

# An Overview of the New Governance Rules in the UAE: Part II

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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Repeal the UAE Ministerial Resolution No. (518) of 2009 Concerning Governance Rules and Corporate Discipline Standards (Repealed Governance Rules).

New provisions were also introduced under the New Governance Rules, that did not exist under the Repealed Governance Rules, such as the provisions related to Insiders Register, Confidentiality of Data & Information, Conflict of Interest, Register of Related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The purpose of this article is to compare the New and Repealed Governance Rules and highlight some of the provisions that we consider would benefit from clarification from SCA.

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

## **Formation of the Board of Directors**

There is no material difference between the New and Repealed Governance Rules since both stipulate that the articles of association shall decide on the method of formation, number of members and tenure of membership of the Board of Directors. However, the New Governance Rules reiterate Article 148 of the CCL which states that if a Government owns 5% or more of a Company's shares, the said Government may then appoint a representative in the Company's Board of Directors pro rata to its shareholding or at least one Board Member if the shareholding percentage required to elect such member is less than the shareholding of the said Government. The Government's right to vote shall expire with respect to the shares utilized to appoint its board representative unless there are remaining shares still to be utilized (other than those already utilized to appoint the Board Members representing the Government).

In accordance with Article 151 of the CCL, the condition to have the Chairman and majority of the Board Members to be UAE nationals continue to be in effect in the New Governance Rules without prejudice to the treaties and agreements entered into by the State (such as the treaties entered with the GCC States).

## **Regulations of Candidature to Board Membership**

Both rules provided for women's representation in the Board of Directors and to disclose in the Company's annual report the reasons for not having a woman Board Member if there are no women that are members. However, the difference is that the Repealed Governance Rules stipulate a requirement to have at least one female Board Member while the New Governance Rules set a minimum percentage of 20% of the Board of Directors to be represented by women with an obligation to disclose the percentage of women represented in the Board of Directors.

The New Governance Rules further sets the rules for board membership candidature, such as having the

process of candidature open for at least ten days (fourteen days in the Repealed Governance Rules), publishing the details of the board candidates in the Company's website two days utmost (five days in the Repealed Governance Rules) prior to the general assembly meeting day, prohibiting assigning candidature after closing the candidature process (did not exist in the Repealed Governance Rules), and providing SCA and the Market with the details of the candidates on the day following the closure of the candidature process (no timeline for providing such details existed in the Repealed Governance Rules).

### **Conditions for Board Membership**

The New Governance Rules referred to the CCL which stipulates that a Board Member must not be a Board Member in more than five companies, or to be a Chairman or Vice Chairman in more than two companies, or to be the managing director in more than one company.

The New Governance Rules, in addition to the aforementioned prohibition of the CCL, stipulates that a Board Member must not (i) have been convicted with a crime of honor or honesty unless pardoned (such prohibition existed in Article 97 of the Old Companies Law No. (8) of 1984 but do not exist anymore in the CCL); (ii) have at least five years of experience in the activity carried out by the Company that he/she is applying for its board membership; (iii) hold a clean record before SCA that no disciplinary action has been taken against him, no court order is issued to dismiss/remove him/her from his/her position as a Board Member, and no outstanding proceedings before the Public Prosecution office in relation to honesty and integrity; and (iv) any other conditions stipulated in the Company's articles of association.

The New Governance Rules also lists the documents required to be submitted by candidates for board membership.

### **Obligations and Duties of the Board of Directors**

The New Governance Rules expanded the duties and obligations of the Board of Directors in Article 43 thereof to ensure its involvement in each and every aspect of the Company's management and operations. The New Governance Rules further provides under Article 11 (did not exist under the Repealed Governance Rules) for the duties and obligations of the Board Members which basically obligate Board Members to (i) preserve the Company's rights and act as a prudent person; (ii) act with honesty and integrity and in accordance with the applicable laws and regulations and the Company's articles of association; (iii) disclose being a Chairman, Board Member or a member of the Senior Executive Management of a company other than the Company itself; and (iv) dedicate sufficient time for his/her duties and obligations toward the Company.

### **Board Members Lack of Independency**

More or less the provisions whereby the Board Member will lack independency are same in both rules. However, two additional conditions were added to the New Governance Rules that needs to be taken into consideration.

The first is that the New Governance Rules has added that a Board Member will lack independency if such Board Member or any of his/her Relatives work or has worked in the Senior Executive Management of the Company or a Subsidiary during the last two years preceding the date of being Board Member candidate.

The second condition is that a Board Member will also be conflicted if such Board Member or any of his/her Relatives has a direct or indirect interest in one or more Deal concluded with the Company or a Subsidiary during the last two years and the aggregate value of such Deals exceeds 5% of the Company paid up share capital or AED 5 million or their equivalent in foreign currency whichever is less unless the Deals fall within the normal course of the Company's activities and there are no preferential conditions whatsoever and that they have been entered on an arms' length basis.

It is worth mentioning that the New Governance Rules also added that a Board Member shall not lack

independency for just being an employee of the Parent Company or a Subsidiary if such Parent Company or a Subsidiary is a Government or is a Company or a Subsidiary that is at least 75% owned by a Government.

Unfortunately, the New Governance Rules are silent in respect to the procedures to be taken if a Board Member lacks independency and just mention the conditions under which a Board Member is conflicted. However, we believe that disclosure obligation under Clause 11(c) of the New Governance Rules is applicable in this regard; i.e. the conflicted Board Member will have an obligation to inform the Board and the Board shall then decide on the action to be taken in this regard.

### **Chairman of the Board of Directors**

The New Governance Rules added new provisions that did not exist in the Repealed Governance Rules regarding the election of the Chairman from amongst the Board Members (by way of cumulative voting), prohibition to combine between the position of the Chairman and General Manager, the right to elect the General Manager from amongst the Board Members and the right to form committees from amongst the Board Members to monitor the progress of the Company's operations and to ensure the implementation of the Board's resolutions.

### **Vacancy of Board Member Position**

The key difference is that the wordings of the New Governance Rules provides that in case 25% or more of the Board Member positions are vacant, then the remaining Board Members have to call for a general assembly meeting within 30 (thirty) days (no more than three months in the Repealed Governance Rules) to elect the members to occupy the vacant positions as per Article 145 of the CCL.

The New Governance Rules has also added a clause regarding the representatives of juristic persons or Governments (did not exist in the Repealed Governance Rules) who can be changed by way of an official letter addressed to the Company and the new representative shall complete his/her predecessor's tenure.

The New Governance Rules further lists the circumstances under which a position of a Board Member shall be vacant. This also did not exist under the Repealed Governance Rules.

### **Dismissal of Board or Executive Management Members**

The Repealed Governance Rules just referred to the Old Companies Law No. (8) of 1984 and accordingly is silent on this matter.

Even though Article 168 of the CCL provides for the circumstances under which a Board Member may be dismissed, the New Governance Rules further stipulates that a Board Member or a member of the Company's executive management shall not continue in his/her position if a court order is issued against him/her with a penalty of imprisonment and/or fine with the dismissal of such member from his position. Such Board Member may not be a member again of the Board of Directors or the Company's executive management at least a year from the date the court order is issued.

### **Board Members Remuneration**

The New Governance Rules provided same as the Repealed Governance Rules that the remuneration of the Board Members shall not exceed 10% of the Company's net profit for the relevant financial year. However, the three key differences between the New and Repealed Governance Rules as per Article 169 of the CCL is that (i) Board Members' remuneration under the New Governance Rules is not subject to the distribution of a minimum percentage of dividends and therefore it is impliedly stated that the general assembly of a Company may resolve that the Board Members shall receive their remuneration even if it is decided that no dividends will be distributed to the shareholders for the relevant financial year but this is subject to the Company generating net profits for such year. The Repealed Governance Rules on the other

hand provided that Board Members remuneration shall be subject to the distribution of at least 5% of the net profits to the shareholders which is not the case any more; (ii) the New Governance Rules further provides that (did not exist under the Repealed Governance Rules) the Company may pay additional expenses, fees or monthly salaries to the extent determined by the Board of Directors to any Board Member if such member works in any committee, makes special efforts or performs additional works to serve the Company beside his ordinary duties as a Board Member. Having said this, no attendance allowance may be paid to the Chairman or Board Member in respect of the board meetings; and (iii) the New Governance Rules additionally provides that (also did not exist under the Repealed Governance Rules) fines imposed on the Company because of the Board of Directors' violation of the applicable laws or the Company's articles of association shall be deducted from the remuneration of the Board of Directors. Having said this, the general assembly meeting of the Company may not deduct all or some of such fines if such fines are not a result of the Board of Directors fault or negligence.

## **Board Meeting**

The Repealed Governance Rules stipulated that the Board of Directors has to meet at least once every two months; i.e. at least six times a year and that no board meeting shall be valid unless attended by the majority of its members and all its resolutions has to be passed by a simple majority voting of the Board Members present at the meeting.

The New Governance Rules on the other hand provides that, in accordance with Article 156 of the CCL, the Board of Directors has to meet at least four times a year and all board resolutions has to be passed by a simple majority voting of the Board Members present at the meeting. As for the quorum required to construe the board meeting being valid, the New Governance Rules is silent referring this matter to the CCL and likewise the Repealed Governance Rules requires the attendance of the majority of the Board Members.

Both rules provide that the Chairman shall have a casting vote.

The New Governance Rules has added additional clauses in relation to:

- the obligation to convene the board meeting calling for a general assembly 30 days prior to the general assembly date (21 days under the Old Companies Law No. (8) of 1984);
- having the board meeting to be held in the Company's headquarter unless the Board believes there is a necessity to convene the meeting in another place;
- having a secretary to the Board of Directors who shall not be a Board Member;
- delegating other Board Members to attend a board meeting provided that no Board Member shall act as a proxy for more than one Board Member; and
- prohibiting any voting by way of correspondence.

## **Participation in Board Meetings via Modern Technology**

Article 6 of the New Governance Rules has provided for the conditions to have a board meeting using modern technology in accordance with Article 156 of the CCL subject to stipulating in the Company's articles of association for using such means to convene a board meeting.

## **Board Resolutions by way of Circulation**

The critical difference between the two rules in this regard is that the Repealed Governance Rules has stipulated that the Board of Directors shall pass no more than four resolutions per year by way of circulation.

The New Governance Rules on the other hand did not set a ceiling to the maximum number of resolutions

that can be passed by way of circulation (unless provided otherwise in the Company's articles of association) and provided that (same as stipulated in the Repealed Governance Rules) the Board Members agree by way of simple majority that the circumstances requires the resolution to be passed by way of circulation and that the resolutions are ratified in the next physical board meeting.

### **Minutes of Board Meetings**

No material difference between the two rules in this regard except that the New Governance Rules are more comprehensive and lists the standards to be taken into consideration when recording the minutes of meeting such as listing the date, venue, attendees, absent board members, date of the invitations sent regarding the meeting, proxies and including the phrase "*Signatories of this minutes shall be responsible of the validity of the date included therein*" in the minutes of meeting.

### **Board Committees, Internal Control and Compliance Officer**

There is no difference between the New and the Repealed Governance Rules in this regard except that the New Governance Rules are more comprehensive in terms of the duties of the audit committee and the elements to be included in the internal control annual revision report.

### **Corporate Governance Report**

The New Governance Rules have expanded the details that should be included in the Corporate Governance Report which has to be as follows:

1. A statement of the details and reasons of any compensations and allowances paid to every Board Member and the members of the Board committees during the fiscal year;
2. A statement of the Company's Board Members and first and second line officers as per the Company organizational structure as well as their positions, appointment dates, salary details, the benefits paid to each of them and any compensation paid to them by the Company and the reason of such compensations; and
3. Remuneration of the Board Members and all the members of the Company management team including the compensations and any motivational programs associated with the securities issued or guaranteed by the Company.
4. The New Governance Rules is silent on the obligation to mention the violations committed during the financial year in the report (such obligation existed in the Repealed Governance Rules). We believe that the report still has to mention the violations committed even if the New Governance Rules are silent on this matter since this is a crucial purpose for issuing the report and presenting it to the shareholders.
5. The obligation to have the report available to the shareholders before submitting the application to approve convening the annual general assembly meeting still continue to be enforceable under the New Governance Rules.