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CORPORATE GOVERNANCE IN THE SULTANATE OF OMAN
Ellen Kerrigan Dry

I. Introduction

While the United States' capital market has had its headline-grabbing scandals involving companies such as World Com and Enron, the capital market in the Sultanate of Oman (Oman) has also experienced its share of corporate troubles affecting not only large Omani companies such as National Rice Mills SAOG¹ and Oman National Investment Company Holding SAOG,² but also dozens of smaller companies, which have had to turn to the government for assistance.³ Over the years, there have been charges that companies "hide information,"⁴ have poor internal controls⁵ and have negligent,⁶ incompetent and "bungling" boards of directors.⁷ In some instances there have been claims of fraud on the part of directors.⁸ Company mismanagement and ineffective boards of directors share much of the blame for the sharp drop in share prices occurring in 1998 and the ensuing loss of investor confidence.⁹ All of which have underscored the need for higher corporate governance standards.

¹ Palazhi Ashok Kumar, *Related-Party Deals Wipe Out National Rice Mills Network (sic)*, TIMES OF OMAN, Mar. 24, 2002, at 12 [hereinafter, *Related Party Deals*].

² Palazhi Ashok Kumar, *CMA Suspends Trading in Onic Holding Shares*, TIMES OF OMAN, Feb. 14, 2001, at 9 [hereinafter, *CMA Suspends Trading*]; *[Four] Jailed for Breach of Trust and Fraud*, TIMES OF OMAN, May 8, 2001, at 1.

³ Palazhi Ashok Kumar, *Revival Package for 50 Sick Firms Soon*, TIMES OF OMAN, May 12, 2001, at 1 [hereinafter, *Revival Package*].

⁴ *CMA Suspends Trading*, *supra* note 2, at 11; Palazhi Ashok Kumar, *CMA To Introduce Fresh Disclosure Norms*, TIMES OF OMAN, Jan. 29, 2001, at 11.

⁵ *Related Party Deals*, *supra* note 1, at 12.

⁶ Palazhi Ashok Kumar, *Brokerages Seek Probe Into Alleged Post-Issue Fiascos*, TIMES OF OMAN, June 11, 2000, at 9 [hereinafter, *Brokerages Seek Probe*].

⁷ Palazhi Ashok Kumar, *Companies May Have to Recast Boards*, TIMES OF OMAN, Jan. 2, 2002, at 7; *Revival Package*, *supra* note 3, at 1.

⁸ *Brokerages Seek Probe*, *supra* note 6, at 9; *[Four] Jailed for Breach of Trust and Fraud*, *supra* note 2, at 1; see Shilpa Mathai, *After the Crash*, ARABIES TRENDS, Oct. 2000, at 60.

⁹ *Revival Package*, *supra* note 3, at 1; *CMA To Introduce Fresh Disclosure*, *supra* note 4, at 12; *Companies May Have to Recast Boards*, *supra* note 7, at 7; *Brokerages Seek Probe*, *supra* note 6, at 9; Mathai, *supra* note 8, at 60.

Since 1998, the Government of Oman has taken steps to address many of the underlying issues that have led to the problems in its capital market, such as lack of transparency and poor internal controls, conflicts of interest, and confusion over the role and responsibilities of board members. Most recently, in June and August 2002, respectively, the Capital Market Authority (CMA) announced new corporate governance standards for companies with securities listed on the Muscat Securities Market (MSM)¹⁰ and Sultan Qaboos issued a Royal Decree amending the Commercial Companies Law to improve companies' internal controls and encourage independence of their boards.¹¹

This article will examine the development of Oman's capital market, concentrating on the evolution of policies involving corporate governance of companies listed on the MSM. The article summarizes and comments on Oman's current position on corporate governance of publicly-traded companies, including the role of the board of directors, conflicts of interest and related party transactions, liability of directors, the role of the audit committee and the internal and external auditors, disclosure and transparency, and enforcement. In order to understand how and why Oman's corporate regulatory environment developed as it has, a short summary of Oman's history since 1970 is included. The article concludes with comments on the current status of corporate governance in Oman and suggestions that might be considered as the Government considers amendments to the laws or implementing regulations involving the capital markets, in order to improve corporate governance further.

II. Background

Oman opened the door to the modern world in 1970, the year Sultan Qaboos bin Said assumed power. A country of 192,315 square miles located on the southeast corner of the Arabian Peninsula, in 1970 Oman had six miles of paved roads, and a native population of less than one million

¹⁰ Code of Corporate Governance for MSM Listed Companies, Circular No. 11/2002 (June 3, 2002) [hereinafter Code of Corporate Governance] available at <http://www.cma-oman.com>. All references to laws, circulars and regulations in this article, with the exception of references to the draft commercial companies law, note 54 *infra*, are to unofficial translations of the original Arabic text.

¹¹ Oman Chamber of Commerce and Industry, Commercial Companies Law No. 4/74, as amended by Royal Decree Nos. 53/82, 13/89, 83/94, 16/96, 39/98, and 77/02 (May 1997). References in this article to the Commercial Companies Law refer to the Commercial Companies Law No. 4/74, prior to the enactment of Royal Decree No. 77/02 [hereinafter 2002 CCL Amendments].

people.¹² Most Omanis were farmers, coastal traders or Bedouin, making their living growing dates or as shopkeepers, fishermen, or camel herders.¹³ Few people had received formal education; in early 1971, Oman had three primary schools and 30 teachers serving 909 boys.¹⁴ Upon entering into power Sultan Qaboos moved quickly to take the steps necessary to modernize his country, from providing education to all children¹⁵ to establishing a legal framework for commercial development.¹⁶

In the 1970s, sole proprietorships and partnerships were the dominant form of commercial enterprise. In 1974, with the promulgation of the Commercial Companies Law, a legal mechanism existed for the creation and operation of partnerships, joint ventures, joint stock companies, and limited liability companies.¹⁷ Even as enterprises incorporated, it was unlikely that owners of those companies had the intention of selling shares to the “public.” Fourteen years after the Commercial Companies Law was promulgated, in 1988, the MSM was established¹⁸ and a year later began operations with eleven companies listing Omani Rials (OR) 28,452,000 (\$73,975,200) worth of securities.¹⁹

Following the establishment of the MSM, the Government of Oman encouraged local companies to expand and issue securities to the public. Then, as now, a large number of public companies were family-owned with some public float or otherwise closely-held with a small minimum investor

¹² MINISTRY OF INFORMATION, OMAN 2000, at 21, 156 (2000); NATIONAL STATISTICAL DEPARTMENT, MINISTRY OF DEVELOPMENT, DEVELOPMENT IN OMAN 1970 - 1974, 43(1975) [hereinafter DEVELOPMENT IN OMAN 1970 - 1974].

¹³ See DEVELOPMENT IN OMAN, *supra* note 12, at 1, 17, 29, 35, 60; PETER VINE, THE HERITAGE OF OMAN 215 (1995).

¹⁴ DEVELOPMENT IN OMAN 1970 - 1974, *supra* note 12, at 66; VINE, *supra* note 13, at 115 (1995).

¹⁵ Within ten years, the number of students, both boys and girls, in Omani schools rose to 122,143 and the number of teachers rose to 6745. VINE, *supra* note 13, at 116.

¹⁶ In 1974 alone, Sultan Qaboos promulgated the Commercial Companies Law, *supra* note 11, the Commercial Registration Law No. 3/74, the Banking Law (Royal Decree No. 7/74), and the Foreign Business and Investment Law (Royal Decree No. 4/74).

¹⁷ Commercial Companies Law, *supra* note 11.

¹⁸ Royal Decree No. 53/88, Muscat Securities Market Law.

¹⁹ Muscat Securities Market, *MSM Statistics: December 2001*, at 30, available at www.msm.gov.om [hereinafter *MSM Statistics*]. By the end of the year, there were 83 companies listed and a total market capitalization of OR 414,700,000 (approximately \$1 billion) (OR 1.000 equals U.S. \$2.60). *Id.* at 36. .

float.²⁰ The Government of Oman owned some companies. Although the owners may have been reluctant to take their companies public for fear of losing control, the Commercial Companies Law offered protections to their ownership rights. A company could “go public” and be listed on the MSM while the founding shareholders maintained 60% of the shares.²¹ Substantial shareholders (those holding 10% or more of the company’s shares) would automatically be represented on the board of directors and the articles of association could be drafted so that there would be a minority of directors elected by the shareholders.²² If there was any question of the need for control by certain shareholders the company could issue a class of shares with superior voting rights,²³ and establish different classes of shares giving the shareholders of each category the right to elect a certain number or proportion of the members of the board of directors.²⁴ Furthermore, joint stock companies could be established one day and go public and be listed on the MSM almost immediately thereafter. Thus, in the boom years of 1997 and 1998, founding shareholders could raise cash fast. These policies encouraged companies to list securities on the MSM,²⁵ which stimulated the

²⁰ Mathai, *supra* note 8, at 60-61.

²¹ Commercial Companies Law, *supra* note 11, at art. 61. There must be at least three founding shareholders. A single founder may not own more than 20% of the capital in his name or in the name of his children under the age of 18. *Id.* at arts. 60 & 61.

²² “Any person who holds at least 10% of the shares of the company shall have the right to be a member of the Board of Directors if he so wishes. The remaining members of the Board of Directors shall be elected from among the shareholders who hold the minimum number of shares specified by the company’s articles of association.” *Id.* at art. 97. If the Government owns an interest in the Company, the Government share is represented on the board of directors by a person appointed by Royal Decree. *Id.* at art. 132.

²³ *Id.* at art. 75(1).

²⁴ *Id.* at art. 76. The Commercial Companies Law limits the number of members on a board to between five and twelve. *Id.* at art. 95.

²⁵ For purposes of comparison, the number and value of issues listed on the MSM during 1996 was 27 and OR 127,813 (\$332,318), respectively. In 1997, the number of listed issues increased to 37 while their value tripled to OR 373,449 (\$970,967). In 1998, the number of issues listed rose to its height of 47 and the value of these issues increased further to OR 439,898 (\$1,143,735). In 1999, the value of listed issues plummeted more than 50%, to OR 189,346 (\$492,300), with 20 listed issues and dropped another 50% to OR 77,150 (\$200,600) in 2000, with 19 listed issues. *MSM Statistics*, *supra* note 19, at 30.

development of a capital market. However, a capital market with certain inherent weaknesses that would appear once the market faltered.²⁶

Throughout the 1980s and 1990s, it was common for company heads to hold many positions. A company's chief executive officer was also the chairman of the board of directors. The majority of the directors were also substantial shareholders. The managers took instruction on day-to-day affairs from the board of directors. Companies spun off subsidiaries and established holding companies. Oman saw its own growth of conglomerates, many of which continued to be closely-held family enterprises. With the restrictions on a person sitting on more than five boards of directors or acting as chairman of more than three joint stock company boards,²⁷ these family-held conglomerates designated relatives or other proxies to represent their interests on boards.²⁸ The number of related corporations coupled with cross- or interlocking boards meant that although subject to restrictions, fertile ground existed for related party transactions and conflicts of interest could easily present themselves in day-to-day operations. Companies were reluctant to comply with disclosure requirements, especially if such disclosure would negatively impact the price of the companies' shares.²⁹ Notwithstanding the requirement for annual general meetings, minority shareholders in effect had no control or voice in the policies or operation of the companies.³⁰ With management ineffective to sway the board of directors,³¹ and with no power provided to minority shareholders, the specter of mismanagement and misuse of power was just below the surface.

²⁶ *Id.*

²⁷ Commercial Companies Law, *supra* note 11, at art. 95.

²⁸ See Minutes of the Meeting of H.E., the Minister of Commerce and Industry and the Chairman of the CMA Board of Directors with the Chairmen, Executive Presidents and General Managers of Public Joint Stock Companies, Sept. 27, 2000, at 5 - 8 [hereinafter MCI Meeting Minutes].

²⁹ *Id.* at 3.

³⁰ *Id.* at 5-6.

³¹ Another factor, which is common in many countries located on the Arabian Gulf, is that third country nationals (expatriates) fill a large number of the positions in middle as well as upper management of companies. Although these expatriates are generally well qualified, they are more dependent on the good will of their employer (i.e., the company and, in effect, the substantial shareholders who are also on the board of directors) than a native national might. For example, were they to lose their job, they would also lose their visa that permitted them to live in the host country and the other perquisites provided to expatriate managers, such as housing, schooling for their children at private schools, generous leave packages, and automobile. This factor may also contribute to a manager putting the needs of the substantial shareholder above the needs of the company or the minority shareholders.

During 1997 and 1998, Oman's capital market enjoyed a period of spectacular growth. Market capitalization rose to a high of just over OR 3 billion (approximately \$7.9 billion) in 1997,³² tempting new investors to enter the market to take advantage of the riches to be acquired through share ownership. However, in 1999 the market dropped precipitously and while stabilized, it has yet to regain its former highs.³³ Some companies sought assistance from the government while others declared bankruptcy and were de-listed from the MSM.³⁴

There are many reasons for the speculative bubble and the crisis of confidence in Oman's capital market that eventually ruptured it. Some claim it was caused by easy credit for investors.³⁵ Others point out questionable practices of company founders whereby money from an initial public offering sometimes was used for investing in the stock market.³⁶ In hindsight, it is clear that whereas there were many factors that contributed to the troubles in the capital market, a stronger system of corporate governance likely would have protected the market from some of the excesses.

Starting in 1998, the Government of Oman began undertaking a series of steps to ensure that a similar speculative bubble would not reoccur and that the market would grow responsibly. One major step involved the promulgation of the Capital Market Law, establishing the CMA, which reports to the Minister of the Ministry of Commerce and Industry (MCI).³⁷ The Capital Market Law grants to the CMA the authority to "organize, license and monitor the issue and trading of securities [and] supervise the operations of the MSM...."³⁸ In 2000, following the questions raised by the public concerning the reasons behind the financial failures involving many

³² See *MSM Statistics*, *supra* note 19, at 36. The value of the bond market has been subtracted from the market capitalization figures for all years in which there were bonds traded on the MSM.

³³ By the end of 1998, the market capitalization had dropped approximately 35%, to OR 1,937.3 million (approximately \$5,037 million). *Id.* As of July 2002, MSM's market capitalization stood at OR 1,529 million (approximately \$4 billion). Muscat Securities Market, *MSM News*, July 2002, at 5.

³⁴ *Revival Package*, *supra* note 3, at 1; *Companies May Have to Recast Boards*, *supra* note 7, at 7.

³⁵ Mathai, *supra* note 8, at 61.

³⁶ See *Brokerages Seek Probe*, *supra* note 6, at 9.

³⁷ Royal Decree No. 80/98, Establishing The Capital Market Law, at art. 46.

³⁸ *Id.* at art. 48. Prior to the establishment of the CMA, the MSM, under the Minister of Commerce and Industry, performed the dual roles of exchange and regulator.

listed companies,³⁹ the CMA issued a circular addressing corporate governance issues by requiring audit committees, defining the role of the internal auditor, establishing requirements for board membership, and regulating related party transactions.⁴⁰

The year 2001 brought several additional substantive changes: In February, the CMA issued a circular urging companies either to disclose information regarding estimates of audited or unaudited results and other material events that would affect these results or ensure that the information is kept confidential and that no insider trades on the basis of this information or passes it on to others.⁴¹ The circular also included as an attachment revised Rules for Disclosure, which elaborate on standards of disclosure and requirements for audited and unaudited accounts.⁴² In April, the MCI issued the Executive Regulations of the CMA, which provide guidance on the issuance of securities and other aspects of the securities market,⁴³ in August, the MCI transferred to the CMA all terms of reference pertaining to the supervision of public joint stock companies⁴⁴ and the CMA issued circulars on its disclosure policy and on director qualifications and responsibilities, and the conduct of general meetings.⁴⁵ In September, the CMA adopted new conditions for listing on the MSM.⁴⁶

³⁹ See *Brokerages Seek Probe*, *supra* note 6, at 9. But see MCI Meeting Minutes, *supra* note 28, at 1 (Minister of Commerce & Industry states that recently-issued regulations did not come as a reaction to the decline in share prices or the malpractice of some directors).

⁴⁰ See CMA Circular (July 3, 2000) [hereinafter July 2000 Circular].

⁴¹ CMA Circular No. 8/01 (Feb. 6, 2001).

⁴² *Id.*

⁴³ MCI Ministerial Decision No. 4/01, issuing the Executive Regulations of the Capital Market (Apr. 29, 2001) [hereinafter Executive Regulations].

⁴⁴ See CMA Circular No. 31/01 (Aug. 28, 2001), at app. 1, The Terms of Reference to be Assumed by the Authority.

⁴⁵ See CMA Circular No. 29/01 (Aug. 7, 2001); CMA Circular No. 31/01, *supra* note 44, at app. 2-4.

⁴⁶ The MSM offers three markets on which to list shares: the Regular Market, the Parallel Market and the Third Market. In general, more established companies are eligible to trade on the Regular Market, less established companies and established companies no longer meeting the requirements of the Regular Market are eligible to trade on the Parallel Market, and initial public offerings and those that do not qualify for the Regular or Parallel Market are eligible to trade on the Third Market. CMA Administrative Decision No. 16/01, Directives for Listing Securities on Muscat Securities Market for the Year 2001 (Sept. 15, 2001) [hereinafter Listing Guidelines]. Also in 2001, the MSM enabled its electronic trading system to provide the immediate disclosure of transactions by members of board of directors of their

Most recently, the capital market saw several significant changes. In March, the Capital Market Law was amended to provide, among other matters, for additional disclosure and to expand the authority of the Board of Directors of the CMA with respect to the discipline of listed companies.⁴⁷ In June, the CMA issued the Corporate Governance Code, applicable to companies whose securities are listed on the MSM.⁴⁸ In August, Sultan Qaboos issued the 2002 CCL Amendments, which, in particular, address problems related to board of director composition and internal controls.⁴⁹

The Code, drawn from codes of best practices from around the world but adapted to the local market, seeks to promote a “culture of compliance, transparency and accountability without restraining ... business initiative.”⁵⁰ Although certain standards set forth in the Corporate Governance Code have appeared in prior circulars issued by the CMA or MCI,⁵¹ the Code pulls many existing corporate governance standards together in one place, which serves to highlight their importance in the eyes of the Government. The

company’s shares. Muscat Securities Market, *2001 MSM Annual Report*, available at http://www.msm.gov.om/html_pages/anval_report2001.htm, at 7. In addition to those circulars cited in notes 38 to 42, the CMA issued other important circulars throughout the year addressing issues such as disclosure (CMA Circular No. 11/01 (Feb. 26, 2001), re Recommendations of the Technical Accounting and Auditing Committee regarding implementation of IAS 39 and Format of Auditor’s Report, and CMA Circular No. 35/01 (Nov. 7, 2001) re Submission of Financial Statements); related party transactions (CMA Circular No. 15/01 (Mar. 31, 2001) re Rules for Related Party Transactions (subsequently revoked by the Code of Corporate Governance, *supra* note 10, at cover letter by Yahya bin Said bin Abdullah Al-Jabri, Executive President of the CMA [hereinafter Cover Letter], item 6.); internal controls (CMA Circular No. 23/01 (May 15, 2001) re Compliance Officers); and procedures and notice requirements for general meetings (CMA Circular No. 40/01 (Dec. 31, 2001) re General Meetings).

⁴⁷ Palazhi Ashok Kumar, *Royal Decree No. 18/02, Changes to Capital Market Law empower*, TIMES OF OMAN, Mar. 10, 2002 [hereinafter *Capital Market Law Amendments*].

⁴⁸ Code of Corporate Governance, *supra*, note 10, at art. 2.

⁴⁹ Commercial Companies Law No. 4/74, *supra*, note 11. In addition, in February 2002, the Central Bank of Oman issued a circular on Corporate Governance of Banking and Financial Institutions, Circular No. BM/932 (Feb. 4, 2002). The primary purpose of that circular is to clarify the distinction in roles, responsibilities and accountability of the board of directors and management of banks and other financial institutions licensed by the Central Bank. *The Central Bank of Oman Issues Circular on Corporate Governance of Banking and Financial Institutions*, AL-MARKAZI, Mar. – Apr. 2002, at 5 (Cent. Bank of Oman).

⁵⁰ Code of Corporate Governance, *supra* note 10, at Cover Letter.

⁵¹ See, e.g., *supra* notes 41 - 46.

Corporate Governance Code goes further in an effort to promote independence of the board of directors, assure adequate internal controls, clarify the responsibilities of the board of directors, and provide greater protection for all stakeholders of a company. It introduces the terms “non-executive”⁵² and “independent”⁵³ directors, emphasizes the vital importance of the role of the audit committee, replaces the rules for related party transactions found in previous CMA circulars, and encourages companies to adopt still higher practices of corporate governance.⁵⁴

The issuance of the Corporate Governance Code and the promulgation of the 2002 CCL Amendments are significant steps toward Oman’s capital market achieving greater board independence and quality corporate governance. The 2002 CCL Amendments omits the Commercial Companies Law’s requirement that substantial shareholders are automatically entitled to a seat on the board of directors.⁵⁵ This requirement reflected the belief that the interests of the substantial shareholders were the same as those of the company whose shares they owned. The likely result were boards of directors manned by unqualified individuals and the inability of a company to achieve an independent board. Although the requirement of representation may have been eliminated, the mindset of investors and other members of the public will take longer to change; there are many who believe it is only right that the substantial shareholders of a public company exercise total control.

The 2002 CCL Amendments does not address all the issues preventing board independence in fact it serves to hinder other corporate

⁵² A “non-executive” director is “one who is not a regular employee of the company and therefore does not oversee the routine functions of the company on a daily basis.” Code of Corporate Governance, *supra* note 10, at Cover Letter, item 1; *see also id.* at art 1.

⁵³ A director is considered “independent” if he or she:

1. or his/her relative of the first degree has not been a key employee of the company, its parent company, its subsidiaries or fellow subsidiaries in the last [two] years.

2. does not have any direct or indirect material pecuniary relationship or transaction with the company, its significant shareholders, its management, its parent company, its subsidiary or fellow subsidiaries.

See id. at art. 1. The CMA has stated that a director may be considered an “independent director” even if he is a substantial shareholder. *Id.* at Cover Letter, item 1. The CMA has not yet clarified who would be considered a “key employee,” or what “direct,” “indirect” and “material” mean in this context.

⁵⁴ *See id.* at Cover Letter.

⁵⁵ *See* 2002 CCL Amendments, *supra* note 11, at art. 97; *see also supra* note 22 and accompanying text.

governance improvements. For example, it has not altered those provisions of the Commercial Companies Law that permit certain interests to be superior to those of other classes of shareholders.⁵⁶ There is the risk that, even if the company scrupulously follows procedures to avoid conflicts of interest, the company will be run ultimately for the benefit of the substantial shareholders, depriving minority shareholders of influence over decisions.

The Commercial Companies Law is in the process of being rewritten and the draft version of the new law⁵⁷ is more balanced with respect to the rights of shareholders. Furthermore, it does not impede the establishment of high corporate governance standards. It is important that those provisions in the Draft Law are not weakened prior to its promulgation.

III. A Survey of the Status of Corporate Governance in Oman

A. The Board of Directors Qualifications

In Oman, the primary qualification for board membership according to the Commercial Companies Law has been share ownership.⁵⁸ Substantial shareholders, unless disqualified by virtue of being convicted of an offense involving moral turpitude, and representatives of the Government of Oman when the Government is a shareholder, must be given the opportunity to sit on the board of directors of the company.⁵⁹ Others, except "experts," who wish to be elected to a board of directors must own the minimum amount of shares as specified in the company's articles of association and be elected by the shareholders at the annual general meeting.⁶⁰ If permitted by the company's articles of association, the shareholders may elect an expert but

⁵⁶ See e.g., *supra* notes 23 & 24 and accompanying text.

⁵⁷ The government is currently reviewing a draft commercial companies law [hereinafter Draft Law], which has been drafted taking into consideration company laws in countries such as the United States, United Kingdom, Singapore and Australia. References to the Draft Law are to the English version dated May 21, 2002.

⁵⁸ In contrast, although the revised article 97 requires a person nominated to be a director to own "a minimum number of shares as stipulated by the company's by-laws," it does not require a substantial shareholder or his representative be given a seat on the board. Whereas the 2002 CCL Amendments entered into effect on October 1, 2002, the revised Article 97 is applicable to a company upon the occasion of the first election of the board of directors thereafter.

⁵⁹ Commercial Companies Law, *supra* note 11, at arts. 95, 97 & 132.

⁶⁰ *Id.* at arts. 96-97.

an expert may not hold any shares in the company.⁶¹ For every board of directors election occurring after October 1, 2002, when the 2002 CCL Amendments enters into effect, substantial shareholders will no longer be automatically entitled to representation on the board of directors. To be eligible for election, the nominated person must own a minimum number of shares as stipulated by the company's by-laws.⁶² The 2002 CCL Amendments authorizes the Minister of Commerce and Industry to stipulate other conditions and regulations for the election of directors.⁶³

In response to problems concerning the performance of board members that came to light in 1999 and 2000, the CMA issued several circulars, including, in particular, the July 2000 Circular,⁶⁴ Circular No. 31/01⁶⁵ and the Corporate Governance Code.⁶⁶ The July 2000 Circular established qualification requirements, such as minimum age (thirty years old), minimum years of experience (three years) and a demonstrated ability to contribute to the company.⁶⁷ The July 2000 Circular strives for more board independence by introducing the requirement that two non-shareholders, presumably with relevant expertise, must be included in a company's board of directors.⁶⁸ In an effort to oversee the process, candidates must submit their nomination for approval to the CMA in the form prescribed by the CMA, and the CMA has the right to exclude a candidate.⁶⁹ Circular No. 31/01, with a few exceptions, reiterates the qualification requirements of Article 95 of the Commercial Companies Law and the July 2000 Circular.⁷⁰

The Corporate Governance Code explicitly seeks boards that are independent and board members who are ethical, intelligent, and wise,

⁶¹ *Id.* at art. 97. A maximum of two expert directors are permitted to be nominated and elected as board members, in which case the number of members of the board of directors must be increased by the number of expert directors elected. *Id.* This, in effect, reduces the likelihood that the expert directors can have an impact on board decisions. This restriction has been eliminated in article 97 of the 2002 CCL Amendments, *supra* note 11.

⁶² 2002 CCL Amendments, *supra* note 11, at art. 97.

⁶³ *Id.*

⁶⁴ July 2000 Circular, *supra* note 40.

⁶⁵ CMA Circular No. 31/01, *supra* note 44.

⁶⁶ Code of Corporate Governance, *supra* note 10.

⁶⁷ July 2000 Circular, *supra* note 40, at part 2, Appointment of the Board of Directors of the Public Shareholding Companies, items 1 & 4.

⁶⁸ *Id.* at item 7.

⁶⁹ *Id.* at items 1 & 12.

⁷⁰ See Circular 31/01, *supra* note 44, at app. 3, items 1 & 2.

financially literate, and assertive.⁷¹ To be considered independent, a board must consist of a majority of non-executive directors; the roles of the chief executive officer or general manager and chairman may not be combined; and a minimum of one-third of the total strength of the board (subject to a minimum of two) must consist of independent directors.⁷² Although the Code of Corporate Governance does not require every board member to meet each standard, a board member is expected to meet at least one of the following characteristics: the ability to “motivate” people; contribute “strategic insight,” and “[understand] management trends,” as well as have: “expertise in ... accounting and corporate finance,” the “[a]bility to perform during periods of ... crises,” “industry specific knowledge;” and, where applicable, “expertise in international markets.”⁷³

The Draft Law does not provide great detail with respect to qualifications of boards of directors, recognizing that in matters involving the management of a joint stock company, such details should be addressed in the listing rules.⁷⁴ The Draft Law requires that there be at least five directors and imposes age restrictions (i.e., the minimum age for board membership is 25 years and the maximum age is 75, with certain exceptions).⁷⁵

B. Responsibilities of the Board of Directors

The Commercial Companies Law sets forth the basic authority of the board of directors, which is, in essence, to perform all acts required for the management of the company, prepare the company’s balance sheet and a profit and loss statement, and call for general meetings.⁷⁶ The 2002 CCL Amendments grants to the Minister of Commerce and Industry authority to establish regulations regarding the responsibilities of directors.⁷⁷

The primary purpose for the issuance of the July 2000 Circular was to clarify the confusion over the respective roles and responsibilities of the board and management.⁷⁸ The July 2000 Circular states that the board is to play the role of policy-maker by monitoring the acts of the executive management, developing the company’s administrative and financial

⁷¹ Code of Corporate Governance, *supra* note 10, at annexure 1, at 1.1.

⁷² *Id.* at arts. 3.1 - 3.3. However, as stated in the Cover Letter at item 1, a director who is also a substantial shareholder may be considered independent.

⁷³ See Code of Corporate Governance, *supra* note 10, at annexure 1 at 1.2.1 - 1.2.7.

⁷⁴ Draft Law, *supra* note 57, at art. 97.15.

⁷⁵ *Id.* at arts. 97.1(b), 97.3 & 97.5.

⁷⁶ Commercial Companies Law, *supra* note 11, at arts. 102, 105 & 116.

⁷⁷ 2002 CCL Amendments, *supra* note 11, at art. 97.

⁷⁸ July 2000 Circular, *supra* note 40, at prologue.

regulations and appointing the internal auditor and the legal advisor.⁷⁹ The July 2000 Circular reminds board members of their responsibility to comply with the disclosure rules of CMA.⁸⁰ The board is also charged with reviewing and approving the company's estimated budget, and discussing the company's financial statement with the auditor.⁸¹ These requirements are reiterated in appendix 3 of Circular 31/01.⁸²

The Code of Corporate Governance addresses the board's responsibilities in detail.⁸³ The Code envisions that the board will support the company's executive management and actively work to improve management's "competence."⁸⁴ Whereas neither the non-executive board members nor the chairman is to involve himself in day-to-day routine matters, the board is responsible for developing policy both business and financial, which the executive management is to put into effect.⁸⁵ The board also reviews the company's performance to evaluate whether the business is properly managed according to the company's objectives.⁸⁶

The board adopts a system of proper internal controls to ensure compliance with applicable laws and regulations.⁸⁷ An important aspect of proper internal controls is the process by which the board of directors reviews material transactions with related parties,⁸⁸ ensures proper disclosure⁸⁹ and prevents and detects insider trading.⁹⁰

⁷⁹ *Id.* at part 2, items 3, 4 & 5.

⁸⁰ *Id.* at item 7.

⁸¹ *Id.* at items 8 & 9.

⁸² CMA Circular No. 31/01, *supra* note 44, at app. 3, section 2, items 2 - 10.

⁸³ *See* Code of Corporate Governance, *supra* note 10, at art. 5, & annex 1.

⁸⁴ *Id.* at art. 5, art. 12 & annex 1.

⁸⁵ *See id.* at arts. 5.9 & 11 - 15. The board must approve the financial policies of the company based on whether they meet the objectives of the business and maximize shareholders' value. *Id.* at arts. 5.1 & 5.2.

⁸⁶ *Id.* at art. 5.6.

⁸⁷ *Id.* at arts. 5.6 & 5.9.

⁸⁸ The board of directors must review material transactions with related parties, which are not in the ordinary course of business, prior to these transactions being brought before the general meeting of the company. *Id.* at arts. 5.4, 5.7 & 5.8.

⁸⁹ The Code states that it is the role of the board to ensure that the financial statements, price sensitive public reports and reports to the regulators are balanced and understandable. *Id.* at annex 1, item 7.

⁹⁰ The Code requires every company with securities listed on the MSM to "establish, maintain and enforce written policies, procedures and systems of supervision reasonably designed" to ensure full and fair disclosure and prevention of insider trading. *Id.* at annex 1, item 11.

The board selects the chief executive officer or general manager and other key executives and specifies their roles, responsibilities and power.⁹¹ It nominates the members of the subcommittees and specifies their roles, responsibilities and power.⁹² The board also evaluates the functions of the sub-committees, the chief executive officer and key employees.⁹³ Finally, in the annual report, the board reports to the shareholders on the status of the company.⁹⁴

To enable the board of directors to perform its responsibilities, the Code lists the minimum information to be made available to it. This list is detailed, and includes financial information such as budgets and quarterly reports; information on personnel matters, such as recruitment, resignations, removal and remuneration of key executives; information on serious accidents, information on regulatory matters, including non-compliance with any requirement, pollution problems, and possible public or product liability claims of a substantial nature; transactions involving the establishment of joint ventures; substantial payments for intellectual property or goodwill; information on sales of investments, assets and divisions which are not in the normal course of business; and details of any foreign exchange exposure and steps taken to hedge the risks.⁹⁵

Thus, article 5 of the Code of Corporate Governance and the Principles of Corporate Governance, found in annex 1 of the Code⁹⁶ address most of the concerns that have arisen regarding transparency, powers of the board, internal controls, division of powers between management and the board, and qualifications.

The Draft Law requires the board of directors to prepare and approve the company's financial statements, which are to be signed on behalf of the board by an appointed director.⁹⁷ Where the board has approved the financial statements, each director is presumed to have given his approval unless he shows that he took all reasonable steps to prevent their approval.⁹⁸

⁹¹ *Id.* at arts. 5.3 & 5.11.

⁹² *Id.* at art 5.10.

⁹³ *Id.* at art. 5.12. The board's role includes approving an organizational manual that clearly sets forth powers and responsibilities and a comprehensive system delegating power throughout the various levels of management, executive committee, subcommittees of the board and the full board. *Id.* at art. 5.5 and annex 1, item 13.

⁹⁴ *Id.* at art. 14.

⁹⁵ *Id.* at annex 2.

⁹⁶ *Id.* at art. 6.

⁹⁷ Draft Law, *supra* note 57, at art. 146.1. The financial statements are to conform to International Accounting Standards and listing rules. *Id.* at art. 143.4.

⁹⁸ *Id.* at art. 146.5.

The board of directors of a company must also prepare an annual Directors' Report, which is to include a review of the development of the business, details on the assets of the company, information on directors' interests in securities of the company and Group Company,⁹⁹ and whether a director or his or her relative received a right to subscribe, or exercised such right, to the company's securities.¹⁰⁰

C. Remuneration

The Commercial Companies Law sets a ceiling for remuneration and shareholders must vote whether to approve the amount at the general meeting of the shareholders.¹⁰¹ Unless expressly provided for in the company's articles of association, board of directors' remuneration may not exceed 10% of the company's net annual profit, after deducting at least 5% for legal and optional reserves and payment of dividends to the shareholders.¹⁰²

Circular No. 31/01 requires that there shall be a "full" and "detailed" disclosure of "remuneration, salaries" or "charges" of directors.¹⁰³ If remuneration is performance-based, the company must disclose how the performance is measured and the method of calculation.¹⁰⁴

The Code requires a company to develop a "transparent and credible policy for determination of remuneration of directors and key executives, with performance-related elements forming a significant portion of the total remuneration package of the chief executive officer, executive directors and key executives."¹⁰⁵

The Draft Law eliminates the cap on remuneration and benefits of board members, but requires remuneration and benefits of board members be approved by the shareholders at the general meeting and prohibits any other payments.¹⁰⁶

⁹⁹ The term "Group Company" includes a Parent Company and its Subsidiary Undertakings. See *id.* at art. 3.3, for definitions of Group Company, Parent Company, and Subsidiary Undertakings.

¹⁰⁰ *Id.* at art. 147.1.a.

¹⁰¹ Commercial Companies Law, *supra* note 11, at art. 101.

¹⁰² *Id.*

¹⁰³ Circular No. 31/01, *supra* note 44, at app. 3, part 1, item 14; see also July 2000 Circular, *supra* note 40, at part 2, item 14.

¹⁰⁴ Circular No. 31/01, *supra* note 44, at app. 3, part 1, item 14.

¹⁰⁵ Code of Corporate Governance, *supra* note 10, at annex 1, item 12.

¹⁰⁶ Draft Law, *supra* note 57, at art. 98.

D. Conflicts of Interest and Related Party Transactions

The Commercial Companies Law identifies several types of activities constituting conflicts of interest and prohibits directors from engaging in such activities without the prior approval of shareholders. A director may not engage in the management of a business that is a competitor of the company;¹⁰⁷ use the company's assets for his benefit or for the benefit of third parties;¹⁰⁸ enter, directly or indirectly, into any agreement with the company for his account;¹⁰⁹ or have a direct or indirect interest in any transactions or contracts concluded by the company.¹¹⁰ It is not considered a conflict of interest where the contract or transaction is entered into following a public tender and it is the best tender or where the company enters into the contract with customers in the normal course of business.¹¹¹ Even with shareholder approval, a person may not be a board member of more than five joint stock companies, or a chairman of the board of more than three joint stock companies. A person may not be a director of two banks or two insurance companies.¹¹² The 2002 CCL Amendments reduces the limit on the number of cross-board memberships from five to four and the number of cross-chairmanships of boards of directors from three to two.¹¹³ It drops the limitation on bank and insurance companies directorships.¹¹⁴

The July 2000 Circular and Circular No. 31/01 address problems concerning failure to follow procedures for related party transactions and other conflict of interest situations, in particular cross-board and cross-chairmanships of boards.¹¹⁵ The Code of Corporate Governance prohibits related party¹¹⁶ transactions except in four circumstances:¹¹⁷

¹⁰⁷ Commercial Companies Law, *supra* note 11, at art. 107. Approval must be renewed annually. *Id.*

¹⁰⁸ *Id.* at art. 8.

¹⁰⁹ *Id.*

¹¹⁰ *Id.* at art. 108. Approval must be renewed annually. *Id.*

¹¹¹ *Id.*

¹¹² *See id.* at art. 95.

¹¹³ 2002 CCL Amendments, *supra* note 11, at art. 95.

¹¹⁴ *See id.*

¹¹⁵ *Supra* notes 40 & 44. With respect to potential conflicts of interest, the July 2000 Circular prohibits the chairman of the board from being the chief executive and a director from being an executive director in more than one company and limits a person to serving on the board of directors of two companies engaged in the same activity, and no more than three boards generally. One year later, Circular No. 31/01, app. 3, item 10, increased the number of boards on which a person may serve

1. Where the transactions in question are “normal” contracts and transactions in the “ordinary course of business.” “Normal transactions” means routine transactions carried out on a regular basis “in order to achieve the company’s objectives,” without which the company’s objective may not be obtained. These transactions must be disclosed to shareholders at the next annual general meeting.

2. Where the contract is entered into through a “transparent mode” of open tender or limited tender after obtaining and evaluating at least three independent bids in accordance with guidelines prescribed by the audit committee. The best tender must be chosen. These transactions must be disclosed to shareholders at the next annual general meeting.

3. Where the transaction has a value within the limits prescribed in the procurement manual of the company, and is entered into in accordance with the procedure approved by the audit committee.

from three to four. Articles 19 through 25 of the Corporate Governance Code, *supra* note 10, at Cover Letter, at item 6, replace provisions in these circulars regarding related party transactions.

¹¹⁶ “Related party” is defined as:

1. Any person who was [a] director ... [of] the company/parent of the company/subsidiaries [of the company], fellow subsidiary [during the last 12 months], or
2. Chief Executive Officer or any employee reporting directly to the board, or
3. Any person who holds or controls 10% or more of the voting power of the Company or ... its subsidiary ... or parent ... or ... fellow subsidiary ... of its parent..., or
4. Any person who is an associate of any natural person as mentioned under 1, 2, and 3 above. Associate shall include parents, sons, daughters, spouses and business entities wherein 25% or more of the voting power is controlled collectively or individually, or
5. Any person who is an associate of any juristic person as mentioned under 1, 2 and 3 above. Associate shall include parent company, subsidiaries, fellow subsidiaries and business entities wherein the concerned juristic person controls 25% or more of the voting power. It shall also include companies whose majority of the directors act as per the wishes of the concerned company.

Code of Corporate Governance, *supra* note 10, at art. 1.

¹¹⁷ The Code of Corporate Governance requires that companies prepare a “works and procurement policy” and follow it when entering into contracts and other transactions. The works and procurement policy must be filed with the CMA. *See id.* at arts. 19 - 21.

4. Where the transaction, with the recommendation of the audit committee, has prior approval by the shareholders at a general meeting of the company.¹¹⁸ The board must provide a statement to shareholders, as part of the notice of the annual general meeting, that the transaction in question “is fair and reasonable so far as the interests of the shareholders of the company are concerned.”¹¹⁹ The notice must include full details of the terms of the transaction.¹²⁰

Any transaction entered into in violation of the guidelines set forth in the Code is null and void. Any damages are to be borne by the concerned related parties.¹²¹

The auditors are to report on the discharge of the responsibilities of the related party under the contract in the following year.¹²²

The Draft Law differentiates between the procedure followed by directors in case of Conflicts of Interest¹²³ and Related Party Transactions.¹²⁴

¹¹⁸ *Id.* at art. 19. For the approval to be valid:

a. the notice to the shareholders for the purpose of obtaining prior approval ... shall contain the following minimum details:

- [N]ame of the related party.
- Nature and extent of the interest of such party in the transaction.
- Value of the transaction.
- Validity period of the proposed arrangement.
- Any other relevant information.
- In the case of an acquisition or disposal of assets, an independent valuation.
- A statement by the audit committee and the board about the suitability of the terms of the transactions.

b. The approval shall be prior to ... the execution of the transaction.

c. The approval shall not be of [a] general nature.

d. The approval shall be explicit for each transaction with full specific details.

e. The concerned related party is not allowed to participate in the voting.

Id. at art. 19(a)-(e).

¹¹⁹ *Id.* at art. 20.

¹²⁰ *Id.* It is not clear whether this article describes the notice requirement in all cases, or just where prior shareholder approval is required.

¹²¹ *Id.* at art. 25.

¹²² *Id.* at art. 22.

¹²³ A “Conflict of Interest” or “Conflicting Interest” is defined as:

[W]ith respect to a Company the Interest a Director of that Company has respecting a matter relating to the Affairs of the Company or a transaction effected or proposed to be effected by the Company, a

Subject to the listing rules, a director or officer who has a Conflict of Interest must give the board of directors notice of such interest.¹²⁵ The remaining directors consider the matter at a meeting at which the director in question may not attend unless required by the other directors.¹²⁶

Subsidiary Undertaking, a Parent Company of the Company or any Other Entity which the Company Controls) if:

- (a) whether or not the transaction or matter is (or would be) brought before the Board of Directors of the Company for action, the Director knows at the time that he or any of his Relatives is a party to the transaction or has a beneficial financial Interest in, or is so closely linked to, the transaction or matter and that it is of such financial significance to the Director or any of his Relatives, that the Interest would reasonably be expected to exert an influence in the Director's judgment if he was called upon to vote on the transaction or matter; or
- (b) whether or not the transaction or matter is (or would be) brought before the Board of Directors for action, the Director knows at that time that any of the following is either a party to the transaction or has a beneficial financial Interest, closely linked to the transaction or matter and that it is of such financial significance to them, that the Interest would reasonably be expected to exert an influence on the Director's judgment if he were called upon to vote on the transaction or matter:
 - (i) a Person ...of which the Director is a Director, Partner, agent, employee or is in a similar position;
 - (ii) a Person that controls one or more of the Persons specified in sub-clause (i) or a Person that is Controlled by or is under common control with one or more of the Persons in sub-clause (i); or
 - (iii) a natural Person who is a Partner, principal or employer of the Director.

Draft Law, *supra* note 57, at art. 3.3.

¹²⁴ *Id.* at art. 112 – 117. The term “Related Party of a Company” is defined in article 115 and includes a Person who is a Substantial Shareholder; where the Substantial Shareholder is a Company, Directors or other Officers of the Substantial Shareholder; Relatives of Directors of the Company or a Related Company and Relatives of the Substantial Shareholder. A Person is a “Substantial Shareholder” for purposes of the Draft Law if “the total votes attached to Voting Shares ..., which the Person, his Relatives or other Persons, which the first Person Controls, owns, is 5% or more of the total number of votes attached to Voting Shares in the Company.” *Id.* art. 226.1.

¹²⁵ *Id.* at art. 110.1. Exceptions to the notice requirement are found in article 110.3 of the Draft Law. *Id.*

¹²⁶ *Id.* at art. 110.4.

With respect to Related Party Transactions, where “a Company or any Person which it Controls ... give(s) a Financial Benefit¹²⁷ to a Related Party of the Company, the Company or such Person must” either obtain the approval of the shareholders in accordance with Article 114 or “the giving of the Financial Benefit must fall within an exception set out in Article 113.”¹²⁸ If the proper procedure is not followed, the transaction is voidable.¹²⁹

Shareholder approval is not needed where the transaction results from the process of public tender and the offer of the Related Party is the best tender, or the transaction is a usual transaction entered into in the ordinary course of its business and the terms are no more favorable than those offered to unrelated third parties; where “the amount of money given to the Director or other Officer ... overtime does not exceed in aggregate the sum of RO 1,000” (\$2600) or where the Financial Benefit is given “by a Company to a Wholly Owned Subsidiary or it; or by a Wholly Owned Subsidiary of the Company to the Company or to a Person that the Company Controls.”¹³⁰

The Draft Law does not conform entirely with either the Commercial Companies Law or the 2002 CCL Amendments in that it limits the number of cross-board memberships to four, cross-chairmanships to three, and restricts a director from serving on more than two banks or insurance companies boards.¹³¹

E. Shareholder Rights

As discussed above,¹³² while the Commercial Companies Law protects the rights of substantial shareholders, it does not provide a mechanism for minority shareholders to exercise influence. The 2002 CCL Amendments do away with the requirement that substantial shareholders be represented on the board of directors but do not specifically support minority shareholders.¹³³

¹²⁷ The Draft Law intends that the term “Financial Benefit” be interpreted broadly. *See id.* at art. 116.1(a). Article 116 lists those factors that are to be taken into consideration when determining whether a Financial Benefit has occurred.

¹²⁸ *Id.* at art. 112.1.

¹²⁹ *Id.* at art. 112.2; *see also id.* at art. 112.3 (stating exceptions).

¹³⁰ *Id.* at arts. 113.1, 113.5 and 113.6; *see also id.* at arts. 113.1(c), 113.2, 113.3 & 113.4.

¹³¹ *Id.* at arts. 101.2, 101.3 & 101.4; *see supra* text accompanying notes 112 – 114.

¹³² *See supra* text accompanying notes 24-32 & 59 – 60.

¹³³ Commercial Companies Law, *supra* note 11; *see supra* text accompanying notes 55 –56.

The Draft Law permits shares in the company to be divided into more than one class with different rights attaching to the classes.¹³⁴ The rights that may be different include: the right to receive dividends, the right to subscribe to new shares, “and the right to receive notice of and the right to participate and vote in General Meetings in person or by proxy.”¹³⁵ The Draft Law permits cumulative voting for board elections.¹³⁶

Audit Committee

The Commercial Companies Law did not require an audit committee until the promulgation of the 2002 CCL Amendments. The 2002 CCL Amendments require the board of directors form an audit committee in accordance with regulations issued by the CMA.¹³⁷ The CMA first established requirements for audit committees in 2001¹³⁸ and the Code of Corporate Governance expands on those earlier requirements.¹³⁹

The Code requires all companies to have audit committees, consisting of at least three non-executive directors as members, the majority of whom must be “independent directors.”¹⁴⁰ The chairman of the committee must be an independent director and at least one member must have finance and accounting knowledge.¹⁴¹ The Code requires the audit committee to meet at least four times a year and that a majority of the independent members be present throughout the meetings.¹⁴² The terms of reference of the committee identify its objectives, powers, responsibilities, liabilities and remuneration. The audit committee must have the power to invite the finance head and head of the internal audit department to meetings of the audit committee, to ask

¹³⁴ Draft Law, *supra* note 57, at art. 41.

¹³⁵ *Id.* at art. 41.2.

¹³⁶ *Id.* at art. 97.13.

¹³⁷ 2002 CCL Amendments, *supra* note 11, art. 103. The 2002 CCL Amendments specifically addresses the additional liability imposed on members of the Audit Committee. *Id.* at art. 103 (citing article 109 of the Commercial Companies Law). The Draft Law states that, unless exempted by the listing rules, every company must have an audit committee appointed in accordance with, and have the duties specified in, the listing rules. Draft Law, *supra* note 57, at art. 184.

¹³⁸ Circular No.31/01, *supra* note 44, at app. 3, item 8.

¹³⁹ Code of Corporate Governance, *supra* note 10, at art. 7, annexure 3.

¹⁴⁰ *Id.* at art. 7(a); *see supra* text accompanying note 53.

¹⁴¹ *Id.* at arts. 7(b). & 7(c).

¹⁴² *Id.* at art. 7(d).

for information from any employee, and to secure advice from outside experts.¹⁴³

F. Internal Auditor

The 2002 CCL Amendments adds to the Commercial Companies Law the requirement for internal auditors, appointed in accordance with the regulations issued by the CMA.¹⁴⁴ Prior to now, the July 2000 Circular imposed the requirement for internal auditors. The July 2000 Circular requires public companies to appoint an internal auditor who is to report directly to the chairman of the board of directors. The internal auditor is to be familiar with accounting and have the “necessary qualifications and expertise.” Among other duties, the internal auditor is to ensure the company’s compliance with regulatory requirements and immediately report violations thereof.¹⁴⁵ The Code refers to the internal auditor’s role in the oversight of the audit function and review of the internal audit plan.¹⁴⁶

¹⁴³ *Id.* at art. 7(f) at annexure 3 of the Code, The Role of the Audit Committee, includes a detailed list of the responsibilities of the audit committee. The following is a summary of those responsibilities:

1. Recommend auditors, considering, among other things, their independence vis-à-vis their non-audit services, fee and terms of engagement.
2. Review auditors’ audit plan and results and assure that auditors have full access to all relevant documents.
3. Oversee the company’s internal audit plan and results and ensure that internal auditors have full access to all relevant documents. The audit committee may hire consultants if necessary.
4. Approve a system to “ensure adoption of appropriate accounting policies and principles.” Look for financial fraud in the form of fictitious and fraudulent material in the financial statement.
5. Oversee financial statements and discussion of accounting principles in annual and quarterly financial reports, with particular attention to any “departure from International Accounting Standards...[,] non-compliance with disclosure requirements” and changes in accounting policies from previous years.
6. Ensure communication between board and external and internal auditors.
7. Review proposed related party transactions and establish policies for “small value transactions” with related parties.

¹⁴⁴ 2002 CCL Amendments, *supra* note 11, at art. 103.

¹⁴⁵ July 2000 Circular, *supra* note 40, at part 3.

¹⁴⁶ *See* Code of Corporate Governance, *supra* note 10, at annexure 3.

G. Auditors

According to the Commercial Companies Law, auditors are appointed at the annual general meeting and serve a one-year term. A company's auditor may "not provide, regularly," the company or its affiliates with technical, administrative or consulting services.¹⁴⁷

The Code of Corporate Governance provides additional procedural detail. A company's auditor is appointed at the annual general meeting by the shareholders upon the recommendation of the board "after considering the views of the audit committee."¹⁴⁸ The term of contract for the auditor is one financial year, with term limits of four consecutive years.¹⁴⁹ The auditor may not provide other services that may affect its independence.¹⁵⁰

The auditor must report to the shareholders if the auditor has concerns of the "adequacy and efficacy of the internal control systems," the adequacy of the procedures to ensure compliance with legal requirements applicable to the company, and whether the company is a "going concern."¹⁵¹ If the external auditor detects or suspects fraud, this must be reported to the board, unless the fraud is "material," in which case the fraud must be reported to the company's regulator.¹⁵²

The Draft Law requires, subject to the listing rules, every public company appoint an auditor,¹⁵³ appointments are for a one-year term.¹⁵⁴ The auditor has the right to access the company's books and is entitled to obtain from the company's directors and officers such information as is thought necessary to perform the auditor's duties. Furthermore, the auditor is also entitled to information from the company's subsidiary undertaking and its officers.¹⁵⁵ The auditor may attend company general meetings and receive all related notices.¹⁵⁶ The auditor is to prepare an auditor's report to the

¹⁴⁷ Commercial Companies Law, *supra* note 11, art. 111. The term "regularly" is not defined.

¹⁴⁸ Code of Corporate Governance, *supra* note 10, at art. 9(a).

¹⁴⁹ *Id.* at art. 9(b). A firm may be reappointed after a two-year "cooling off period."
Id.

¹⁵⁰ *See id.* at art. 9(c). Item 1 of annex 3, Role of the Audit Committee, states that when evaluating auditors from the perspective of their independence, the audit committee should consider their other, non-audit services.

¹⁵¹ *Id.* at art. 9(d).

¹⁵² *Id.* at art. 9(e).

¹⁵³ Draft Law, *supra* note 57, at art. 167.1.

¹⁵⁴ *See id.* at art. 168.1.

¹⁵⁵ *Id.* at arts. 174.1 & 174.3.

¹⁵⁶ *Id.* at art. 175.

shareholders each year on the company's financial statements and comment on whether the information given in the directors' report is consistent with those financial statements. The auditor's report is to be in accordance with International Auditing Standards and listing rules.¹⁵⁷

H. Disclosure and Transparency

Although the Commercial Companies Law requires reporting of semi-annual and annual financial statements, as well as directors' reports on the company's operations for that year,¹⁵⁸ it does not impose other periodic disclosure requirements.

The Capital Market Law requires an initial prospectus when a company goes public, with subsequent disclosure consisting of annual, semi-annual and quarterly reports on its activities and financial results. In addition, it requires notification of the CMA when a change or amendment to the information provided in the prospectus occurs, a substantial shareholder increases his ownership interests or where a person acquires 35% or more of the securities for the purpose of dominating the company.¹⁵⁹

In March 2002, the Capital Market Law was amended to authorize the CMA to issue rules requiring disclosure of "events and information that may have an impact on their activities or financial position, any change deemed by the Board of Directors of the [CMA] to have an impact on the value of the security."¹⁶⁰

As a result of charges that companies were not being open and transparent, the CMA issued several circulars addressing these issues. Chairmen of the boards of directors are required to attend the company's annual general meeting and answer questions raised by shareholders.¹⁶¹ Companies are required to have procedures that enable them to disclose "material information" in a "fair and timely" fashion and the disclosed information must be "honest, correct, straightforward, and reasonably complete."¹⁶² The board must see that procedures are developed to ensure compliance with disclosure requirements.¹⁶³ As an attachment to Circular No. 29/01, the CMA issued a Disclosure Policy Reference Paper. This Disclosure Policy Reference Paper attempts to clarify terms such as

¹⁵⁷ *See id.* at art. 149.

¹⁵⁸ *See* Commercial Companies Law, *supra* note 11, at arts. 104(1) & 105.

¹⁵⁹ Capital Market Law, *supra* note 37, at arts. 3, 5 & 6.

¹⁶⁰ Capital Market Law Amendments, *supra* note 47, at art. 50.10.

¹⁶¹ July 2000 Circular, *supra* note 40, at part 2, item 15.

¹⁶² CMA Circular No. 29/01, *supra* note 45, part 1, items 1 - 2.

¹⁶³ *Id.*

“important” and “material” information, “fair,” and “timely,” as well as to provide guidance to companies concerning what should be covered in a company’s disclosure policies.¹⁶⁴

The Code of Corporate Governance requires companies to disclose information that will enable shareholders to understand how the company is being run, not just its financial status. The company must include a section in its annual report that describes the company’s corporate governance philosophy and how the company has applied the principles of corporate governance set forth in annex Annexure 1 of the Code;¹⁶⁵ it must provide detail on each member of its board of directors, including whether he is an executive, independent or nominee director, number of other boards or board committees of which he is a member, and his attendance record;¹⁶⁶ it must summarize the terms of reference of the audit committee and other committees, including descriptions of their membership and their attendance records;¹⁶⁷ it must provide details of remuneration and any applicable performance criteria, to all directors and top five officers, including “salary, benefits, perquisites, bonuses, stock options, gratuities, pensions” and severance fees;¹⁶⁸ and it must provide details regarding any penalties or restrictions imposed on the company by the MSM, CMA, or any statutory authority on any matter related to capital markets, within the last three years.¹⁶⁹ Finally, companies are required to include in their annual report a section highlighting non-compliance with any requirement of the Code.¹⁷⁰

According to the Draft Law, in addition to disclosing matters that may be a conflict of interest according to the law, directors must disclose ownership interests in shares and debentures of the company, any of its subsidiary undertakings, parent companies, or subsidiary undertaking(s) of the company’s parent company.¹⁷¹ There is no requirement to disclose transactions occurring during the tenure of the director that do not result in either the initial acquisition of shares or debentures or the termination of

¹⁶⁴ The Disclosure Policy Reference Paper draws on standards applied in the United States, India and United Kingdom. *See id.* at 1.

¹⁶⁵ *See, e.g., supra* text accompanying notes 89, 90 & 93.

¹⁶⁶ Code, *supra* note 10, at annexure 4, item 2.

¹⁶⁷ *Id.* at annexure 4, item 3.

¹⁶⁸ *Id.* at annexure 4, item 5.

¹⁶⁹ *Id.* at annexure 4, item 6.

¹⁷⁰ Code, *supra* note 10, at art. 26.

¹⁷¹ Draft Law, *supra* note 57, at art. 110.8. The Draft Law also authorizes the company to require disclosure by shareholders of the beneficiaries of any voting shares held by the shareholder. *Id.* at art. 233.

ownership. Companies must also disclose when it grants a director the right to subscribe for shares or debentures.¹⁷²

Directors must prepare an annual report, which includes a review of the development of the business, details of each director's interest in the shares or debentures of the company or any group company, whether any rights to subscribe for shares or debentures were granted to or exercised by the director or any relatives of his, and any other information as required by the listing rules.¹⁷³

I. Liability, Defenses, and Enforcement

The Commercial Companies Law sets forth directors' liability where: (1) they engage in prohibited transactions (i.e., conflicts of interest); (2) damage the company through their acts or inaction described below; (3) engage in insider trading; or (4) conceal the true financial position of the company.¹⁷⁴

A director who engages in prohibited transactions, listed below, without the consent of the shareholders at a general meeting, shall be "liable to the company for the profits they have gained from such violation and for the damages arising thereof." Such transactions are voidable.¹⁷⁵ A director may also be held criminally liable and subject to a fine of OR 10 to OR 5000 (\$26 to \$13,000).¹⁷⁶ A prohibited transaction occurs where the director: uses[s] the company's assets or properties for their benefit or for the benefit of third parties, or enter[s], directly or indirectly, into any agreement with the company for their account, except for the ordinary contracts of the type which the company concludes with its customers within the ordinary course of its business.¹⁷⁷

Directors are liable "to the company, the shareholders and third parties for the damages caused by their acts in violation of the law and their acts which fall beyond the scope of their power or by any fraud or negligence in the performance of their duties or by their failure to act as prudent men

¹⁷² *Id.* at art. 110.10(c).

¹⁷³ *Id.* at art. 147.

¹⁷⁴ Commercial Companies Law, *supra* note 11, at arts. 8, 107, 109 & 170.E.

¹⁷⁵ *Id.* at art. 8.

¹⁷⁶ *Id.* at art. 171.C.

¹⁷⁷ *Id.* at art. 8.

under certain circumstances.”¹⁷⁸ If more than one director is liable, each director may be held jointly or severally liable for damages.¹⁷⁹

A director or any “key staff” member is also prohibited from dealing in the company’s securities while using information accessible to him because of his position for the “achievement of a benefit” for himself or his relatives, or from having an “interest, directly or indirectly, with any person involved in activities intended to affect the prices of the securities issued by the company.”¹⁸⁰ If there is more than one director liable, each director may be held jointly or severally liable for damages.¹⁸¹ A director or manager may also be held criminally liable and subject to a fine of OR 10 to OR 5000 (S26–to S13,000).¹⁸²

In these cases, as well as where there has occurred a prohibited related party transaction or other transaction involving a conflict of interest as described above,¹⁸³ either the company may bring an action against the director or a shareholder may propose at the ordinary general meeting that the company sue the director. If the proposal is not adopted, the shareholder himself may bring the action on behalf of the company.¹⁸⁴ Any provision limiting the liability of the members of the board of directors is “null and void.”¹⁸⁵

A director or manager may be held criminally liable if he is found to have intentionally included false information in financial statements or intentionally omitted any essential fact from these documents if the result is to conceal the true financial position of the company.¹⁸⁶ In the case of a criminal conviction, a director or manager is subject to a fine ranging from

¹⁷⁸ *Id.* at art. 109. The term “prudent man” is not defined. Article 103 of the 2002 CCL Amendments, *supra* note 11, states that members of the audit committee are subject to the provisions of article 109.

¹⁷⁹ Commercial Companies Law, *supra* note 11, at art. 109.

¹⁸⁰ *Id.* at art. 107. “Relatives” is defined as minor children and “immediate relatives up to the fourth degree.” *Id.*

¹⁸¹ *See id.* at arts. 107, 109 & 110. Although both directors and key staff members are prohibited from engaging in insider trading and manipulation of the market, the provisions referring to damages only refer to directors, whereas the criminal penalties affect directors and “managers.”

¹⁸² *Id.* at art. 171.C.

¹⁸³ *Id.* at art. 108.

¹⁸⁴ *Id.* at art. 110.

¹⁸⁵ *Id.* at art. 109.

¹⁸⁶ *Id.* at 170.E. In case of conviction, a director may be subject to a fine ranging from OR 10 – 5000 (S26 to S13,000) or to imprisonment from three days to three years, or to both. *Id.* at art. 170.

OR 10 – 5000 (\$26 – \$13,000).¹⁸⁷ The Capital Market Law imposes penalties on directors, managers, and other employees if they engage in insider trading, market manipulation or the intentional filing of “incorrect statements, declarations or information” with the intention of affecting investment decisions.¹⁸⁸ The penalties for these crimes are not less than one month in jail and a fine ranging from OR 10,000 to OR 50,000 (\$26,000 to \$130,000), or both.¹⁸⁹

The 2002 Capital Market Law Amendments authorizes the Board of Directors of the CMA to form a Disciplinary Committee to rule on violations by “the companies whose shares are listed on the Market.”¹⁹⁰ The Disciplinary Committee may impose a caution, warning, or a fine not exceeding OR 5000 (\$13,000) on companies whose shares are listed on the MSM.¹⁹¹

The July 2000 Circular states that board members are subject to joint and several liability for damages caused by their acts in violation of the law and their acts which fall beyond the scope of their powers or by any fraud or negligence in the performance of their duties.¹⁹² However, Circular No. 31/01 changes the standard to joint liability,¹⁹³ which appears to conflict with article 109 of the Commercial Companies Law.¹⁹⁴

The Code states that any transactions in conflict with the related party transaction provisions¹⁹⁵ shall be null and void,¹⁹⁶ in comparison to the Commercial Company Law, which says transactions involving conflicts of interest are voidable.¹⁹⁷ Any damages are to be borne by the related parties.¹⁹⁸ Companies are required to include in their annual report a section highlighting their non-compliance with any requirement of the Code.¹⁹⁹ The Draft Law has not yet elaborated on the penalties for breach in detail,²⁰⁰ but it

¹⁸⁷ *Id.* at art. 171.

¹⁸⁸ Capital Market Law, *supra* note 37, at arts. 64 & 65.

¹⁸⁹ *Id.* at arts. 64–66.

¹⁹⁰ Royal Decree 18/02, *supra* note 47, at art. 63A.

¹⁹¹ *Id.* These provisions do not refer to a penalty on the people as individuals, just on the company.

¹⁹² July 2000 Circular, *supra* note 40, at part 2, item 1.

¹⁹³ CMA Circular No. 31/01, *supra* note 44, at app. 3, item 1.

¹⁹⁴ 2002 CCL Amendments, *supra* note 11.

¹⁹⁵ See *supra* text accompanying notes 116-21.

¹⁹⁶ Code of Corporate Governance, *supra* note 10, at art. 25.

¹⁹⁷ See Commercial Companies Law, *supra* note 11, at art. 8.

¹⁹⁸ Code of Corporate Governance, *supra* note 10, at art. 25.

¹⁹⁹ *Id.* at art. 26.

²⁰⁰ See Draft Law, *supra* note 57, at art. 341.

does provide more guidance and protection to directors. Directors and officers “must exercise their powers and discharge their duties in good faith for a proper purpose, and must always act in the best Interests of the Company ... with prudence, care and diligence in all of the circumstances.”²⁰¹ Directors “who [make] a Business Judgement”²⁰² meet this requirement if they:

- (a) make the Business Judgment in good faith and for a proper purpose;
- (b) do not have a material personal Interest in the subject matter of the Business Judgment;
- (c) inform themselves about the subject matter of the Business Judgment to the extent that it is appropriate in the circumstances;
- (d) rationally believe that the Business Judgment is in the best Interests of the Company....²⁰³

The Draft Law adds protection for directors by permitting directors and officers to rely on information and advice so long as that reliance is “reasonable.” The reliance is presumed to be reasonable if:

- (a) he relies on information, or professional expert advice, given or prepared by:
 - (i) an employee ... whom the Director or Officer believes on reasonable grounds to be reliable and competent in relation to the matters concerned; or
 - (ii) a professional adviser or expert in relation to matters that the Director or Officer believes on reasonable grounds to be within the Person’s professional expertise and competence; or
 - (iii) another Director or Officer in relation to matters within such Director’s or Officer’s authority; or
 - (iv) a committee of Directors or Officers on which the Director or Officer did not serve in relation to matters within such committee’s authority;”
- (b) the reliance was made in good faith and after making an independent assessment of the information or advice; and

²⁰¹ *Id.* at art. 107.1.

²⁰² A Business Judgement means “any decision to take or not to take action” with respect to “any matter relating to a Company.” *Id.* at art.3.3.

²⁰³ *Id.* at art. 107.2.

- (c) the question of whether or not the Director or Officer was exercising his powers or discharging his duties in accordance with Article 107.1 in relying on the information or advice, arises in proceedings brought to determine whether a Director or Officer has performed a duty under this [Draft] Law or an equivalent duty under any other Law of Oman.²⁰⁴

If the proper procedures for approving a conflict of interest transaction are not followed, the relevant board resolution is “null and void and any advantages secured to the Director shall be owed to the Company and any loss incurred by the Company as a result of the Resolution shall be made good by the Director.”²⁰⁵ With respect to a related party transaction, if the proper procedure is not followed the transaction is voidable.²⁰⁶

Directors and officers are responsible for actions taken by others pursuant to a delegation of power, duty, or responsibility. They are not responsible for improper actions of the delegate so long as they “believed: (i) on reasonable grounds; (ii) in good faith; and (iii) after making proper inquiry, (if circumstances indicated the need for inquiry), that the delegate was reliable and competent in relation to the power delegated.”²⁰⁷

The Draft Law prohibits a director or officer from improperly using his position to gain advantage for himself or “someone else” or causing “detriment” to the company²⁰⁸ and improperly using information obtained because of his position to gain an advantage for himself or another person²⁰⁹ or otherwise causing “detriment” to the company.”²¹⁰

The directors and officers must compensate the company, its shareholders, and third parties “for any losses caused to them by any breach or failure to comply with the provisions of [the Draft Law] by such Directors

²⁰⁴ *Id.* at art. 108.

²⁰⁵ *Id.* at art. 110.5.

²⁰⁶ *Id.* at art. 112.2; *see also id.* at art. 112.3 (noting exceptions).

²⁰⁷ *Id.* at art. 109.

²⁰⁸ *Id.* at art. 107.3. This provision is broader than that set forth in article 107 of the Commercial Companies Law, *supra* note 11, because, instead of being limited to certain relatives, it applies to a more general “someone else.”

²⁰⁹ A “Person” can be either a natural or juristic person. Draft Law, *supra* note 11, at art. 3.3.

²¹⁰ *Id.* at art. 107.4. This clause is also broader than that found in article 107 of the Commercial Companies Law in that it applies to both current and past directors and officers who because of that position obtain and use the information.

or Officers, or by any acts or omissions that are beyond the scope of the authority of such Directors or Officers.”²¹¹

In the event the company enters into the insolvency process, and if the receiver or liquidator or other administrator forms the opinion that a director has, among other acts, breached any duty owed to the company, then a motion may be made to the court to require the director to “make any contributions to the company’s assets that the court thinks proper in the circumstances.”²¹²

The Draft Law provides that an officer may use as a defense against any claim made under the Draft Law evidence that he took all “reasonable steps in the circumstances.”²¹³ The “reasonableness of such steps shall be determined by reference to the nature and extent of the obligation which it is alleged such Officer failed to comply with.”²¹⁴

Although the Corporate Governance Code institutes many important requirements, it is not evident from the text of the Code how the CMA plans to enforce the provisions of the Code and to what extent it will rely on voluntary compliance. The Code requires shareholders be informed in a section of the annual report of the composition and independence of board members and the company’s efforts on corporate responsibility. The report must highlight areas in which the company is not in compliance.²¹⁵

IV. Conclusions, Recommendations and Comments

Oman is well on the way to implementing a model corporate governance system for its capital market. The Code of Corporate Governance incorporates many important measures, which will provide greater transparency, director responsibility, and independence of the board. The latest revisions to the Commercial Companies Law, by eliminating the right of substantial shareholders to seats on the board, eliminate a major hurdle to achieving board independence. The adoption of a new Commercial Companies Law, substantially similar to the draft currently under consideration, will facilitate the CMA’s efforts to institute a high standard of corporate responsibility and related accountability. These are significant achievements in a relatively short period of time, yet there are other

²¹¹ *Id.* at art. 107.5.

²¹² *Id.* at art. 338.

²¹³ *Id.* at art. 343. The Draft Law includes directors in the definition of the term “officer.” *See id.* at art. 3.3.

²¹⁴ *Id.* at art. 343.

²¹⁵ Code of Corporate Governance, *supra* note 10, at arts. 26 & 27.

measures that could be considered to advance improved corporate governance.

In Oman, it is the government regulator, rather than the exchange, that promulgates listing standards. By stating that the listing rules govern in certain instances,²¹⁶ the Draft Law acknowledges that companies with securities listed on the MSM should be held to a different standard than privately held companies and that the CMA is the appropriate institution to determine that standard. By including corporate governance standards in listing rules, the CMA can not only be more flexible and amend the listing rules as it identifies problems, but can wield a potent enforcement mechanism: the threat of delisting. The Listing Guidelines currently establish entry requirements for companies wishing to list their securities on the MSM.²¹⁷ These entry requirements focus primarily on the size and strength of the company to determine on which level of the market (i.e., Regular, Parallel or Third Market) the company's securities should be traded, rather than on other substantive issues, now addressed in the Code of Corporate Governance and other circulars, that are important for ensuring the quality of ongoing operations of the companies themselves as well as the reputation of the MSM.²¹⁸ Even before the Draft Law is promulgated, the CMA could incorporate, either directly or by cross-reference, many or all of the provisions of the Code of Corporate Governance and other ongoing disclosure requirements into its Listing Guidelines, thereby tying non-compliance with the Code to the threat of de-listing or relegation to a lower rung of the trading markets on the MSM.

A. Boards of Directors

The 2002 CCL Amendments moves Oman in the right direction by eliminating the correlation between substantial share ownership and board membership. The 2002 CCL Amendments gives the Minister of Commerce and Industry the authority to establish regulations regarding the authority of boards of directors. The Minister should use this authority to formalize and thereby add more regulatory weight to the provisions found in the Code of Corporate Governance.²¹⁹

Although the CMA in its Code of Corporate Governance goes far in promoting independence of the board, it stopped short when it concluded that

²¹⁶ See, e.g., Draft Law, *supra* note 57, at arts. 11.1, 13.3, 20.3, & 76.1.

²¹⁷ See *supra* text accompanying note 46.

²¹⁸ *Id.*

²¹⁹ See *supra* text accompanying notes 77, 83-96.

until such time as the director who is also a substantial shareholder is involved in a material transaction with the company, he can be considered an "independent" director.²²⁰ Whether or not the substantial shareholder can be objective in performing his role as a director should not be the dispositive issue. Just as important is the value that attaches to a market that is seen to avoid even the appearance of impropriety. This is especially true in Oman where substantial shareholders are often the founding shareholders, are likely to be controlling shareholders and in any event are assumed by many to have a more personal interest and influence in the affairs of the company even if they are not part of management. If this interpretation of the Code stands, the two independent directors who are required by the Code of Corporate Governance to serve on the audit committee, as well as the audit committee's chairman, could be substantial shareholders.²²¹ The audit committee is charged with many important functions, such as the approval process for related party transactions.²²² It is not enough that the Code does not permit the members of this committee to be part of management.²²³ They should also not be substantial shareholders. Furthermore, the Draft Law should incorporate provisions requiring a minimum number of truly independent board members serve on boards and certain committees, such as the audit committee.

The Draft Law appears to raise the standard of responsibility of individual board members for the accuracy of a company's financial statements by stating that all members are presumed to have approved the financial statements unless they can show that they took "reasonable" steps to prevent their approval.²²⁴ Although this does not appear to go so far as to require the board to "certify" the financial statements, it does seem to impose a higher duty to inquire deeply into the details of what they are approving, which should lead to increased investor confidence. Furthermore, both directors and officers are subject to personal liability for losses to the company, its shareholders and third parties caused by their breach of or

²²⁰ See *supra* text accompanying note 53.

²²¹ Code of Corporate Governance, *supra* note 10, at arts. 7(a) & 7(b).

²²² *Id.* at art. 19. The audit committee also is charged with, for example, oversight of the internal audit and internal control functions. *Id.* at annexure 3, items 4 & 5.

²²³ See *id.* at art. 7(a).

²²⁴ See *supra* text accompanying notes 97 & 98. It is noteworthy that in Oman it would be the directors who are asked to approve the statements whereas in the United States it is the chief executive officer or chief financial officer. This may be in recognition of the fact that, in Oman, the board continues to have as great as if not greater influence in the operation of the company and knowledge of the facts than management.

failure to comply with the provisions of the Draft Law or by any of their acts or omissions beyond the scope of their authority.²²⁵

It appears that the Draft Law would relax the existing provisions on board remuneration. Whereas the Commercial Companies Law imposes a cap on remuneration and Circular No. 31/01 and the Code of Corporate Governance require disclosure and a credible policy for establishing remuneration, respectively, the Draft Law merely requires that the remuneration be approved by shareholders at the general meeting.²²⁶ Although it is appropriate that shareholders be required to approve the remuneration package and that no other remuneration is permitted, the CMA should be aware of trends in compensation and whether some forms of compensation are going unreported. The CMA should periodically examine executives' and directors' compensation packages in Oman in order to understand compensation trends, such as the amount or value of the different forms of compensation, the extent to which stock options are utilized and, if so, how such stock options are treated on the books of the company. The CMA should be aware of alternate forms of remuneration, such as the granting of low interest loans to board members and executives so as to determine whether such forms should be either disclosed or prohibited.

Whether or not remuneration is seen to be a problematic issue in Oman, it may be appropriate to lay the groundwork for regulation in this area, either by stating in the Draft Law that the issue of remuneration may be dealt with in the Listing Rules or by specifically including in the Draft Law parameters on the purposes of and types of compensation (e.g., benefits, stock options, cash, other perks), amount of compensation, and the basis of calculation of compensation if performance-related, and establishing the approval and disclosure requirements.

Although the Draft Law does not address the issue, it is apparent by the fact that cross-board memberships is referred to in the Commercial Companies Law, several subsequent circulars, and the 2002 CCL Amendments, that the issue of how many and what types of cross-board memberships should be permitted is of concern in Oman.²²⁷ Cross-board memberships create potential conflicts of interest, especially in a small capital market. If interlocking boards are also prevalent, there is even greater danger of conflicts of interest and related party transactions. Also, it takes time to do a good job as a director. It is not in the best interests of a company to have as a director someone who is over-committed. Therefore,

²²⁵ See *supra* text accompanying note 211.

²²⁶ See *supra* text accompanying notes 101-06.

²²⁷ See *supra* text accompanying notes 112 & 115.

it is reasonable to impose a limitation on board memberships in the case of companies whose securities are listed on the MSM. Although the 2002 CCL Amendments provide the most recent determination on the limits of cross-board membership,²²⁸ it may be best to provide in the Draft Law that the Listing Guidelines address this issue. This change would grant more flexibility to address changing conditions in the capital market. Although the Draft Law, like the 2002 CCL Amendments, permits the possibility that substantial shareholders will not control the board, it continues to permit companies to control which shareholders have the right to vote on issues that the law says must be approved by shareholders through the creation of different classes of shares.²²⁹ This poses the question as to why Oman considers it necessary to grant voting rights to the shareholders of one class of shares while denying voting rights to those holding another class of shares? What type of shareholder is the provision designed to protect? In some countries foreigners are permitted to buy only non-voting shares in order to protect the local shareholders. In other countries, the restriction is permitted so that the founding shareholders can prevent others from affecting policy. The CMA should seriously consider whether it is in the best interest of the capital market to allow a listed company to issue shares that do not permit shareholders of such shares to vote. If it is deemed appropriate that certain types of companies should be permitted to create different classes of shareholders with unequal voting rights, is it really necessary to extend the right to all types of companies?

B. Audit Committee

It is important that the provisions in the 2002 CCL Amendments regarding audit committees be incorporated into the final version of the Draft Law.²³⁰ The Listing Guidelines should include the audit committee requirements similar to those currently found in the Code of Corporate Governance.²³¹ Having the requirements for audit committees in the Listing Guidelines will give the CMA flexibility if the need arises in the future to adjust the requirements.

²²⁸ 2002 CCL Amendments, *supra* note 11, at art. 95.

²²⁹ Draft Law, *supra* note 57, at art. 41

²³⁰ 2002 CCL Amendments, *supra* note 11, at art. 103; *see also supra* text accompanying notes 137- 43.

²³¹ *See supra* text accompanying notes 140 - 43.

C. Internal Auditor

The role of an internal auditor is important, especially for publicly-traded companies. As permitted by the 2002 CCL Amendments, the Listing Guidelines should set forth minimum requirements for internal auditors along the lines of those currently set forth in the July 2000 Circular and the Code of Corporate Governance.²³²

D. Auditors

The Draft Law addresses an important issue by clearly stating that auditors are entitled to obtain information.²³³ It may be reasonable to incorporate additional provisions, already found in the Commercial Companies Law and circulars, given what other authorities have found recently. For example, the Draft Law states that the auditor's term is one year.²³⁴ Because it is not specifically addressed, it is assumed that the auditor may be elected for subsequent terms and there are no term limits. The Code of Corporate Governance provides for one-year terms and a term limit of four consecutive years.²³⁵ Although it is true that auditors may not note some problems until the second year of their term, it is also true that periodic changes in auditors may serve to identify areas that have gone unquestioned. On the other hand, commentators have pointed out that it is illogical to require companies to terminate an auditing relationship without a reason, especially since there are now fewer auditors in business from which to choose.²³⁶

The second issue is whether to permit the auditor to provide other consultancy services. The Commercial Companies Law prohibits auditors from providing on a "regular" basis other services to the company.²³⁷ The Code of Corporate Governance prohibits an auditor from providing "non-audit" services that "might affect their independence" to the company.²³⁸ The Draft Law is silent on the issue. The issue of whether or not a company's auditors may also act as the company's consultants is important. It should be determined which types of consulting services are inappropriate,

²³² See *supra* text accompanying notes 144 - 46.

²³³ Draft Law, *supra* note 57, at arts. 177-78.

²³⁴ See *id.* at art. 168.1.

²³⁵ Code of Corporate Governance, *supra* note 10, at art. 9(b).

²³⁶ See, e.g., Jim Peterson, *Rotating Auditors Doesn't Add Up*, INTERNATIONAL HERALD TRIBUNE, Aug. 31 - Sept. 1, 2002, at 15.

²³⁷ 2002 CCL Amendments, *supra* note 11, at art. 111.

²³⁸ Code of Corporate Governance, *supra* note 10, at art. 9(c).

allowing the remaining services to be provided with appropriate limitations, if determined necessary. Although this issue does not necessarily have to be addressed at the level of law, instead being covered in the Listing Guidelines, it may be that Oman would want to take a stand on this issue at the highest level as is now being considered in other countries.

E. Disclosure and Transparency

As noted above, the Commercial Companies Law requires companies to report financial statements annually and semiannually, but does not require other periodic reporting.²³⁹ The Capital Market Law requires an initial prospectus when a company goes public, with subsequent disclosure consisting of annual, semiannual and quarterly reports on its activities and financial results. Notification of the CMA is required when information provided in the prospectus changes, where certain changes of share ownership occurs and where events and information that may have an impact on their activities or financial position occur.²⁴⁰ The Draft Law requires annual financial statements and certain other disclosure.²⁴¹ Other specific disclosure requirements are set forth in circulars.²⁴²

Although the CMA has relied upon the general authority set forth in article 6 of the Capital Market Law when requesting companies to submit information,²⁴³ the authority of the CMA to require disclosure of relevant data or information on a regular or periodic basis should be specifically addressed in either the Commercial Companies Law or in the Capital Market Law. Assuming that the Code of Corporate Governance is incorporated into the Listing Guidelines as recommended above, the Listing Guidelines should be further revised to incorporate other regular or periodic disclosure requirements.

F. Liability, Defenses and Enforcement

The Capital Market Law lays a basic foundation for the regulation of the capital market in Oman, but more detail might be desirable both at the level of law and at the level of Executive Regulations. Thus far, many issues

²³⁹ See *supra* text accompanying note 158.

²⁴⁰ See *supra* text accompanying note 159.

²⁴¹ See *supra* text accompanying notes 171 – 73.

²⁴² See *supra* text accompanying notes 161 – 70.

²⁴³ Capital Market Law, *supra* note 37, at art. 6 (reading as follows: “The company and the auditors must provide the [CMA] with all information requested”)

are addressed in circulars, in particular as they relate to disclosure, and it is unclear whether the standards set forth in the circulars are mandatory or serve merely as guidance. As the capital market develops, the regulatory framework should be as precise as practicable to avoid ambiguities and misinterpretation by both local and foreign investors. In addition, without certainty there can be claims of selective enforcement of regulations, which leads to distrust of the regulators and the market.

As corporate governance standards are improved and directors and officers are held to higher standards, it is important that the Draft Law has incorporated a Business Judgment Rule and provides guidance concerning when reliance on information and advice would be considered to be "reasonable."²⁴⁴

Finally, as is the case in many jurisdictions, without the will and the proper means to enforce existing laws and regulations, there is little reason to adopt more, even arguably better, regulations. Oman has shown that it will prosecute board members in egregious cases.²⁴⁵ However, all companies need to know that they will be held to high standards; that they must comply with the rules of the game in order to play. The annual reports published in 2003 will give a very good indication of the extent of compliance with the new corporate governance requirements. The manner in which the CMA reacts to those not fully complying will set the tone for the coming years.

²⁴⁴ See *supra* text accompanying notes 201 - 04.

²⁴⁵ See, e.g., [Four] Jailed for Breach of Trust and Fraud, *supra* note 2, at 1 (four board members and employees of Oman National Investment Holding SAOG convicted for crimes involving breach of trust, fraud, and manipulating the market).