

Foundations in the Middle East

General Overview

The passing of wealth from one generation to the other with a public benefit has been done in the Muslim world since the times of Prophet Mohammed in the form of Waqfs, the Islamic form for an endowment. It has been typically done with a donation of buildings, schools and land for public use. Many of the ancient mosques are administered by Waqfs which take care of these institutions for centuries. They are mostly done for charitable purpose.

The same is applicable for foundations which were originally mostly used for charitable purposes. Nearly hundred years ago, Liechtenstein started to allow the use of foundations for other purposes which was instrumental in making Liechtenstein a centre for legacy planning.

In 1995, Panama copied this successful instrument and issued its own foundation law and managed within just a few years to become the leader in setting up foundations. Subsequently this was copied by common law countries which issued their own "common law foundations". This trend has now also reached the Middle East where the two financial centres, Abu Dhabi Global Market (ADGM) and the Dubai International Financial Centre (DIFC) issued their adapted foundation laws on a common law basis. In addition Ras Al Khaimah another Emirate of the UAE also joined them and introduced their own foundation law under RAK ICC.

However, to obtain a permission to set up a charitable organisation or a NGO (non-profit organisation) in the Middle East to receive donations can be a rather challenging task in lengthy proceedings. The reason being that in the last 30 years "charitable" organisations were occasionally used to collect money for extremist activities. This might be the reason that the ADGM concept excludes charitable purposes for a foundation. The DIFC foundation regime on the other hand does not have such an exclusion.

Trusts – Foundations – Waqfs

Foreign trusts and foundations have been regularly set up for High-Net Worth Individuals (HNWI) in the Middle East. But the demand for such entities was never as high as in western countries. A main reason is the absence of taxes in the Middle Eastern countries. There were also attempts to adapt the old concept of Waqfs to achieve the same as with trusts or foundations. However, these efforts have never been very successful.

Since 2005, it is possible to set up DIFC Trusts. But the demand has been rather subdued. Some assume that Arabs are closer to civil law and therefore would prefer using the similar concept of foundations. This was a reason for the ADGM to introduce in 2017 a foundation law which was followed by the DIFC in 2018 and by RAK in 2019.

UAE Foundations became quickly popular. Generally speaking, foundation regimes provide more flexibility with regards to the powers of the founder. Foundations having their own legal personality may offer advantages in the management of the operations, and they are more widely accepted in civil law jurisdictions, where trusts may face ownership restrictions.

We see that a major demand is coming from Muslims who cannot register a Will for their UAE assets. But with a foundation they have the possibility to distribute assets without taking into consideration the Shariah inheritance rules, where for example daughters only receive half of what a son would receive. Up to now the UAE foundations can only own property in their own Emirate.

Advantages of UAE Foundations

Anybody who has set up trusts or foundations for Middle Eastern clients knows that most HNWI's who have accumulated substantial wealth in the last few decades do not like to relinquish the control over their wealth. This is a main reason why the interest in the concepts of trusts and foundations has been very limited. This is most probably the reason why the ADGM as well as the DIFC foundation, which target above all people from the Middle East region, allow that the founder still has an influence over the assets devoted to the entity. This represents a major deviation of the original (Western) foundation concept where a person separates completely from his or her assets transferred and therefore subsequently places it irrevocably in a foundation.

The assets are then solely administered and managed by the foundation council in accordance with the foundation charter and by-laws. If such an ADGM, DIFC or RAK ICC foundation will ever be challenged in a Western court, it is to assume that the judge will come to the conclusion that the founder still has control over it and therefore is also liable / taxable for the assets.

The ADGM and DIFC foundation are also managed by a foundation council (at least two members) and, as in other foundation jurisdictions, a guardian / protector can supervise it. They can either be individuals or corporate entities. The ADGM offers more privacy in this respect as the council members are not publicly available.

Migration of Foundations

A main attraction for the UAE is the concept that the foundation law allows the migration of foundations from other jurisdictions to this country where no tax is imposed (besides a VAT of 5%), where anybody is welcome to take up residency (90% of the population is foreign) and which has a well-developed infrastructure to accommodate underlying companies.

It is straight forward and inexpensive to setup a foundation in the UAE. It can also be done through portals and a physical submissions of the documents is not necessary. The founder can set it up without the help of a registered agent. However, each foundation needs to have a registered office address in the jurisdiction, which can be provided by any company based in that free zone.

Are UAE Foundations an alternative to other Jurisdictions?

Since the 80s it has become essential that the founder of a foundation separates from the assets which he or she placed in the foundation and that there is no control over it so that courts could not come to the conclusion that the founder has still control over the assets. This has become very important to avoid that a court considers the foundation a sham.

However, the UAE foundation has the flexibility that the founder can maintain a certain control over the foundation. This flexibility has been included to make it attractive for the people in the Middle East. But at the same time it might be a reason for people from other jurisdictions to abstain from using such a foundation.

But an exception could be if such a foreign person has assets in the UAE which he or she would like to place in a UAE foundation as foreign foundations cannot own property in the UAE and major restrictions would apply for owning assets of local UAE companies.

Summary

Within 3 years the UAE foundations have become quite popular in the UAE and are mostly used for holding UAE assets. Many Muslims for whom DIFC Wills are not an option see its advantages in wealth structuring, succession and estate planning. For holding assets in other jurisdictions it is advisable to use entities from other countries which have a long tradition and track record, as the UAE foundations bear the risk that they might be considered shams by courts in the western world.

In any case it is advisable to get some general guidance in it. The lawyers of the Swiss Group, who already in the 80s established foundations and trusts for clients in the Arab world, have the necessary knowhow and experience to handle also complicated situations.

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Swiss Group is an international group specialized in corporate, management consulting and legal advisory, composed of the two companies Swiss ILC Services DMCC based in Dubai and Swiss International Legal Consultants Ltd based in Abu Dhabi. We offer to our clients a wide range of comprehensive and practical advice to navigate through the legal and administrative pitfalls in the UAE, providing support in setting up a presence or taking up residence in the United Arab Emirates while also planning and setting up the appropriate structures. Our international team of qualified practitioners, lawyers, accountants and business consultants who speak 8 different languages under Swiss Management combines expertise and capability with an intimate and profound knowledge of the local requirements in the Middle East since the 1970s.

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