

## **Public Companies ... How to bring a Strategic Investor on board**

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Bringing a strategic investor on board of a public joint stock company means in legal terms allowing such strategic investor to inject funds as tier 1 capital, by way of subscribing to a capital raise and becoming a shareholder in the public company. At first glance, the feasibility of such scheme may be defeated by the provisions of Article (204) of the UAE Commercial Companies Law.

In fact, Article (204) confers a preferential right of subscription on shareholders, and precludes waiving such right, even by the Extra-Ordinary General Meeting of the shareholders. Any decision or provision to the contrary is considered null and void. It is our opinion that the text of Article [204] is of public policy related to the protection of minority shareholders upon raise of capital by issue of new shares, to prevent any abuse by majority shareholders and dilution of the shareholding of minority shareholders.

Furthermore, coming from personal experience, the Ministry of Economy is stringent in the application of Article (204) and makes no exceptions.

However, such obstacle may be circumvented by applying a somewhat different scheme whereby capital is raised in the form of bonds mandatory convertible into shares.

In fact, on one hand there exists no provision giving shareholders such preferential right towards subscription to bonds in general or convertible bonds.

On the other hand, Article (204) of the Commercial Companies Law conferring a preferential right of subscription on shareholders, specifically refers to “new shares”, whilst Article (201) provides that “*A raise of capital is effected in one of the following ways: 1) By issuing **new shares**; 2) Merging reserves into the capital; 3) **Converting bonds into shares.***”

Hence, it is our opinion that under UAE laws, the shareholders’ preferential right of subscription is restricted to newly issued shares, and does not encompass convertible bonds.

Shareholders may waive any rights they may have towards subscription to the convertible bonds, by a resolution passed at the Extra-Ordinary General Meeting held to authorize the issue of such bonds.

Accordingly, a public company may adopt a scheme for bonds mandatory convertible into shares, and structure the issue in a way to reflect the special purpose of such scheme.

We shall outline hereunder the rules governing such issue and bonds in general, the rights and obligations of bondholders thereunder, and special provisions and considerations related to convertible bonds.

Articles (177) to (186) of the UAE Commercial Transactions Law lay down the rules governing bonds, rights of holders and the conversion thereof.

A commercial company may, subject to the approval of its general assembly, acquire loans by issuing equal value negotiable bonds. The general assembly may authorize the board of directors to specify the amount of the loan and its conditions. The loan and the terms thereof must be recorded in the Commercial Register and the Ministry of Commerce & Industry and the Competent Authority must be notified.

Hence basically, issuance of bonds may be resolved by an ordinary general assembly's meeting. Bonds are negotiable securities which have equal nominal value, and are issued to subscribers in respect of a loan made to the company. The power to set the amount and terms of the loan may be delegated to the board of directors. However, a resolution of the extraordinary general meeting of shareholders is required to authorize the issue of convertible bonds, given the fact that such issue may eventually involve an increase of capital.

Bonds may be either in the registered/nominal form or in the bearer form. Bonds that are partly paid up must be in the registered/nominal form until they are fully paid.

Loan bonds may not be issued prior to the full payment of the company capital and the publication of at least the balance sheet and profit and loss account for the first financial year, unless the State or one of the banks operating in the UAE guarantees the repayment of such bonds or issues instruments guaranteeing repayment.

Bonds of the same series are to rank equally and without priority one over the other, and shall grant their holders equal rights, notwithstanding any provisions to the contrary.

A bond issue is a global issue; therefore, bondholders are gathered into a general body and are given a collective status. In fact, the established rights of bondholders may not be amended by way of a resolution passed by the shareholders assembly's meeting, except with the approval of bondholders in a special assembly convened in accordance with the same provisions governing the extra-ordinary general assembly of shareholders.

The value of the bond issue should not exceed the amount of the capital as it is displayed in the last approved balance sheet, unless the company was permitted to do so under its incorporation decree or unless the bonds are guaranteed by the State or by a bank operating therein. The resolution concerning the issue of bonds shall only be effective after its registration in the Commercial Register.

The Commercial Companies Law imposes neither a minimum nor a maximum nominal value on bonds. However, bonds of the same issue must have an equal nominal value. Although the bond has to remain as a whole unit and is not divisible into fractions, it is subject to co-ownership.

Bonds are usually issued for consideration equivalent to their principal amount; they may also be issued with a premium or at a discount.

Bonds may also be classified according to whether they are secured or not.

Convertible bonds confer on their holders the right of converting a loan to the company into shares of that same company.

Convertible bonds present a double advantage: safety on the one hand (the holder enjoying a creditor status) and on the other hand opportunity of a speculative gain (the holder benefiting by any increase in the value of the shares upon conversion).

Basically, an issue of bonds convertible into shares is subject to the same provisions as ordinary bonds.

However, certain special provisions and considerations are attached to the issue of convertible bonds.

A resolution of the extraordinary general meeting of shareholders is required to authorize the issue of convertible bonds given the fact that such issue may eventually involve an increase of capital.

As we noted earlier, although convertible bonds confer on their holders the right of converting them into shares, shareholders may not have a preferential right to subscribe to such bonds.

The terms of the issue must contain all items of information concerning the loan (e.g. the basis of conversion) and must specify the date or the periods during which a bondholder may exercise his conversion privilege.

The prospectus for convertible bonds requires the approval of the competent authorities.

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