

Establishing a presence - KSA



The Kingdom of Saudi Arabia (**KSA**) is the world's top oil exporter and one of the top 20 destinations in the world for foreign direct investment. This guide provides a high level overview of some of the key legal issues relating to the establishment of a business presence in the KSA by a foreign-owned entity. The regulatory system in the KSA is dynamic and subject to frequent changes in application and interpretation. It is essential to obtain specialist legal advice at the outset in order to select the most appropriate structure and to obtain confirmation as to how the law applies to the particular investment or business activity.

Legal framework

Saudi Arabian law is based on Islamic law (Shariah). In Islamic law there are four main schools of jurisprudence, namely, Hanbali, Hanafi, Shafai, and Maliki. The Saudi Arabian courts generally apply the Hanbali school as set out in a number of specified scholarly treaties by Authoritative Jurists, Schools of Law, State Regulations, Royal Decrees and (where these are relevant) custom and practice. In the event of a conflict between Islamic law and government rules and regulations, Islamic law will prevail.

Structures for doing business in the KSA

In order to conduct business legally in the KSA a foreign-owned entity must have a legal presence in the country. Once established it can then conduct activities in accordance with its licence and permits which are obtained from the Saudi Arabian General Investment Authority (**SAGIA**), the Saudi Ministry of Commerce and Industry and other government departments.

The Foreign Investment Law issued by Royal Decree in 2000 regulates the procedures and process for



investing in KSA. Foreign ownership (of 100%) is permitted unless the proposed activity appears on a negative list (which restricts any foreign ownership). Certain activities which do not appear on the negative list may still fall into a sector where foreign ownership is restricted in amounts generally ranging from 25% to 75%. It is important that a thorough examination of the proposed activity is undertaken to ascertain if any of these restrictions apply and/or whether any additional consents are required from relevant authorities in KSA. In general foreign investment is permitted in most manufacturing, technical services and trading activities.

Set out below are the main establishment options that are typically available to a foreign-owned entity:

Limited liability company (LLC)

- For various practical reasons, the LLC is generally considered the most appropriate corporate form for foreign-owned entities that wish to establish a subsidiary company in KSA. A LLC must not have less than 2 nor more than 50 shareholders and the liability of each shareholder in the LLC is generally limited to their capital contributions. The shares of a LLC should be of equal value and must each be fully paid up in cash or kind. A LLC cannot offer their shares to the public and it is not permitted to undertake business activities in commercial banking or insurance.
- If a LLC incurs losses amounting to 50% or more of its share capital, the shareholders must resolve either to continue the LLC on the basis that they will be responsible for its debts or liquidate the LLC otherwise the protection afforded by limited liability status will be lost. For this and other reasons (see taxation section below) the foreign-owned entity should consider carefully the corporate entities it uses as shareholders in the LLC.
- There are some limits on the ability of a LLC to distribute profits because at least 10% of its annual net profits must be transferred into a reserve fund until the amount in such reserve fund is equal to and not less than 50% of the LLC's share capital.

Branch office

- A foreign-owned entity may establish a branch office in the KSA (free from any local participation) by obtaining a foreign investment licence from SAGIA and the approval of the Saudi Ministry of Commerce and Industry. It is often the case that activities that are available to a branch office will also be available to a limited liability company and the foreign-owned entity will have the option to select either structure. A key characteristic of a branch office is that it is not a separate legal entity from the entity it represents.

Temporary commercial registration

- A foreign-owned entity undertaking public sector contracts may obtain a “temporary commercial registration” licence from the Saudi Ministry of Commerce and Industry. A temporary commercial registration office may supervise and coordinate the entity's administrative activities within KSA (it is however prohibited from engaging in commercial activities in KSA). A temporary commercial registration office is similar in form to a branch office.

Scientific and technical office

- A foreign-owned entity that has products in KSA and a registered Saudi commercial agent or distributor can establish a scientific and technical office in KSA. The purpose of the scientific and technical office has to be to support the foreign-owned entity's registered agent(s) or distributor(s) and to assist the end users of the product (it is however prohibited from engaging in commercial activities in KSA). A scientific and technical office is similar in form to a branch office.

Joint stock company (JSC)

- A JSC is a corporate vehicle that is required to be used for specific activities (such as insurance or banking) or where a public share offering/IPO is planned in KSA. The capital requirements of a JSC are dependent upon its proposed activities. Shareholders are liable only to the extent of the paid up value of their shares and the par value of each share cannot be less than SAR 10 (upon incorporation, its issued paid-up capital must be no less than one-half of the authorised capital). A JSC involved in businesses such as mineral exploration, administration of public utilities,



banking and finance will require authorisation by Royal Decree prior to incorporation. The management of a JSC is undertaken by a board of directors consisting of a minimum of 3 members who are appointed by the shareholders. Each director is required to own shares with a value of no less than SAR 10,000.

Taxation

It is mandatory for every company or branch office in the KSA to register with the Department of Zakat and Income Tax. A foreign-owned entity which is either a shareholder in a resident LLC or which does business in KSA through a permanent establishment is subject to 20% corporate taxation on income and realised capital gains. Any shares held by a KSA and/or GCC national in a corporate structure will also be subject to a levy (Zakat) of 2.5%. Withholding tax is payable on a range of payments including dividends, interest, lease payments and consultancy fees. There are a small number of double taxation treaties that a foreign-owned entity may wish to take into account when selecting the most appropriate establishment option.

Summary

Specialist advice should be taken by any foreign-owned entity wishing to enter the KSA market. As part of the establishment process a large number of documents will need to be submitted to the relevant authorities in KSA. In general and if managed properly, the process should take between 2 and 4 months to complete. As a final point, there will in all likelihood be several other laws and requirements that should be considered when carrying on business in KSA. These may include employment and immigration laws, competition laws, general corporate governance and/or intellectual property laws and regulations.

Further information

If you would like further information on any issue raised in this fact sheet please contact:

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