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HAWKAMAH
THE INSTITUTE FOR CORPORATE GOVERNANCE

IIF Equity Advisory Group

Corporate Governance in United Arab Emirates
– An Investor Perspective

Task Force Report
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Corporate Governance in United Arab Emirates—An Investor Perspective

CONTENTS

PREFACE

In view of the importance of portfolio equity flows to emerging markets, the Institute of International Finance (IIF) established in January 2001 the IIF Equity Advisory Group (EAG), consisting of senior executives from leading asset management firms throughout the world. The EAG, chaired by Edward Baker, Chief Investment Officer of Global Emerging Markets, AllianceBernstein L.P., is seeking implementation of its Code of Corporate Governance (the "IIF Code") in key emerging market countries that are of particular interest to the Institute's membership base. The IIF Code, which was first released in February 2002 and revised in May 2003,[1] endeavors to improve the investment climate in emerging markets by establishing practical guidelines for the treatment of minority shareholders, the structure and responsibilities of the board of directors, and the transparency of ownership and control of companies.

The strategy for promoting the implementation of the IIF Code, as the standard by which the company/ shareholder relationship is measured, is country and regional focused. Country Task Forces have been set up for Brazil, China, India, Lebanon, Mexico, Poland, Russia, South Africa, South Korea, and Turkey. Reports on all these countries have been published, including second reports on several countries.

In June 2006, the IIF entered into a partnership with Hawkamah, the Institute for Corporate Governance,[2] to jointly conduct a two phase corporate governance survey of countries in the MENA region. Phase 1 of the survey covers countries in the Gulf Cooperation Council (GCC) – Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates (UAE). The motivation for such a survey was prompted by the extraordinary growth in GCC equity markets over the past few years, growing international interest in the region and the importance of helping officials in the GCC identify areas of weakness and potential improvements in current corporate governance frameworks. For Phase 1 of the project Hawkamah provided IIF with financial support to defray most of the cost of the work. In phase 2, the survey will be extended to other countries of the MENA region.

In July 2006, the GCC Task Force held meetings in Abu Dhabi, Manama, Doha, Dubai, Kuwait, Muscat and Riyadh to assess the corporate governance practices in GCC countries. Meetings were held with senior officials from the capital market authorities, central banks and stock exchanges, local fund managers, lawyers, experts, accountants and management consultants involved in corporate governance in GCC countries. Keith Savard, Director Global Economic Analysis, IIF and Dr. Nasser Saidi, Executive Director, Hawkamah, co-chaired the GCC Task Force. Other Task Force members include Nicolai Nadal and Rashid Bin Shabib of the Hawkamah staff and Rakhi Kumar of the IIF staff.

[1]Investors' poor experience in a generally weak corporate governance environment in many emerging markets led to relatively strict and comprehensive original IIF guidelines. Nevertheless, more detailed standards were considered desirable in a few areas in light of far-reaching new legislation such as the Sarbanes-Oxley Act passed by the U.S. Congress in the summer of 2002. The revised standards offer guidance to emerging market officials as they decide what rules and regulations must be put in place to satisfy investors.

[2]The Hawkamah Institute for Corporate Governance is an autonomous, international association, hosted by the Dubai International Financial Center (DIFC), and serving the MENA and Central Asia countries. Hawkamah was launched in partnership with the Organisation for Economic Cooperation and Development (OECD), the International Finance Corporation (IFC), the Dubai International Financial Centre (DIFC), the World Bank Global Corporate Governance Forum, the Center of International Private Enterprise (CIPE), the Union of Arab Banks (UAB), Young Arab Leaders (YAL) and the countries participating in the OECD-MENA Investment Programme. Its mission is to assist the countries and companies of the region to develop sound and globally well-integrated corporate governance frameworks. It provides technical assistance and cooperates with decision makers to coordinate and sequence the designing, planning and implementation of corporate governance reforms and monitoring the outcome of corporate governance policies at the private sector level. See www.Hawkamah.org

The aim of this report is to offer an assessment as to where countries in the GCC stand relative to the investment environment that members of the IIF Equity Advisory Group would like to see develop in key emerging market countries. Since this is a first-time survey of corporate governance frameworks in the region, the report does not treat all relevant corporate governance matters in depth. Instead, it focuses on the important initial steps that need to be taken to improve the investment environment in GCC countries. We will review at a future date the corporate governance regimes in more detail to assess progress. This report focuses on corporate governance standards and practices only in GCC countries and not those in dedicated free zones like the DIFC, which operates to international best practices. Any references made to the DIFC is based on the assessment of the IIF only. Further, the report is not meant to provide an exhaustive survey of corporate governance in the GCC and, as with other Task Force Reports, neither the Task Force nor the IIF or Hawkamah can in any way attest to or guarantee the accuracy or completeness of the information in the report despite the best effort that has been made. To the extent guidance is given, or advice is inferred, the reader is urged to fully apprise him/herself of the relevance of such content to current or contemplated operations.

TENETS OF THE IIF CODE AND BASIC DIFFERENCE WITH THE OECD PRINCIPLES OF CORPORATE GOVERNANCE

Through its Equity Advisory Group (EAG), the IIF published a code of corporate governance in February 2002 which was revised in May 2003. IIF's analysis of a country's corporate governance framework focuses on five broad areas – (i) minority shareholder rights, (ii) structure and responsibilities of the Board of Directors, (iii) accounting and auditing, (iv) transparency of ownership and control, and (v) the regulatory environment. A detailed explanation of these areas can be found in the "Comparative Analysis of Corporate Governance Frameworks in the GCC" section. These key ideas appear in the OECD Principles of Corporate Governance and the OECD Corporate Governance Guidelines that accompany it. However, the IIF Code has constructed a more detailed set of guiding principles in order to enhance their practical usefulness.

For example, with regards to minority shareholder rights, the IIF Code clearly endorses the one-share one-vote principle and proxy voting. In addition, the IIF Code supports cumulative voting for director elections. However, while the OECD Principles emphasize the importance of giving equal voting rights to all shareholders and allowing votes to be cast by nominees when agreed upon with the share owner, cumulative voting is not addressed. Furthermore, the IIF Code clearly defines independent directors and requires that at least one-third of the board be independent. The OECD Principles require that board members disclose whether they are regarded as independent by the company, but do not specifically identify how many members should be independent, nor what characteristics classify them as independent.

The IIF Code also requires that conflicts of interest for board members and key executives be disclosed publicly and that the head of the audit committee never have a conflict of interest. The OECD Principles agree that this information must be disclosed, however, they limit the scope of disclosure to the board of directors. Because it views accurate accounting and auditing as the core of transparency and good corporate governance, the IIF Code requires that semi-annual reports be filed in addition to the annual audited financial report. The OECD Principles, in contrast, only require an annual audited financial report.

Both the IIF Code and the OECD Principles encourage the implementation of good corporate governance practices, however; the IIF Code was created to promote specific actions and criteria, which, if followed, will

This report forms part of a country-by-country analysis of corporate governance practices in each of the six member states of the Gulf Cooperation Council (The UAE, Bahrain, Kuwait, Oman, Qatar, and Saudi Arabia), based on country missions by staff members of the IIF and Hawkamah. This report should be read in conjunction with a regional overview report—Comparative Survey of Corporate Governance in the GCC—published in September 2006.

EXECUTIVE SUMMARY

The IIF-Hawkamah survey analyzes the corporate governance frameworks of Abu Dhabi and Dubai Emirates as these are the only Emirates that have established stock exchanges. Due to its federal structure, the corporate governance framework in the United Arab Emirates (UAE) could differ among the Emirates. Nevertheless, the IIF-Hawkamah survey found that the corporate governance frameworks of Abu Dhabi and Dubai listed companies are similar. Furthermore, the Emirates Securities and Commodities Authority (ESCA) regulate both the Abu Dhabi Securities Market (ADSM) and the Dubai Financial Market (DFM).

The current corporate governance framework of the UAE is weak and complies with less than 50 percent of the IIF's guidelines. However, the ADSM has issued its code of corporate governance for public comment and plans to implement the code soon. Further, ESCA has prepared and issued for public comment a code of corporate governance for listed companies that would be applicable to the Dubai and Abu Dhabi stock exchanges, which when implemented should improve the UAE's overall corporate governance framework.

The development of capital markets in the UAE has created a complicated and weak regulatory structure. The Abu Dhabi Securities Market, the Dubai Financial Market, and the Emirates Securities and Commodities Authority were established in 2000. ESCA has financial, administrative and operational independence but reports to the Ministry of Economy. The Minister of Economy chairs the board of ESCA. To be a truly independent authority, ESCA has to look at its governance structure and address questions about its independence from political institutions. The close relationship between the ESCA and the Ministry of Economy creates a dynamic that might diminish ESCA's ability to

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[3]The DFM was subject to an IPO issue in November 2006.

make decisions based solely on the requirements of developing sound and efficient capital markets. The ADSM is an independent entity of autonomous status while the DFM is a public institution[3].

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ESCA has yet to establish itself as a strong regulator. It needs to strengthen surveillance and enforcement of rules and regulations. Moreover, reporting relationships between ESCA and the stock exchanges need to be improved. ESCA already has sufficient powers in terms of current laws and regulations as well as the full support of the Minister of Economy. Nevertheless, ESCA needs to be more proactive in introducing new laws and rules to strengthen corporate governance practices.

The IIF's corporate governance guidelines recommend that the regulator be a politically independent entity in accord with best intentional standards and practice. This is important in order to maintain credibility within the regulatory environment as it is imperative that regulators not be perceived as under the control or influence of any particular interest group, albeit government. Accordingly, the GCC Task Force calls for ESCA to be given full autonomy from the Ministry of Economy. This will allow ESCA to speed up the introduction and implementation of new rules and regulations.

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At the federal level, the locus of reform initiatives remains the Ministry of Economy, which has recently drafted a new Companies Law that is expected to allow majority foreign ownership of UAE firms that reside outside of the country's free zones. This will be an important step forward for a country where expatriates already constitute about 85 percent of the population. However, there are two glaring anomalies in the existing Company Law, which impede the development of capital markets in the UAE:

"There are two glaring anomalies in the existing Company Law, which impede the development of capital markets in the UAE—IPO pricing and minimum sale percentage for public listing."

IPO pricing: Often times IPOs are deliberately under-priced by the authorities (specifically, the Ministry of Economy) which by law sets the prices of IPOs for both state-owned and private companies at a notional value of the company's shares, rather than through accurate assessment of the fair market value of the firm. Current procedures and practices are inefficient and leads to market distortions with large premiums emerging on IPOs. The large premiums have generally been followed by loss of market value following discovery of 'fair market value'. IPO issue prices should be determined by the market, with the investment advisors, major accounting firms and management consultants advising companies as to IPO pricing. Sound, market pricing requires reliable, verifiable up-to-date information and reporting by companies with availability of financial information and reports based on international accounting and auditing standards (IFRS).

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Minimum sale percentage for public listing: Companies that want to list in the domestic market have to offer a minimum 55 percent stake to the public, which acts as a disincentive for FOEs and SMEs wishing to go for a public listing, as these may not wish a loss of corporate control prior to realizing their full market value. Both of these requirements deter family-owned conglomerates, who wish to raise funds in the equity market, to list on the domestic exchange.

These anomalies are perhaps the most important feature of an imperfect capital market regulatory environment in the UAE. In addition, current procedures on the local exchanges only allow for shares to be listed at nominal value. This results in market distortion. As in pricing IPOs, market forces should determine offer prices, including the freedom to issue shares at a premium or discount relative to nominal value.

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The GCC Task Force also recommends that ESCA harmonize capital market laws and regulations between Abu Dhabi and Dubai. This will lay the foundation to promote cross listing of stocks within the UAE. Individually, the stock exchanges of Abu Dhabi and Dubai are relatively small with market capitalization of about US$190.7 billion and US$88.5 billion, respectively. However, their combined value would make them the second largest stock exchange in the GCC after that of Saudi Arabia. Moreover, the two markets combined posted the highest turnover and largest number of IPOs in the GCC region in 2005. A unified equity market would raise the status of the UAE equity markets within the GCC.

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Equity culture in the UAE is extremely weak. Inexperienced investors invested heavily in the equity market in 2005, driving the price-to-earning ratio to 45 in Abu Dhabi and about 30 in Dubai at their peak in November 2005. Anxiety among retail investors (who dominate both markets) in the face of slowing, albeit still high, corporate profitability growth triggered a sharp sell-off. By early August 2006, Dubai's main index had fallen close to

400 points, a 60 percent decline since the beginning of 2006 that nullified the gains made in 2005. The smaller ADSM fell around a third more. ESCA has begun promoting investor education by printing pamphlets that warn investors of investing based on rumors, incorrect financial information and speculative behavior. Nevertheless, more needs to be done if the equity culture in the UAE is to improve.

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Based on its findings, the Task Force recommends that the following improvements be given priority to help strengthen the framework for corporate governance in the UAE:

- Implement the draft code of corporate governance making compliance mandatory for all listed companies
- Strengthen surveillance and enforcement functions at the regulatory and stock exchange level
- Strengthen the regulatory structure by making ESCA a truly independent entity
- Pursue legal reforms to provide investors with a mechanism by which they can redress grievances in a timely and cost-effective manner
- Introduce rules and regulations to curb insider trading
- Strengthen the corporate governance infrastructure to improve the equity culture
- Increase transparency and disclosure requirements in financial reports through the adoption of International Financial Reporting standards and establish an association of accountants

KEY CORPORATE GOVERNANCE ISSUES

Weak corporate governance framework

The UAE's corporate governance framework is laid out in the UAE companies law that applies to all companies incorporated in the UAE and in the listing requirements of the Abu Dhabi Securities Market (ADSM) and the Dubai Financial Market (DFM). The Emirates Securities and Commodities Authority (ESCA) regulates capital markets in both Abu Dhabi and Dubai. The ADSM has issued corporate governance guidelines for listed companies but has yet to finalize the guidelines. Moreover, the ADSM Corporate Governance Code is intended for voluntary compliance by ADSM listed companies. Both ESCA and DFM are also drafting their own versions of corporate governance codes. It is unclear if these codes will require mandatory compliance.

"The Emirates Securities and Commodities Authority (ESCA) regulates capital markets in both Abu Dhabi and Dubai."

Currently, corporate governance frameworks in Abu Dhabi and Dubai are similar and comply with less than 50 percent of IIF's corporate governance guidelines. However, once Abu Dhabi implements its code of corporate governance, compliance of the Emirate's framework with the IIF code will increase from one-half to over two-thirds. Requirements of the proposed ADSM code of corporate governance include:

- Separating the roles of chairman and CEO
- Defining the concept of independent directors
- A majority of board members to be independent
- The board to meet at least six times a year
- Boards to form sub-committees, in particular, an audit, nomination, remuneration and risk management committee
- Audit committees to consist of at least 3 members, one of whom must have financial and accounting experience and that the committee meet at least once a quarter
- Boards to conduct self assessments through a nomination committee

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- Companies to display all information on their websites or publish it in a newspaper
- Full disclosure of director remuneration and remuneration paid to senior employees above a specified amount
- Board members to disclose any personal interest and company dealings
- The risk management committee to provide risk oversight and to prepare a report
- The audit committee to submit a report on potential risks facing a company
- Immediate disclosure of related-party transactions to the market and shareholders

The GCC Task Force strongly recommends that compliance with any code of corporate governance introduced by ESCA, the ADSM or the DFM should be mandatory if real and significant change is to take place in corporate governance practices in the UAE. Furthermore, ESCA needs to streamline corporate governance requirements between the two UAE stock exchanges. It also needs to involve market participants such as chambers of commerce, accountants, lawyers and consultants in the drafting and finalizing of its code of corporate governance. The recent issuing of the draft code of corporate governance for public comment will help ensure buy-ins from various constituents in the corporate world and strengthen the implementation of the law. ESCA also needs to better assert its regulatory powers over the ADSM and the DFM.

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Legal reform required to enable capital market development

The Ministry of Economy governs the UAE Commercial Companies Law, which lays the basic foundation for capital market development in the Emirates. The UAE's Commercial Companies Law, which focuses heavily on incorporation of companies and is sparse on other issues, is under review, although it is not clear what changes are being considered by the Ministry.

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Several weaknesses have been cited in the existing Commercial Companies Law, particularly with regard to corporate governance. These include weak financial disclosure requirements, no guidance on board structure and no regulation pertaining to related-party transactions. The GCC Task Force calls for a review and revision of rules, regulations and practices influencing capital market development, such as the companies' law and listing rules, to eliminate anomalies that impede growth.

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For example, the Ministry of Economy has been pricing IPOs at a low share price for both state-owned and privately-owned companies to ensure subscription, rather than allowing market forces to indicate an IPO price. As a result, IPOs in the UAE markets are oversubscribed many times and investors are unable to benefit from market signals in making initial investment decisions. This artificial pricing process has discouraged privately-owned companies that would otherwise have gone public and raised funds through an IPO.

Another weakness is the "55 percent" rule, under which companies that list on the ADSM or the DFM have to offer at least 55 percent of shares to the public. This rule is unpopular among the private owners as it requires them to concede control of the company. The GCC Task Force learned that there are several privately held family-owned firms that are in need of equity funding but they are staying away from equity markets because of this rule. There has been discussion of reducing the minimum share offering from 55 percent to between 25-35 percent. However, it is unclear if and when this change might take place.

The authorities also need to address neglected issues in the Commercial Companies Law. For example, the law does not recognize or promote holding company structures, or allow a separation of Board and executive functions, through, for example, separating Chairman and CEO functions and positions and responsibilities. This results in group companies having complicated cross-holding ownership structures that are opaque to investors. Moreover, majority shareholders can exploit cross-holding structures and enter into self-dealing and related-party transactions between individual companies. Nevertheless, several conglomerates in the UAE have created a holding company-like structure, by adopting practices such as preparing financial accounts on a consolidated basis.

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UAE law requires a majority of the board of directors to be UAE nationals which limits the level of expertise and skill on the board as companies struggle to find suitably trained directors. This law could create some difficulties in recruiting independent directors on the board and on various board-level committees. As UAE companies expand business operations beyond the GCC, companies that wish to add international directors to their board will be restricted by the requirement to appoint a majority of UAE nationals.

"ESCA, the federal regulator, is administratively independent but reports to the Ministry of Economy. New laws and requirements must be approved by the Ministry before they are implemented. This reduces the effectiveness of the regulator by stalling the introduction and implementation of decisions."

Need to strengthen regulatory structure and oversight

The UAE's weak regulatory structure affects the overall quality of enforcement of rules and regulations. ESCA, the federal regulator, is administratively independent but reports to the Ministry of Economy because the Minister is the Chairman of ESCA's Board. New laws and requirements must be approved by ESCA's Board before they are implemented. The IIF guidelines recommend a more evolved regulatory structure through the establishment of a fully independent regulator free from political interference, perceived or otherwise.

"ESCA needs to build regulatory capacity and train and develop personnel, especially in its surveillance and enforcement divisions. Moreover, it needs to strengthen the reporting relationship with each stock exchange and increase disclosure requirements."

Operational independence would allow ESCA to react faster to market movements and introduce rules in a timely manner. It would also allow ESCA to assert more authority over the two stock exchanges. ESCA needs to build regulatory capacity and train and develop personnel, especially in its surveillance and enforcement divisions. Moreover, it needs to strengthen the reporting relationship with each stock exchange and increase disclosure requirements.

Sector-specific reforms

In the UAE, Abu Dhabi is the main proponent of privatization and has pushed forward with a number of innovative public-private financing deals in the power and water sectors, a template that is expected to be extended to other areas of infrastructure development in the medium term. The GCC Task Force recommends that the government undertake corporate governance-related reforms in the public sector. Better corporate governance structures in state-owned companies will likely increase the sale value of these companies, thereby realizing greater revenues for the exchequer. Corporate governance-related reforms in line with

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best international practice that need to be implemented in state-owned companies include:

- Increased autonomy for management
- Independent board-level nomination committees to appoint directors
- Reliance on policy-setting by independent regulatory authorities (as in the case of the Telecommunications Regulatory Authority) as opposed to sector ministries
- Focus on profitability by linking senior management compensation to performance

The UAE has a significant number of family-owned conglomerates. Some conglomerates such as Dubai-based Jumeirah and the Majid Al Futtaim Groups have voluntarily improved their corporate governance practices as they look to expand their businesses beyond the Middle East region. However, the broader corporate governance structure in UAE companies generally remains poor. The ownership structure of individual companies within the conglomerates are usually opaque. Often the controlling family retains control by creating complex cross-holdings among subsidiaries. Related-party transactions among subsidiaries and, in particular, related lending is a concern. Reforms need to be tailored to address the specific concerns facing the family-owned conglomerate structure. It is important that, among other things, family-owned companies focus on:

- Voluntarily adopting mechanisms for governance of the family's ownership stake; for example, creating family councils that deal with family disputes
- Reforming company boards by increasing overall board independence and reducing the number of family member-directors
- Limiting the role of family members in senior management
- Increasing transparency of ownership structure and related-party transactions

Targeted reforms in state-owned and family-owned businesses will help strengthen corporate governance practices in listed companies.

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DIFC a catalyst for change[4]

The Dubai International Financial Center (DIFC) has gained some traction since its launch in September 2004. The Center, which was conceived to help position Dubai as a financial hub bridging Europe and Asia, is a purpose built financial free zone with a self-contained regulatory, legal and judicial region based on international best standards and practices. This means that no UAE civil or commercial laws apply in the DIFC and it specifically has its own employment law and independent court and independent financial services regulatory authority. The DIFC's regulatory authority the Dubai Financial Services Authority, is modeled on the UK's Financial Services Authority, and is the sole integrated regulator for the DIFC. However, the actual volume of business conducted at DIFX is still relatively small.

The DIFC has helped raise awareness of corporate governance in the local market. Nevertheless, interest in the Dubai International Financial Exchange (DIFX), which opened in the DIFC in September 2005, has been subdued. It had hoped to attract a large number of bonds, Sukuk (Islamic bonds) and new issues by the end of 2006, along with a draft of secondary listings of companies from various countries. It is still unclear what impact the DIFX will have on the domestic exchanges. Regulatory requirements are stricter for those companies listed on the DIFX, which is looking to attract regional and international firms. If a local company can meet DIFX requirements, it could be advantageous for it to list on the exchange, as new listings will be priced independently of the Ministry of Economy and a minimum stake of only 25 percent has to be listed, compared with a 55 percent minimum on the domestic market.

"It is still unclear what impact the DIFX will have on the domestic exchanges. Regulatory requirements are stricter for those companies listed on the DIFX, which is looking to attract regional and international firms."

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Growing Economic Impact of UAE's Equity Market

Established in 2000, UAE's equity markets are the youngest in the GCC after Saudi Arabia. UAE has two local equity markets – the Dubai Financial Market (DFM) and the Abu Dhabi Securities Market (ADSM). The UAE's equity markets posted strong performances in 2005, with the DFM and ADSM indices gaining 132 percent and 65 percent, respectively (Chart 1 and Chart 2). Together, the two markets posted the highest turnover and largest number of IPOs in the GCC region. Strong corporate earnings were the principal drivers of growth, supported by excess liquidity, low interest rates, and few alternative investment options.

Given this environment, it was little surprise that both markets became seriously overvalued. At their peak, in November 2005, price/earnings ratios were running at 45 in Abu Dhabi and about 30 in Dubai. Inexperienced retail investors, who dominate both markets, lost their nerve in the face of slowing, albeit still high, corporate profitability growth, which triggered a sharp sell-off. By early November 2006, Dubai's main index had hit an 11 month low that nullified the gains made in 2005. The smaller ADSM was around a third lower.

The UAE authorities have attempted to support the market by adjusting the rules governing share buybacks. Buybacks support the market by indicating that firms believe their shares to be undervalued, and by releasing liquidity to chase (fewer) existing shares. However, no firms have yet made any concrete moves to buy back their shares. Meanwhile, second-quarter corporate results have not been strong enough to prompt many retail investors to re-engage. The sharp corrections in the two bourses were also partly attributable to high demand in the primary market, which led to the liquidation of secondary market positions to fund subscriptions for IPO activity.

Chart 1
Comparison of the Dubai stock market index with the MSCI EMEA index from January 1, 2003 to November 15, 2006

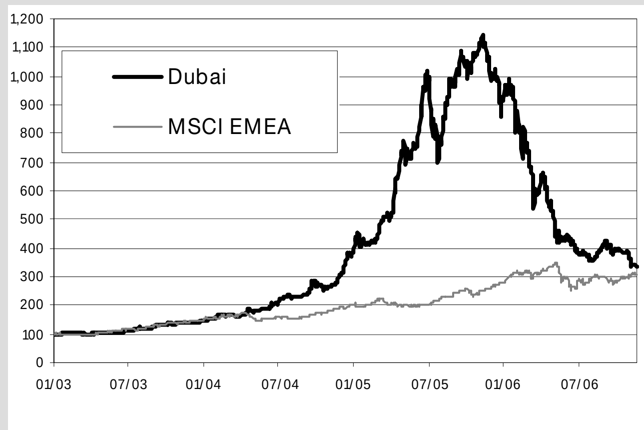
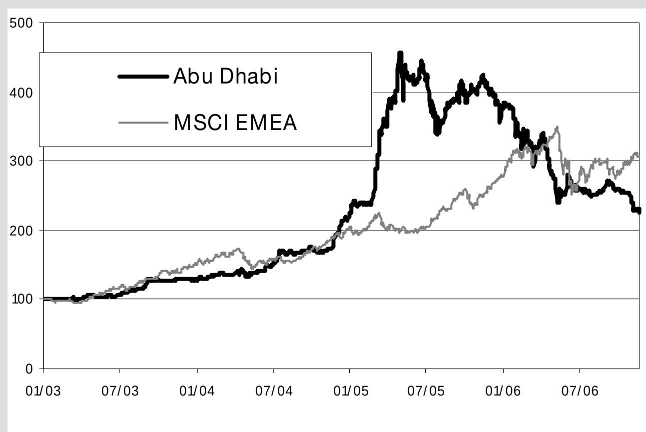


Chart 2
Comparison of the Abu Dhabi stock market index with the MSCI EMEA index from January 1, 2003 to November 15, 2006



UAE's Banking Sector

In broad terms, the UAE's banks are well managed, and effectively supervised. The sector is also enjoying strong growth in assets and profitability. However, there are 47 banks in the UAE, and while most of the major players appear well provisioned against various risks, the level of exposure of some of the smaller institutions to the real estate and equity markets warrant ongoing assessment.

Led by robust growth in deposits and credit, the overall size of banks' balance sheets increased by 40 percent to $166 billion in 2005, while profits more than doubled to $5.1 billion. Macroprudential indicators generally remained strong, with the capital-assets ratio increasing slightly to 17.4 percent. The stock of nonperforming loans rose by 2.4 percent in 2005, but reflecting strong credit growth, the ratio of NPLs to total loans declined to 8.3 percent from 12.5 percent in 2004. Including provisions, the NPL ratio was under 2 percent. Maturity mismatches are still prevalent, however, since lending for infrastructure and construction projects are of a long-term nature and the average maturity of deposits is only three months. While banks have a substantial long dollar position, foreign exchange risk is mitigated by the government's credible commitment to the dollar peg.

Noninterest income, which increased by 112 percent, accounted for about one-third of banks' total earnings in 2005. This reflected the exceptional performance of the UAE's equity markets which generated enhanced revenue streams from sales of mutual funds, brokerage fees, margin lending, and the banks' own investments. Margin lending was perhaps the strongest area of growth, along with healthy gains from interest and arrangement fees for loans made to investors buying IPO shares, subscriptions for which were generally hundreds of times oversubscribed. Income from banks' investment in the markets was also considerable.

Nevertheless, there are concerns that some segments of the population may have over-leveraged themselves in order to increase their exposure to the stock markets, which, given the markets' sharp correction during 2006, may have enhanced systemic risks for the banking sector. The central bank has capped IPO leverage at five times an investor's cash stake, but in practice many banks have been offering leverage at ratios in excess of 1:20. The direct impact of margin lending may be less problematic than the indirect impact, since many banks are unable to say what proportion of their personal or corporate loans have been channeled to the equity markets (insufficient data leads us to be cautious).

In May the central bank issued a circular to commercial banks requiring them to report their estimated level of exposure and instructing them to provide full details of their outstanding loans to both institutional and individual investors. Meanwhile, the sector's profits eased in the first quarter of 2006 and weakened sharply in the second quarter (although by most measures, profitability was still strong).

More generally, there are concerns that in a crowded market, risk assessment procedures are not sufficiently rigorous. There are indications that smaller banks have improved their margins by lending to riskier clients such as expatriate consumers and unproven companies, whose ability to repay has not yet been tested under adverse economic conditions. The situation is not helped by the lack of a functioning credit bureau, which has made it difficult for lenders to gauge a potential borrower's credit history, or their exposure to other organizations. The Dubai Department of Economic Development is working on developing a national credit bureau, but the project has been in the development stages for well over a year and the timetable for launch appears to be edging backwards.

Nevertheless, risk management techniques are likely to become more sophisticated over time, and lending practices should become more discerning, particularly if the market begins to consolidate. Improvements in risk management practices will depend partly on the adoption of Basel II recommendations for capital adequacy and risk categorization. The central bank has completed a detailed study on banks' preparedness for Basel II and is using this as the basis for an implementation plan, although a timetable has not yet been announced. In terms of risk management, the standardized approach will be adopted, although the central bank notes that a lack of corporate ratings in the UAE will hamper the effectiveness of this approach. As a partial remedy, the central bank is encouraging data pooling among banks.

OUTLOOK AND RECOMMENDATIONS

The Emirates have been making efforts to diversify their non-hydrocarbons sector by promoting trade and infrastructure logistics, tourism, real estate development, new economy activities and finance. The authorities have put considerable effort into raising the Emirates profile in the world through marketing strategies and real investment. However, the authorities have made little progress in improving the underlying legal and governance-related framework. A strong commitment to implement better corporate governance practices from the political authorities as well as from senior government officials involved with capital market development is needed for real change to take place.

With the introduction of codes of corporate governance by ESCA, the ADSM and the DFM, the UAE's corporate governance framework is set to improve over the coming year. Current corporate governance-related requirements comply with less than one-half of IIF's corporate governance guidelines. Much needs to be done by way of addressing the weak corporate governance framework and regulatory structure of the country. The GCC Task Force recommends the following action plan to strengthen corporate governance in the UAE:

- Increase compliance of UAE's corporate governance framework with the IIF's guidelines by introducing a code of corporate governance and making compliance mandatory for all listed companies
- Strengthen ESCA as a capital market authority making it fully independent from the government
- Address weaknesses in the legal framework identified in this report
- Harmonize rules and regulation between Abu Dhabi and Dubai to allow for cross-listing of shares in the short-term, with a medium-term objective of unifying the two exchanges
- Strengthen surveillance and enforcement functions at the stock exchange and regulator level
- Introduce a compatible information platform between ESCA and the stock exchanges to allow for easy exchange of data
- Introduce sector specific reforms to improve corporate governance practices in state-owned and family-owned businesses
- Adopt IFRS as an accounting standard for the corporate sector
- Establish an association of accountants or other mechanisms that can spearhead development of accounting practices and regulations in the country
- Invest in building a good corporate governance infrastructure that will strengthen the equity culture by:
  - √ Establishing director training institutes
  - √ Promoting shareholder activism
  - √ Encouraging business schools to provide management training and promote business ethics
  - √ Training journalists in financial and investigative reporting

Specific changes that would strengthen the existing corporate governance framework and make it fully compliant with the IIF's *Policies for Corporate Governance in Emerging Markets-Revised Guidelines* include a number of provisions that will require change in laws and regulations to allow for:

- Introducing cumulative voting in director elections

- Requiring shareholder approval for mergers and major asset transactions such as takeovers
- Establishing a trigger that will instigate a public offer when ownership exceeds 35 percent
- Introducing rules regarding share buybacks
- Establishing a mechanism to resolve conflicts between shareholders and for minority shareholders to formally present a view to the board
- Separating Board Chairman and CEO positions, functions and responsibilities
- Defining "independent" and "non-executive" director
- Requiring that a majority of board members be independent
- Establishing frequency of shareholder and board meetings
- Requiring that the quorum for board of director meetings consist of executive, non-executive and independent directors
- Requiring the board to create audit, compensation and nomination committees
- Mandating full disclosure of all forms of director remuneration
- Requiring board members to abstain from voting if they have a conflict of interest pertaining to the matter being considered and disclosing all material related-party transactions
- Assigning the audit committee the duty to monitor and report risk factors
- Introducing disclosure requirements for off-balance-sheet transactions in the annual report
- Strengthening enforcement

APPENDIX

UNITED ARAB EMIRATES CORPORATE GOVERNANCE FRAMEWORK

The UAE's two financial markets, Abu Dhabi Securities Market (ADSM) and the Dubai Financial Market (DFM), are relatively new entities, both having commenced operations in 2000. Both DFM and ADSM are governed by the same Commercial Companies Law (CL) and Capital Markets Laws (CML). Currently, Abu Dhabi and Dubai have similar corporate governance frameworks and comply with less than 50 percent of IIF's corporate governance guidelines. However, this is expected to change in the near future with the implementation of the ADSM's voluntary corporate governance code, which will strengthen the corporate governance framework of Abu Dhabi.

Minority Shareholder Protection

DFM and ADSM's corporate governance frameworks address about one-half of the minority shareholder protection guidelines contained in the IIF Code. Scope for further improvement in both markets exists by allowing cumulative voting in director elections, treating foreign and domestic investors equally, and requiring shareholder approval for major corporate changes such as takeovers and mergers.

Voting Rights

The voting rights of both ADSM and DFM shareholders are governed by the UAE Commercial Companies Law. The Commercial Companies Law partly complies with the IIF Code's provision on proxy voting. The law stipulates that the proxy must be appointed in writing and be someone other than a member of the board. The representative appointed may not hold more than 5 percent of the company's capital. As a best practice, the IIF Code suggests that proxy voting should be universally available to all shareholders.

The Commercial Companies Law endorses the one-share, one-vote principle by clearly stipulating that every shareholder has a number of votes equal to the number of shares held. This complies fully with the IIF Code's one-share, one-vote requirement for all new issues. However, neither the ADSM nor DFM have provisions regarding cumulative voting, which the IIF Code strongly encourages in director elections.

Company Capital Structure

The IIF Code provides that mergers and other major asset transactions should require shareholder approval, and a public tender offer should be made when ownership exceeds the 35 percent trigger level. There are no provisions in the rules and laws governing DFM regarding shareholder approval of takeovers and mergers. However, ADSM's proposed Corporate Governance Code requires companies to obtain approval from the Emirates Securities and Commodities Authority (ESCA) and ADSM regarding procedures following any takeover, merger, or due diligence investigation. Neither ADSM's nor DFM's legal framework includes provisions on making a public offer when ownership exceeds a certain trigger level.

Both the ADSM and DFM comply with the IIF Code's guidelines regarding capital increases. The IIF Code calls for shareholder approval for any capital increase over a period of one year, and suggests that any capital increase above a minimum threshold should first be offered to all existing shareholders. The UAE's Commercial

Companies Law states that, “capital may be increased with a resolution by the EGM indicating the amount of the increase and the issue value of the new shares.” It goes on to state that companies must publish a notice in two Arabic local daily newspapers notifying shareholders of their priority for subscription to the new shares, its commencement, closing date and value of new shares. The proposed ADSM Code goes further to require that, when issuing new shares to members the company must first consult with ADSM about the method of distribution and communicate with its members at least 10 trading days before commencing the capital increase.

The IIF Code also recommends the disclosure of share buybacks to all shareholders. There are no provisions in the UAE’s laws or regulations regarding this issue.

Shareholder Meetings/Other Rights

According to the Commercial Companies Law, a general shareholder meeting, or Ordinary General Assembly, must be called by the board at least once a year during the first four months following the end of the financial year. Additionally, a meeting notice and agenda must be sent by registered mail to each shareholder at least 21 days prior to the date of the meeting. The notice must also be published in two local daily newspapers issued in Arabic. A copy of the papers must be sent to both the Ministry of Economy and the competent authority. The proposed ADSM Code specifically requires notice for any meeting where an Ordinary Resolution will be considered to be accompanied by an Appraisal Report which contains all information necessary for shareholders. This complies with the IIF Code’s requirement to send a meeting notice and agenda to all shareholders within a reasonable amount of time prior to a meeting.

The UAE’s laws and regulations also comply with the IIF’s Code requirement to allow shareholders controlling a minimum threshold of outstanding shares to be able to call a special meeting. The Commercial Companies Law states that if at least 10 shareholders holding a minimum of 30 percent of the capital request the general assembly to convene, the board must do so within 15 days from the date of the request. In addition, the Ministry of Economy may issue a call for the meeting at the request of the said shareholders or a lesser number who hold a minimum of 30 percent of the capital. Special meetings of the EGA may also be called if requested by shareholders representing at least 40 percent of the company’s capital.

The provisions regarding a quorum in the UAE’s legal framework stipulate that shareholders representing at least 50 percent of the company’s capital must be present to form a quorum. The IIF Code’s best practice recommends a quorum of around 30 percent of shareholders and suggests that some independent non-majority-owning shareholders be present.

The IIF Code also strongly encourages companies to have a mechanism whereby a majority of minority shareholders can trigger an arbitration procedure to resolve conflicts between minority and controlling shareholders. ESCA has the power to arbitrate disputes arising from trades in securities and commodities. However, there is no law that specifically protects minority shareholders. There are no provisions within the UAE’s legal framework to provide minority shareholders with the right to formally present a view to the board of directors if they own some predefined minimum threshold of outstanding shares. The IIF Code strongly encourages this and minority shareholder rights would benefit from the adoption of such a provision.

The IIF Code strongly promotes the equal treatment of domestic and foreign investors. Unfortunately, both the DFM and ADSM only allow foreign investors to own up to 49 percent of a company’s share capital.

Structure and Responsibilities of the Board of Directors

The existing corporate governance framework for both Abu Dhabi and Dubai comply with a little over one-fourth of IIF's guidelines. However, the proposed ADSM corporate governance framework encompasses three-fourths of the guidelines pertaining to the board of directors in the IIF Code. The adoption of a code of corporate governance by ESCA and/or the DFM would help improve board structure in Dubai and the UAE.

Board Structure

The IIF Code encourages the presence of independent directors, or directors who do not have a business or personal relationship with the management or company and are not controlling shareholders on the board of directors. More specifically it recommends that at least one-third of the board should be non-executive, and, as best practice, a majority of board members should be independent.

The proposed ADSM Code defines an independent director as one who has not held a key position in the company during the last three years, had substantial dealings with the company, received additional remuneration apart from director's fees, held a position in the company's audit firm, represented a significant shareholder, held cross directorships, or had a close relative who did. The proposed ADSM Code does specifically mention that the majority of board members must be independent.

The DFM does not specifically have such a principle but adheres to the composition of the board as suggested by the UAE Commercial Companies Law. The Commercial Companies Law states that the board of directors of a company should have three to twelve members, the majority of whom must be UAE nationals. The chairman must be a UAE national. The Commercial Companies Law also states that no one can be a director in more than five public joint-stock companies.

Current requirements in the UAE lack a provision regarding the frequency of board meetings, but the Commercial Companies Law requires the minutes of board meetings to be signed by the directors in attendance in addition to the board secretary and recorded in a book. The proposed code of the ADSM, however, specifically requires directors to meet at least six times a year. This is more frequent than suggested in the IIF Code which calls for a meeting every quarter. The proposed ADSM Code also mentions that an appointed person record the minutes of the meeting with all facts and details discussed in the meeting. Neither the ADSM nor the DFM require the minutes of the meeting to be made a matter of public record. This is one of the IIF Code's stipulations and would improve the disclosure policies of the UAE.

According to the Commercial Companies Law, DFM and ADSM listed company's Ordinary General Assembly elect board members by secret ballot. The law also states that a company has the right to initiate proceedings against board members claiming damages suffered by the assembly of shareholders caused by the board. Any shareholder can independently initiate proceedings when the company fails to do so. The ADSM Code specifically states, "shareholders are responsible for the choice and appointment of the directors on the board." There are no provisions in UAE legislation for nomination committees. Under the IIF Code, a committee, chaired by an independent, non-executive director, should nominate board members.

As for term limits for directors, the Commercial Companies Law states that terms for all directors on the board cannot exceed three years, but a director's term can be renewed at that time. The best practice of the IIF Code recommends that independent directors should be re-elected every three years for no more than three terms.

Board Committees

While the DFM has no provisions for the creation and maintenance of board committees, the proposed ADSM Code calls on boards to form subcommittees which have clearly defined tasks, rights and obligations. The Code states that ADSM listed companies should form a nomination committee, remuneration committee and a risk management committee. This mostly complies with the IIF Code recommendations to establish an audit, nomination and compensation committee to enhance the board's efficiency and the effectiveness of its involvement in the company. The IIF Code, however, also suggests that an independent director chair each of these committees. There is no provision in the ADSM Code regarding the qualifications of the chairmen of these committees.

Disclosure

Both the ADSM and the DFM are subject to the ESCA Board's jurisdiction which requires that companies promptly furnish any information which affects the share price of their securities immediately and states that insider trading deals will be considered null and void. In addition, the ADSM requires companies to disclose all price sensitive information to its members and the ADSM, and immediately disclose to it any changes to information companies previously provided. The DFM specifically requires companies to immediately disclose and report to it any material information that is likely to affect the price of securities or the decision-making of investors. For funds active in the DFM, material disclosure must be accompanied by management reports on business activities which cover full details of the fund's investment portfolio and net value of the fund.

The IIF Code recommends that information be disclosed through local exchanges, and as best practice, through company websites. The Commercial Companies Law requires all accounts and notices to be published in two Arabic local daily newspapers, submitted to the Ministry of Economy for further circulation, and sent via registered mail to shareholders. In addition, the ESCA Board may publish any information that it deems appropriate in the local press or media. The ADSM specifically requires a company to display all information on its website. If it doesn't have a website, the information must be published in a local newspaper.

With regard to remuneration of directors, the Commercial Companies Law requires a company's articles to specify the terms of fixing directors' remuneration. Additionally, the proposed ADSM Code requires the remuneration of senior employees to be disclosed by grouping them into bands of AED 100,000 for anyone receiving AED 300,000 or more, and showing how many employees are in each band. All remuneration paid to directors including share options, incentives, pension, preferential entitlements must be disclosed to shareholders, ESCA, and the ADSM.

Other Responsibilities

With regard to conflicts of interest, the proposed ADSM Code requires board members to disclose to the board of directors any personal interest in any of the company's dealings. The DFM fails to mention the same.

The ADSM and the DFM fail to make provisions for investor relations programs and statements regarding the social responsibility of the company which the IIF Code strongly encourages.

Accounting/Auditing

Current laws for listed companies comply with a little over one-third of guidelines in the IIF Code. With the implementation of the proposed ADSM Corporate Governance Code, Abu Dhabi's corporate governance framework will comply with four-fifths of the IIF's guidelines in this area. The UAE does not have its own accounting standards. The Commercial Companies Law states that accounting principles and practices should be in line with the generally accepted practice and principles of accounting.

<u>Standards</u>

Both the DFM and the ADSM act in accordance with the IIF Code's guidelines to apply accounting rules which comply with International Accounting Standards (IAS). However, the legal frameworks of both the DFM and the ADSM lack any provision regarding the quality of the auditor. The IIF Code encourages companies to appoint independent public accountants that, as a best practice, adhere to the global standards devised by the International Forum on Accountancy Development (IFAD).

The provisions of the IIF Code are also met regarding audit frequency. The ADSM requires companies to provide it and the general public with quarterly un-audited financial reports along with annual audited reports. The DFM requires companies to publish their audited annual financial statements within 120 days of the end of the financial year. DFM listed companies are also required to provide quarterly and half-yearly financial statements and make them publicly available within 30 days of the end of the period. In addition, each report must be accompanied by a management report on the business activities for the period under review. UAE's Commercial Companies Law states that if a company has more than one auditor, each must prepare a separate report.

Further improvements can be made by requiring UAE firms to comply with the IIF Code's guidelines on disclosure of off-balance sheet transactions. Although the proposed ADSM Code complies with the IIF Code by requiring a risk management assessment to be prepared and included in the annual report, the DFM has no such provision.

<u>Audit Committee</u>

While the DFM has no provision for the creation and maintenance of an audit committee, the ADSM's proposed Code requires an audit committee be appointed by the board which provides oversight of the system of internal and external controls. Furthermore, it requires that the committee must consist of at least three members, at least one of whom must have financial and accounting experience, and it must meet at least once a quarter. ADSM listed company boards are also required to review internal control and audit procedures at least once a year and inform ESCA and the ADSM of the results. The committee is also responsible for determining the policy on what non-audit services are acceptable for auditors to engage in. As a best practice, the IIF Code suggests making the details of the external auditor's services and fees a matter of public record and including them in the annual report.

Transparency of Ownership and Control

ADSM's and DFM's current corporate governance frameworks also differ with the ADSM's proposed Corporate Governance Code in terms of their compliance with the IIF guidelines in the areas of firm ownership and control. At present, both the ADSM and the DFM comply with less than one-half of the IIF guidelines in this area. However, with the implementation of the proposed code, ADSM's compliance with the IIF Code would increase to three-fourths. Major improvements could be made by requiring the disclosure of buyout offers and the disclosure of director's and senior executives' shareholdings.

The Commercial Companies Law governing both the ADSM and the DFM require shareholders owning 10 percent or more of the shares of any company, its parent or subsidiary, affiliate or allied company to disclose such information to the market. In addition, anyone owning 10 percent or more of any company and wanting to purchase 20 percent or more shares of the same company must notify the market before placing the purchase order. The DFM adds that a company must include the names of persons who own, with their minor children, more than 5 percent of the company's shares in the board report submitted to the DFM.

Both the UAE legal framework and the laws and regulations governing the DFM lack provisions regarding related-party transactions. In contrast, the proposed ADSM Corporate Governance Code requires companies to immediately disclose to the market and shareholders any material transactions that take place with a related-party. Transparency could be improved with the inclusion of IIF Code provisions that order companies to disclose directors' and senior executives' shareholdings and all insider dealings by directors and senior executives.

Regulatory Environment and Enforcement

Currently, the UAE's regulatory environment complies with a little over one-third of the guidelines of the IIF Code. Improvements could be made by making ESCA a fully independent regulator and training by enforcement authorities.

Comparison of IIF Code and

United Arab Emirates Commercial Companies Law (CL) Securities and Commodities Authority (SCA), Dubai Financial Market (DFM) Listing Rules, Abu Dhabi Securities Market (ADSM) Listing Requirements,

Note: ADSM Corporate Governance Code (Code) is intended for voluntary compliance

		United Arab Emirates	
	IIF	**Dubai Financial Market** **Commercial Companies Law (CL), Securities and Commodities Authority (SCA), Dubai Financial Market (DFM) Listing Rules**	**Abu Dhabi Securities Market** **Commercial Companies Law (CL), Securities and Commodities Authority (SCA), Abu Dhabi Securities Market (ADSM) Listing Requirements, and ADSM Corporate Governance Code (Code)**
Minority Shareholder Protection			
Voting rights			
Proxy voting	Firms are encouraged to allow proxy voting.	Whoever is entitled to attend the general assembly can appoint a representative, other than a member of the board, with authorization in writing. Representatives cannot hold more than 5% of the company's capital. (CL Article 126)	Whoever is entitled to attend the general assembly can appoint a representative, other than a member of the board, with authorization in writing. Representatives cannot hold more than 5% of the company's capital. (CL Article 126)
One share, one vote principle	"One share, one vote" should be a threshold requirement for new issues.	Every shareholder has a number of votes equal to the number of stocks he/she holds. (CL Article 125)	Every shareholder has a number of votes equal to the number of stocks he/she holds. (CL Article 125)
Cumulative voting	Cumulative voting should be permitted.	No provision.	No provision.

Capital structure			
Take-over/buyout/merger -Procedures on major corporate changes	Shareholder approval of mergers and major asset transactions should be required. If an offer is made above a reasonable minimum threshold of outstanding stock, a significant portion of that purchase must be through a public offer. Ownership exceeding 35% triggers a public offer in which all shareholders are treated equally. Under a merger or take-over, minority shareholders should have a legal right to sell shares at appraised value.	No provision.	*The company is required to propose arrangements and procedures to be followed covering any takeover, merger or due diligence investigations or proposals and must obtain approval for those arrangements and procedures in writing from the SCA and ADSM before commencing any formal negotiations or discussions.* *(Code Article 1.2)*
Capital increases (pre-emptive rights)	Shareholder approval is required. Any capital increase over a period of one year and above a minimum threshold must first be offered to all existing shareholders.	Capital may be increased with a resolution by the EGM indicating the amount of the increase and the issue value of the new shares. (CL Articles 199, 201) A statement will have to be published in two Arabic local daily newspapers notifying shareholders of their priority for subscription to the new shares, its commencement, closing date and value of new shares. (CL Article 205)	When issuing new shares to members, the company must agree with ADSM about the method of distribution and communication with its members at least 10 trading days before commencing. (ADSM Article 4.11) Capital may be increased with a resolution by the EGM indicating the amount of the increase and the issue value of the new shares. (CL Articles 199, 201) A statement will have to be published in two Arabic local daily newspapers notifying shareholders of their priority for subscription to the new shares, its commencement, closing date and value of new shares. (CL Article 205)

Share buybacks	Details of share buybacks should be fully disclosed to shareholders.	No provision.	No provision.
Shareholder meeting			
Meeting notice and agenda	Meeting notice and agenda should be sent to shareholders within a reasonable amount of time prior to meetings.	The company must have an Ordinary General Assembly (OGA) at least once a year. (DFM) OGA must be called by the board at least once a year during the first four months following the end of the financial year. (CL Article 119) Notice must appear in two Arabic local daily newspapers in addition to registered letters addressed to each shareholder at least 21 days before the date of the assembly. A call notice must include the agenda of the meeting. A copy of the papers must be sent to both the Ministry of Economy and Commerce and the competent authority. (CL Article 123)	Ordinary General Assembly (OGA) must be held once a year. (ADSM Article 3.2) *A notice of meeting to consider an Ordinary Resolution must be accompanied by an Appraisal Report and contain all information necessary to shareholders.* *(Code Article 2.28)* OGA must be called by the board at least once a year during the first four months following the end of the financial year. (CL Article 119) Notice must appear in two Arabic local daily newspapers in addition to registered letters addressed to each shareholder at least 21 days before the date of the assembly. A call notice must include the agenda of the meeting. A copy of the papers must be sent to both the Ministry of Economy and Commerce and the competent authority. (CL Article 123)

Special meetings	Minority shareholders should be able to call special meetings with some minimum threshold of the outstanding shares.	Auditor can call for a general meeting. (CL Article 120) If at least 10 shareholders holding a minimum of 30% of the capital request that a general assembly be convened, the board must do so within 15 days from the date of request. The ministry may issue a call for a meeting at the request of the said shareholders or a lesser number who hold a minimum of 30% of the capital. (CL Article 121) EGAs can only be called the by the Board. The board can issue this call if requested by shareholders representing at least 40% of the company's capital. (CL Article 139)	Auditor can call for a general meeting. (CL Article 120) If at least 10 shareholders holding a minimum of 30% of the capital request that a general assembly be convened, the board must do so within 15 days from the date of request. The ministry may issue a call for a meeting at the request of the said shareholders or a lesser number who hold a minimum of 30% of the capital. (CL Article 121) EGAs can only be called for by the Board. The board can issue this call if requested by shareholders representing at least 40% of the company's capital. (CL Article 139)
Treatment of foreign shareholders	Foreign shareholders should be treated equally with domestic shareholders.	The maximum foreign investment is 49%. The Articles of incorporation may (or may not) be accompanied by "management" arrangements by which management (and possibly commercial) responsibility is entrusted to the foreign partner. They are required to maintain detailed accounts that should be audited on an annual basis by a firm of auditors with a recognized presence in the UAE. (CL)	The maximum foreign investment is 49%. The Articles of incorporation may (or may not) be accompanied by "management" arrangements by which management (and possibly commercial) responsibility is entrusted to the foreign. They are required to maintain detailed accounts that should be audited on an annual basis by a firm of auditors with a recognized presence in the UAE. (CL)

Conflicts between shareholders	Should have mechanisms whereby a majority of minority shareholders can trigger an arbitration procedure to resolve conflicts between minority and controlling shareholders.	SCA has the power to arbitrate disputes arising from trades in securities and commodities. (SCA, Federal Law No.4 of 2000, Article 4)	SCA has the power to arbitrate disputes arising from trades in securities and commodities. (SCA, Federal Law No.4 of 2000, Article 4)
Quorum	Should not be set too high or too low. Suggested level would be about 30% and should include some independent non-majority-owning shareholders.	This set at shareholders representing at least 50% of the company's capital. (CL Article 128)	This set at shareholders representing at least 50% of the company's capital. (CL Article 128)
Petition rules/objection to majority shareholder actions	Minority shareholders should have the right to formally present a view to the board if they own some predefined minimum threshold of outstanding shares.	No provision.	No provision.
Structure and Responsibilities of the Board of Directors			
Board structure			
Definition of independence	Cannot have a business or personal relationship with the management or company, and cannot be a controlling shareholder such that independence, or appearance of independence, is jeopardized.	No provision.	*Independent director is one who has not held (or his immediate family) during the last 3 years a key position in the company, had substantial dealings with the company, received additional remuneration apart from director's fees, hasn't held a position in the company's audit firm, doesn't represent a significant shareholder and doesn't hold cross directorships.* *(Code, Definitions)*
Share of independent directors	At least one-third of the board should be non-executive, a majority of whom should be independent.	No provision.	*The majority of board members must be independent.* *(Code Article C.1)*

Frequency and record of meetings	For large companies, board meetings every quarter, audit committee meetings every 6 months. Minutes of meetings should become part of public record.	Minutes of the board meeting should be signed by the directors in attendance and the board secretary and recorded in a special book. (CL Article 107)	*The board must meet at least 6 times a year.* *(Code Article C.2)* *An appointed person must record the minutes of the meeting with all facts and details discussed in the meeting.* *(Code, Appendix 2)* Minutes of the board meeting should be signed by the directors in attendance and the board secretary and recorded in a book. (CL Article 107)
Quorum	Should consist of executive, non-executive, and independent non-executive members.	The articles of association of each company specifies the method of its composition, number of members and their term of membership, provided that it should not be less than 3 and not more than 12 years. (CL Article 95)	The articles of association of each company specifies the method of its composition, number of members and their term of membership, provided that it should not be less than 3 and not more than 12 years. (CL Article 95)
Nomination and election of directors	Should be done by nomination committee chaired by an independent director. Minority shareholders should have mechanism for putting forward directors at Annual General Meeting (AGM) and Extraordinary General Meeting (EGM).	The company's ordinary general assembly elects board members by secret ballot. (CL Article 96) The company has the right to initiate proceedings against board members claiming damages suffered by the assembly of shareholders caused by the board. Any shareholder can independently initiate proceedings when the company fails to do so. (CL Article 113)	*Shareholders are responsible for the choice and appointment of the directors on the board.* *(Code, Appendix 2)* The company's ordinary general assembly elects board members by secret ballot. (CL Article 96) The company has the right to initiate proceedings against board members claiming damages suffered by the assembly of shareholders caused by the board. Any shareholder can independently initiate proceedings when the company fails to do so. (CL Article 113)

Term limits for independent directors	For large companies, re-election should be every 3 years with specified term limits.	Terms for all directors on the board cannot exceed 3 years, but a director maybe elected to more than one term. (CL Article 95)	Terms for all directors on the board cannot exceed 3 years, but a director maybe elected to more than one term. (CL Article 95)
Board committees	The board should set up 3 essential committees: nomination, compensation and audit.	No provision.	*The board must form subcommittees which have clearly defined tasks, rights and obligations. Companies should form a nomination committee, remuneration committee and a risk management committee.* *(Code, Appendix 3)*
Formal evaluation of board members	For large companies, nomination committee must review directors ahead of formal re-election at AGM.	In their appraisal and supervision of companies, the Ministry of Economy and Commerce can demand particulars they require from the Board. (CL Article 319)	*The board must conduct a self assessment through a Nomination/Corporate Governance Committee. This should involve the regular review of required mix of skills and experience and recommendations should be submitted to the General Assembly.* *(Code, Appendix 2)* In their appraisal and supervision of companies, the Ministry of Economy and Commerce can demand particulars they require from the board. (CL Article 319)

Disclosure			
Immediate disclosure of information that affects share prices, including major asset sales or pledges	Any material information that could affect share prices should be disclosed through stock exchange. Material information includes acquisition/disposal of assets, board changes, related-party deals, ownership changes, directors' shareholdings, etc.	The company must immediately disclose and report to DFM any material information that is likely to affect the price of the securities or the decision-making of investors. For funds active in DFM, the above must be accompanied by management reports on business activities which cover, full details of the fund's investment portfolio and net value of the fund (DFM). The SCA board can compel anyone with a connection to activities in securities to make a public or private disclosure relating to his activities. Companies must promptly furnish any information which affects the share price of their securities as soon as they are aware of them (SCA, Federal Law No.4 of 2000, Articles 33-34). Insider trading deals will be considered null and void (SCA, Federal Law No.4 of 2000, Article 37).	Companies must disclose all price sensitive information to its members and ADSM. Within 3 months of each financial year, companies must disseminate year end accounts, profit & loss statements, report on company's liquidity. The company must also disclose as soon as it is aware of any changes to information already provided by it. (ADSM Articles 4.1-4.3) The chairman, board of directors or employees of the company cannot exploit inside information or spread rumors for the purpose of buying and selling information. (ADSM Article 4.10) The SCA board can compel anyone with a connection to activities in securities to make a public or private disclosure relating to his activities. Companies must promptly furnish any information which affects the share price of their securities as soon as they are aware of them. (SCA, Federal Law No.4 of 2000, Articles 33-34) Insider trading deals will be considered null and void. (SCA, Federal Law No.4 of 2000, Article 37)

Procedures for information release	Through local exchanges, and as best practice, through company website.	Publication in 2 Arabic local daily newspapers. Submission to the Ministry for further circulation. Registered mailing of notices and circulars. (CL) The SCA Board has the right to publish all information in its knowledge in the local press or media it deems appropriate. (SCA, Federal Law No.4 of 2000, Article 34)	*The company must display all information on its website. If it doesn't have a website, the information must be published in a local newspaper.* *(Code Article C.6)* Publication in 2 Arabic local daily newspapers. Submission to the Ministry for further circulation. Registered mailing of notices and circulars. (CL) The SCA Board has the right to publish all information in its knowledge in the local press or media it deems appropriate. (SCA Federal Law No. 4 of 2000, Article 34)
Remuneration of directors	Should be disclosed in annual report. All major compensation schemes, including stock options, should be fully disclosed and subject to shareholder approval.	The company articles should specify the terms of fixing directors' remuneration. The remuneration must not exceed 10% of the net profit after deduction of depreciation, the reserve and the distribution of a dividend not less than 5% of the capital among shareholders. (CL Article 118)	*The copany must disclose the remuneration of senior employees in bands of AED 100,000 above AED 300,000, showing the number of employees in each band. All remuneration paid to directors including share options, incentives, pension, preferential entitlements must be disclosed to shareholders, SCA and ADSM.* *(Code, Appendix 3, No. 13)* The company articles should specify the terms of fixing directors' remuneration. The remuneration must not exceed 10% of the net profit after deduction of depreciation, the reserve and the distribution of a dividend not less than 5% of the capital among shareholders. (CL Article 118)

Other responsibilities			
Conflict of interest	Any potential or actual conflicts of interest on the part of directors should be disclosed. Board members should abstain from voting if they have a conflict of interest pertaining to that matter.	No provision.	*Any board member must disclose to all board members any personal interest in any of the company's dealings.* *(Code, Appendix 2)*
Integrity of internal control and risk management system	Should be a function of the audit committee.	No provision.	*Risk Management Committee is primarily entrusted with the duties.* *(Code, Appendix 3)* *The Audit committee is also responsible for submitting its report on potential risks faced.* *(Code Article 1.11)*
Investor relations	Should have an investor relations program.	No provision.	No provision.
Social responsibility and ethics	Make a statement on policy concerning environmental issues and social responsibility.	No provision.	No provision.

Accounting/Auditing			
Standards			
National/ International GAAP	Identify accounting standard used. Comply with local practices and use consolidated accounting (annually) for all subsidiaries in which sizable ownership exists.	Companies need to comply with the International Accounting Standards or US GAAP (DFM). The UAE does not have its own accounting standards. The CL states that accounting principles and practices should be in line with the generally accepted practices and principles of accounting (CL).	Companies need to comply with the International Accounting Standards. (ADSM Article 4.2) The UAE does not have its own accounting standards. The CL states that accounting principles and practices should be in line with the generally accepted practice and principles of accounting (CL).
Frequency	Semi-annually audited report at end-FY.	The company must provide and also publish its audited annual financial statements within 120 days of the end of the financial year. The company shall also provide quarterly and half yearly financial statements and make it publicly available within 30 days from the end of the period. Each of the above should be accompanied by a management report on the business activities for the period under review (DFM). The company must issue annual, half-yearly or quarterly reports. (SCA, Federal Law No. 4 of 2000, Article 14) If the company has more than one auditor, each must prepare a separate report. (CL Article 150)	Along with its annual audited yearly report, each company must publish to ADSM and the general public quarterly un-audited financial reports. (ADSM Article 4.2) The company must issue annual, half-yearly or quarterly reports. (SCA, Federal Law No. 4 of 2000, Article 14) If the company has more than one auditor, each must prepare a separate report. (CL Article 150)

Audit quality	Independent public accountant. As a best practice, auditors should adhere to the global standards devised by the International Forum on Accountancy Development (IFAD).	Auditor cannot participate in company incorporation or be a member of the board or be involved in any other technical, administrative or advisory work with the company. Auditor must not be a partner or agent of the company's founder members or a relative of the board up to the fourth degree. Auditor must be registered in the Register of Accountants and Auditors, complying with UAE Federal Law No. 9 of 1975. (CL Article 145)	Accounts must be audited by a legally certified auditor. (ADSM Article 4.2) *Auditor must be proposed by the board. Auditor appointment can be only for one year. No audit firm may be appointed for more than 5 years without approval of a specific shareholders resolution to that effect. No individual partner in the firm may be responsible for the audit for more than 3 consecutive years. Audit firms and audit partners may not be re-appointed before two years having lapsed since their previous appointment ceased.* *(Code Article 1.8)* Auditor cannot participate in company incorporation or be a member of the board or be involved in any other technical, administrative or advisory work with the company. He must not be a partner or agent of the company's founder members or a relative of the board up to the fourth degree. Auditor must be registered in the Register of Accountants and Auditors, complying with UAE Federal Law No. 9 of 1975. (CL Article 145)
Off-balance sheet transactions	Listing requirements should specify disclosure of off-balance-sheet transactions in the annual report with materiality level for disclosure.	No provision.	No provision.

Risk factors/ monitoring procedures	Should be statement from audit committee in reports and accounts addressing business risks. Need a mechanism for review by auditors.	No provision.	*Risk Management Committee must prepare its report.* *(Code, Appendix 3)*
Audit Committee			
Audit committee	For large firms, must be chaired by qualified independent director with a financial background	No provision.	*An Audit committee must be appointed by the board which provides oversight over the system of internal and external controls. Consist of at least 3 members, at least one of whom must have financial and accounting experience and the committee must meet at least once a quarter.* *(Code Article. 1.10)*
Relationship/ communication with internal and external auditors	Committee should approve services provided by external auditor. Breakdown of proportion of fees paid for each service should be made available in annual report. As a best practice, communication with auditors should be without executives present. Contemporaneous provision of audit and non-audit services from the same entity should be prohibited.	No provision.	*The board reviews internal control and audit procedures at least once a year and informs the SCA and ADSM of the results.* *The committee is responsible for determining the policy on what 'non-audit' services are acceptable for auditors to engage in.* *(Code Article 1.8)*

Transparency of Ownership and Control			
Majority ownership	Significant ownership (20-50% including cross-holdings) is deemed to be control.	Company must include the names of persons who own, with their minor children, more than 5% of the company's shares in the board report submitted to the DFM. (DFM) Anyone owning 10% or more of the shares of any company, its parent or subsidiary, affiliate or allied company must disclose the same to the market. (SCA, Federal Law No. 4 of 2000, Article 5) Anyone owning 10% or more of any company and wanting to purchase 20% or more shares of the same company must notify the market before placing the purchase order. The director general of the market in consultation with the Authority may prohibit such a transaction if it is not in the interest of the national economy. (SCA, Federal Law No. 4 of 2000, Article 5) The founding members must subscribe to a minimum of 20% and a maximum of 45% of the share capital of the company. (CL Article 78) A bank or financial institution must get the approval of the Central Bank before any transaction leading to the acquisition of 5% or more of any company. (SCA, Federal Law No. 4 of 2000, Article 5)	Anyone owning 10% or more of the shares of any company, its parent or subsidiary, affiliate or allied company must disclose the same to the market. (SCA, Federal Law No. 4 of 2000, Article 5) Anyone owning 10% or more of any company and wanting to purchase 20% or more shares of the same company must notify the market before placing the purchase order. The director general of the market in consultation with the Authority may prohibit such a transaction if it is not in the interest of the national economy. (SCA, Federal Law No. 4 of 2000, Article 5) The founding members must subscribe to a minimum of 20% and a maximum of 45% of the share capital of the company. (CL Article 78) A bank or financial institution must get the approval of the Central Bank before any transaction leading to the acquisition of 5% or more of any company. (SCA, Federal Law No. 4 of 2000, Article 5)

Buyout offer to minority shareholders	Ownership exceeding 35% triggers a buyout offer in which all shareholders are treated equally.	No provision.	No provision.
Related-party ownership	Companies should disclose directors' and senior executives' shareholdings, and all insider dealings by directors and senior executives should be disclosed.	No provision.	*The company must disclose to the market and shareholders immediately when any material transaction takes place with a related-party.* *(Code Article 1.17)*
Minimally significant shareholders	Shareholders with minimally significant ownership (greater than 3-10%) of outstanding shares must disclose their holdings	Anyone owning 10% or more of any company and wanting to purchase 20% or more shares of the same company must notify the market before placing the purchase order. The director general of the market in consultation with the Authority may prohibit such a transaction if it is not in the interest of the national economy. (SCA, Federal Law No. 4 of 2000, Article 6)	Anyone owning 10% or more of any company and wanting to purchase 20% or more shares of the same company must notify the market before placing the purchase order. The director general of the market in consultation with the Authority may prohibit such a transaction if it is not in the interest of the national economy. (SCA, Federal Law No. 4 of 2000, Article 6)

Regulator			
Enforcement powers	The supervisory authority and the exchange must have adequate enforcement powers. Exchanges should have the power to grant, review, suspend, or terminate the listing of securities. Enforcement authorities should have adequate training and an understanding of the judicial process.	SCA can propose regulations to be issued by the Council of Ministers. It can also make regulations to dictate the functioning, disclosures and the arbitration of disputes within the market. It supervises and controls the functioning of brokers, trading, and membership and has the power to form specialist technical committees. (SCA, Federal Law No.4 of 2000, Article 4) Arbitration Panel of the Authority is presided over by a member of the Judiciary, nominated by the Minister of Justice or the head of the Justice Department and has two members – one nominated by the director general of the market in question and the other by the chairman of the board of the SCA. (SCA, Federal Law No. 4 of 2000, Article 10)	ADSM Board has the right to regularly monitor companies' balance sheets, supervise media activities and reporting to ensure only sound information that conforms to markets rules and regulations are passed to the investing public. (ADSM) SCA can propose regulations to be issued by the Council of Ministers. It can also make regulations to dictate the functioning, disclosures and the arbitration of disputes within the market. It supervises and controls the functioning of brokers, trading, and membership and has the power to form specialist technical committees. (SCA, Federal Law No.4 of 2000, Article 4) Arbitration Panel of the Authority is presided over by a member of the Judiciary, nominated by the Minister of Justice or the head of the Justice Department and has two members – one nominated by the director general of the market in question and the other by the chairman of the board of the SCA. (SCA, Federal Law No. 4 of 2000, Article 10).
Independence of supervisory body and of exchange	The supervisory body and the exchange should be independent from government and industry	SCA enjoys juristic personality and financial and administrative independence. It has the supervisory and executive powers to perform its functions according to the UAE Federal Law No.4 of 2000, Article 2.	SCA enjoys juristic personality and financial and administrative independence. It has the supervisory and executive powers to perform its functions according to the UAE Federal Law No.4 of 2000.

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