New Corporate Governance Code for UAE PJSCs: what, why and how?

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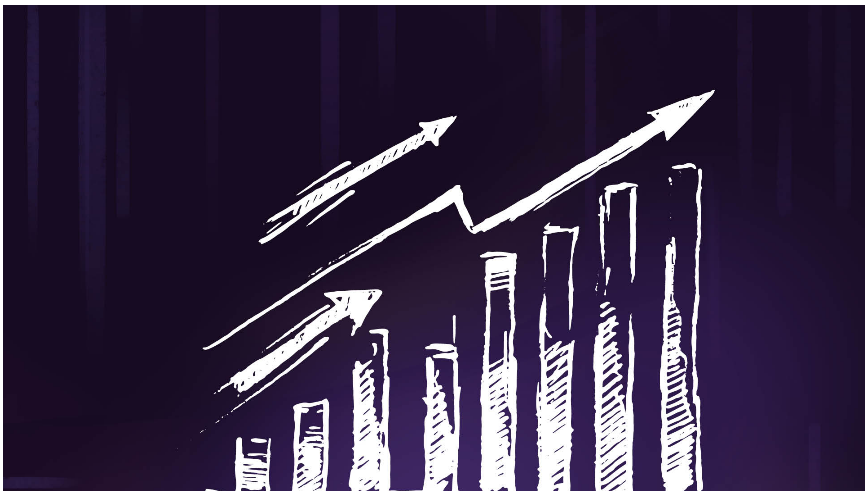
The United Arab Emirates ('UAE') Securities and Commodities Authority ('SCA') issued new corporate governance rules under Chairman of SCA Board Decision No. (03 R.M.) of 2020 concerning adopting the Corporate Governance Guide for Public Joint Stock Companies ('New Rules'). The New Rules, which were published on 27 February 2020 and came into force on 28 April 2020, repeal the previous corporate governance rules (Chairman of SCA Board Decision No. (7 R.M) of 2016 concerning the Standards of Institutional Discipline and Governance of Public Shareholding Companies). The New Rules apply to Public Joint Stock Companies ('PJSCs') listed on the Abu Dhabi Securities Exchange or the Dubai Financial Market. This article provides a summary of the key elements of the New Rules.



What is corporate governance?

Corporate governance is the collection of rules, practices, mechanisms and processes by which corporate entities are operated, directed and controlled. Good corporate governance should create a balance between the interests of an entity's shareholders, its senior management, its other stakeholders and the wider community.

Good corporate governance should promote the rule of law, transparency, responsiveness, inclusion, efficiency, equality, accountability and participation and should be executed through a cultural mindset rather than treated as a 'tick-box' compliance exercise. Corporate governance best practices for PJSCs can assist in building and maintaining investor confidence and can mitigate the risks of corruption and mismanagement, all of which can enhance the reputation of a PJSC, and potentially improve its share price. It is very important for PJSCs to remember the "G" for governance in ESG (Environmental, Social and Governance) that is having an increasing impact on investor decision-making.

Corporate governance should not interfere in the day-to-day activities of the PJSC; instead, it should set out the framework for the different roles and responsibilities of the stakeholders in the PJSC such as its shareholders, board members, committee members, senior management, and auditors.

What do the Corporate Governance Rules require?

The Corporate Governance Rules set out the minimum corporate governance standards required of a PJSC. The constitutional documents of the relevant PJSC may impose higher standards.

1. **The shareholders and the general assembly**

The New Rules provide certain protections and rules relating to a PJSC's shares. These include the following:

- all shares must be of the same class;
- all shareholders must be treated equally;
- a share grants its holder the right to receive profits if and when distributable, and the free disposal thereof;
- a shareholder has the right to review the PJSC's financial reports and approve them;
- each shareholder enjoys the right to attend, participate in, and vote at general assembly meetings;
- a shareholder may delegate another person, save for a board member of the PSJC, to attend a general assembly meeting on his orher behalf. When signing the proxy document, the relevant shareholder should use the signature certified by either a notary public, the UAE chamber of commerce or economic department, a licensed bank in the UAE where the shareholder has an account, or any authority authorised to undertake notarisation activities;
- a PJSC shall appoint two representatives from law or audit firms certified by the SCA to represent shareholders at general assembly meetings. Lawyers from law firms operating in the UAE, financial consultancies and analysts approved by SCA, or any other body approved by the SCA are eligible for such appointment;
- in order to avoid consolidation of shares, a person attending by proxy may not represent more than one shareholder where such representation would exceed five per cent of the issued share capital of the PJSC; and
- certain actions of the PJSC can only be taken with the approval of a simple majority of the shares represented at the meeting, or in the case of very important matters, such as amending the PJSC's constitutional documents, a majority of 75 per cent is required.

2. **The Board**

The board of directors (the 'Board') manages and supervises a PJSC's business and operations. The New Rules place a number of obligations on members of the Board including the following:

- a Board member is expected to safeguard the PJSC's interests, exercise reasonable care, and undertake all acts required for the benefit of the PJSC;
- a Board member shall act with honesty and integrity and observe all applicable laws and the PJSC's constitutional documents;
- a Board member must avoid conflicts of interest – including abstaining from voting on matters where such member has an interest, and must disclose such interests to the remainder of the Board. Board members must fill in a specific form, to be kept by the Board Secretary declaring any interests or relationships that may affect their ability to perform their tasks as a Board member, which is to be reviewed quarterly or updated at the time as any existing interest changes or new interest arises.
- Board members should avoid the acceptance of gifts (gifts below AED500 (approximately US$136) are acceptable));
- the Board has to appoint an independent secretary that directly reports to it;

- the Chairman and majority of the Board members must be UAE nationals; and
- the majority of Board members have to be non-executive and independent.

The New Rules introduce the option for a PJSC to implement a dual governance structure under which the management function is separated from the supervisory function. This is achieved by establishing two Board committees: (i) a supervisory committee; and (ii) an executive committee. These committees will be required to co-operate to realise the PJSC's objectives.

3. **Board committees**

- The New Rules provide that the Board shall establish a nomination and remuneration committee and an audit committee. Each committee shall comprise not less than three non-executive Board members, two of which must be independent. Each committee must be chaired by an independent Board member.
- ***The nomination and remuneration committee*** prepares policies relating to remuneration, benefits, and incentives of the Board and the PJSC's employees.
- ***The audit committee*** reviews the financial and audit policies and regulations of the PJSC and works closely with the external auditor of the PJSC to ensure that it carries out its engagement in accordance with applicable law.
- In addition, the New Rules encourage the establishment of two non-mandatory committees, a risk committee and a technology committee. The risk committee sets out the risk management strategy of the PJSC and the implementation of such policy. The technology committee will review and approve the PJSC's technology plans and strategy and ensure the implementation of such plans and strategy.

4. **Internal audit and compliance officer**

- The New Rules provide that each PJSC must develop an internal audit system and have a specific department in charge of its implementation. This manages and assists the implementation of the PJSC's corporate governance rules in an efficient and effective manner.
- Each PJSC must also appoint a compliance officer who monitors compliance by the PJSC and its employees with applicable laws and regulations as well as their compliance with the PJSC's own constitutional documents.

5. **The auditor**

- Pursuant to the New Rules, a PJSC must have an external auditor who is an impartial and independent person. The auditor must be registered with the SCA.
- The auditor audits the PJSC's activities and examines its administrative and financial regulations and internal audit functions to ensure their effectiveness and appropriateness to the PJSC. The auditor also reviews the PJSC's financial statements and confirms the existence of its assets.
- The auditor is required to report any non-compliance with relevant laws to the SCA.

6. **Related party transactions**

- The New Rules contain restrictions on transactions between a PJSC and its related parties. For the purpose of the New Rules, those considered to be related parties are the chairman, the members of the Board, senior executives and employees, as well as any company in which such persons hold 30 per cent or more of the share capital, and such company's subsidiaries, sister companies, or affiliates.
- Any transaction with a related party that does not exceed in value five per cent of the share capital of

the PJSC must have prior approval of the Board. Where such deals are of a value exceeding five per cent of the share capital of the PSJC, the general assembly’s approval is required. The related party may not vote with regards to either approval.

- Where the value of the transaction exceeds five per cent of the share capital of the PJSC a valuation by an SCA approved valuer is required. Following such valuation, the transaction must be approved by the general assembly through an ordinary resolution.
- Any related party transaction must be disclosed to SCA together with a confirmation that the transaction is at arms-length and in the interest of the PJSC’s shareholders.

7. **Corporate Governance of group subsidiaries**

- Where there is a group of companies, the parent company shall set out the group corporate governance framework with appropriate authorities and monitor their implementation across the group.

Application to banks

The New Rules apply to all PJSCs without exception, including banks. However, there are additional separate rules issued by the Central Bank that apply to banks. Accordingly, this article should not be considered a summary of corporate governance requirements for banks or a complete list of requirements for PJSCs. This is a summary only of the New Rules.

Conclusion

Corporate governance aims to create a check-and-balance system within a PJSC so it may realise an acceptable level of professionalism, accountability, impartiality and independence. This should lead to better performance by the PJSC, a potential uptick in share price, and increased investor confidence in the PJSC.

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