

An Overview of the New Governance Rules in the UAE: Part I

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- list a set of new corporate governance rules in accordance with, and to adhere to, the Federal Law No. (2) of 2015 on Commercial Companies (CCL); and
- repeal the UAE Ministerial Resolution No. (518) of 2009 Concerning Governance Rules and Corporate Discipline Standards (Repealed Governance Rules).

New provisions were also introduced under the New Governance Rules, that did not exist under the Repealed Governance Rules, such as the provisions related to Insiders Register, Confidentiality of Data & Information, Conflict of Interest, Register of Related Parties, General Assembly Meetings, Capital Increase, Dividends Distribution, Investors Relation, and Obligations of the Auditor.

The purpose of this article is to compare the New and Repealed Governance Rules and highlight some of the provisions that we consider would benefit from clarification from SCA in relation to the following:

- Definitions;
- Scope of Application and Enforcement; and
- Parent, Subsidiary and Allied Companies.

It is worth mentioning that any capitalised terms shall have the same meaning to those mentioned in the New Governance Rules.

Definitions

In addition to the reference of the CCL, the New Governance Rules introduced the following new definitions that were not defined under the Repealed Governance Rules:

“State”: *The United Arab Emirates*

“Government”: *The Federal Government or any of UAE’s governments member to the federation in addition to any authority, entity, council, institution, body or public company wholly owned by any of them whether directly or indirectly.*

“Senior Executive Management”: *The company’s executive management, including the general manager, executive director, chief executive officer, and managing director authorized by the Board Members to manage the Company, and their delegates.*

“Deals”: *Transactions, contracts or agreements entered into by a public joint stock company that is listed in the market and do not fall under the main activity of such company or by way of including preferential terms that are not usually granted by the company to its clients, in addition to any other deals to be specified by SCA from time to time by virtue of a resolution, instruction or circulation issued thereby.*

“Remuneration”: *The amounts received by the Company’s staff, employees or Board Members from the Company; i.e. salaries, bonuses, attendance bonus, transportation allowance, or any other allowances, benefits, and the like.*

Other definitions had some amendments such as:

“Executive Board Member”: Even though it may seem that the difference between the old and new definitions is immaterial, the new definition requires the Board Member to hold a position at the Company and to receive a monthly or annual salary from the Company to be considered as an Executive Board Member while the old definition requires either of them. Practically speaking, a Board Member shall not receive a salary from the Company unless he holds an executive position within the company to manage it.

“Independent Board Member”: The new definition removed any reference to the disclosure obligations on the relatives of a Board Member towards the Company. The new definition has also referred the conditions under which a Board Member shall not be construed as an Independent Board Member to a separate article (Article 45) in the New Governance Rules while in the Repealed Governance Rules such conditions were listed in the definition itself.

“Relatives”: The new definition added brothers and sisters to the definition of relatives.

On a further note, the definitions of “Parent Company”, “Subsidiary” and “Allied Company” were significantly amended as illustrated later in this article.

As for the remaining definitions, they either have exactly the same meaning given to the terms defined under the Repealed Governance Rules or the meaning is substantially similar.

Scope of Application and Enforcement

The New Governance Rules made it clear under Article 2 that the rules are subject to the provisions of the:

- the CCL;
- Federal Law No. 10 of 1992 on Evidence in Civil and Commercial Transactions (“Evidence Law”); and
- Federal Law No. 11 of 1992 on Civil Procedure (“Civil Procedure Law”).

Although the Repealed Governance Rules are subject to same laws mentioned above by way of default, this was not explicitly mentioned.

The important difference in the scope of application and enforcement between the two rules is that the Repealed Governance Rules exempt banks and financing, investment, banking and financial intermediation companies that are subject to the control of the UAE Central Bank from the scope of its rules. The New Governance Rules on the other hand made the provisions of Part 1 – Corporate Discipline Standards (Articles 3 to 39) and Part 3 – General Provisions (Articles 53 to 55) applicable to the said companies but exempted them from the provisions of Part 2 – Corporate Governance (Articles 40 to 52).

Exemption of foreign listed companies from the scope of application and enforcement continues to apply in the New Governance Rules.

Parent, Subsidiary and Allied Companies

When comparing the definitions of “Parent Company” under the New and Repealed Governance Rules, it is notable that the new definition uses the term “juristic person” to expand the reach to all types of entities whether it is a company or not. The reason for using such term can be attributed to the fact that parent companies can be located in any jurisdiction worldwide which some of them will allow for different types of entities such as governmental entities or NGOs to carry out commercial activities and incorporate commercial companies permitting them to have control on other companies. It is worth mentioning that the new definition excludes natural persons from the scope of the definition.

Another difference is that the old definition defines parent companies as companies that own 50% of another company. This definition raised confusion as to whether or not such shareholding is only limited to direct ownership. Another issue with the old definition is that some companies may own less than 50% of a listed company's shares and yet have indirect control over that company (for example by getting its Subsidiaries to own shares of the listed company in which it control whereby each Subsidiary will own less than 50% of the controlled company yet together directly/indirectly own more than 50% in aggregate). The new definition resolved this confusion by considering a Parent Company to be the juristic person who have control to pass a resolution in a general assembly.

Nevertheless, the new definition is not clear on whether the power to pass the resolution is limited or unlimited; i.e. is it enough in order to be considered as a Parent Company to have the power to pass a resolution in most general assemblies with restriction to some matters (such as liquidation) or it has to be an unlimited power to pass any resolution whatsoever. The articles of association of some companies may stipulate that some matters are reserved and have to be taken unanimously even though one partner may be controlling more than 90% of the shares whilst in other companies you will find that one shareholder will indirectly hold an unlimited power to pass any resolution whatsoever in a general assembly (whether directly or indirectly) even though his/her shareholding can sometimes be less than 50%. Our interpretation is that the new definition considers Parent Companies to be the companies that hold the power to pass a resolution in a general assembly in a majority of the matters discussed as the purpose of the New Governance Rules is to restrict the powers of those who have influence on a publicly listed company.

As for "Subsidiary", the new definition includes the power to appoint the board of directors. Therefore, a company can still be considered to be a subsidiary even it is not more than 50% owned by another company only if the other company has the power, whether directly or indirectly, to appoint all of its board of directors. Furthermore, and even though this is not mentioned in the definition, we believe that "the ownership of more than 50%" can be either direct or indirect since indirect ownership will still grant the owning company the power to act as a shareholder subject to one condition, namely; it must have full control over the company that divrectly own the shares thus enabling the indirect owner to have full powers to appoint the board of directors of the owned company.

Regarding the definition of "Allied Company", we consider that the new definition is a better definition since the terms "cooperation" and "coordination" used under the Repealed Governance Rules does not promote a company to be allied with another company unless one company owns shares of the other. It should be noted that the New Governance Rules defines an "Allied Company" as being "the company owned by another company by more than 25% and less than 50% of its capital". We consider that restricting the minimum shareholding threshold to more than 25% in order to consider a company as an allied company is valid since 25% or less can be considered to be merely an investment with no actual control over the owned company.

However, there is one area of confusion that arises in terms of whether owning just 50% still promotes the owning company to be an allied company or not. The new definition is vague on this point since the wordings consider Allied Companies as companies that are less than 50% owned by another company, while owning more than 50% will consider the owned company to be a Subsidiary. We believe that a company owning 50% of the shares of another company means that the owning company falls under the definition of an 'Allied Company' since the owning company has some control over the other company yet such control is not sufficient to pass a resolution at a general assembly meeting.

Another question that may rise is whether or not to consider the company that owns only 25% of another company is an 'Allied Company' or not. Unfortunately, the current wordings of the new definition excludes such a company from the definition of 'Allied Companies' and it cannot be implied that it falls within the scope of such definition.

In addition, as mentioned above in the paragraph related to the "Subsidiary", the ownership can be either

direct or indirect since indirect ownership will still grant the owning company the power to act as a shareholder subject to one condition which is to have full control over the company that directly own the shares.

This article is part one of a series of four articles with the other articles being published in subsequent editions of Law Update.