

DIFC Foundations Law

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Jurisdiction : Dubai International Financial Centre

Overview

The DIFC Foundations Law DIFC Law No. 3/2018 (the Foundations Law) has taken the best of the different Common and Civil Law legislations on foundations and blended it in one unique law.

Amongst the innovations in the Foundations Law are:

- The DIFC Courts have the power to set aside transactions for mistake, along the lines of the jurisprudence which developed in England following the decision in *Hastings-Bass-v-IRC* [1974] 2 All ER 193 (*Hastings-Bass*) prior to its limitation by the decisions of the Supreme Court in *Pitt v Holt* [2013] UKSC 26 and *Futter v HM Revenue and Customs* [2013] UKSC 26 (Foundations Law articles 50-52).
- The capacity to compulsorily settle intra-Foundation disputes by arbitration (Foundations Law articles 54-55).
- Re-domiciliation of foundations (Foundations Law, articles 57-61), available also in the ADGM (ADGM Foundations Regulations 2017 articles 32-36) but not in the QFC.
- Recognition of foreign foundations (Foundations Law, article 65).
- Conversion of DIFC private companies to DIFC Foundations (Foundations Law, article 66) which is available to any company whose domestic law permits its domiciliation to the DIFC as a preliminary step since the DIFC Companies Law DIFC Law No. 2/2009 permits that (DIFC Companies Law, articles 144-150.)
- Provisions for depositary certificates within DIFC Foundations are modelled on the Netherlands STAK (being the abbreviation in Dutch of “Stichting Administratiekantoor”) practice.

Definitions

- *DIFC Foundations Law*: The DIFC Foundations Law DIFC Law No. 3/2018.
- *DIFC Foundation*: A foundation whose governing law is DIFC law.
- *DIFC Trust*: A trust whose governing law is DIFC law.
- *DIFC Courts*: The Courts of the DIFC.

Practical Guidance

The concept of the foundation

A foundation is an entity with a legal personality. As a result, it can own property in its own right. This is the case of the DIFC Foundation.

The DIFC Foundation does not follow the traditional notion of a foundation as a “dedicated fund appropriated to a specified purpose” (which derives from the Germanic *Zweckvermögen* tradition, as for instance found in article 552(1) of the Liechtenstein legislation). Notwithstanding the precedent, the two requirements of “capital” and “object” (see article 12 Foundations Law) are necessary for the creation of a DIFC Foundation.

For foundations the usual principles of private international law, will apply the law of the place of establishment (or domicile) to determine whether or not a foundation has corporate personality, with the result that the recognition of the DIFC Foundation as a legal entity outside the DIFC will be automatic.

Analogues of foundations – trusts

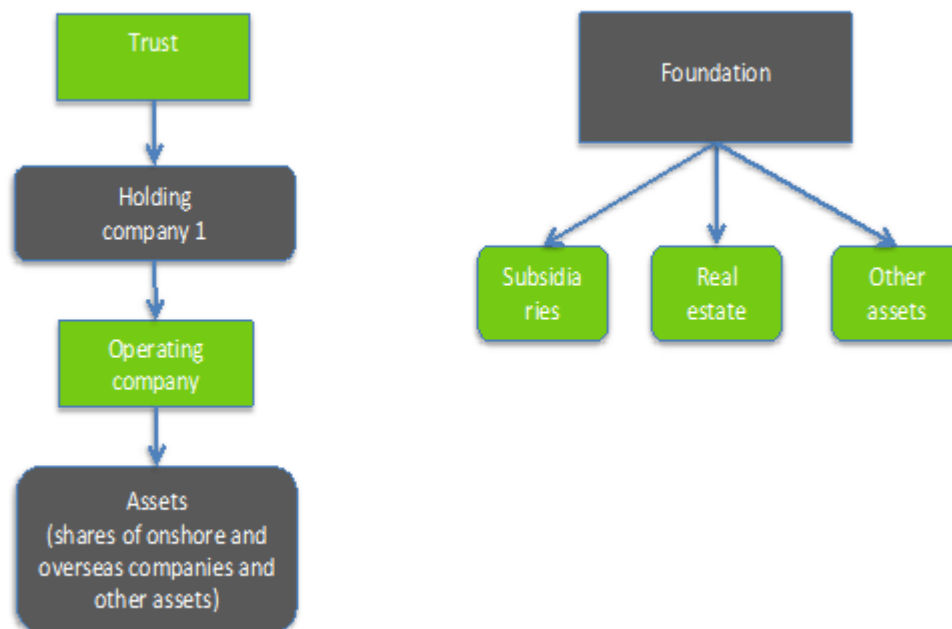
A trust is a relationship, not an entity.

In principle, the location of the trust assets is irrelevant.

Foundations have a comparable outcome in private international law terms. The rights of parties inter se are determined in accordance with governing law in the courts of domicile of the foundation.

Some uncertainty exists as to tax treatment of foundations in Common Law countries, but such little authority as exists supports corporate treatment, *Canada v Sommerer* 2012 FCA 207 highlights this point.

Use of trusts and foundations



Why a foundation or a trust?

Corporate structures are inherently inflexible.

Family member share ownership means that although the worst consequences of fractional interests are avoided on death of a founder, the potential for disruptive disputes remains.

It is very difficult to engraft family governance structures onto companies as shareholder agreements usually only bind signatories.

Sham

This is applicable to companies, trusts and foundations but in different ways.

For companies and foundations, the question is whether they acted beneficially or as agent/nominee.

For trusts the question is whether or not they exist at all, and the consequence of their non-existence.

Sham will usually involve tax evasion (as could non-compliance with attribution regimes where there is no sham).

Revenue authorities are likely to be looking for indications of sham, Sharia courts may also look for this.

Is a foundation or a trust appropriate to family needs? – Questions to consider

- Does the family understand the legal consequences of the structure?
- Is the family prepared to accept these consequences and live with them?
- Do those involved in its establishment understand the legal consequences of structure?
- Are they prepared to comply with and implement them, even if individuals prefer otherwise?
- Is everyone prepared to give evidence about it?
- Will there be scrupulous onshore compliance?

The favourable regime of DIFC Foundations with respect to mistake

Article 50 - 52 of the Foundations Law correspond to the doctrine of equitable mistake and improper deliberation (formerly known as the Hastings-Bass rule in UK trusts law). The Foundations Law provisions relating to the Hastings-Bass rule are modelled on the [Jersey Trusts Law \(https://www.jerseylaw.je/laws/revised/Pages/13.875.aspx\)](https://www.jerseylaw.je/laws/revised/Pages/13.875.aspx) as of 2013. Article 50 of the Foundations Law deals with the general possibility to avoid, upon review and decision of the DIFC Courts, a transfer/disposition of property, but only if the mistake was sufficiently serious enough to render it just for the DIFC Courts to do so.

Compulsory arbitration

Article 54 and 55 of the Foundations Law set out the option of alternative dispute resolution (ADR). Arbitration can be made compulsory, either through the Charter, by-laws, or via a separate arbitration agreement.

A major hindrance to the enforceability of an arbitration clause in a classic foundation is the fact that the beneficiaries are usually not part to the agreement. However, article 54 of the Foundations Law expressly addresses that issue and binds any party in relation to the foundation to an eventual arbitration outcome.

Domiciliation of DIFC Foundations

Article 57 to 61 of the Foundations Law provide for the domiciliation of a foreign foundation by providing for it to be “continued” as a DIFC Foundation. The procedure relies on the grant of a Charter of Continuance (similar to that in the [St Kitts Foundations Act \(http://www.ilo.org/dyn/natlex/natlex4.detail?p_lang=en&p_isn=92711\)](http://www.ilo.org/dyn/natlex/natlex4.detail?p_lang=en&p_isn=92711) of 2003).

This might be interesting for families looking to relocate their already existing (family) foundations into the DIFC and thus allowing them to continue their original foundation as a DIFC Foundation, granting them all the legal advantages and flexibility of a DIFC Foundation. However, this is provided that the jurisdiction in which their original foundation is located does not deem such a domiciliation as a dissolution/liquidation event (Malta and Cyprus seem to allow such a domiciliation without triggering a dissolution/liquidation event) and that such a domiciliation does not trigger any exit taxes with respects to the assets of the original foundation (to be analysed on a case by case basis).

Recognition of foreign foundations

Article 65 of the Foundations Law permits a foreign foundation, which wishes to operate in the DIFC without applying to be domiciled, to do so by applying for registration. A recognised foreign foundation may not carry out any commercial activities, except those necessary for, and ancillary or incidental to, its objects.

This provision ensures that foreign foundations can operate in the favourable and stable business environment of the DIFC, should for instance their home jurisdiction not permit a domiciliation to the DIFC.

Conversion of a DIFC Company into a DIFC Foundation

Article 66 - 69 of the Foundations Law provide the possibility for a DIFC company to be “continued” as a DIFC Foundation. The procedure is similar to that applicable to a foreign foundation seeking to be re-domiciled in the DIFC under articles 57 - 61 of the Foundations Law. The procedure is not available under most foundations legislations.

Depositary certificates

Article 30 of the DIFC Foundations Law allows for the issuance of depositary certificates “representing specific rights to payment quantified by reference to specific parts of the property owned by the Foundation or relating to other rights or interests, whether present or future, to which the Foundation is or might be entitled.”

The Foundation retains full ownership of the relevant assets (such as shares in an underlying company) but all the economic benefits (such as dividend payments) are passed on to the certificate holders.

Related Content

Legislation

DIFC

- DIFC Foundations Law DIFC Law No. 3/2018
- DIFC Companies Law DIFC Law No. 2/2009

ADGM

- [ADGM Foundations Regulations 2017](http://adgm.complinet.com/en/display/display_main.html?rbid=4503&element_id=19329)
(http://adgm.complinet.com/en/display/display_main.html?rbid=4503&element_id=19329)

Jersey Legislation

- [Jersey Trusts Law as of 2013](https://www.jerseylaw.je/laws/revised/Pages/13.875.aspx) (<https://www.jerseylaw.je/laws/revised/Pages/13.875.aspx>)

St Kitts Legislation

- [St Kitts Foundations Act of 2003](http://www.ilo.org/dyn/natlex/natlex4.detail?p_lang=en&p_isn=92711) (http://www.ilo.org/dyn/natlex/natlex4.detail?p_lang=en&p_isn=92711)

Case decisions

- [Hastings-Bass-v-IRC \[1974\] 2 All ER 193](http://swarb.co.uk/re-hastings-bass-hastings-v-inland-revenue-ca-14-mar-1974/) (<http://swarb.co.uk/re-hastings-bass-hastings-v-inland-revenue-ca-14-mar-1974/>)
- [Pitt v Holt \[2013\] UKSC 26](https://www.supremecourt.uk/cases/docs/uksc-2011-0091-judgment.pdf) (<https://www.supremecourt.uk/cases/docs/uksc-2011-0091-judgment.pdf>)
- [Futter v HM Revenue and Customs \[2013\] UKSC 26](https://www.supremecourt.uk/cases/docs/uksc-2011-0091-judgment.pdf)
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- LL.M, University of Queensland, Brisbane, Australia
- LL.B, University of Queensland, Brisbane, Australia
- B.A, University of Queensland, Brisbane, Australia

Biography

- David was admitted as a solicitor in 1974, and was first called to the Bar in 1977.
- David is admitted to practise in Australia, England and Wales (where he is a member of Lincoln's Inn), the Courts of the Dubai International Financial Centre, New York (Legal Consultant), New Zealand, the Singapore International Commercial Court and Papua New Guinea. He was first appointed Queen's Counsel in 1986.
- David has lectured at the University of Sydney for the Master of Taxation course, the University of Queensland for the Master of Laws course and served as an Adjunct Professor of the University of Queensland. He is the co-editor of the Oxford University Press Journal *Trusts & Trustees*.
- He was the inaugural Chairman of the STEP International Client Special Interest Group, a director of STEP (and, for 2018, Deputy Chair) and a member of its World Wide Council and various Committees, a co-chair of the United Arab Emirates Chapter of the International Section of the New York State Bar Association, and a member of the Executive Committee of the Section, an Academician of The International Academy of Estate and Trust Law, a Member of the Middle East and North Africa Branch Committee of the Chartered Institute of Taxation (UK), a member of the Worshipful Company of Tax Advisers, a Freeman of the City of London and an Honorary Member of the Taxation Institute of Hong Kong. From 2016, he has chaired the DIFC's Wealth Management Review Working Group.
- In 2010, David was awarded the Order of the Rising Sun (with Gold Rays and Neck Ribbon) for his services to Australia-Japan relations. In 2012, he was appointed a Member of the Order of Australia for, among other things, "service ... to taxation law and legal education".

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- Maîtrise, Université Paris I Panthéon-Sorbonne, Paris, France
- Magister Legum, University of Cologne, Cologne, Germany

Biography

- Christophe was first admitted as a lawyer in 2008 in Luxembourg.
- Christophe is a dual French and German citizen and admitted to practise in Luxembourg, Paris and New York.