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Saudi Arabia

Companies

1. What are the main forms of business structure used in this jurisdiction and what are their main advantages?

The main forms of business structure used in the Kingdom of Saudi Arabia (KSA) are:

- Limited Liability Companies;
- Joint Stock Companies; and
- Branches of a company.

<u>Limited Liability Companies (LLCs)</u>

Part Seven of Saudi Arabia Royal Decree No. M6/1965 dated 22 July 1965 (as amended) (the Companies Law) sets out the laws regarding the formation and operations of LLCs.

The amount of shareholders in an LLC may be between two and fifty. Their liability is limited to the amount of their contribution for their respective shares in the company (Article 157, Companies Law). There is no minimum statutory share capital requirement for LLCs under the Companies Law (Saudi Arabia Ministerial Decision No. 221/2007 amending the previous minimum statutory capital requirement of SAR 500,000).

However, there are certain sectors where a minimum share capital is required by the Saudi Arabian General Investment Authority (SAGIA). For example, the minimum acceptable capital in the industrial sector is SAR 1,000,000. In the agricultural sector, the minimum acceptable capital is SAR 25,000,000. SAGIA and the Commerce and Industry Ministry (MOCI) have discretion to require larger capitalisation.

There are no separate capital requirements for foreign investors in law. However, there are certain sectors where foreigners are not allowed to invest which are contained in the 'negative list' and other sectors where these investments require a minimum acceptable capital and is limited by way of a minimum KSA participation.

These activities are excluded from foreign investments:

Manufacturing Sector:

1. Oil exploration, drilling and production, except the services related to mining sector which are internationally classified under the codes (5115-883);
2. Manufacturing of military equipment, devices and uniforms.

Services Sector:

1. Catering to military sectors;
2. Security and detective services;
3. Real estate investment in Makkah and Madina;
4. Tourist orientation and guidance services related to Haj and Umrah;
5. Recruitment and employment services including local recruitment offices;
6. Real estate brokerage;
7. Printing and Publishing Services, except the following activities:

    a. Pre-printing services internationally classified under the code 88442;
    b. Printing presses internationally classified under the code 88442;
    c. Drawing and calligraphy internationally classified under the code 87501;
    d. Photography internationally classified under the code 875;
    e. Radio and television broadcasting studios internationally classified under the code 96114;
    f. Foreign media offices and correspondents internationally classified under the code 962;
    g. Promotion and advertising internationally classified under the code 871;
    h. Public relations internationally classified under the code 86506;
    i. Publication internationally classified under the code 88442;
    j. Press services internationally classified under the code 88442;
    k. Production, selling and renting of computer software internationally classified under the code 88;
    l. Media consultancies and studies internationally classified under the code 853;
    m. Distribution of movie and video tapes internationally classified under the code 96113;
    n. Typing and photocopying internationally classified under the code (87505 + 87904); and

8. Commission commercial agents internationally classified under the code 621;
9. Audiovisual services;
10. Land transport services, except inter-city train transportation;

11. Services rendered by midwives, nurses, physiotherapists and paramedics internationally classified under the code 93191;
12. Fisheries;
13. Blood Banks, Poison Centers and Quarantines.

LLCs with foreign shareholders require a foreign capital investment license as issued by SAGIA. (Saudi Arabia Royal Decree No. M1/2000 dated 10 April 2000 and its Rules of Implementation published on 16 August 2002 (the Foreign Investment Law)).

The LLC must obtain a commercial registration certificate from MOCI before starting operations in KSA. The shares in an LLC must be fully paid up at the time of subscription and the monies need to be paid into a KSA bank designated by MOCI (Article 162, Companies Law).

Shares in an LLC need to be of equal value (Article 158, Companies Law).

Shares in an LLC cannot carry different voting rights. For each share held by the shareholder, they are entitled to one vote (Article 171, Companies Law).

10% of the annual net profits of an LLC must be set aside for the formation of a statutory reserve until it reaches 50% of the capital of the LLC (Article 176, Companies Law).

The articles of association must closely reflect the standard form of the articles published by MOCI and must be approved by MOCI. They must be broad enough to facilitate the operations of a LLC, but if too broad, MOCI is unlikely to approve them.

If the losses incurred by an LLC are in excess of 50% of its capital, the general manager of the LLC, within thirty days, must convene a meeting of the shareholders to consider whether the company should be dissolved or continue to exist as a going concern (Article 180, Companies Law).

A unanimous shareholder's resolution is required in order for the company to validly continue as a going concern. In the case of dissolution of the company, a shareholder's resolution must be adopted by a majority of shareholders representing at least three-quarters of the company's capital (Article 173, Companies Law).

Once the shareholders have passed a resolution in line with the above, it must be published in the Official Gazette. The publication should take place within a thirty-day period from the date of the shareholder's resolution (Article 164, Companies Law).

If the shareholders of the LLC decide to continue the company as a going concern, they need to provide an undertaking to be jointly liable to pay all company debts on a pro-rata basis (based on their shareholding percentage) (Article 180, Companies Law). Furthermore, shareholders of the LLC must recapitalise the share capital of the LLC immediately following a special resolution (based on their shareholding percentage).

If the general manager fails to convene a meeting in line with Article 180 of the Companies Law or if shareholders are unable to approve a resolution, each shareholder will be held jointly and severally liable for the company's debts and any concerned party may request for the dissolution of the company. LLCs are not permitted to undertake insurance or commercial banking activities (Article 159, Companies Law).

The main advantages of an LLC are that it is a separate legal entity; there are no minimum statutory capital requirement, except as provided in the table issued by SAGIA and the liability of the shareholders is limited to their shareholding in the LLC, subject to Article 180 of the Companies Law.

The disadvantages of an LLC are shares must be fully paid up at the time of subscription; shares cannot be offered to the public and the shares need to be of the same class, i.e. carrying the same denomination and equal voting rights.

Joint Stock Companies (JSCs)

Part Five of the Companies Law governs the formation and operations of JSCs. There needs to be a minimum of five shareholders to form a JSC and the shares need to be of equal value. There is no maximum number of shareholders as shares can be offered to the public, subject to approval from the Capital Market Authority. The nominal value of a share will be SAR 10. The liability of the shareholders is limited to the amount of their contribution for their respective shares in the company (Article 48 and 49, Companies Law).

The minimum statutory share capital requirement for JSCs is SAR 2,000,000. If shares of the JSC are offered to the public, the minimum statutory capital requirement is SAR 10,000,000 (Article 49, Companies Law). There are also certain industry specific minimum capital requirements as well.
There are no separate share capital requirements for JSCs incorporated by foreign shareholders. The 'negative list' will also apply to a JSC.

JSCs with foreign shareholders require a foreign capital investment license issued by SAGIA.

The JSC must obtain a commercial registration certificate from MOCI before commencing operations in KSA.

The shares of a JSC can be partially paid up on incorporation. The paid in capital of a JSC not offering its shares to the public will be no less than one half of the prescribed minimum on incorporation (Article 49, Companies Law).

Subject to the approval of MOCI, if the JSC issues an invitation to the public to subscribe to its shares, the amount payable per cash share upon subscription will be no less than one quarter of its par value (Article 58, Companies Law).

10% of the annual net profits of a JSC must be set aside for the formation of a statutory reserve until the reserve reaches 50% of the capital of the JSC (Article 125, Companies Law).
If the statutory reserve exceeds 50% of the capital of the JSC, the ordinary general assembly may decide to distribute the excess to shareholders in the years when the JSC's net profits is not sufficient for the distribution as set out in the JSC's articles (Article 126, Companies Law).

The JSC's articles must state the percentage of net profits payable to the shareholders after setting aside the statutory reserve and the conventional reserve. The percentage should not be less than 5% of the JSC's capital (Article 127, Companies Law).

JSCs – a) manage a public utility; b) is provided a subsidy by the State; c) involves the State or other public legal persons; d) are privileged and e) practise banking businesses, are required to, prior to incorporation, obtain a licence issued by a Royal Decree on the approval of the Council of Ministers and the presentation of MOCI (Article 52, Companies Law).

For other types of JSCs, the incorporation is conditional upon a licence being issued by MOCI and published in the Official Gazette (Article 52, Companies Law).

The main advantages of a JSC are its ability to increase share capital by way of a public offering. The share capital in a JSC does not need to be fully paid up on incorporation. Finally, unlike an LLC, a JSC can issue different classes of shares.

The main disadvantages of incorporating a JSC are the higher statutory minimum capital requirements, a longer timeframe for the incorporation of certain JSCs and in the case of shares being offered to the public, being subject to Capital Market Authority requirements.

Branch of a company

Branches are subject to the provisions and regulations regarding the type of activity intended to be carried out and require a licence from SAGIA. Certain branches (like branches of professional companies) do not need a SAGIA licence but do need a commercial registration certificate issued by MOCI.

A foreign company cannot establish a branch without obtaining a licence from MOCI (Article 228, Companies Law). In addition to this licence issued by MOCI, branches of a foreign company require a foreign capital investment license issued by SAGIA.

A foreign company establishing a branch is required, as is the case with LLCs and JSCs, to deposit an amount equivalent to the capital required by SAGIA with a KSA bank until the licence has been issued by MOCI. There are also minimum capital requirements.

Branches of foreign companies are subject to the 'negative list'.
The main advantage of establishing a branch is that it is relatively easy to set up. The main disadvantage of establishing a branch is that it is not a separate legal entity and it must carry out the same activities as the parent company.

2. What is the main legislation covering the establishment of a business entity?

The main piece of legislation governing the establishment of a business entity is the Companies Law.

3. What are the main differences in setting up a business entity in this jurisdiction than in other major jurisdictions?

The main difference in the setting up of a business in the KSA as opposed to other major jurisdictions is the Kingdom adheres to a strict form of Sharia law. Any investor seeking to set up a business entity needs to make themselves aware of the principles governing Sharia law. Whilst the Kingdom allows 100% foreign owned entities to be incorporated, this is limited by SAGIA. Apart from the restrictions discussed above, there are several requirements investors need to be aware of when setting up an entity in KSA. Although implemented primarily in the construction and oil and gas sectors, there are certain technology transfer, skills transfer and local content requirements which need to be met.

Companies established in KSA are subject to the policy of Saudisation, whereby, companies are required to employ a certain percentage of Saudi citizens, ranging from 5%-75% based on the type of business, the relevant sector and the availability of Saudi employees.

In terms of enforcement of contracts and corporate disputes, prospective investors seeking to invest in KSA need to be aware of the fact litigation can take several years to resolve in KSA courts. As an alternative to litigation in KSA, disputes could be referred to domestic arbitration under Saudi Arabia Royal Decree No. M34/1433 (the Saudi Arbitration Law) or international arbitration. In principle, foreign awards are recognisable and enforceable in KSA, given KSA is a signatory of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Saudi courts can however deny enforceability of foreign arbitral awards on the grounds of non-compliance with public policy and Sharia law.

4. Are there any specific rules around ownership of businesses in this jurisdiction?

The Foreign Investment Law permits foreign ownership. However, there are certain exceptions. In particular, SAGIA maintains a 'negative list' of activities expressly excluded from foreign investments.

This list is regularly revised and therefore it is recommended foreign investors keep up-to-date with the most recent and updated list.

In addition to the 'negative list', there are certain industry licences issued by the SAGIA, whereby foreign ownership is limited (i.e. a 100% foreign ownership is not permitted). These industry licences include licences like commercial; communications; insurance; real estate financing and management of construction projects. Minimum Saudi participation as per the SAGIA licensing regime can range anywhere between 25%-40%.

The 'negative list' is regularly revised and therefore it is recommended foreign investors keep current with the most recent and updated list.

5. Is it possible for a multinational company to establish a branch in this jurisdiction? How is this done?

Branches are subject to the provisions and regulations regarding the type of activity intended to be carried out and require a licence from SAGIA. Certain branches (like branches of professional companies) do not need a SAGIA licence but do need a commercial registration certificate issued by MOCI.

A foreign company cannot establish a branch without obtaining a licence from MOCI (Article 228, Companies Law). In addition to this licence which is issued by MOCI, branches of a foreign company require a foreign capital investment licence issued by SAGIA.

A foreign company establishing a branch is required, as is the case with LLCs and JSCs, to deposit an amount equivalent to the capital required by SAGIA with a KSA bank until the licence has been issued by MOCI. The minimum capital required for the branch of a foreign company is set out.

Branches of foreign companies are subject to the 'negative list'.

6. Is it possible for a multinational company to establish a subsidiary in this jurisdiction? How is this done?

A multinational may set up a business entity (preferably in the form of a LLC or a JSC) with a 100% ownership, save for certain sectors where ownership by foreign investors is prohibited (as per the 'negative list') or limited.

7. Is it possible for a multinational company to enter a joint venture in this jurisdiction with a local company? How is this done?

Typically, two types of joint ventures (JV) are entered into in KSA: contractual JVs and corporate JVs. A contractual JV is an association of which third parties are not aware of and which does not enjoy a legal personality and is not subject to the publication procedures (Article 40, Companies Law). Contractual JVs usually operate for a brief amount of time and are limited in the scope of activities they undertake. Furthermore, contractual JVs have the disadvantage the JV partner dealing with third parties is the sole partner bearing risk and therefore, has unlimited liability with respect to all of the contracts it has entered into, unless the relevant third party is aware of the contractual JV, in which case, the JV partners are jointly liable, and the contractual JV will be construed as a general partnership by the third party (Article 46, Companies Law).

Contrary to the contractual JV, corporate JVs are generally used by multinational companies seeking to operate in KSA for a longer period. A corporate JV is a type of a JV whereby shares in the JV are owned by both the multinational company and the local company. Corporate JVs with a foreign shareholder require a foreign capital investment licence issued by SAGIA.

In addition to the foreign capital investment licence, the corporate JV must obtain a commercial registration certificate issued by MOCI. There may be additional licences required for particular sectors. This process can be both cumbersome and time consuming. However, SAGIA have introduced reforms in an effort to simplify the process and shorten the time required to obtain the licence.

In addition to the above, as with all entities with a foreign investor, multinational companies must ensure their activity does not fall under the 'negative list' and their level of participation by way of equity is permissible by KSA law and the SAGIA.

LLCs are the most common form of business structures for corporate JVs.

8. Are there differences if a multinational company enters into a joint venture with a government owned entity?

There is no specific legal provision whereby entering into a JV with a government owned entity is governed by a different regime than the existing regime applicable to any other joint venture.

9. How are the main forms of business registered with the authorities? What documentation is required? What fees need to be paid? How long does this normally take?

The main forms of businesses registered in the KSA take shape in the form of an LLC. In order to establish and register the LLC, the following steps need to be taken:

a. Submission of an application to SAGIA to obtain an investment licence. In principle, the application will be reviewed and resolved in a maximum period of 30 days and costs SAR 2000. The following documents must be submitted to SAGIA:

    - Completion of electronic investment license application;

- Copies of commercial registration and company's articles of association in its country of incorporation duly attested by the competent authorities and the Saudi consulate;
- Copy of trade name reservation issued by MOCI;
- Draft articles of association;
- Shareholders' resolution to invest in KSA;
- Copy of manager's passport;
- Copy of national ID and Family Register of Saudi shareholder (if any) and a relevant offprint from the Civil Status Department;
- A detailed business plan;
- Financial statements covering a period of 3 years at least and reflecting the solid financial position of the company, duly certified by a recognised public accountant and authenticated by the body concerned with the trade and tax activity in the applicant's country and legalised by the Saudi consulate;
- Evidence of financial capability to invest in line with the action plan submitted for the project;
- Any other documents, data or information required by SAGIA.

b. Obtain approval from the Companies Department at MOCI after submitting the articles of association and the company name;
c. Sign the articles of association in front of a notary public;
d. Publication of the company name and a summary of the articles of association in the Official Gazette. This costs approximately SAR 5500;
e. Open a bank account, transfer an amount equal to the initial share capital and obtain a certificate stating the capital has been deposited;
f. Register with the General Department of Passports, Interior Ministry and the Labor Ministry and obtain a work visa for the company manager;
g. Company manager getting their visa stamped at the Saudi consulate and obtaining their work permit and residence permit on arrival in KSA;
h. Registrations with the Commercial Registry at the Ministry of Commerce and Industry and the Chamber of Commerce;
i. Obtain a file number and certificate of business commencement by registering with the Department of Zakat and Income Tax (DZIT), Finance Ministry; and
j. Register with the General Organisation of Social Insurance.

The overall process generally takes approximately 30 to 60 days.

In addition to the steps above, there could be other stages to the application process determined by the specific sector in which the business wishes to take part in.

10. What qualifications are required for directors?

The main forms of companies used in KSA are LLCs and JSCs:

- JSCs must have a board of directors with a minimum of three directors. Directors must hold (or one of the shareholders must pledge the shares on behalf of the Director) a minimum of SAR 10,000 shares to be deposited with a bank and held as a guarantee for the director's liability. No special provisions require directors to be KSA nationals.
- There are no specific qualifications for directors in LLCs. Directors do not have to be shareholders.

11. Can directors be disqualified?

Directors of LLCs may only be disqualified for legitimate reason.

As far as JSCs are concerned, the articles of association must specify the manner under which board of directors' membership terminates. Furthermore, the ordinary general assembly may, at any time, revoke all or some of the directors, notwithstanding any contrary provision in the articles of association and without prejudice to the revoked director's right of indemnification if the revocation occurs for no acceptable cause or at an improper time.

12. If there are freezones or enterprise zones operating in the country, what are the main differences between setting up a business in one of these or onshore?

KSA established numerous industrial cities and technology zones. These zones do not have specific regulations governing business entities incorporated in the relevant zones. Therefore, business entities set up in these zones will be subject to the same regime as the onshore business entities. However, it is worth mentioning the following industrial cities and technology zones offer the following business incentives:

- Jubail City: aimed at energy industries, offers tax holidays and customs exemptions
- Yanbu Industrial City: home to large-scale oil refining and petrochemical production plants offers tax holidays and customs exemptions

13. Once a business entity is registered, what annual processes and payments are needed to ensure ongoing registration?

Once a business entity is registered, the following annual fees must be paid to the commercial register:

- SAR 1,600 for JSCs and partnerships limited by shares;
- SAR 1,200 for LLCs;

- SAR 800 for the remaining companies; and
- SAR 200 for sole establishments.

In addition, SAR 10,000 must be paid for subscription to SAGIA's services.

Furthermore, every business entity registered with the commercial register should subscribe as a member of a Chamber of Commerce and Industry and pay an annual subscription fee. The Chambers of Commerce and Industry Law states the annual subscription fee depends on the category which the business entity applies for as described below:

- Traders and manufacturers have the option to apply for the Excellent Category subject to the payment of an annual fee of SAR 10,000;
- JSCs, currency exchange and funding companies, banks, LLCs whose share capital is over SAR 5 million and first class contractors must apply for the First Category subject to the payment of an annual fee of SAR 5,000;
- General partnerships, limited partnerships, partnerships limited by shares, LLCs whose share capital is less than SAR 5 million, and second class contractors must apply for the Second Category subject to the payment of SAR 2,000;
- The remaining contractors, real estate offices and commercial agents must apply for the Third Category subject to the payment of SAR 800; and
- The remaining business entities which do not fall within the scope of these categories must apply for the Fourth Category subject to the payment of an annual fee of SAR 300.

14. Are there any unique or unusual forms of business entity in this jurisdiction? When are they used and why?

KSA law does not have unique or unusual forms of business entities.

15. Is it possible to have dormant business entities? What are the minimum regulatory requirements for these?

SAGIA does not accept a foreign entity to be dormant.

16. What are the rights of shareholders?

JSC:

- Under Article 83 of the Companies Law, the articles of association will specify who is entitled to attend general assembly meetings. Nevertheless, every shareholder owning 20 shares or more is entitled to attend general assembly meetings notwithstanding any disposition to the contrary in the articles of association. A shareholder may give proxy, in writing, to another shareholder who is not a member of the board of directors, to attend the general assembly meeting on their behalf.

- Under Article 107 of the Companies Law, shareholders must exercise their right to vote in the general assembly in line with the articles of association. In principle, each share gives the right to one vote. JSCs may not issue shares conferring multiple votes. However, the company may issue preferred shares with no voting rights, which cannot exceed 5% of the company's share capital. Furthermore, the articles of association may provide for a cap for the voting rights of shareholders holding more than one share.
- Under Article 101 of the Companies Law, the articles of association may provide for restrictions relating to the disposal of shares by shareholders, provided the restrictions do not lead to a complete prohibition to dispose of the shares.
- Under Article 108 of the Companies Law, shareholders have the following rights:

    - receive a portion of the profits which are decided to be distributed and a portion of the company's assets on liquidation (in proportion to their shareholding);
    - dispose of their shares;
    - request access to the company's books;
    - monitor and supervise the acts of the board of directors and file a liability claim against its members; and
    - apply to the courts for the annulment of the shareholders' assemblies' resolutions, subject to the conditions and restrictions stated in the articles of association.

LLC:

- Under Article 171 of the Companies Law, each share gives equal rights to profits and asset distribution on liquidation, unless the provisions of the articles of association provide otherwise. Each shareholder has the right to vote and each share gives the right to one vote. Each shareholder may give proxy, in writing, to another shareholder who is not a director, to attend the shareholders' meeting and vote on his behalf, unless the articles of association provide otherwise. Each shareholder may also request access to the company's books.
- Under Article 165 of the Companies Law, a shareholder has the right to sell their shares to another shareholder or third parties in line with the terms of the articles of association. If the shareholder intends to sell to non-shareholders, they must give notice to the other shareholders, through the directors, regarding the terms and conditions of sale. Each non-selling shareholder has a preemption right, whereby they have the option to acquire the relevant shares of the selling shareholder for their fair market value during the 30-day period following notification.

17. Are there any types of international company would not be allowed to establish a branch or subsidiary in this country, either as a result of their country of origin, countries of operation or type of business?

Under Article 1 of the Israel Boycott Law (Saudi Arabia Royal Decree No. (M28/1962) dated 23/11/1962), natural or legal persons are prohibited, whether personally or through agents, to conclude agreements with bodies or persons residing in Israel or affiliated thereto by virtue of nationality or working for the account or in the interest of Israel wherever they may reside, if the subject of agreement is business transactions, financial operations or any other kind of dealing. National and foreign companies and establishments having business interests, branches or general agencies in Israel shall be treated as the bodies and persons banned to deal with a fortiori, and such international companies would not be allowed to establish a branch or subsidiary in KSA.

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