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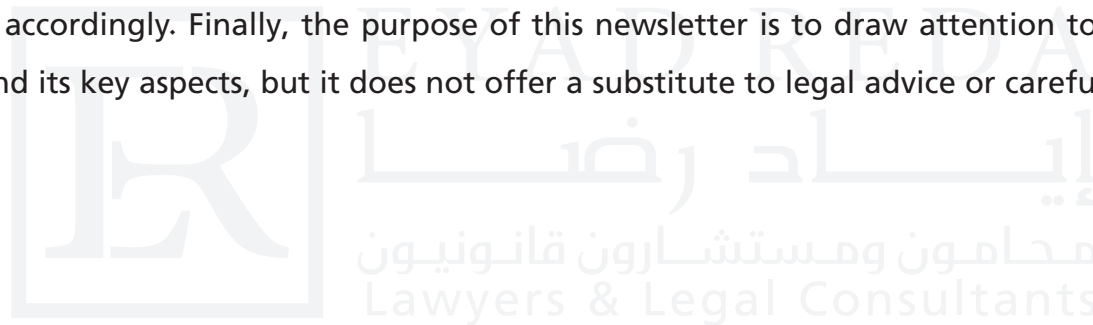
Beyond Covid-19 Pandemic - Significant Legal Dimensions

An Analytical View of the Importance
of Legal Inspection



Disclaimer:

This newsletter does not constitute a legal advice; neither does it contain the entire legal procedures stipulated in relevant laws. Moreover, the cited cases are presented as examples and abbreviated versions of the original text. It should be stressed that the context of facts and documents affects the outcome of the judgment, which may change accordingly. Finally, the purpose of this newsletter is to draw attention to the significance of legal inspection and its key aspects, but it does not offer a substitute to legal advice or careful and detailed inspection.



Introduction

World Health Organization has already declared **COVID-19** a “Pandemic”. Linguistically, “pandemic” describes the act of “invasion”, which means the extermination of assets; this precise linguistic term applies to the reaction and precautionary measures taken by the Kingdom of Saudi Arabia against the pandemic to restrict it, ensure its receding and reduce the assets and souls it exterminates. There is no doubt that the precautionary measures, be it the decision to limit attendance at workplaces and halt international and domestic air traffic, or the 24-hour lockdown, have created a crisis that has made us realize the importance of taking such measures that prevent the greater harm and give priority to the public interest.



The fact that the private-sector enterprises will exit this crisis with some [negative] effects and impacts of whatever size and form is the result of a normal situation imposed by the nature of the pandemic and the conditions that surround it and, at the same time, shape human history. Therefore, the objective of this newsletter is to draw attention - after the crisis has ended with the lifting of precautionary, corrective and reformative measures - to legal inspection for the legal treatment of the [negative] effects and impacts on enterprises, in four dimensions:

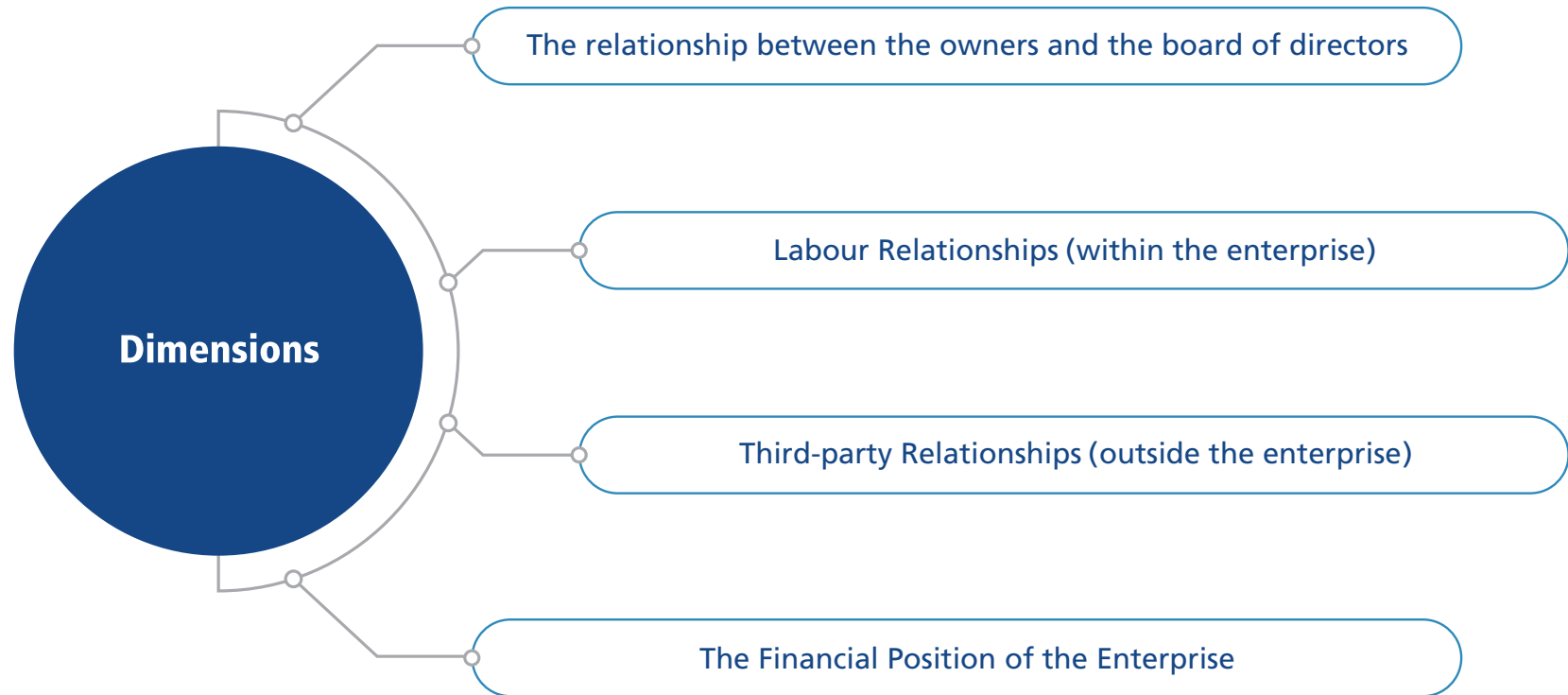
1 The relationship between the owners and the board of directors

2 Labour relationships (within the enterprise)

3 Third-party relationships, whether with public or private entities (outside the enterprise)

4 The financial and regulatory position of the enterprise.

In this newsletter, we demonstrate the components of each dimension and the mechanism and importance of their legal examination and treatment throughout the enterprise to achieve a stable financial recovery - God willing.



A collection of medical supplies including several blue surgical masks, a white box, a bottle of 'SAFERCARE' hand sanitizer, and a clear spray bottle, all arranged on a surface with a blurred background.

First Dimension

The relationship between the owners
and the board of directors

Components - Content



Partners'
meetings



Board of Directors
meetings



General Assembly
meetings



Minutes of
Partners' meetings



Minutes of Board
of Directors
meetings



Minutes of
General Assembly
meetings



Partner
decisions



Board of Directors
decisions



General
Assembly decisions

Mechanism

The enterprise exposure to a crisis may cause anxiety among owners and members of the board of directors, which may hinder the decision-making process or cause the issue of hasty decisions beyond legal procedures. Despite the speedy nature of trade and business world, which requires the same speed in issuing and implementing decisions, the decision-making method, as well as the decision content, formulation and application mechanism, if failing to consider such legal intersections, problems and procedures arising therefrom, may affect the decision's sustainability, lead to its nullification and give rise to liability claims, which undoubtedly impedes the enterprise's journey towards financial recovery.



Checklist

- ☒ Has the meeting been called in accordance with sound legal methods?
- ☒ Does the quorum for meeting meet the requirements of the enterprise's memorandum of association or articles of association?
- ☒ How was the decision issued? (Unanimously - majority - half - less than half)
- ☒ Is the decision-making process consistent with the Companies Law and the enterprise's memorandum of association or articles of association?
- ☒ Taking into consideration the Companies Law and the enterprise's memorandum of association or articles of association, can the content or subject matter of the decision be issued in the manner described in the answer to question 3 above?
- ☒ Who has issued the decision (present in person or a representative of the member or partner)?
- ☒ Is the board member or partner representation legally valid?
- ☒ Is the authorized representative's attendance and voting on the decision valid and consistent with the enterprise's memorandum of association or articles of association?
- ☒ Has the decision been documented (in the case of a partner decision or an extraordinary general assembly decision to amend the memorandum of association) according to the mechanism set forth in the Companies Law?

- ☒ Has the decision been published (in the case of a partner decision or an extraordinary general assembly decision to amend the memorandum of association) according to the mechanism set forth in the Companies Law?
- ☒ Has the decision been published (in the case of a partner decision or an extraordinary general assembly decision to amend the memorandum of Association) according to the deadlines specified in the Companies Law or prior to its implementation?
- ☒ Does the decision affect the creditors of the enterprise?
- ☒ Have the procedures set forth in the Companies Law been followed in the issue of the decision reducing the enterprise's capital?
- ☒ Have the above requirements been followed, taking into account the restrictions issued by the corporate supervisory authorities?
(All companies and commercial establishments: Ministry of Commerce - Joint stock companies listed in the capital market: Capital Market Authority - Finance and insurance companies and banks: the Saudi Arabian Monetary Authority - Professional enterprises: according to the profession - Foreign enterprises: Ministry of Investment)
- ☒ Are the supporting documents on which the decision is based (financial statements - accounting documents, etc.) or that reflect the implementation or application of the decision available?
- ☒ Is there a clear separation, no overlap and organization between the roles of the partner, manager or board member within the enterprise, in line with the Companies Law and other relevant regulations, such as (The Capital Market Authority and the Saudi Arabian Monetary Authority regulations)?
- ☒ For joint stock companies, is there a governance regulation that is consistent with the Companies Law and other relevant regulations, such as (the Capital Market Authority and the Saudi Arabian Monetary Authority regulations)?

Relevance- A similar judicial precedence

The following Judgment was issued in Case No. 3/5305/J of 1433 AH:

"Having reviewed the case documents and the documentary evidence attached thereto, the Circuit establishes its conclusion on the outcome it is satisfied with, based on the pleadings and arguments raised by the litigants. However, it has disregarded the digressions of the litigants that go beyond the scope of litigation, and focused on the matters that have material impact on the course of litigation and the intentions of the litigants, which are established in the signed memorandum of association dated 17/03/1417 AH, corresponding to 01/08/1996, and the annexes made based thereupon, as per the Partners Decision dated 20/06/1419 AH, corresponding to 10/10/1998. In this context, Article 13- "Partners Decisions" of the memorandum of association stipulates that decisions shall be issued in three manners; unanimously, by a majority representing 75% of the capital, or the approval of members representing 50% of the capital. It is evident from the decision, subject of the revocation petition, that the legal quorum, being the attendance of partners representing 100% of the shares or 50% thereof, has not been satisfied, which renders the decision defective and revocable. This conclusion is in line with Article 171 and last part of Article 172 of the Companies Law, which gives priority to the provisions of the enterprise's memorandum of association, and requires subjecting the matter to the provisions of the partners' contract. The Circuit; therefore, establishes and declares the validity of the Plaintiffs' petition to revoke the decisions of the Partners' Assembly for non-satisfaction of partner attendance and representation quorum, as failure to meet the said quorum renders the issued decisions invalid and revocable. As such, the Circuit decided to revoke the decisions of the Partners' Assembly. While considering the case, the Circuit disregarded the arguments raised by the litigants as to the details included in the decisions given the absence of the quorum element, as the main determinant of the soundness of the decision and the satisfaction of all its elements is the satisfaction of the quorum prescribed in the law. For these reasons, the disputed decision shall be revoked. Therefore, the Circuit rules as follows: Revoke the decisions of the Partners' Assembly of (...) Company, which convened on 20/08/1432 AH, corresponding to 21/07/2011. May God grant us success; prayers be upon Prophet Mohammad, his family and companions."

Conclusion

The significance of this dimension is manifested in achieving sustainability in the business practiced by the enterprise, where decisions are made in accordance with the relevant regulations, in a manner that preserves the rights of the partners or owners and maintains a healthy regular relationship between them. Altogether, this reflects on the performance of the enterprise and its ability to develop, innovate and continue.



Second Dimension

Labour Relationships (within the enterprise)

Components - Content



Labour
regulations



Employment
contracts



Labour cases



Contents of
employee files
with the Human
Resources
Department



Employee
nationalities



Enterprise file with
the Ministry of
Human Resources
and Social
Development



Enterprise's file with the General
Organization for Social Insurance



Enterprise data
relating to labour
spending



Company's financial
statements -
Company's financial
position



Article No. (41) added to the
Executive Regulations of the Labour
Law and its explanatory note

Mechanism

Labour relationships have caused the most controversy and caught attention since the beginning of the crisis. Subsequently, enterprises turned to government initiatives that mitigate the effects of the continuity of these relations. As such, the legal inspection stage and the treatment of this dimension involve qualifying the enterprise to be legally prepared for any similar circumstances that may occur not far from this crisis. In other words, the crisis in employment contracts and work organization bylaws have revealed a serious shortage of legal provisions on crisis management and handling within the enterprise. On the one hand, it is not permissible to agree with the employee on violating the Labour Law, that is, an employee consent does not validate the act if it violates the Labour Law. On the other hand, labour relationships that are not addressed in accordance with the Labour Law add financial burdens to the enterprise, represented in compensations.



Checklist

- ☒ Does the enterprise have a work organization regulation approved by the Ministry of Human Resources and Social Development, as required by Article 13 of the Labour Law?
- ☒ Is the work organization regulation consistent with the Labour Law amended by Royal Decree No. 46/M dated 05/06/1436 AH [26/03/2015]?
- ☒ Is the work organization regulation consistent with the employment contract concluded with the employee?
- ☒ Has the enterprise taken any punitive action against one employee or more? (Salary deduction - warning - termination- suspension - deprivation from bonus or promotion)
- ☒ Have the procedures stipulated in the Labour Law been followed when taking the punitive action?
- ☒ Has one or more employee contracts been terminated according to the terms, procedures, and reasons set forth in the Labour Law?

- ☒ Have the provisions of Decision No. 50945 dated 011438/05/ AH [292017/01/] by the Minister of Human Resources and Social Development, restricting the collective dismissal of Saudi employees, been observed?
- ☒ Have the initiatives of the Ministry of Human Resources and Social Development been examined and leveraged?
- ☒ Have the regulatory options set forth in Article No. (41) of the Executive Regulations for the Labour Law, for which explanatory note has been issued by the Ministry of Human Resources and Social Development, been utilized?
- ☒ Are the supporting documents reflecting the factual and legitimate reasons upon which the employment contract was terminated, available?
Do the company's financial statements reflect the benefit from the initiatives introduced by the Ministry of Human Resources and Social Development and their impact on the enterprise?
Does the enterprise expect labour claims to be filed against it due to certain procedures or termination? Have the costs of these claims been considered in terms of the amount of compensation to be paid? Success rate?

Relevance- A similar judicial precedence

Decision No. 431/1/1456 dated 19/08/1431 AH [31/07/2010] by the Labour Disputes Settlement Committee introduces the following principle: "The provisions and rules organizing labour affairs, which are set forth in the work organization regulation of the employer approved by the Ministry of Labour must be observed."

Moreover, Decision No. 661/2/432 dated 04/07/1432 AH [06/06/2011] by the Labour Disputes Settlement Committee introduces the following principle: "The dismissal of an employee due to the deterioration of the financial situation of the employer, without providing evidence establishing such deterioration, makes the dismissal unlawful."

Conclusion

The relevance of this Dimension is attributed to being a true investment in a human resource by the enterprise. This investment reflects on the enterprise's workplace, professional performance and creativity. It further reflects on the national economy as a whole. Without paying attention thereto or investing therein, the costs incurred by the enterprise become exhausting and accumulate or increase in the long run.



Third Dimension

Third-party Relationships
(outside the enterprise)

Components - Content



Enterprise contracts with suppliers



Enterprise contracts with government agencies



Enterprise contracts with lessors



Enterprise contracts with banking or finance entities



Enterprise contracts with the consulting or service sector (law / accounting / marketing / others)



Enterprise files with government agencies (the General Authority of Zakat and Income/Ministry of Commerce/Ministry of Municipal and Rural Affairs/Passports Department/ Others)



Enterprise contracts with clients or third parties in general

Mechanism

Relationships with third parties concluded by the enterprise vary; on the one hand, the enterprise exercises its business after obtaining several licenses and opening several files with several public governmental bodies, which requires consistence in terms of commitment and satisfaction of requirements and procedures. On the other hand, the enterprise concludes many contracts with private entities and individuals practicing the business. This diversity and multiplicity in relationships results in a set of affairs, relationships and obligations.



Checklist

- ☒ Does the enterprise have clear lists of the concluded contracts affected by the crisis (suppliers/lease/consulting or service/ loans/ financing/ facilities/ with a government body)?
- ☒ Does the enterprise have (financial or accounting) statements/data and documents that explain how it was affected by the above-mentioned contracts during the crisis?
- ☒ Do these contracts contain provisions for an emergency, force majeure or inability to perform obligations? Have they been applied or utilized?
- ☒ Do the regulations relevant to the type of contract contain provisions for an emergency, force majeure or inability to perform obligations? Have they been applied or utilized? (E.g. Government Tenders and Procurement Law, Financial Leasing Law, Disaster and Emergency Identification Regulation, Commercial Court Law, etc.)
- ☒ Do these contracts include a penal clause or clauses for terminations that result in compensation?
- ☒ Has the enterprise begun to negotiate or discuss with the other party in the above-mentioned contracts the options that can be applied to reduce or remedy the impact of the crisis?
- ☒ Are there claims filed against the enterprise due to any of the contracts mentioned above? How does the enterprise intend to proceed with these claims?
Has the initiatives (whether occurring before or as a result of the crisis) introduced by government bodies been reviewed and leveraged?
- ☒ Do the company's financial statements reflect the benefit from the initiatives introduced by government bodies and their impact on the enterprise?
How does the enterprise assess its relationship with government bodies in terms of compliance with regulations? Has the enterprise made plans to address this issue?

Relevance- A similar judicial precedence

The Commercial Court issued the following judgment in Case No. 3/29/J of 1421 AH: "The Defendant's suspension of supplies to the Plaintiff [sic-does not constitute] a breach to the contract made between them, as this suspension is beyond its control, falls within the concept of emergency conditions, and is just a precaution intended to improve the quality of the product and achieve public interest. In addition, the Defendant had no choice but to suspend this product as a necessary measure to avoid production that contradicts with applicable specifications and is dangerous to people's lives. By providing the Defendant with iron quantities, the Plaintiff aims to achieve more profit, without taking into consideration public interest, which is the responsibility of the official body, being the Ministry of Commerce. The Ministry has broad powers in organizing commerce and delegating whatever it deems fit for this purpose. The fact that the Defendant continued to provide the Plaintiff with iron wire rolls after the elimination of the impediment, which was beyond its control, is substantiating evidence of the Defendant's commitment to implement the Contract made between them. As such, the Defendant may not be accused of breach, so long as it is beyond its control. The Defendant only applied the instructions of the competent authority, which aims at achieving public interest. Moreover, the Defendant's conduct is in line with the rules of Islamic Sharia and achieves their purpose; particularly, the fundamental rules stating, "a private injury is tolerated in order to ward off a public injury," "Do not inflict injury nor repay one injury with another," and "Harm must be eliminated as much as possible". In light of the above, the Circuit concludes that both claims filed by the Plaintiff for the damages it alleges as a result of the Defendant's suspended provision of iron coil rolls under the contract made between them."

Conclusion

The importance of this dimension means resorting to investment in the relationship with the third party and activating alternative means to address the dispute or misunderstanding between both parties, as this investment is more effective and less costly. The newly enacted Saudi regulations encourage resorting to alternative means and put forward options including reconciliation, mediation and arbitration to reduce the burden on commercial courts, in addition to the fact that resorting to the commercial court is supposed to be a final option and a final solution for the enterprise, given the incurred cost when compared to other methods, at many financial, time and business relation levels.



Fourth Dimension

The Financial Position of the Enterprise

Components - Content



Enterprise
financial
statements



Accounting
reports



Partners' decisions



Board
decisions



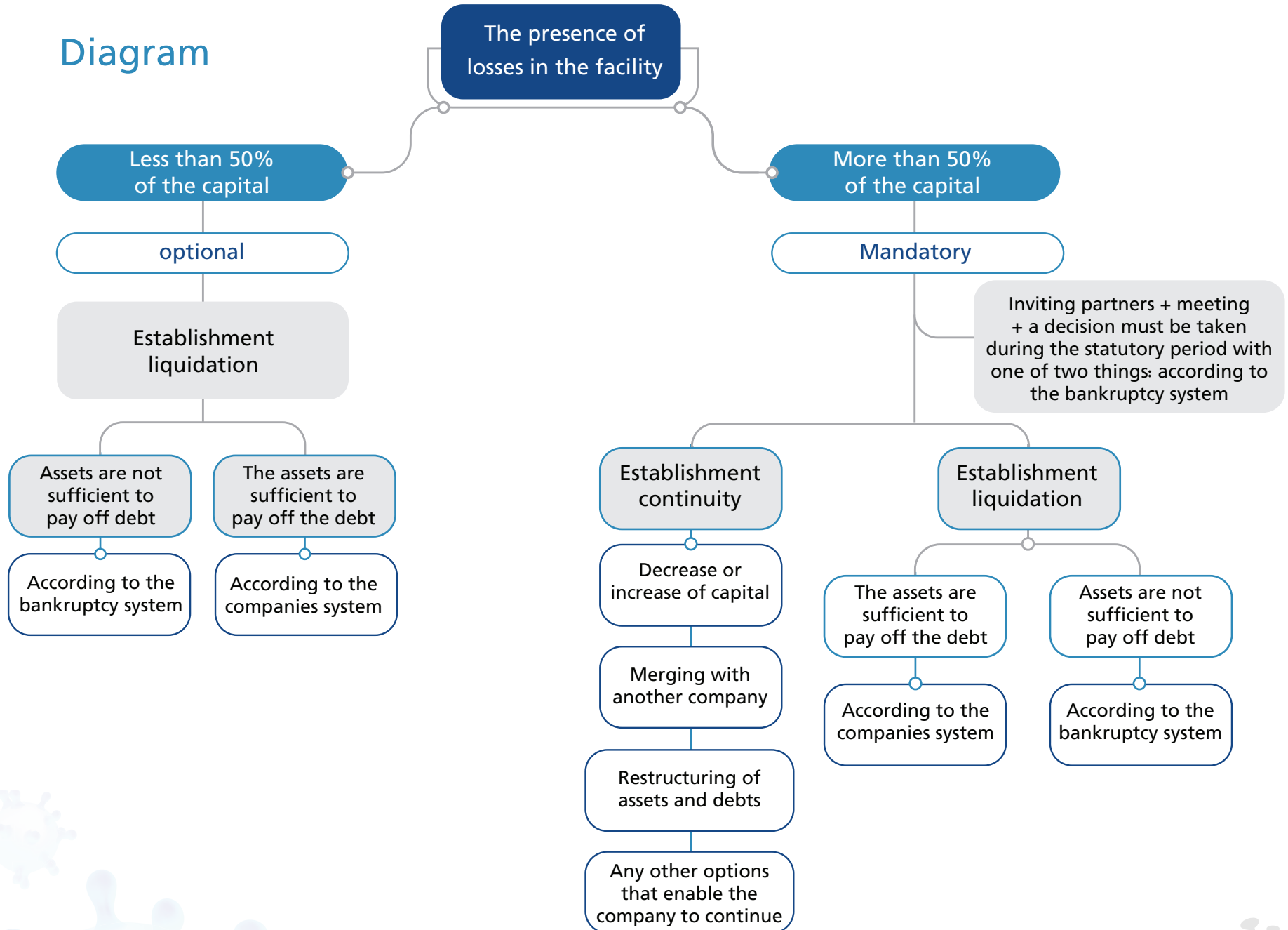
Board
performance

Mechanism

The financial position of the enterprise pertains to its financial reputation, which, despite reliance on realistic numbers, represents a moral currency that helps the enterprise to attract and win opportunities. The occurrence of financial confusion, default, or loss that reflects on this reputation is common in the life cycle of enterprises. The Companies Law and the Bankruptcy Law and its Executive Regulation have addressed this matter by offering enterprise restructuring as an option that does not exclude it from the national economy system, but rather helps it maintain its business and achieve financial recovery.



Diagram



Note:

- ❏ Failure to follow the obligatory procedure renders the enterprise vulnerable to termination by the force of the Law. This means that one or a group of Enterprise creditors may appear before the Commercial Court to request the liquidation of the Enterprise in accordance with the Bankruptcy Law. If it was proven that the Enterprise debts exceed more than (50%) of its capital, as well as proving that the Partners did not reach a decision to the continuation or dissolution and liquidation of the Enterprise within ninety days of learning of this loss, this would support the creditors' position with respect to the liquidation application, and, possibly, to the establishment of the partners or directors' liability.
- ❏ Failure to follow the obligatory procedures prescribed by the Law may lead to the joint and personal liability of the partners or directors.
- ❏ A partners' decision must be issued in respect of the foregoing and the applicable mechanism, in accordance with the Companies Law and the enterprise memorandum of association and articles of association.
- ❏ The enterprise director must register the loss incident in the commercial register with the Ministry of Commerce.
- ❏ The Bankruptcy Law provides for two options that would not remove the enterprise from the national economic system, but would keep it to conduct its business and urge it to pay debts and return to the profit level. These options are: Preventive settlement and financial reorganization.

Relevance- A similar judicial precedence

The Commercial Court rendered the following judgment in Case No. 751 of 1440 AH:

In light of the documents and evidence presented by the Plaintiff, the Circuit rules as follows: As the Circuit has already issued a judgment obliging (...) Construction Company Limited to pay to the Plaintiff SAR 123,268.68 (one hundred twenty-three thousand two hundred sixty-eight Saudi Riyals and 50 Halalas); whereas the judgment issued by the Circuit could not be enforced due the fact that the Defendant is short of funds and assets, according to the following statement of the Honourable Judge of the First Circuit of the Execution Court, Makka Al-Mukarrama: (This is to inform you that no assets were found for (...) Construction Company ... The total financial claims filed against the enterprise total SAR 525,784 (five hundred twenty-five thousand seven hundred eighty-four Saudi riyals, while the funds available in its bank accounts amount SAR 11,575 (eleven thousand five hundred seventy-five Saudi riyals). This being said, the Companies Law identified the powers and responsibilities of a limited liability company. For example, Article 165.2 thereof stipulates as follows: "The Directors shall be jointly liable for damages sustained by the Company, the partners or third parties as a result of violating the provisions of the Law or the company's memorandum of association, or as a result of wrongs committed by them in the performance of their duties. Any condition to the contrary shall be considered null and void". Moreover, Article 181.1 stipulates: "If the losses of a limited liability company amount to half its capital, the company directors shall record such incident in the Commercial Register and call the partners for a meeting within ninety days from the date of being aware of such losses to consider the continuation or dissolution of the Company. Whereas the capital of (...) Construction Company Limited amounts SAR 100,000 (one hundred thousand Saudi riyals),

as indicated in its commercial register; whereas the debts of the enterprise for which executive decisions have been issued exceed SAR 500,000 (five hundred thousand Saudi riyals), based on the statement of the Execution Court, which means that its debts of the enterprise exceed five times the amount of its capital; whereas the Defendant has not taken the regulatory procedures required for the continuity or dissolution of the enterprise, the Circuit establishes the liability of the Defendant's Director (...) who undertakes its management as indicated in the commercial register for the Plaintiff's debt, which has been proven against (...) Company. Concerning the Defendant Partners, the enterprise is a limited liability company. Article 151 of the Companies Law stipulates, "The liability of the limited liability company shall be separate from the financial liability of each partner, and the company shall be solely liable for due debts and liabilities. The owner of the company or the partner therein shall not be liable for such debts and liabilities." Therefore, the Circuit rules that the Defendant Partners have no capacity in settling the Company's debts. For these reasons, the Circuit rules as follows: First: Hold the Defendant (...), holding Civil Register No. (...), liable for the payment of SAR 123,268 (one hundred twenty-three thousand two hundred sixty-eight Saudi Riyals) to the Plaintiff (...), holding Civil Register No. (...)."

Note: If the director of the enterprise in the above case proves having taken the procedures provided for in the Law (i.e. registering a loss incident in the Commercial Register with the Ministry of Commerce+ calling for a partners' meeting), his liability will be eliminated and transferred to the Partners, if they fail to follow the obligatory procedures provided for in the Companies Law.

Conclusion

The relevance of this dimension is manifested when the enterprise considers following regulatory procedures an ongoing approach, even when being exposed to a financial crisis, as this will affect its ability to exit the crisis and leverage and achieve maximum benefit from the options offered by the law. Moreover, such approach is considered a moral credit to be added to the enterprise's position and reputation.

The background of the slide is a close-up photograph of a blue and white striped fabric, possibly a towel or a piece of clothing. The stripes are diagonal and run from the top-left towards the bottom-right. A semi-transparent white rectangular box is centered on the image, containing the word "Conclusion" in a dark blue, serif font.

Conclusion

Francis Bacon, an English philosopher and author, said:

«A wise man makes more opportunities than he finds».

This statement applies to the call for the enterprise to conduct a carefully managed and detailed legal inspection to address the effects of the crisis within the scope of the enterprise's four dimensions. The implications of the crisis may introduce opportunities and gains for the enterprise to restore balance, achieve financial recovery and redress losses.

A speedy action by the enterprise to submit to legal inspection and follow legal rehabilitation and treatment stages against the crisis effects from a legal perspective means, in other words, to promptly take the injured to a doctor who treats the injury and limits its impact and effects on the remaining parts of the body. The inspection step, followed by the treatment of effects, embodies the aspiration for sustainability and the keenness to achieve the interests of both the enterprise and the national economy, based on a stable and established element, in order to support the enterprise's journey towards profitability and success.



Our best wishes to you
Good luck and success ...



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