



STARTUP PANORAMA

EDITION 9.0

A GUIDE TO LEGALITIES FOR STARTUPS IN DUBAI AMID COVID-19
































دبي للمشاريع الناشئة

DUBAI STARTUP HUB

AN INITIATIVE OF DUBAI CHAMBER OF COMMERCE & INDUSTRY

Relief and support measures for startups and SMEs

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NAVIGATING COVID-19 MARKET CONDITIONS

Startup Panorama Edition 9.0 features practical advice from legal experts on how founders can navigate their existing contractual obligations in the short term and beyond COVID-19 times. From how to manage short-term liabilities, implement cost-cutting measures, reduce risks and rethink operating models, to dealing with cash flow disruptions, the pressures of reduced demand, and preparing well for the post-coronavirus phase - read on for some proactive responses to timeless business challenges.

OLD CONTRACTS, NEW MODELS

Companies from nearly every industry have overnight, in varying degrees, had to adjust their way of working as the UAE and countries across the world imposed distancing measures and movement restrictions to control the pandemic.

"COVID-19 has forced many businesses to move to an online operating model," **Simon Bryan**, Principal at Global Legal Solutions Group, says. "**Turning an analogue business into a digital business is not necessarily complicated** but nevertheless it needs to be done correctly and in accordance with the law."

Businesses that are making this transition need to ensure that their legal and operational structures are properly set up to support their day-to-day activities, he adds, such as transacting via e-commerce, customer contracts, supply chain management and logistics. Online privacy and data protection also need to be taken into account.

Lara Barbary, Partner at BSA Ahmad Bin Hezeem & Associate LLP, adds that all customers must be kept updated about



Simon Bryan, Principal at Global Legal Solutions Group

the business model to meet a new manufacturing or service need," he says. "The business terms and conditions of sale and use should be reviewed and amended accordingly as the need arises."

Some local manufacturers are also adjusting their businesses to accommodate the production of supplies currently in need, such as hand sanitizer, ventilators and face masks. "They, however, need to consider the long-term impact of the supply and distribution agreements entered not to mention the standards that must be adhered to," Barbary says. "The liability the business may be subjected to and the restrictions imposed or permits required must all be taken into consideration."

The BSA expert further advises companies to take measures to protect their supply chain operations by reviewing and re-negotiating their existing contracts with vendors and suppliers to avoid cancellations or postponements.

products or services in a timely manner. "Many businesses have looked at taking their services online for instance such as gyms now providing online fitness classes or maybe through renting out their equipment, restaurants and cafes moving to home delivery of meals, and even adjusting

"It is imperative that businesses promptly document reasons for any failure to perform contractual obligations or difficulty faced in doing so," he says. "The companies may be able to pursue force majeure in cases where it is impossible for them to perform a contract. It is recommended that any audit of contracts or review is done by the legal in-house team and/or a reputable specialized legal firm to mitigate further complications."

Barbary says companies should ask their debtors to send proposals on how they intend to pay. "This will serve as an acknowledgement of the claim and by doing so, the debtor confirms that he owes the entire outstanding claim to a company. In this way the company will have legal recourse against its debtors and may be able to make recoveries."

Businesses also need to check their insurance policies for any applicable business disruption event insurance, he says.

If execution of contractual obligations is arguably impossible due to the COVID-19 situation, **Jaanine De Keersmaecker**, Counsel at Argentum Law, says SMEs may consider relying on the "hardship doctrine" - Article 249 of the UAE Civil Code - to push for renegotiation of the agreement and a re-balancing of rights and obligations or as grounds to suspend performance or terminate the agreement.

Force majeure, widely known as the "Act of God" clause, refers to a clause that is included in contracts to remove liability for natural and unavoidable catastrophes.

CASH FLOW MANAGEMENT

Barbary recommends businesses actively evaluate their cash flow requirements and develop appropriate actions under various scenarios. "Cash flow management is critical, especially if the existing income and trade has been significantly disrupted by COVID-19," he says. "Apart from restrictions imposed by government, the ability to trade through this period, pay outstanding debts, keep employees or meet existing leasing or loan repayments will be determined by the SME's financial position."

Barbary says **solutions that can help release cash to cover a business day-to-day expense include tapping into comprehensive relief packages offered by banks in Dubai to ease the financial pressure on their customers, approaching lenders to refinance existing loan obligations, or seeking fresh financing.** "Another option is to approach private equity firms who with their extensive investment and portfolio management expertise may be well positioned to partner with such SMEs and support them."

In addition, Barbary advises auditing all transactions as well as monitoring and expediting accounts receivables. "In a downturn, some customers will delay payment and some will default, whereas others may dispute charges. Now is the time to monitor these things closely and come up with a plan for how to deal with issues that may arise. Firms should also encourage customers to pay faster and may offer prompt but careful payment discounts. [Meanwhile] Contact the biggest suppliers and negotiate for lower prices. Consider entering a longer-term agreement with them in exchange for lower prices. Selling assets and then leasing them back is one way to raise emergency cash. Cutting



Lara Barbary, Partner at BSA Ahmad Bin Hezeem & Associate LLP

reduction through judicial intervention, De Keersmaecker says. "In case your revenues have dropped to a level where you are unable to pay the rent due to COVID-19, assess your rights to whether you may suspend your obligations or terminate the agreement based on force majeure with the assistance of legal counsel," she explains.

Barbary adds that companies could reference the total lockdown, the stringent operating restrictions for all commercial enterprises, decreased footfall, decreased permitted capacities, reduced operating hours, reduced sales and income, and new operating procedures, which also include increased hygiene and sanitization requirements.

"Also, reference can be made to the fact that the business has not been able to generate any income during the closure period, notwithstanding which, the business has still incurred ongoing expenses including loan repayments for insurance, utilities, purchases, and salaries, the repayment of which were to be

or reducing marketing programs may provide additional relief."

Clients who have a somewhat sufficient cash flow "must not be complacent", he says. "If they still have [the] ability to tap on loans, they should do so."

SMEs can also consider use of the hardship doctrine to obtain a rent

funded by the income that was anticipated which has not been realized," he says. "It is better for landlords to negotiate a fair relief with tenants in order to avoid the risk of going to courts which they will not have a control over, and which may not fit their cash flow needs."

Bryan suggests founders manage issues with creditors by being honest with both themselves and their counterparties. "Be proactive," he says. "Do not do nothing or ignore it and wait until the situation is beyond recovery. Many counterparties will respond positively to businesses who are not trying to ignore or avoid their obligations. Doing nothing invariably only makes things worse. [And] seek professional help. Consider speaking to your bank, shareholders or investors, and also do not wait to speak to advisors including lawyers."

SMEs may consider requesting waivers of defaults if they can give lenders sufficient comfort that their business will continue running, De Keersmaecker adds. "Remind customers [and] suppliers that this will pass and that treatment will not be forgotten," she says. "Ultimately, it is in the interest of the lender that the business survives."

Meanwhile, she also recommends developing routes to alternative suppliers, and taking advantage of deals and discounts currently on offer. And similarly placed companies in a sector can consider aligning purchase requirements, for example, by establishing shared resource pools, which is an approach companies in China have used in the past in times of crisis. "COVID-19 is a time of unprecedented crisis, but it also presents an opportunity to stress-test the resilience of your business, your relationships with your customers, shareholders, officers, directors, counterparties and lenders," De Keersmaecker says.

CO-FOUNDER RELATIONSHIPS IN CURRENT TIMES

In 2013, Jonathan Hefter, CEO of New York-based technology startup Neverware, described starting his company as a sole founder as “the most isolating experience” of his life - and the statement, which has deeply resonated with entrepreneurs over the years, could not be truer for entrepreneurs in this period of global isolation.



Jonathan Hefter, founder and CEO of Neverware

Having a co-founder to help carry the weight can make all the difference now. But the pressure of making decisions amid pandemic-driven uncertainty around the future of their businesses can also adversely strain the relationship.

“The single biggest piece of advice here is to communicate,” Bryan says. “There is significant truth in a problem shared is a problem halved and if you cannot be honest with your founders then who can you be honest with?”

Bryan adds that many disputes between founders arise simply due to a “breakdown” in communication or “dashed

expectations as a result of misunderstanding of circumstances or situations”.

Differences of opinion and disagreements in some form and degree are unavoidable even in the best of times, but are far more likely to surface in a climate of macroeconomic turbulence and in the face of numerous unseen problems that may not be resolvable in the short term. In such circumstances, Barbary advises founders to tackle conflict head-on.

“Address co-founder conflict early on, thus reducing the chances of it escalating, repeating or permanently damaging the relationship, and the company,” he says. “Avoiding conflict will not salvage partnerships. The moment conflict comes up, put aside time to meet. Don’t discuss co-founder conflict in front of employees, as this could cause further complications.” And while it may sound cliché, like with any good relationship, Barbary adds, “compromise is key”.

“The partnership could be battered due to the macroeconomics of the situation and the ramifications may run deep. Keep an open mind and remember the need to give and take. The business will be most successful if partners capitalize on each other’s strengths. The collective goal should always be to run a successful business, not to control it.”

FOUNDERS’ AGREEMENTS

However, Barbary says, co-founders should be prepared with a plan to manage conflict before it even arises. “Have a plan of action and an agreement in writing,” he insists. “Creating a formal shareholders’ agreement putting the roles, liability, profits distribution and conflict resolution strategies in writing gives partners reference. If such [an] agreement exists, review

it to add potential amendments [that] may entail negotiations. Refer to this agreement for governance and execution during conflicts especially amidst the trying times of today.”

A Founders’ Agreement is a legal contract that outlines the roles, rights, and responsibilities of each founder.

With all of the things that go into building a startup, it can be tempting to forget or forego drafting a Founders’ Agreement in favour of likeability and friendly rapport. But not making the deal clear with co-founders amid the excitement and rush to get the new venture off the ground is a common and problematic legal mistake.

“Regrettably, we see a lot of issues arising because the founders either did not enter into any agreements at all when then started their business, or the documents they did sign were poorly drafted or inadequately captured the full extent of the roles and responsibilities of the parties and specifics about what happens if things didn’t go to plan,” Bryan adds.

For co-founders who do not currently have partnership or shareholders agreement in place, De Keersmaecke recommends getting one in place as soon as possible. And for those who already have a Founders Agreement, she suggests revisiting the document to consider questions that may arise amid unpredictable market conditions.

“Assess what rights and obligations you have in respect of the ongoing business, as a shareholder and as a director,” De Keersmaecker advises. “How is decision making structured? Have you followed the corporate governance set out in the Memorandum of Association or have you derogated from those requirements in any respect? If you hold board seats you likely owe fiduciary duties to the company. Assess past corporate



Janine De Keersmaecker, Counsel at Argentum Law

governance and your role and direction going forward at the board level. Review your ability to approve or veto which matters and types of decisions in respect of the business - whether as a shareholder or director - keeping in mind any required thresholds to the extent they apply.”

Ideally, co-founders would have thought through any potential issues that they might face and outlined solutions in the agreement for the various scenarios, including selling of the business or shares, a co-founder leaving the country, or non-performance.

“Assess your transfer rights and exit options,” De Keersmaecker says. “Founder Agreements often include explicit permitted transfer rights and if addressed in the drafting stage, voluntary exit rights, and sometimes even forced exit clauses, based on certain circumstances occurring. Understand the dispute resolution clause, it will help you to make decisions. Whether it’s a local court under a familiar law, or arbitration in a far-off country, or with an embedded mediation clause, it’s critical to

know what is in the dispute resolution clause as it informs you about the true cost of an unresolved dispute.”

Most contractual disputes will never end up in a formal resolution process, she adds.

“But knowing what your ultimate resolution backstop is can enable you to make more informed decisions and work on a strategy for a successful negotiation. Does it include well-drafted deadlock provisions? What is the process for resolving a deadlock which arises? What are the consequences of an unresolved deadlock? If there is a buyout process? Is it linked to market-based value or another manner of valuation? How valuation is determined is particularly important in light of the crisis. Are the funding requirements reasonable in light of the current circumstances? Evaluate transfer and exit options as you may, or your co-founders may try to exit or transfer equity in crisis mode.”

THINK LONG-TERM

For some businesses, Barbary suggests, maintaining “at least a baseline presence” through the turmoil may enable them to hit the ground running on the other end. “Breaking agreements may be a tempting solution during stressful conflicts but it’s important to weigh the significant and irreparable harm this will do to the business, not to mention potential exposure to litigation,” he says.

Echoing the sentiment, Bryan adds: “Almost always, a founder will realize greater value from their business if it is sold or reorganized or consolidated as a going concern, rather than as a business that is bankrupt or where creditors have enforced any events of default against it.”

But as companies, especially those with physical operations, struggle to cope with a significant drop in revenues, and with demand is likely to remain weak for the foreseeable future, selling or shutting shop may be the only recourse for some founders as piling costs continue to deplete cash reserves.

“In terms of selling your business in distress, make sure potential purchasers are not taking advantage of you in a distressed situation, and always follow best practices in protecting your confidential information and IP in a potential acquisition scenario,” De Keersmaecker says. The expert adds that founders can expect difficulties determining valuations in current circumstances. “It may be challenging to agree a fair price for your shares,” she says, also cautioning entrepreneurs not to sign overly burdensome non-compete or non-solicits.

Before resorting to any extreme recourse however, De Keersmaecker says, companies should consider following government recommendations and taking economic aid where available. **“The UAE has acted fast to support the economy by announcing a generous stimulus package by the UAE Central Bank and the executive councils in both Dubai and Abu Dhabi in mid-March 2020, which was later increased to the tune of Dh256 billion. The primary purpose of the targeted economic bailout is to decompress the bottlenecks and provide temporary relief from the payments of principal and interest on outstanding loans for all affected private sector companies and retail customers in the UAE.”**

HUMAN RESOURCES AND WELL-BEING

Unquestionably, businesses need to be taking a long, honest and pragmatic look at what work they are currently doing, where they are doing it, but more importantly how they are doing it, Bryan says. “We recognize that most businesses are not going to be able to hire more people or spend more money to be able to get more done – and many are faced with both budget and headcount reductions,” he explains.

“This is the reality of business life from well before the advent of COVID-19. For businesses to survive this period and beyond, we believe more businesses are going to have to refocus their efforts on optimizing the way that they deploy and utilize their diminishing resources, still with a focus of being able to achieve more (better, faster, cheaper) with less (time, budget, headcount).” Examples of this include defining and automating standard processes, implementing standard form documentation - to enable faster contracting with third parties - and defining and implementing more streamlined but robust internal operating policies procedures to drive efficiencies in their business from within.”

Each business should attempt to quantify its burn rate and runway to begin with, Barbary adds. “Reducing variable costs from there on is often a quick way to immediately reduce cash outflows,” he says. “There are variable cost-reduction levers such as imposing hiring freezes and placing restrictions on discretionary spend like training. When labour is a significant cost line in the business, consider avenues that might help reduce spend to avoid getting to a situation where layoffs are required. For example, encourage employees to take available

leave balances to reduce liabilities on the balance sheet. If necessary, consider offering leave without pay to preserve cash.” De Keersmaecker cautions however that employers in the private sector can only reduce the salary of a non-national employee with the consent of that employee. “An addendum to the employment agreement must be signed,” she says, stressing the importance of providing on-going support, listening to concerns and making crystal clear communication to staff to keep them well informed about company policies and contingency plans. We are seeing SMEs that can no longer pay salaries and have no choice but to make redundant a number of employees and hire them back as freelancers on a project to project basis.”

De Keersmaecker also urges companies to keep in mind anyone who may be more vulnerable due to a pre-existing health condition, age, disability or pregnancy.

As businesses continue to evaluate how to adapt their business in light of the COVID-19 pandemic, Barbary adds, it is imperative to consider legal implications of any decisions and ensure the correct steps are being taken. For example, some businesses may require their employees to take on different roles than they were hired for. Employers with a surplus of employees are encouraged to register their data in a [Virtual Labour Market](#) system to allow them to be rotated with other companies, he adds. “This provides some flexibility if the employees can work for another company for a limited period of time. This is a constantly evolving situation, employers and employees alike are encouraged to work together to create the right balance between rights and obligations.”

LEGAL CHECKLIST FOR STARTUPS

This legal checklist was prepared to help founders lead and protect their businesses. Whether you've just setup a new venture, are navigating the current pandemic or have been in business for a few years, run through these actionable items to give your business a legal tuneup and make sure you're covered.

- Address co-founder conflict early on
- Have a formal shareholders' agreement and a plan of action in writing
- Assess rights and obligations in respect of the ongoing business as a shareholder and as a director
- Protect confidential information and IP in a potential acquisition scenario
- An addendum to the employment agreement must be signed in case of pay revisions
- Evaluate immediate financial liabilities and proactively engage in early discussions with creditors, suppliers, landlords, customers and investors
- Review existing agreements to add potential amendments that may entail negotiations
- In case of shifting operating models, review and amend terms and conditions of sale
- Develop routes to alternative suppliers, and take advantage of deals and discounts currently on offer
- Promptly document reasons for any failure to perform contractual obligations or difficulty faced in doing so
- Tap into comprehensive relief packages offered by banks in Dubai or approach lenders to refinance existing loan obligations