy and is therefore not currently a preferred jurisdiction for investment funds. However, efforts are being made to help grow the jurisdiction as an asset management centre such as reductions in fees payable by firms looking to establish a presence in the ADGM. Private equity funds established in the DIFC, however, are more commonplace and are typically structured as investment companies and limited partnerships, both of which have separate legal personality under law. Private equity funds in the DIFC are generally established as either 'exempt funds' or 'qualified investor funds'. Both classifications require that the fund be offered to professional clients only and the offering be made by private

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placement only. The qualified investor fund regime was introduced to provide a lower cost and less regulated alternative to the exempt fund. Fund managers of qualified investor funds are exempt from many of the detailed requirements applicable to exempt funds. While exempt funds must have a minimum subscription amount per investor of US$50,000, qualified investor funds require a minimum subscription amount per investor of US$500,000. Until 18 December 2018, the DFSA imposed limits on the number of investors in the various categories of regulated funds (i.e., public funds had to have a minimum of 100 investors, exempt funds could have a maximum of 100 investors and qualified investor funds could have a maximum of 50 investors). These limits were recently abolished, giving managers additional flexibility when establishing and offering funds in the DIFC. Other amendments to the funds regime adopted in December 2018 include the concept of open-ended real estate funds and private REITs, which may be attractive to real estate private equity managers.

All UAE-based managers owe a level of fiduciary obligations to investors in funds that they manage. An SCA-regulated manager is required by law to manage the fund in a 'manner that preserves the rights of the fund and its holders'. The manager may not obtain any 'special gains or privileges' from the fund other than the agreed disclosed fees. Additionally, the manager must 'exert due care' in the performance of all tasks. In the DIFC and the ADGM, the fund manager must, among other things, manage the fund, including the fund property, in accordance with the fund's constitution and its most recent prospectus; perform the functions conferred on it by the fund's constitution and applicable laws; and comply with any conditions or restrictions imposed by the DFSA or the FSRA (as applicable) including those on its licence or in respect of the fund. In exercising its powers and carrying out its duties a fund manager is required, among other things, to do the following:

a act honestly;
b exercise the degree of care and diligence that a reasonable person would exercise if he or she were in the fund manager's position;
c act in the best interests of the unitholders and, if there is a conflict between the unitholders' interests and its own interests, give priority to the unitholders' interests;
d treat the unitholders who hold interests of the same class equally and unitholders who hold interests of different classes fairly;
e not improperly make use of information acquired through being the fund manager to gain an advantage for itself or another person; or
f not cause detriment to the unitholders in the fund.

These duties can be expanded in the fund's constitutional documents. However, the relevant statutory duties cannot be reduced or removed.

III REGULATORY DEVELOPMENTS

Primary responsibility for overseeing the licensing, regulation and marketing of investment funds was transferred from the UAE Central Bank (the Central Bank) to the SCA, with the SCA confirming the implementation in the UAE of a 'twin-peaks' model of financial services regulation and supervision. Under this model, the Central Bank remains responsible for systemic stability, prudential oversight and monetary policy, while the SCA is responsible for conduct of business matters (including consumer protection and financial markets oversight). Any firm (whether based inside or outside the UAE, including free zones in the UAE) that intends to conduct investment management activities in the UAE outside a free

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zone must obtain a licence from the SCA prior to conducting those activities. In the DIFC and the ADGM, the DFSA and the FSRA respectively have regulatory authority over private equity funds and their managers in those jurisdictions. Fund managers are required to make accounts, records demonstrating compliance with the relevant laws and regulations, and delegation and outsourcing agreements available to the DFSA and the FSRA for inspection.

On 27 November 2018, the SCA and the regulators in the UAE's two main financial free zones – the DFSA of the DIFC, and the FSRA of the ADGM – announced that they had reached an agreement to facilitate the licensing of funds domiciled in each other's jurisdictions. While the agreement does not create a passporting regime across all products and services between the DIFC, the ADGM and the rest of the UAE, it implements a passporting regime for the promotion of domestic funds across the two jurisdictions. This announcement bolsters the efforts of each regulator in the area of investment funds and is expected to encourage the development of the domestic fund markets across the wider UAE.

Under the proposed new arrangements (which only apply to locally domiciled funds and do not apply to the marketing of foreign funds), DIFC-authorised firms that currently use an SCA-authorised distribution agent to distribute units of DIFC-based funds in the UAE outside the DIFC may decide instead to follow the proposed passporting regime and market and distribute the units themselves. A fund manager of a DIFC-domiciled fund can follow the passporting regime and, subject to satisfying certain requirements, the fund would then be registered by the DFSA, which will notify the other regulators, namely the FSRA or the SCA. The FSRA or the SCA will then include the fund on their own register of funds. Similarly, the FSRA issued a consultation paper outlining its proposed changes to the ADGM's regulations and the FSRA rulebook. As with the DFSA's proposed changes, the FSRA's proposed amendments enable both public and private ADGM-domiciled funds to be registered for passporting through the same register of passported funds mentioned above, and to be marketed by an FSRA Authorised Person in either the DIFC or territory regulated by the SCA without obtaining an additional licence.

Historically, the UAE has been a tax-free jurisdiction. However, in October 2016, the UAE federal law establishing the UAE Federal Tax Authority (FTA) was issued. The FTA has been tasked with oversight over taxation in the UAE and, in particular, the implementation of the newly introduced VAT at a rate of 5 per cent, which became effective in January 2018. This has had an effect on advisers and managers of local funds as payments to local service providers are subject to VAT. Notwithstanding the introduction of VAT, the following taxes are not applicable in the UAE: withholding tax, corporate tax, personal income tax and capital gains tax. Oil, gas and petrochemical companies and branch offices of foreign banks are, however, required to pay taxes. Entities established in the DIFC and the ADGM and their employees are subject to a zero rate of tax (income tax, corporate tax, withholding, capital gains, etc.). It is not expected that the new proposed taxes will be assessed on free zone entities. Therefore, it is hoped that the tax regulations will have a negligible effect on the asset management industry in the UAE.

Additional developments that were welcomed in 2018 include the signing of memoranda of understanding between the Dubai Land Department (DLD) and each of the DIFC and the ADGM, pursuant to which DIFC and ADGM companies are permitted to own real estate in Dubai, subject to satisfying certain conditions and requirements. Historically, the DLD has limited types and jurisdictions of corporate vehicles that could own real estate assets in Dubai to (1) ensure legal and beneficial ownership of certain real estate assets were held only by UAE nationals and (2) enforce and simplify the collection of transaction fees

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on direct and indirect transfer of real estate assets. DIFC or ADGM companies seeking to acquire real estate in Dubai must first obtain a non-objection certificate from the DIFC authorities or a certificate of incumbency from the ADGM authorities. The DIFC or ADGM authorities will be required to determine the direct and indirect shareholders of the applicant entity and will report to DLD with any changes to the shareholding structure and require the approval or non-objection of the DIFC or the ADGM in relation to the issuance or transfer of shares and payment of fees, with certain exceptions provided under specific circumstances.

IV OUTLOOK

Despite the challenges posed by geopolitical and global economic factors, stakeholders remain optimistic about the private equity terrain in the UAE. Against the backdrop of a financial downturn and the decline in oil prices that characterised 2017 and part of 2018, the UAE has shown its resilience. It has proved that its economy operates outside the oil and energy sectors, and that it has the infrastructure to maintain and grow its private equity and the wider asset management industry. The introduction of VAT in the UAE marks the implementation of a strategy aimed at augmenting and diversifying government revenues. Persistent low oil prices over the past three years has created an urgent need to diversify revenue streams through measures such as taxation. Regional and international participants in the venture capital and private equity arena see the UAE as the logical regional centre for their industries, with Dubai serving as the hub. In an effort to stimulate the investment funds industry, asset managers in the DIFC and the ADGM can now benefit from the newly introduced passporting regime, and real estate asset managers can start targeting onshore Dubai real estate assets for their various products. Fundraising is becoming more challenging with negative perceptions (particularly on the part of investors outside the region) of current regional geopolitical factors and following the recent collapse of Abraaj, long seen as the country's leading asset manager. Consequently, general partners are continuing to explore alternative means of fundraising and limited partners are more willing to consider direct or co-investment options as preferred alternative to blind pool investing.

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Appendix 1

ABOUT THE AUTHORS

JAMES STULL

King & Spalding LLP

James Stull is a partner at King & Spalding LLP. His practice covers a broad range of corporate, finance and investment matters. He primarily focuses on asset management and the formation of investment funds, including venture capital funds, private equity funds, real estate funds, credit and debt funds, hedge funds and shariah-compliant funds. His practice includes advising domestic and international clients on the corporate and regulatory aspects of structuring, establishing and liquidating various fund structures, and he has substantial experience with securities regulations in the UAE, Saudi Arabia and other Middle East jurisdictions, as well as in the United States.

MACKY O'SULLIVAN

King & Spalding LLP

Macky O'Sullivan is a senior associate at King & Spalding LLP. Mr O'Sullivan mainly advises clients on financial services regulation, investment funds and cross-border mergers and acquisitions. He has represented and advised clients on a broad range of corporate and investment fund matters, including the formation of and investment in conventional and shariah-compliant investment funds.

SAYF SHUQAIR

King & Spalding LLP

Sayf Shuqair is an associate at King & Spalding LLP, based in the firm's affiliated Riyadh office. Mr Shuqair mainly advises clients on the structuring, formation and governance of various types of investment funds, including private equity, venture capital and real estate investment funds, and also generally advises clients on innovative corporate and investment structures. He also advises clients on private equity, capital markets and real estate transactions in the UAE and Saudi Arabia.

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ISBN 978-1-83862-013-4

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