

LEGAL NATURE OF PREFERRED STOCK SUBSCRIPTION IN JORDANIAN LEGISLATION

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ABSTRACT: *This research shows the legal nature for preferred stock subscription and issuance according to Jordanian Law. When reviewing the Jordanian Companies Law No. 22 of 1997 and amended by Law No. 34 of 2017 that repeated of the Jordanian Companies Law which guarantees the organization of the legal provisions related to the preferred stocks, in addition to the laws and instructions that cover the subject that does not provide clear legal prospect regarding the provisions and legal actions that fall on the preferred stocks subscription. Who reads the provisions of the Jordanian Securities Law No. (18) of 2017 and the instructions issued there under, which placed the matter of organizing the subscription of the securities did not mention, even marginally, the process to be followed in the case of subscription in preferred stocks. Therefore, legal regulation preferred stock provisions under the Jordanian Companies Law is not sufficient and does not contain preferred stocks' privacy. Consequently, Jordanian legislator needs to add or amend current texts in a way covers the nature of the preferred stocks and its rules and how to deal with them.*

KEYWORDS: Preferred Stocks, Common Stocks, Preferred Shareholder, Contractual Nature, Private Shareholding Company.

INTRODUCTION

Joint-stock companies are the most significant pillars for growth and maintenance of the national economy. Therefore, the legislations provided legal texts regulating the provisions of such company from A-Z.

Joint-stock companies are always concerned mainly in establishment large projects that aiming to create financial stability, and the concentration of wealth in the hands of a few. However, such projects often need funds flow. Therefore, the joint- stock companies possess two types of securities.¹ Enabling them to obtain the largest amount of capital so that they can survive and continue in achieving their goals and objectives. Securities are (stocks, bonds) stocks are differ from bonds in being a proprietary instrument, while bonds represent a debt instrument used by a company for the purposes of lending and borrowing.

Nevertheless, a stock issued by joint-stock-company is often divided into two types and can be classified according to rights linked to them. Stocks are either ordinary or preferred, it is the first type (i.e. it must be issued by the company), while the second type is an exception as the company has the choice to wither issuance or not, which will be clarified deeper through our study.

¹Securities: Stocks and bonds are traded in a stock market that represent a property and debt instrument of the company.

Stocks are the most significant and the fastest financing tools of a company, due to their advantages. The most important advantages are ease of trading and specific responsibilities that shouldered by the shareholder in addition to other advantages, which made them of the most effective tools in forming the capital and run giant commercial entrusted projects.

With regard to preferred stocks, they are often being leveraged in financing commercial projects in initial phases, in cases of stumbling or when cash is needed to execute new projects and continue to progress to achieve future goals or the purpose of issuing Preferred stocks is the stability of the company's Board of Directors.

It was found when reviewing the Jordanian Companies Law No. 22 of 1997 and its amendments and amended by Law No. 34 of 2017 of the Jordanian Companies Law which guarantees the organization of the legal provisions related to the preferred stocks, in addition to the laws and instructions that cover the subject does not cover the nature and legal characteristics of the preferred stocks and therefore does not provide a clear legal prospect regarding the provisions and legal actions that fall on the preferred stocks of subscription and circulation and rights and obligations.

It is noted that the Jordanian legislation of securities does not establish a legal mechanism that can be relied, to decide unequivocally in the event of legal problems related to the rights and obligations of the preferred shareholders towards the company issuing this type of stocks in addition to ordinary shareholders without the need for diligence and interpretation.

Who reads the provisions of the Jordanian Securities Law No. (18) of 2017 and the instructions issued there under, which placed the matter of organizing the subscription of the securities did not mention, even marginally, the process to be followed in the case of subscription and trading in preferred stocks.

This study is significant because it addresses the legal basis that will indicate the nature and characteristics of the preferred stocks by setting the defects and legislative limitations regarding the mechanism of issuing and subscribing to the preferred stocks.

Definition of preferred stock

Preferred stock has not been defined by laws. The majority of legislations such as Lebanese, Moroccan and French legislations have delegated legal and financial specialists the mandate of definition, so that it is defined as "The stock which maintains preferential rights in profits collection or liquidation distribution amounts or both".² Another definition is "A type of company stocks grants holders the priority in dividends and assets distribution in case of solving the company against ordinary shareholders".³ Proffered stock defined as "A type of stocks has the preference over the ordinary stocks in the capital structure of a company".⁴

2Available at <<http://legal-dictionary.thefreedictionary.com/preferred+stock>> accessed on 15th April, 2018.

3Available at <<http://definition.uslegal.com/p/preferred-stock>> accessed on 15th April, 2018.

4Available at <<http://www.djcl.org/wp-content/uploads/2014/09/The-peril-and-promise-of-preferred-stock.pdf>> accessed on 15th April, 2018.

There is another definition is “A hybrid security that combines ordinary stocks advantages and bonds”.⁵

Most of preferred stocks definitions concentrated on the objective and formal criteria. However, it has deviated from four key elements. Firstly, all of the mentioned above definitions were legally addressed at one aspect, namely, rights, and did not state the aspect of commitment, which is in line with rights. Secondly, the previous definitions did not address the trade feature which distinguishes between stock and share in people's companies.⁶ Thirdly, the previous definitions addressed that preferred stock has financial preference in collecting dividends and the priority in sharing the liquidation, but did not mention the non-financial advantage such as precedence of subscription to new shares and the right of double voting. Fourthly, it well noted that the previous definitions did not address the legal basis that authorized the company to issue preferred stocks.

Therefore, we defined the preferred stock as (A tradable compound Security⁷ issued by the company representing the shareholder's share in capital, granting its owner rights and financial and non-financial value prepositions and imposing commitments against ordinary shareholders under the law). The researchers believe that this definition covers all missing elements in previous definitions; it shows that stock is a tradable security, i.e. can be waived by granting or selling. It also addresses the commitment aspect imposed over the shareholder specified through stock amount owned by the company. It also defined that preferred shareholders have physical and non-physical privileges such as priority to subscribe new shares and the right to double vote which sometimes granted by some legislations and international companies.⁸ The researchers referred through the previous mentioned definition to law which considered the basis of issuing this kind of law relied by joint stock company. However, the joint stock company cannot issue preferred stock in case of law prevention, prohibition is either expressly or implicitly.⁹ On the basis of this, the company cannot take a decision to issue preferred stocks in the event that this matter is contrary to the law and in the event that take that step, it is void for violating the provisions of the law on which the company was founded accordingly.

The characteristics of preferred stock

5Available at < <http://www.forkeylaw.com/Securities-Commodities-and-Precious-Metals-Terms/Preferred-Stocks.Shtml>> accessed on 15th April, 2018.

6 It is known that people's companies rely on personal consideration and hence the partner who desires to waive his share, they must obtain all other partners' approvals unlike the shareholder who waives their shares without the need for prior approval by shareholders.

7Compound or hybrid means that it combines the characteristics of stock and bond.

8An example of such legislation is Moroccan and Lebanese legislations, which gives preferred shareholders two votes per share. Companies, for example, Google, which gives the preferred shareholder up to ten votes .

9An example of expressed prohibition is the article 29 of Companies Law in Iraq which stipulates “The capital of the joint-stock company and the limited liability company shall be divided into shares of equal cash value. The shares shall be indivisible.” However, the implicit prohibition such as what stated by Jordanian legislator with regards Joint-stock-company in article (95/F); “The Board of Directors may issue shares as provided for by the provisions of the Securities Law in force” it did not prohibit companies expressly to issue preferred stocks but implicitly when the issue of shares shall be subject to the provisions of the Securities Law, which did not imply, even implicitly, preference stocks.

The priority in dividends

Means that preferred stocks give their holders priority in obtaining profits so that the holder, for example, a fixed rate of profits not less than 4% of their nominal value, while the rest of dividends distributed equally to all shares. This advantage does violate general rules that allow expenses over dividends distribution across partners at varying rates.¹⁰

preferred stocks without voting right

The joint-stock- companies usually issue preferred stocks without voting right leading to loss of control and management across the company regarding to preferred stock holders, they neither maintain the right in discussing the decisions issued by Company General Assembly of the company nor to run for membership of the Board of Directors of the Company. However, depriving preferred stock holders from voting right is not absolute while it is limited by tow conditions, otherwise, the company must run voting again. The conditions are: (1) Either the company will be delayed in paying preferred stocks on time (2) or a decision by the company to address the rights and advantages granted to the holders of such shares.¹¹

The right of double voting

Such stocks grant their holders two or more votes, and many legislations have approved this type of stock¹² The advantage of multiple votes may proper to joint- stock- companies in some circumstances, such as, the approval of this right to citizens in companies that have foreign shareholders, in order to have a majority vote in the General Assembly. If they do not have the majority of the financial capital of the company or to decide this advantage to the founders of the company so they can oppose the serious actions that may be required shareholders such as dismiss managers without justification. This kind of shares are not free of defect, because they limit the effectiveness of participation and the control of company's business and the election of a Bod which has been elected by only preferred stock holders.¹³

Priority in liquidation

The preferred stocks grant their holders the preference to meet the liquidation outcome of the company, the procedures are either selling the company or distributing its returns to preferred shareholders before ordinary shareholders or to be liquidated due to bankruptcy or due to prescribed period expiry or achieving the objective that is established for. In all cases, preferred shareholders apply to meet the liquidation outcome on ordinary shareholders, but after the creditors obtain their rights.¹⁴

10Available at <<http://www.investopedia.com/walkthrough/corporate-finance/3/stock-valuation/preferred-stock.aspx>> accessed on 18th April, 2018.

11Ordinary stocks may also be issued without the right to vote as in the case of the US state of California. Available at < <http://calcorporatelaw.com/2011/12/no-voting-rights-no-problem-for-california-corporations> < <http://m.jonesday.com/introduction-of-preferred-shares-in-french-law-09-03-2004>> accessed on 18th April, 2018.

12Such as the Moroccan companies law in article 257, Jordanian Companies Law in Article (68) *bis*, Lebanese Trade Law in article (117), French Companies Law in Article (492).

13Mustafa, Taha (D.T), *The basics of Commercial law*, (Manshourat Alhalaby, Lebanon, 1st edition, 2006), P.437.

14 Available at < <http://www.startuplawblog.com/2009/03/21/what-rights-come-with-preferred-stock>> accessed on 18th April, 2018.

Preferred stocks, Limitations and shareholders' rights

Preamble and segmentation:

Jordanian legislator has not force joint-stock-companies to issue preferred stocks like many other legislators, because such stocks are an execute from the company's asset. The company only recognizes its needs to issue those stocks. Consequently, the legislator authorizes the company to issue stocks at any type in accordance to legal text allows such action. The text is either expressed or implied, which sought by legislator through developing legal provisions clarifying how the joint-stock-company must follow to issue its shares in order to protect the issuing company, shareholders and customers. However, Jordanian legislator did not specify legal mechanism be followed to issue preferred stocks, which leads to the provide an unclear prospective for those who interested in dealing with this type of shares and reluctance to subscribe due to the fear of losing their rights and cannot protect them. Procedures without clear text would be in diligence position; such issue leads to instability of legal transactions for the company and its shareholders. On this basis, this part will be divided into three sections. We will discuss the private shareholding company independently. In this section, we explain the reason for choosing this company without other companies. The second section is to discuss the issuance of preferred stocks. Third section will discuss shareholders' rights in general and the rights of preferred shareholders and how to protect their rights in particular.

Private Shareholding Company

The Private Shareholding Company is defined as "a company of funds whose capital is divided into negotiable shares and the liability of the shareholder is limited to the contribution to the capital and has a trade mark that does not conflict with its objectives".¹⁵ Jordanian legislator introduced this type of companies for creating an investment environment to attract international companies and investors to Jordan.¹⁶ In addition to the contractual nature of this company, which is one of the important drivers that drives the investment of this type of companies the right to issue several types of shares, including preferred shares, under Article (68) *bis*¹⁷ of the Jordanian Companies Law? However, the law of Jordanian companies not

¹⁵ Available at < www.amawi.info > accessed on 18th April, 2018.

¹⁶ Kharabsheh, Sami. (DT), *Legal System of Private Shareholding Companies* (Dar Al-Nasher- Amman – Jordan, 1st edition 2005) P. 23.

¹⁷ See The Jordanian Companies Law, Part Five *bis* Private Shareholding Company, Article (68) *bis* Share Types and Shareholding Options stipulates:

A- Subject to any provisions in this part, the Company may, according to its Memorandum of Association, issue various types and categories of shares which differ in their terms of nominal value, voting force and method of profit and loss distribution among shareholders. These shares also differ in respect of their rights and priorities upon liquidation and their aptitude to be converted into other types of shares besides their related rights, advantages, priorities and other restrictions, provided that these be implied or summarized in the shares' certificates if found.

B- The Memorandum of Association of a Private Shareholding Company may stipulate its right to issue recoverable shares either upon the Company or shareholder's request or upon the availability of certain conditions.

C- Any type or category of the Company's shares may have priority over other categories and types regarding profit distribution. Furthermore, these shares may be entitled to a lump sum or a specified percentage of the profit that are subject to conditions and periods set by the Memorandum of Association. Moreover, any of these types and categories may have priority in receiving profits due to them, for any year during which no profit was distributed, in addition to profits due in that fiscal year.

only the right to issue preferred stocks to the private shareholding company alone, but added to the recommendation company shares Which also allowed it to issue preferred stocks.¹⁸ But this type of companies does not exist on the ground due to the lack of investors to establish such type of companies, especially after the emergence of both the private shareholding company and Limited Liability Company.¹⁹ In addition to the essence of which a shareholding company is formed that prevent them from establishing, it comprises from two types, type 1: Joint partners managing the company and accounting for their own funds, debts and commitments, while type 2: is contributing partners who do not accounting for company's debts and liabilities except for what they contribute to the company's capital, We understand through this company the reason behind non-existence, since it is rare for a part of the partners to shoulder the commitments imposed on them and the company and ask through their own money as well as they have the burdens of managing the company in return for the other part, which is not responsible only insofar as it contributes to the capital. Therefore, there is no need to talk about the preferred stocks issued by the recommendation company due to the above-mentioned reasons. As for the public shareholding company as for the public shareholding company.²⁰ The Jordanian Companies Law implicitly prohibits the issuance of preferred stocks based on the provisions of Article 95 (f), which stipulates the following "The Board of Directors may issue shares as provided for by the provisions of the Securities Law in force" When referring to the Securities Law, they found that they did not address the preferred stocks, On this basis, it is clear from the above why the scholar said that the for the Private Shareholding Company in respect of the issuance of the Preferred Shares in Jordanian Law without other companies.

Preferred stocks issuance conditions

D- The Memorandum of Association of a Private Shareholding Company may provide for the possibility of converting or replacing any share type or category issued by it into any other type or category upon the request of the Company or a shareholder or upon the fulfillment of a certain condition according to rates and method set in the Company Memorandum of Association.

E- A Private Shareholding Company may buy any shares it had previously issued. It may also re-issue or sell same for the price deemed proper by the Board of Directors or cancel them and accordingly decrease its capital on the basis set out in its Memorandum of Association and this Part. Company owned shares shall not be taken into consideration for the purpose of ascertaining a quorum for attendance at the General Assembly's meeting and for taking decisions therein, provided that the Securities Law and regulations and instructions issued pursuant thereto are observed.

F- Subject to the Company's Memorandum of Association, the Securities Law and regulations and instructions issued in pursuance, a Private Shareholding Company may issue share options that permit their holders to buy or request the Company to issue shares. The options' conditions, date of implementation and implementation prices of same shall be determined in the Company Memorandum of Association or pursuant to a decision by the Board of Directors provided that it is authorized to do so by the extraordinary General Assembly.

¹⁸See Article (78) Jordanian Companies Law which stipulates "The general and limited partners may agree in the Limited Partnership's Articles and Memorandum of Association to the existence of types of shares that have a voting power and on the method of distributing profits and losses".

¹⁹The opinion of the Jordanian Companies Monitor. See Al Aquely, Aziz, *Commercial Law*, (Dar Al thaqafa, Amman – Jordan, 1st edition, 1997)P.387.

²⁰ Public Shareholding Company is a "company that undertakes to introduce its securities to the public to subscribe to them." Available at < <http://www.alastairhudson.com/companylaw>> accessed on 25th April, 2018.

In reviewing the texts of the Jordanian Companies Law, it is noted that the legislator did not clearly indicate the conditions required by the joint stock company to issue the preferred stocks. Although the Jordanian legislator authorized the shareholding company to issue the preferred stocks in accordance with its statute, according to article (68) *bis* of Jordanian Companies' Law. But this article is not enough, i.e. Shareholding Company is not always authorized to issue the preferred stocks, regardless of being ordinary or preferred related to set of regulations and laws. There is securities law the regulates legal provisions related to stock, in addition to the instructions of companies' governance of 2017 that works on clarifying some legal provisions related to listed and non-listed Joint Stock Companies. Accordingly, this sector will be divided into three issues; we address the legal conditions and the agreement for the issuance of preferred stocks and allocate the third issue to indicate the restrictions on the issuance of such stocks.

Legal conditions to issue preferred stocks

Jordanian legislator authorized Joint Stock Company to issue preferred stocks only by article (68) *bis* of Jordanian Companies' Law. However, it does not necessary mean that article (68) *bis* is separated from the rest of legal texts and related regulations, assuming that article (68) *bis* is a special article for issuance of preferred stocks. Consequently, it does not need other legal texts to regulate legal provisions related to preferred stocks, which will lead to legal contradictions on the issuance of preferred stocks. Therefore, the scholar needs to address the legal contradictions, with considerations that article (68) *bis*, the subject of research, has privacy and independence. Accordingly, legal requirements added by Jordanian legislator and related to preferred stocks must be clarified and compared with other legal texts. The conditions are the following:

According to the Companies law

We previously addressed that Private Shareholding Company shall issue preferred stocks pursuant to the provisions of the article (68) *bis* of Jordanian Companies' Law. However, if this text is taken directly and relied upon without paying attention to the rest of the texts, there is a contradiction in the above mentioned Companies Law. When reading the article (67) *bis* ²¹ Jordanian Companies Law that organizing legal provisions relating to the

21 See The Jordanian Companies Law, Part Five *bis* Private Shareholding Company, Article (67) *bis* Foundation Application stipulates:

A- An application for the foundation of a Private Shareholding Company accompanied by its Articles, Memorandum of Association and names of its founders shall be submitted to the Controller. The Company's Articles and Memorandum of Association shall be in Arabic. However, they may be accompanied by a translation into another language. The Arabic text shall be adopted in the case of conflict between the texts.

B-A Private Shareholding Company's Articles of Association shall contain the following statements as agreed upon by the founders or shareholders of the Company:

1. The name of the Company.
2. Its headquarters and approved notification address.
3. The objectives of the Company.
4. The founders' names, nationalities, chosen notification addresses and number of shares held by each upon the Company's inception.
5. The Company's authorized capital and the number of authorized shares, their type, category and nominal value.

establishment of a private joint stock company, we note through articles that Jordanian legislator obliged the company to stipulate the number of authorized stocks number, types and nominal value in its Memorandum of Association. Hence, there is no way to apply article (68) *bis* to issue preferred stocks unless it is consistent with Article (67) *bis* of Jordanian Companies Law, where benchmarked laws such as Lebanon code of commerce which stipulates in the article (110) nominal value and voting power in terms of how dividends and losses are distributed to shareholders "However it is permitted to create, by a resolution of an extraordinary meeting deliberating as shall be indicated hereinafter, preference shares whenever the Articles are not formally against them" as well as Moroccan company law that stipulates in article (262) "Upon the establishment of the company or during the period of its establishment, priority shares may be established that confer privileges that are not granted to other shares". On the basis of this, the joint stock company established in accordance with the provisions of the Moroccan and Lebanese laws may issue the preferred stocks upon two conditions 1- That no explicit prohibition is contained in the Statute prevents this 2- And to obtain the approval of the Extraordinary General Assembly.

According to Securities Law

We said that preferred stocks are a security Thus, the Jordanian Securities Law ²² the instructions issued under it is a special law for them. Although the Jordanian legislator did

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6. The methods for managing the company, and the number of Board of Directors' members and their powers.
 7. Names of those to call the convention of the constituent General Assembly and who will also manage the Company until the first Board of Directors is elected.
- C- A Private Shareholding Company's Memorandum of Association shall contain the following information as agreed upon by the founders or shareholders of the Company:
1. The Company's name.
 2. Its main office and approved notification address.
 3. The objectives of the Company.
 4. The founders' names, nationalities, chosen notification addresses and number of shares held by each upon the Company's inception.
 5. The authorized capital of the company and the authorized number of shares, their type, nominal value, rights, quality and advantages.
 6. The general conditions of for the transfer of the title of a Company share, and the procedures that should be followed in this regard.
 7. The Company's management method and number of members of the Board of Directors, their powers and the basis of decision taking therein.
 8. Procedures and rules of the shareholders' General Assembly meetings, both ordinary and extraordinary, their legal quorum and convening principles in addition to their powers and decision-taking method and issues related thereto.
 9. Procedures and rules for the liquidation of the Com
 10. Names of the persons who shall invite the constituent General Assembly to convene and who shall manage the Company until the first Board of Directors is elected, and the method of inviting the first Board of Directors to convene.
 11. Whether the shareholders and the holders of securities issued by the Company have priority rights in new Company issuances.
- D- Any person may view the Company's Articles of Association in accordance with the instructions issued by the Minister. It is not permissible for any other person other than the Company's shareholders to view the Company's Memorandum of Association, only under the shareholder's or the Company's authorization, or if this is required by any other legislation.

22Jordan Securities Law No. 18 of 2017.

not specify a special section for the Securities Law clarifying the conditions that are required to be achieved, in order for the private shareholding company to issue the preferred shares. However, the issue of Preferred stocks shall be subject to the Securities Law under the provisions of article (5) herein "Every Issuer in the Kingdom shall submit to the Commission an application for registering securities therewith in accordance with the instructions issued by the Board" This article obligates each issuer of securities, including the private joint stock company, to register its securities with the Securities Commission.²³ In accordance with instructions issued by the Board of Commissioners of the Securities Commission, the text of the above article has come in the form of the launch and therefore even the Preferred stocks are not included in its provisions. However, there is a question whether the Securities Law has the right to impose on the issuing company to hold on issuing its securities, including preferred shares. To answer this question, reference should be made to the Securities Law, in particular Article (12 / e) thereof "Suspending or ceasing dealings in any security for the period it deems appropriate;" This Article shall determine the right of (the Board of Commissioners of the Securities Commission).²⁴ That the issuer must comply with its decisions regarding suspension of dealing with any securities including preferred stocks within the period deemed appropriate by the Board. Thus, it becomes clear to us that the issue of preferred stocks should be subject to the Securities Law. The Lebanese legislator differs in this regard from the Jordanian legislator, as he did not give the power to suspend the issue of preferred stocks by Securities Law. According to the scholar's view, Jordanian legislator was closer to the right point, when he imposed the shareholding company to abide by the provisions and instructions of the Securities Law if wanted to issue securities, including preferred shares, because it is not equal to the dissolution of the preferred stocks of the Securities Law as it is a special law as has been done.

According to Corporate governance rules²⁵

Corporate governance has become significant after the bankruptcy of several companies, which used to provide false financial reports for investors and shareholders that there are sufficient guarantees in the company in order to motivate them to invest in it. Therefore, in line with the requirements of economic modernity and to maintain the stability of the financial markets and bring peace of mind and establish the principle of cooperation and share responsibilities among all shareholders, the Jordanian legislator issued corporate governance guidelines for the year 2017. In order to provide a favorable environment of transparency and credibility in financial transactions; The Jordanian corporate governance guidelines are divided into two parts: 1-The part related to joint stock companies unlisted in Stock Exchange 2- The part related to joint stock companies listed in Stock Exchange licensed by Securities Commission pursuant to the provisions of article (2) of the Jordanian Securities Law. The Private Shareholding Company, in accordance with the Corporate

23Jordan securities commission is a legal entity with financial and administrative independence and the right to carry out all legal actions necessary to achieve its objectives.

24The Council of Commissioners is the Board which is responsible for the management and supervision of the Securities Commission and consists of five full-time commissioners to perform the duties entrusted to them.

25Corporate governance: (Set of legal rules regulating the relationship between corporate management and partners and other stakeholders on the basis of the determination of rights and implementing obligations as required by good faith in the management and control of the company), see Jahlul Ammar, D., T., *The Corporate Governance Law*, (Dar Niebur , Qadisiyah, Iraq, 1st edition , 2011) P. 31.

Governance Guide, is not obliged to apply the Corporate Governance Regulations except for the Private Shareholding Company, which has a capital of (500) thousand JDs, subject to the provisions of the Corporate Governance Law under articles (89) and (151). We find that it restricted the private shareholding company listed in the issue of preferred stocks, as stipulated in Chapter 5 of the Corporate Governance Guide on Shareholders' Rights. Although the said chapter indicated that shareholders' equity depends on the categories of shares they own, the term (Categories) of the Preferred stocks are intended for the same ordinary stocks as they can be classified into categories that differ from each category to the other. (1) Of shareholders maintaining voting rights of up to ten votes per share while shareholders of the category (2) Their shares have one vote for each share they own in the company. Our findings can be inferred by reference to article (68) *bis* of the Jordanian Companies Law, which states "the Company may, according to its Memorandum of Association, issue various types and categories of shares which differ in their terms of nominal value". Through this text, it is clear that the word (categories of shares) contained in the Corporate Governance Guide does not include the Preferred stocks; for the existence of the contrary presumption in article (68) *bis* of the Jordanian Companies law. Many countries have introduced the corporate governance system into their legislation in view of the benefits offered by this system to the companies operating in terms of risk management and protection of the rights of shareholders and other stakeholders dealing with the company and raising the level of performance of the company to achieve its objectives and the benefits of that system. Legislation of governance is divided into three sections.²⁶ The first is the legislation that requires the company to apply the rules of governance such as the Sultanate of Oman and the UAE, while the second is the legislation that does not impose the company to abide by the rules of governance, but to take them in a guiding manner, such as Egypt, but third section is for those who follow moderation principle to apply the rules of corporate governance such as to give some of its provisions mandatory, and that is the position of Jordanian and Saudi legislators. Jordanian law differs from other laws that stipulated the rules of governance in terms of reference to the rights of the preferred shareholders in accordance with the instructions of the governance of the unlisted share companies. Otherwise, everything stipulated in the Jordanian corporate governance rules is very similar to what was stated in other benchmark laws.²⁷

Terms of the agreement for issuing preferred stocks

After the explanation of legal requirement for issuing preferred stocks in the previous issue as we concluded that there should be no conflict between these terms. We will move to this requirement in order to show the agreement terms for issuing preferred stocks which has the same level of importance as legal requirements. Therefore, it will be clear to us that it is the basis of issuance of preferred stocks. Otherwise, companies lack the right for issuing those stocks. The requirements are the following:

1. The article (67/ B) *bis* that states the data must be provided by the company in Memorandum of Association, is the data according to article (67/ B) *bis* which stipulates founders and shareholders must agree, i.e. everything stated in Memorandum of Association including company's right to issue preferred stocks as stipulated in

²⁶Essalhin, alaish, "Corporate governance between laws and regulations", *International Review of Law*, Faculty of Law, Benghazi, Libya, available at < <http://www.qscience.com/doi/pdf/>> accessed on 23th April, 2018.

²⁷ An example of such laws is Egyptian, Saudi and Omani law.

paragraph 5 in the Memorandum of Association “The authorized capital of the company and the authorized number of shares, their type, nominal value, rights, quality and advantages” sourced by agreement and not law. Law is only a regulator. However, although paragraph 5 included preferred stocks but not categorical that the intended types of stocks are preferred. Consequently, can be converted to other types such as capital stock and enjoyment stock as well as ordinary and preferred stocks. Therefore, article (68) *bis* aims to show company’s ability in issuing preferred stocks.²⁸

2. Article (67/ C) *bis* of Jordanian companies' law related to basic system data. Such data are obligatory and must be agreed upon by founders or shareholders. Basic system data stipulated in paragraph 5 matches Memorandum of Association. The core difference between Memorandum of Association and basic system is presented in some added terms to basic system because it gives more details for data provided in Memorandum of Association, the relationship between Memorandum of Association and the basic system as same as the relationship between constitution and law. The researchers believe that the mentioning private shareholding company’s right in its Memorandum of Association and basic system is the source of issuing while the article (68) *bis* confirming and justifying this right, for example, company maintains the right in issuing preferred stocks as it knows its interest, with regard to the conditions stipulated in the Lebanese legislation related to issue preferred stocks mentioned in the article 110 paragraph B of Lebanon Code of Commerce “However it is permitted to create, by a resolution of an extraordinary meeting deliberating as shall be indicated hereinafter, preference shares whenever the Articles are not formally against them”. This article did not oblige the company to provide in its statute the issuance of preferred stocks and resorted to the words explicitly banning the text in the company's system but cannot say the possibility of issuing preferred stocks only when the availability of two conditions. First, no explicit prohibition in the company's system. Second, issuing a decision by the Extraordinary General Assembly to issue the Preferred stocks. This means that these two conditions must be combined, according to article (110), we cannot consider one condition, comparing to Jordanian Law on Issuance of Preferred stocks, we believe that Jordanian legislator is more obvious than Lebanese in providing protection to all shareholders. However, Lebanese code realized that later after requiring Extraordinary Assembly’s approval. But, the clarity of the Jordanian legislation by stipulating that the company should mention in its Memorandum of Association and its Articles of Association the possibility of issuing preferred stocks are good points for Jordanian legislator, because they adapted Jordanian Companies Law with regards grant freedom of choice to shareholders of the company. They provided clear image about the stocks types issued by the company with a freedom of choice for either subscribes to the shares offered by the company or withdraw subscription. If the Company's Articles of Association do not provide regulations for issuing Preferred stocks and the wishes thereafter to issue such type of stocks, it shall decide to meet the Extraordinary General Assembly to amend the Articles of Association which require a percentage exceeded 75% of shares, that maintains right to vote in Extraordinary General Meetings. In this way, the Jordanian law shall give the shareholder the right once again to allow the company to issue the preferred stocks.

28 Mustafa, Taha, note 13 above, P. 431.

Subscription by preferred stocks and legal adaptation

Preamble and segmentation

The subscription is “The announcement of the will to share in the company's project with contributing in the capital by certain number of shares”²⁹ The opinions of jurists have been conflicted with regards delaminating the legal nature of subscription. Some jurists consider it as a legal action by subscriber to enroll to the company, while others believe that the subscription is a contract concluded between the subscriber and the company as a juridical person in the process of formation represented by the founders in the contract. While there is another trend considering subscription legal nature of shares as a contract, not only with the company, but also between the subscriber and the founders on the grounds that the company does not have a legal presence. However, such jurisprudential views did not address the issue of subscription legal nature of preferred stocks or the legal adjustment of such stocks. Jordanian legislator is different from others. As legal nature of the subscription shares after the registration of the shareholding company and before registration.³⁰ However, realizing subscription and its nature under Jordanian law, in this part, we will explain by analyzing the legal texts addressing the issue of subscription, through which we can determine the position of the Jordanian legislator and the jurisprudential direction that adopted.

In the light of the above mentioned and to be able to explain preferred stock subscription legal nature and legal adjustment, we will divide this part into four sections. Section one for jurisprudent opinions that raised to define legal nature for subscription. Section two for legal nature for preferred stock subscription. Then in section three we will address required legal procedures and limitations of preferred stock subscription in accordance with the provisions of Jordanian law. Finally, in section four, is determined to show legal adjustment of preferred stocks.

Legal nature of subscription

The jurists differed on legal nature of shares subscription and each trend had its own perspective in this regard.³¹ A tendency to consider the nature of the subscription as a legal act with a individual will where subscriber discloses his intention to join the company. The rationale is, companies under establishment are not considered existed companies as in this case there are no shareholders as they cannot waive rights that are not theirs. In addition, companies cannot claim the subscriber with the rest of the subscribed shares value and cannot be said that the subscriber contracts with the founders in their capacity as deputies representing companies will because it has not yet acquired the moral personality in order to have representatives acting in its conduct.

While other side considers that the legal nature of the subscription is a contract concluded between the subscriber and the company as a legal person in the role of construction represented by the founders in the contract.³² The company at this stage has an incomplete moral character only authorized to handle necessary biasness to complete its establishment

²⁹Ibid.

³⁰ Such as Iraqi, Egyptian, Tunisian, Algerian and Saudi law.

³¹ Ali, Younis, *Broker in Commercial companies*, (Dar Alfikr Al-Araby, Egypt, 1st edition, 1960) P.56.

³² Muhsen Shafiq, Muhsen (D.T), *Mediator in Egyptian Commercial Law*, (Part 1, Al nahda Almasria, Egypt, 1st edition. 1957)P.190.

while another tends to consider the nature of the subscription held between the subscriber and the founders in their personal capacity because the company at the stage of incorporation does not legally exist.

Accordingly, this section will be divided to three issues presenting; juristic opinions to explain legal nature of subscription. We address in first issue subscription as an expression of the individual will of the subscriber, and then we will move to second issue to talk about subscription as a contract between subscriber and company and third issue to talk about Subscription as a contract to be concluded between the subscriber and the founders of the company.

Subscription as an individual will

Supporters of this trend ³³ believes that subscription is an expression of individual will show the intent to join and share in a shareholding company. As they refuse the contractual concept for subscription, with consideration that whatever related to individual will is not necessary a contract. Because it is not possible to include all that is shown by the individual will within the contract. The owner of this trend added other rationale; Subscriber does not know the rest of the subscribers and this is not compatible with the nature of the contract, in which each party knows the other. According to this opinion, the subscription is an expression of a single will to accept the subscription does not need to meet another will. However, this trend has faced many criticisms such as if the subscription is the sole will of the subscriber as stated by the supporters of the individual will the subscriber to retreat from the subscribed shares and this is inconsistent with the provisions of the legislation that imposed on the subscriber commitment to subscribe. The other matter is that if the subscription is linked to the will of the subscriber, it makes the company based on subscribers' will in the event they wish to complete the subscription procedures or unwillingness to do so and this is contrary to the nature of the subscription. ³⁴

The Subscription is held between the Subscriber and the Company

The owners of this trend believe that subscription is a concluded contract between subscriber and the company, to protect subscribers' rights. However, they disagreed about contractual nature which meant by other party as the subject of contract. ³⁵

Different trends will be addressed in this issue. Trends found to define subscription's nature, parties and subject, through discussing three jurists' opinions came up to address the problem of realizing the legal nature of subscription and appointing parties and subject.

The theory of agency

According to this theory, the subscription contract is established between the subscribers themselves. When first subscriber agrees to be a member in the company to be established, he hereby provides an implicit agency to the founders of the company, authorizing them to

³³ Awad. Ali. reviewed by Mohammad Basuony. Abd alawal, *The principle of free circulation of shares in joint stock companies*, (Dar Al-Fikr Al-Jami, Alexandria – Egypt, 1st edition 2007) P.279.

³⁴ Burberry, Mahmoud, *The moral personality of the trading company* (Dar Alfikr Al Araby Cairo, 1st edition, 1985) P. 416.

³⁵ Abu Zeid, Radwan, *Joint Stock Companies and public sector*, (Dar Alfkr Al-Araby, Cairo, 1st edition, 1983) P. 97.

appoint other subscribers, to comply with them sequentially. As a result, the founders are only representatives of the subscriber according to agency rules, and the subscription contract is held between all subscribers. The founders consider business managers of the group of subscribers are self-employed.³⁶

However, this theory was not removed from the shares of criticism for the following reasons:³⁷

- A: The consideration of the legal relationship between subscribers and founders is an implied agency contract is merely an assumption that has no basis in the law and is not linked to the will of the subscribers.
- A: Subscription is far from the founders, which means they do not know the potential and ability of subscribers to meet the company's obligations.
- C: Only founders are committed to fund the establishment of the company, and in case of company failure, there won't be any obligation shouldered by subscribers.
- D: Work with the theory of the agency would undermine the interest of the founders of the future of the company, which is always the founders are keen on the success in achieving its goal and purposes in order to preserve their money.
- E: That the acceptance of this theory (the theory of the agency) leads to the consideration of the subscribers are the founders, which entails their responsibility in the event of the project failed and establish the company was not completed.

As a result, for the criticism of this theory, it is not possible to take it to explain the legal nature of the subscription contract.

The theory of direct relationship

Some jurists believe³⁸ the subscriber is directly responsible to the company under establishment. According to this opinion, the subscription is a contract between the subscriber and the company acquired for the moral personality at this stage, in relation to the moral personality that the company has during its liquidation.

But this legal opinion is not based on most legislation, because there is legislation does not confer on the company that is in the stage of establishing the moral personality only after the completion of the subscription. So, the owners of this theory sought to find a way out of this problem by adapting the idea of the internal personality. Where the owners of this trend believe in the need to recognize in such legislations the company's ability to conclude the subscription contract with the subscriber provided that this recognition remains limited

³⁶ Ahmad Mohammed, Mehraz, *Legal System of Joint Stock Companies*, (Dar Al kotob Al qanounia. Cairo, 1st edition, 1997) P. 53.

³⁷ Salem Abdel Rahman, Gumed, "The legal nature of the Memorandum of Association of the Joint Stock Company and its impact on the small shareholders in Bahraini law", (2015) Journal of Legal and Legal Sciences, Number 1717-229. available at <<http://www.zu.edu.ly/jsls/issus-7/pdf>> accessed on 23th April, 2018.

³⁸ Aktham, Khuli, *Lebanese Trade Law part 2 Commercial Companies* (Dar Al-Nahda Al-Arabia, Lebanon , 1st edition, 1968) P. 241.

between the company represented by the founders and subscribers and therefore cannot be invoked in the face of others.³⁹

The interpretations and solutions offered by the supporters of this theory have not been dismissed from the criticism. If we assume that the subscription is a contract between the subscriber and the company by the founders on behalf of the company, fraud issued by these founders will result in cancellation of the subscribers' obligations towards the company. Therefore, a juristic trend has emerged. The subscription is a contract whose first party is the founders and the second party subscriber who expresses his will to accept the subscription arises between him and the founders. The contract, which includes mutual legal effects between two parties, is subject to obligations and has rights since the establishment of the contract until the formation of the company. However, this opinion did not find a solution in case non-eligibility or bankruptcy of one of them for not being able to repay the debts owed to him.

Adaptation of the subscription contract

The owners of the contractual theory agreed to adapt the subscription as a contract, whatever the reason for the subscription, the problem of this theory related to the type of contract, either contract of a company or a contract of sale, or requirement for third parties (Pledge to third parties) or an indefinite contract.

Subscription of Company Contract

Several opinions in this regard, including one⁴⁰ believes that Joint Stock Company is a contract concluded between subscribers and shareholders who accept its regulation. Such action shall be considered as a disclosure to participate in the establishment of the said company. Accordingly, each Subscriber shall be liable in return for the other Subscribers.

But this view was not accepted and criticized for how the agreement between the subscribers to a contract committed to each other without prior knowledge between them. Another trend is that the company contract is between subscribers and founders. Subscriber when it is accepted by the founders the contract is established and the contract has mutual rights and obligations across the parties, starting from the conclusion of the contract and until the formation of the company. However, this view cannot be accepted. If we assume that the establishment of the joint stock company was the result of subscribers' participation with the founders, why are the founders alone responsible for the failure of the establishment of the company?

Subscription sale contract

From German jurist Orbach point of view, the subscription contract is a sale contract between the founders and the subscriber whereby the latter buys the temporary shares document in return for payment of its nominal value, which represents the price.⁴¹

³⁹ Murtada, Nasrallah, *Commercial Companies*, (Al-Ershad Press, Iraq, 1st edition, 1969) P. 128.

⁴⁰ Fareed, Mashriqy, *Origins of Egyptian Commercial Law* (edition 3. Anglo - Egyptian Library, Egypt, 3rd edition, 1959) P. 243.

⁴¹ Fawzi Mohammed, Sami, *Commercial companies general and special provisions*, (Dar Al Thaqafa for Publishing and Distribution, Jordan, 1st edition, Jordan, 2006)P. 345.

While Al-Faqih Sebah believes that the temporary stock documents cannot be considered a place of obligation. Therefore, the subscription contract is not a sale contract.⁴²

Subscription is a requirement for third parties

Some jurists interpret⁴³ the legal nature of the subscription contract in relation to the idea of third party liability. From this point of view, the subscription is a contract of condition for the benefit of third parties, the founding parties who contract with the subscribers in favor of the company to be established and under this contract; the subscribers are directly committed to the company to pay the value of the shares they subscribed to.

The third person (the contractor) is required to fulfill their obligation for the benefit of the third person (beneficiary) which will exist in the future provided that the contractor is ready to implement his commitment and declare the beneficiary. But this trend is criticized for the idea of undertaking for the benefit of others that would prevent the founders from forcing the subscriber to implement his obligation or claim compensation in accordance with the rules of the benefit of others.

Subscription is an informal contract

Under this contract, each party is committed to the other in the fulfillment of their obligations. Subscribers are obliged to provide the nominal value of the subscribed shares. The founders are committed to issue shares corresponding to the value paid by the subscribers.

Another view of jurisprudence is that the subscription contract is a contract of acquiescence since the subscribers agree on conditions imposed by the founders without having the right to negotiate, modify or cancel some of them. But this view cannot be recognized, especially at present, because of the prosperity of trade and the presence of a large number of companies entrusted with the holding of public service facilities in addition to the fierce competition between companies to provide the best services and offers to work to win the trust of their customers.

Accordingly, the subscriber is no longer obliged to accept the subscription contract, the terms of which are not suitable for them.

Subscription is a group work

Jurisprudential trend believes that subscription is not a contract and does not express individual will. But this trend is a collective action related to and under which the subscribers undertake to contribute to the capital of the company to be established, considering that this work is beneficial to all.

But this view is criticized because it weakened the role of founders who put corner stone for the establishment of the company. In addition, this opinion makes the legal relationship is limited only to subscribers, ignoring the relationship that links them to the company.

⁴²Ibid, P. 347.

⁴³ Abu Zeid, Radwan, note 35 above, P 127.

In conclusion, the Jordanian legislator has adopted the trend of direct relationship theory, whether the subscription was before or after the registration of the company. The legal adaptation of the subscription is a sale contract.

Legal nature of preferred stock subscription

After we addressed the Jurisprudent views that explaining the legal nature of the subscription, we realized the possibility of endorsing and applying them to the nature of the preferred stock subscription, in terms of its general framework. As the subscription to the preferred stocks is only a contract to be concluded between the subscriber and the company. The link between them shall be either directly if the company is registered or indirectly if it is not registered yet. The subscriber and the founders are contracted as representatives of the company. In terms of the special framework, the difference between the legal nature of the subscription to the ordinary stocks and the subscription of the preferred stocks of the first two aspects of the nature of the preferred stock subscription and the second legal adjustment of the subscription contract.

The jurists differed ⁴⁴about the nature of subscription, Is it civil or commercial business? The trend is to be considered a civil act and their argument that the subscription is a contract between persons who do not qualify as a merchant.

With regard to the nature of the subscription to the Preferred stocks, we have a contract and legal adaptation (purchase contract to participate in an investment project) for the following reasons:

First: The characteristics granted by the Preferred stocks to the shareholders in terms of priority of profits and precedence by dividing the liquidation product can be only investment.

Secondly, we have already mentioned that the joint stock company is offering the preferred stocks for the purpose of enhancing its commercial project in the event of default. This means that there is a risk to the subscribers' funds in the event of project failure. Accordingly, the subscription of the stocks of this company is a risk that is not normally performed by investors except by virtue of their experience in addition to their knowledge of financial markets and their economic and financial movement.

Third, one of the most important types of preferred stocks is convertible stocks, usually involving venture capitalists whose focus is on companies with revolutionary ideas in technology or a pioneering investment idea that is expected to succeed in the future. But they are not capable and qualified for continuity, they need two basic things that enable them to continue and survive. (A) Having large funds spent on this type of project (B) The need for business relations and adequate experience for the company's founders in the labor market. This is what ordinary shareholders cannot offer

On this basis, all the above confirm our result of the Subscription of the Preferred stocks can be only an investment.

⁴⁴Yaqoup, Sarkhwa, *Shares and their circulation in companies contributing to Kuwaiti law* (comparative Study), (al Kuwait, 3rd edition, 2nd esition, 1993) P. 79.

CONCLUSION

Due to the significance of preferred stocks as one of the most important securities used by Joint Stock Companies in order to develop and progress in mega-business ventures, this is because the security offers advantages made it shareholders' investors' target and to subscribe.

The researchers found, through deep analytical reading for Jordanian law articles regulating this type of stocks is insufficient to cover preferred stocks' legal aspects.

According to the foregoing, the researchers summarized the research contents by a set of outcomes and recommendations that show the key elements of this study.

Outcomes

1. According to Jordanian Companies Law, preferred stocks can only be issued by Private Equity Company and Private Shareholding Company.
2. Joint Stock Company is not obliged to issue the Preferred stocks and shall have absolute freedom in this regard, in accordance with the provisions of the law in which the company operates under its provisions.
3. The issuance of the Preferred stocks shall be subject to the Securities Law and the instructions issued thereunder. Such stocks shall be traded in a private money market.
4. Private shareholding companies have to state issuing preferred stocks in their interior basic regulations to be able to issue such stocks.
5. Preferred stocks go through several phases before being registered in shareholder's name. The phases are; legal text allows issuance, stipulated in Memorandum of Association and Basic Company's regulations, then subscription phase followed by contracting phase that distinguishes between preferred and ordinary stocks.
6. Issuing preferred stocks is not a deviation from the principle of equality if the law allows issuing and because general system and exception are identified according to law.
7. Both researchers found throughout search, study, comparison and analysis that the preferred stocks not only include the contractual nature, but also refer to both the nodal and systemic nature, which we mean the Memorandum of association and the basic law of the company.

Recommendations

1. Both researchers recommend Jordanian legislator to specify preferred stocks given to their different contractual nature against ordinary stocks, special regulations explain subscription process in addition to other regulations that maintains shareholders and to prevent conflicts in future.
2. Jordanian legislator has to oblige companies to stipulate clearly the types of preferred stocks in its memorandum of association and basic law in addition to concluded

contract between companies and shareholders to avoid future conflicts either among shareholders or shareholders and companies.

3. We recommend Jordanian legislator to stipulate an article to differentiate between joint stock companies that issue their stocks to public subscription against for private subscription, such article to be added article (68) *bis*. In terms of preferred stocks, the company that offers only this type of stocks to a certain group of businessmen and investors does not necessarily have to prove their rights in private contracts. Because they usually aware of and know enough about the risks in stock market and their rights and commitments. We only have to confirm the rights and commitments as stated in the Memorandum of Association and Articles of Association of the company in addition to what was included in the share certificate, while joint stock company whose shares are offered to the public for subscription, the researchers recommend that the legislator provide in the paragraph added to the above article the following " If the company issues shares for public subscription, including preferred shares, it must fix the rights and obligations of the preferred shareholders on the Memorandum of Association and the Company's Articles of Association, in addition to the contract concluded between the Company and the preferred Shareholder". The motive behind this recommendation is to respect and establish the principle of power of will, which are the contracts of the most sophisticated images and to reduce the occurrence of legal conflicts that may arise between the shareholders and ordinary shareholders.
4. Jordanian legislator should make obligatory the jurisprudence that is issued to explain the nature of some of the paragraphs of the Preferred stocks from the ambiguity until the issuance or amendment of the articles on the provisions of the preferred stocks and clearly leaves no room for diligence and interpretation.

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