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Iraq

Corporate Governance

Contributor

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This country-specific Q&A provides an overview of corporate governance laws and regulations applicable in Iraq.

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Iraq: Corporate Governance

1. What are the most common types of corporate business entity and what are the main structural differences between them?

The most common types of corporate business entities registered by entities conducting business in Iraq are subsidiary limited liability companies (LLCs), joint-stock companies (JSCs) and branches of foreign companies.

An LLC is established by a minimum of one and maximum of 25 shareholders. The shareholders may be legal entities or individuals or a combination of both. A general assembly of shareholders is formed and shall be responsible for appointing and determining the powers of the managing director. The minimum capital for an LLC is 1,000,000 Iraqi Dinar. An LLC may not hold public subscription of shares.

A JSC must be founded by a minimum of five shareholders. The liability of the shareholders is limited to the amount payable on their shares. The JSC also has a general assembly of shareholders which also elects the board of members to govern the JSC. The chairman or deputy chairman may not also be the managing director of the JSC. The minimum share capital of a JSC is 2,000,000 Iraqi Dinar. Part of the shares of the JSC must be offered to the public for subscription, unlike that of an LLC. The public subscription must be completed before a certificate of establishment of the JSC is issued. Insurance and financial investment companies may only be registered as JSCs in Iraq.

The board members of a private JSC are composed of five to nine members. The board then elects the chairman and deputy chairman from among its own members. A member of the board of directors is subject to the following eligibility requirements:

- Must be legally qualified and not banned from managing a company under law or legal decision; and
- Must own at least 1,000 shares. Any number below this must be increased to meet the minimum within 30 days of membership.

Another common entity registered is the branch of a foreign company. In order to establish a branch, the parent company must have been established for at least one year and shall have profitable financial statements, not losses, for the last audited financial statement.

Moreover, it should be noted that the commercial activity of the branch is limited to the registered activity of the foreign company. The foreign company shall also be liable for any liabilities of the branch. The requirements for branches in Iraq are stipulated in Regulations No. 2 of 2017 on Branches of Foreign Companies. Any managerial changes must be approved through a shareholders' resolution by the parent company.

The Companies Law No. 21 of 1997 as amended by Law No. 17 of 2019 (Companies Law) now requires LLCs and JSCs to have at least 51 percent Iraqi shareholders, whether corporations or individuals. It should be noted that the Companies Law as amended does not apply to the Kurdistan Region of Iraq (KRI), as the Kurdish Parliament has not to date passed the amended law. As such, 100 percent foreign participation is still permissible in the KRI.

The Iraqi Constitution provides the Kurdish Parliament with legislative powers, with the exception of certain matters that are reserved to the federal government. As far as the Kurdish legislature has not made use of the legislative competencies conferred on it, Iraqi federal law applies if it has been either adopted by the Kurdish legislature or enacted prior to 1992. Unless otherwise expressly indicated, references to any law, instruction, regulation is a reference to such statute as applied in Federal Iraq.

Under Iraqi law, LLCs, JSCs, and branches must fulfill certain post-registration obligations. These include registering for tax purposes and enrolling in the social security system. Compliance with these requirements is essential to maintain legal and operational status.

2. What are the current key topical legal issues, developments, trends and challenges in corporate governance in this jurisdiction?

A key legal issue affecting new players entering the Iraqi market is the restriction on foreign shareholding of companies, brought into effect by the Companies Law in 2019. Branches are often considered in lieu of registering a company for this reason. Another option considered in the company's entry strategy to Iraq is signing a nominee director agreement in which a local individual or entity is granted shareholding capital but is significantly restricted

in any decision-making powers.

3. Who are the key persons involved in the management of each type of entity?

The general assembly of an LLC appoints and determines the authorities of the managing director and deputy managing director. The deputy managing director may carry out the managing director's responsibilities in the latter's absence. A managing director's functions involve carrying out the day-to-day business operations of the LLC.

The board of directors in a JSC must elect the chairman and deputy chairman from among its members. The managing director is not required to be a board member. However, the managing director may not also be the chairman, and cannot be the managing director of any other JSC.

A branch is managed by the branch manager appointed by the parent company through a shareholders' resolution.

4. How are responsibility and management power divided between the entity's management and its economic owners? How are decisions or approvals of the owners made or given (e.g. at a meeting or in writing)?

Shareholders

The general assembly of shareholders is the governing body of the LLC. It may deal with any matter that is in the company's interest. The shareholders appoint, remove and determine wages and powers of the managing director and must also approve the LLC's budget, final accounts and annual plan.

Managing Director

Under the Companies Law, the responsibilities of the managing director in an LLC are the same as that of the board of directors of the JSC, subject to the decisions of the general assembly. The managing director must carry out the tasks within the powers assigned by the general assembly (or board of directors in the case of a JSC).

Board of Directors

In a JSC, the board of directors must meet at least once every two months at the request of the chairman or any one of its members. The board is responsible for the

necessary administrative, financial, planning, organizational and technical duties of the company's business, except those which fall under the powers of the general assembly. In particular, the board of directors has the following powers:

- Appointment and dismissal of the managing director and determining their remunerations and authorities;
- Implementation of the general assembly's decisions and follow-up thereof;
- Evaluate annual plan for company's activities as prepared by the managing director;
- Preparing final accounts of the previous year, to be reported to the general assembly along with the results of the annual plan;
- Follow up on implementation of the annual plan with periodic reports to the auditor;
- Prepare statistical studies to further develop company's business;
- Make decisions related to loans, mortgages and securities;
- Establish an audit committee within its board to recommend external, independent auditors. The audit committee is responsible for meeting the auditors and ensuring the accuracy of their work; and
- Establish a compensation committee from its board to recommend the compensations for the board and managing director. These committee members must be impartial and may not be employees or own 10 percent or more of the company's share.

The chairman must sign any decision made by the board of directors and follow up on the implementation of such decisions.

Board decisions are reached through an absolute majority of the votes. In the case of a tie, the chairman's vote prevails.

Decisions or Approvals of Owners

The general assembly of shareholders make decisions through meetings, which are required to be held twice a year, or once a year in the case of a JSC. In an LLC, the general assembly may determine appointment, wages, managerial authority, as well as approve budgets and annual plans. In the JSC, the general assembly elects and determines the wages of the board of directors.

Decisions by the general assembly are to be kept in a special register, and signed by the chairman.

The company administration should inform members on their invitation to the meeting or send it to their postal addresses. In a JSC, the invitation to a meeting must be

issued in the Registrar's bulletin, two daily newspapers and the Baghdad Stock Exchange.

5. What are the principal sources of corporate governance requirements and practices? Are entities required to comply with a specific code of corporate governance?

The Companies Law No. 21 of 1997 as amended by Law No. 17 of 2019 and its regulations mainly govern corporate governance rules and requirements in Iraq. No code or regulation has to date been enacted specifically to regulate corporate governance matters. Most of the corporate governance rules determining powers and responsibilities of the different bodies in the company are set in the Companies Law.

6. How is the board or other governing body constituted? Does the entity have more than one? How is responsibility for day-to-day management or oversight allocated?

The board of directors is comprised of between five to nine members elected by the general assembly. The board members may be freely determined by the shareholders, as long as they are legally qualified under the applicable laws. The membership lasts three years and is renewable. The board of directors appoint a chairman and deputy chairman.

The shareholders appoint, remove and determine wages and powers of the managing director in an LLC. A managing director carries out the day-to-day business operations of the LLC.

The board of directors of a JSC is required to establish an audit committee within the board that will recommend external, independent auditors. These members may not be officers or employees of the company, or hold 10 percent or more of its shares.

Please see questions 5 and 6 for more detail.

7. How are the members of the board appointed and removed? What influence do the entity's owners have over this?

In a JSC, the general assembly of shareholders has full influence in selecting members of the board as this is one of the powers entrusted to the assembly in the Companies Law. The shareholders elect or dismiss a chairman or board member through a secret ballot held

during their meeting. The chairman or deputy may also be considered as having resigned if they fail to attend three consecutive meetings or successive meetings for over six months and without a legitimate reason.

In an LLC, the managing director and deputy managing director are appointed by the shareholders and may only be removed by the shareholders.

8. Who typically serves on the board? Are there requirements that govern board composition or impose qualifications for board members regarding independence, diversity, tenure or succession?

There must be between five to nine members of the board of directors in a private JSC. Each board member must own at least 1,000 shares in the company. The board members are chosen at the full discretion of the shareholders, as long as they are legally qualified under the applicable laws. There are no diversity, tenure, or succession requirements.

In a mixed JSC, where public sector participation is at least 25 percent, the requirements are rather different. For example, the board of directors consists of seven members, two of whom represent the public sector and five members who are elected by the general assembly. The composition would be three and four members respectively if the public sector's share capital exceeds 50 percent.

9. What is the role of the board with respect to setting and changing strategy?

The board of directors has the power to manage and carry out the administrative and technical duties of the business as well as having an advisory role. The Companies Law provides that the board of directors shall serve the company's best interests and is liable before the general assembly. Its responsibilities include preparing the company's financial report as well as statistical studies aimed at further developing the company's business. The board also determines the powers of the managing director it appoints.

10. How are members of the board compensated? Is their remuneration regulated in any way?

In a JSC, the general assembly of shareholders determine the remuneration of the members of the board of

directors, which must be in proportion to the latter's scope of work and fulfilment of the company's plans and profits. All payments to current or previous board members must be included in a detailed report on the final accounts to be submitted to the shareholders. One of the responsibilities of the board includes the establishment of a compensation committee from within the board to recommend the compensations for the board. The members must be impartial and may not be employees or own 10 percent or more shares.

11. Do members of the board owe any fiduciary or special duties and, if so, to whom? What are the potential consequences of breaching any such duties?

Members of the board of directors owe a fiduciary duty to the company to serve in its best interests and run it in a sound and legal manner, in accordance with the Companies Law. They are liable to the general assembly in carrying out these duties. They are expected to disclose any direct or indirect interests with regard to transactions and dealings with the company. An inspection may also be requested by a shareholder (with over 10 percent share capital), the managing director or a board member if there are reasonable grounds to believe that there has been a breach of duty. The inspectors are determined by the Registrar, who would then inform the relevant authorities in the case of a breach so that action may be taken accordingly. The Registrar would then also guide the company based on the findings of the inspectors' report. Potential consequences include suspension of the company's file with the Registrar and payment of fines.

12. Are indemnities and/or insurance permitted to cover board members' potential personal liability? If permitted, are such protections typical or rare?

According to the Companies Law the members of the board of directors are held liable and indemnities or insurance may not hold in court to cover the member's potential personal liability. However, Iraqi courts have yet to develop a consistent doctrine concerning the liability of board members and this has not to our knowledge been tested out in practice.

13. How (and by whom) are board members typically overseen and evaluated?

The general assembly of shareholders in a JSC has the power and authority to elect and dismiss the board members. This is done through a secret ballot held during the shareholders' meeting. The board must submit periodic reports to the auditor and an annual report to the general assembly regarding the results of the implementation of the annual plan. The general assembly evaluates the reports and accounts and makes decisions accordingly. The final accounts are also to be audited by external auditors appointed by the general assembly. The external auditors provide a report addressing their findings and the extent of the accounts' compliance with the law and articles of association of the company. Copies of the reports must be submitted to the Registrar.

14. Is the board required to engage actively with the entity's economic owners? If so, how does it do this and report on its actions?

Iraqi laws mostly govern the reporting and follow-up duties of the board on the final accounts and results of the annual plan of the company. The provisions do not, however, address the regular communication between the board and the shareholders. Nevertheless, the parties are permitted to engage actively as the board reports on the company's information and activities to the shareholders who in turn shall make decisions and approvals based on the reports.

15. Are dual-class and multi-class capital structures permitted? If so, how common are they?

Dual-class and multi-class capital structures are not permitted and have not to date been implemented in Iraq.

16. What financial and non-financial information must an entity disclose to the public? How does it do this?

Information on capital, shareholders, shareholders' minutes of meeting and related decisions that could affect the company must be made available to the public for companies listed on the stock exchange. Information on the final accounts, annual plan and related reports must be sent to the Registrar. The shareholders' meeting notes and decisions must be sent to the Registrar in a minute of meeting. The filings made with or sent to the Registrar are not made available to the public.

17. Can an entity's economic owners propose matters for a vote or call a special meeting? If so, what is the procedure?

According to the law the shareholders must hold meetings at least twice a year, or once a year in the case of a JSC. However, it may also be requested in certain cases. Iraqi law does not distinguish between ordinary and extraordinary shareholders' meetings. The general assembly of shareholders hold meetings by invitation of the founder of the company (for the constituent meeting held within 30 days of the issuance of the company's certificate of establishment), chairman of the JSC or managing director in other companies, or at the request of members of the company who own at least 10 percent of the paid-up capital. The meeting may also be called upon by the Registrar or the auditor. Shareholders of over 10 percent of the shares of the company may propose items to be included in the agenda of the general assembly meeting, which must then be passed by the majority of shareholders present there.

General assembly resolutions are passed through a simple majority of votes, which may be made in person or by proxy. A proxy may be issued to another shareholder or a third party, and must be deposited with the company three days prior to the meeting. Resolutions may not be passed unless a majority of the members are present.

18. What rights do investors have to take enforcement action against an entity and/or the members of its board?

Generally speaking, board members are liable towards the company and its shareholders in the event of a breach of duties or violation of laws. A shareholder (of more than 10 percent share capital) or a board member may request inspection if it is believed that a violation of the law, resolution or company's articles of association has taken place.

Shareholders of at least five percent capital may object to decisions of the general assembly by submitting an objection to the Registrar within seven days of their adoption. The Registrar shall issue its decision within 15 days of the submission. This decision may be contested before the competent court and the decision of the court shall be final.

According to the Companies Law, anyone whose rights are affected by a violation of the subscription rules may take action before a court and request a cancellation of subscription due to a breach in the subscription process.

19. Is shareholder activism common? If so, what are the recent trends? How can shareholders exert influence on a corporate entity's management?

Shareholder activism is a relatively unknown practice in Iraq and has not to date been exerted by shareholders in Iraqi corporate entities.

20. Are shareholder meetings required to be held annually, or at any other specified time? What information needs to be presented at a shareholder meeting?

In an LLC, the shareholder meetings are required to be held at least twice a year. In a JSC, the meeting is required once a year. The constituent meeting shall be held within 30 days of the issuance of the company certificate of establishment. The topics to be included in the agenda may be proposed by shareholders of over 10 percent of shares.

The shareholder meeting regarding the final accounts must be notified to the Registrar along with the following information:

- the annual list;
- the final accounts of the previous year and the auditor's report; and
- the managing director's or board of directors' report on the annual plan of the previous year.

Furthermore, the shareholders have the authority to make decisions regarding the following matters in the company:

- remuneration of chairman and board members;
- discussing and approving the founder(s)' report regarding establishment procedures;
- appointment and dismissal of representatives of shareholders within the board of directors;
- reports from the board of directors or managing director, as well as the auditor;
- final accounts;
- proposed annual plan and budget (not applicable to JSCs);
- remuneration of the auditor (not applicable to JSCs);
- proposals regarding loans, mortgages and securities (for LLCs);
- approving the percentage of profits to distribute among members; and
- approving employment rules in the case of a mixed JSC.

21. Are there any organisations that provide voting recommendations, or otherwise advise or influence investors on whether and how to vote (whether generally in the market or with respect to a particular entity)?

There are no known organisations providing voting recommendations, and Iraqi regulations do not include provisions to this effect, nor any proxy advisors for investors of Iraqi companies. Instead, local law firms are often solicited for assistance with shareholder resolutions, meetings and related legal advice.

22. What role do other stakeholders, including debt-holders, employees and other workers, suppliers, customers, regulators, the government and communities typically play in the corporate governance of a corporate entity?

Other stakeholders do not typically have a direct role in the corporate governance of a corporate entity in Iraq. The board of directors and the chairman and other officers of the company are expected to do their best to serve the company's interests. Mixed companies (where public sector participation amounts to 25 percent or more) are subject to slightly different governance and oversight regulations. For instance, two to three members of the board shall be appointed by the competent minister or deputy minister in the sector to which the company belongs, depending on whether public sector shares are above or below 50 percent. These members are selected to represent the state sector. Furthermore, the accounts of a mixed company must be audited by the Financial Control Bureau.

23. How are the interests of non-shareholder stakeholders factored into the decisions of the governing body of a corporate entity?

Iraqi legislation does not directly address any decisions to be taken in the interests of non-shareholder stakeholders, except that members must serve the company's interests. Furthermore, the law provides that anyone whose rights are affected by a violation of subscription rules may take action before the court. The decisions and votes of the governing body must be protected from any direct or interest interests that the board members and officers may have, unless permission is granted by a majority of the members once the nature of the interests are fully disclosed. The articles of association of the company may also set forth the

principles and core values that the company shall abide by.

24. What consideration is typically given to ESG issues by corporate entities? What are the key legal obligations with respect to ESG matters?

There are no legal obligations with respect to ESG matters to date, and no laws and regulations that might refer to some of these issues are currently enforced. Instead, these provisions may be included in the company's articles of association and internal policies and regulations.

25. What stewardship, disclosure and other responsibilities do investors have with regard to the corporate governance of an entity in which they are invested or their level of investment or interest in the entity?

Please see question 20 on the responsibilities and powers of the shareholders with regard to the corporate governance of an entity. The shareholders have the authority to appoint and remove board members and other officers and determine their remuneration (please see questions 7 and 10). The articles of association should typically include further responsibilities of the shareholders. With regard to voting rights, each shareholder is entitled to a number of votes equal to the number of shares they own.

All information with regard to the subscription process, names of subscribers, number of shares and amounts paid against the value of shares must be submitted to the Registrar.

26. What are the current perspectives in this jurisdiction regarding short-term investment objectives in contrast with the promotion of sustainable longer-term value creation?

There have not been initiatives or legislations promoting sustainable long-term value creation in Iraq. Capital owners have been reluctant to invest in long-term projects and have instead exited after their short-term profit objectives have been met. This is currently taking place in many of the M&A projects in Iraq where short-term investment objectives are prioritised and investors then exit the project even at its peak. The risks of short-term investment have not been taken up by legislators and are not addressed as a concern within the business

community of the country.

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