

Supreme court judgment: New approach on the issue of side agreements

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In a dispute between a UAE investor and a foreign investor, the parties disputed over whether a side agreement or the official Memorandum of Association (MOA) governed their relationship. The UAE investor insisted that the official MOA is the valid document whereas the foreign investor argued that the side agreement states that the foreign investor has a greater percentage in shares and that the side agreement is the valid/ applicable agreement to govern the relationship between the two parties.

As outlined in the previous article, the matter had been decided in favour of the UAE investor at the first instance and appeal levels, however the foreign investor appealed further to the Supreme Court.

In its judgment, the Supreme Court held that the side agreement can be established by any means of evidence and allowed the parties to hear testimony of witnesses.

When the Court of Appeal heard witnesses brought in by the foreign investor and rejected the claim, the parties appealed again to the Supreme Court. The Supreme Court considered the evidence and decided that there was enough evidence to prove the existence of the side agreement and subsequently directed the Court of Appeal to look into this. Upon review of the evidence, the Court of Appeal issued its judgment confirming the existence of the side agreement.

The UAE investor appealed for the third time to the Supreme Court contesting the validity of the side agreement and it is this appeal which is the subject matter of this update.

LATEST SUPREME COURT JUDGMENT

The Supreme Court ruled on this matter for the third time and in this latest judgment, the Supreme Court decided very differently to the last decision and declared that the official MOA as registered with the authorities is the valid agreement that governs the relationship between the parties and not the side agreement.

The Supreme Court relied on Articles 8, 10 and 11 of the Commercial Companies Law (CCL) and held that it is imperative for all agreements relating to commercial companies to be in writing, notarised and registered in the Companies Commercial Register so as to comply with the requirements of the CCL and that all amendments to the company documents (i.e. Memorandum of Association) must also be duly notarised and registered in the same manner as the MOA.

In this case, the Supreme Court concluded that as the side agreement was not notarised or registered in the Companies Commercial Register, it is therefore null and void.

BACKGROUND

A dispute arose in relation to a limited liability company in Abu Dhabi between a UAE shareholder and a foreign shareholder over the ownership of the actual shareholding in a limited liability company. Legal action was commenced by the UAE shareholder requesting confirmation of its entitlement to 51% of the shares, assets and profits of the company according to the official memorandum of association (MOA) of the company as officially registered and declared with the competent authorities. The foreign shareholder, however, claimed that it owned more than its registered shares (as reflected in the side agreement).

COMMENTS ON THE JUDGMENT

1. It is apparent that this Union Supreme Court judgment contrasts with the previous two judgments by the same court (in the same dispute) which previously decided that side agreements are not null and void if they were not notarised or registered pursuant to Articles 8,10 and 11 of the CCL. The court in the former two rulings held that the parties can even hear witnesses to prove this matter. The court also held that the side agreement can be concluded from various documents and not necessarily from a single written agreement and that such agreement is valid even without notarisation.
2. The new ruling is therefore a material change from the Supreme court's former rulings on the issue of side agreements. As side agreements are not official agreements, they can not be notarised or registered in the Commercial Register.
3. The main purpose of the side agreement is that it is binding between the two parties only and concealed from the Commercial Register. This purpose would not be achieved if there was a requirement to notarise it or file it with the Commercial Register. This has been confirmed by the Supreme Court itself in former rulings. The side agreement also includes provisions that can not be notarised or accepted by the official authorities such as the shareholding percentage which is usually different from the official documents.
4. It is to be noted that this latest judgment did not address the effect of Article 395 of the Civil Code. Article 395 provides that: *"If the contracting parties conceal a true contract with an apparent contract, the true contract will be the effective one as between the contracting parties and a special successor."* If Article 395 had been addressed by the Supreme Court, it is possible that the court would have produced a different result.
5. It should also be highlighted here that although this judgment addressed the issue of the validity of the nominee agreement with regard to the official MOA, it has not however, addressed the issue of whether the rights of the parties under the MOA should be liquidated as a result of the invalid nominee agreement.
6. The judgment also did not address the issue of the date the invalidity occurs i.e. whether it is from the inception of the company or from the date of the judgment.
7. In view of the above judgment and the previous Supreme Court decisions on the same matter, it should be noted that the courts in future cases, will not necessarily decide that all side agreements are null and void. Each case will be decided on a case by case basis and the arguments raised above (in paragraphs 3, 4, 5 and 6) may also appear in separate matters in the future.