

# Guide on Doing Business in the Kingdom of Saudi Arabia - Part I

2020-2021



# Guide on Doing Business in the Kingdom of Saudi Arabia Part - I

## I. What is the legal system in the Kingdom of Saudi Arabia (KSA)?

The legal system in the Kingdom is primarily based on:

- i. Civil law, heavily relying on Sharia law and Islamic teachings on matters that are not codified under the statute. The Constitution of the KSA is the Quran (Holy Book) and the traditions of Prophet Mohammed (PBWH) (**Article 1** of the *Basic Law of Governance, issued by Royal Order Number A/90 dated 27/8/1412H*) (the "Basic Law").
- ii. The traditions of Prophet Muhammad (PBUH) Sunnah.
- iii. Ijma, the scholarly consensus developed after the Prophet's death.
- iv. Qiyas (analogy).

Where the sources of law fail to provide an answer, the judges shall apply their personal interpretation and render their judgments and legal reasoning without regard to previous cases (Ijtihad). The judicial precedents system is not acknowledged in the Kingdom. The Nizam, (Royal decrees) supplement the Sharia in modern areas such as intellectual property, labor, commercial and corporate law. Other forms of regulations include Royal Orders, Council of Ministers Resolutions, Ministerial Resolutions and Ministerial Circulars, and are similarly subordinate to Sharia. Western commercial laws or institutions are adapted and interpreted from the standpoint of shariah law. As per **Article 45** of the *Basic Law*, the Board of Senior Ulema and the Department of Religious Research provide a legal opinion on matters that need interpretation, termed as Fatwa, and is deemed as the highest in ranking for providing legal opinions.

Furthermore, under **Article 81** of the *Basic Law*, treaties and agreements with states and international organizations and agencies to which the KSA is committed, form part of local law and regulations.

In case of dispute in commercial law, particularly sale-purchase transactions, the court applies Islamic Sharia principals, as specified by the Quran and the

Sunnah, and the laws that are not in conflict with the Quran and Sunnah which the authorities may promulgate (**Article 48** of the *Basic Law*).

There are general limitations under the Sharia law; however, there is considerable freedom to agree on contract terms for the parties. The prohibited contracts which are not enforceable are the contracts which involve speculation and the payment of interest. On breach of a contract, the KSA courts will only award compensation for proven direct damage. Any claim for loss of profit or opportunity will not be allowed as these constitute speculation, which is not permitted.



## II. How are the transactions by organizations incorporated in the KSA with foreign companies governed?

- i. For a trade contract assumed to be concluded with any private entity, and as per the privacy of contract doctrine, the terms and conditions agreed by the contracting parties mutually shall be applicable to the extent that they are not in conflict with the principals of Sharia. If no relevant provision is stipulated in the contract to decide the matter in hand, the judge will resort to state regulations, then to the writings of Hanbali scholars.
- ii. For an administrative contract entered into with a governmental agency, a ministry or a public corporation, the contract will be governed by its terms and conditions which must not deviate from the provisions and spirit of the Government Tenders and Procurement Law enacted by *Royal Decree Number M/58 dated 4.9.1427H*.

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***“Never depend on a single income, make an investment to create a second source.”***

***– Warren Buffet***

When there is no relevant provision provided in the contract or in the law to decide the issue in hand, the judge will invoke the contractual provisions contained in the books of Hanbali scholars.

### **III. What are the recent Legislative updates adopted in the KSA?**

#### ***i. The Ministry of Investment of Saudi Arabia (MISA)***

The Saudi Arabian Investment Authority (SAGIA) became the MISA, an independent ministry in February 2020. This was done to provide the authority with powers enjoyed by Ministries and further improve and increase its effectiveness to attract qualitative investments that would ultimately add value to the KSA economy.

#### ***ii. Revisions to the Companies' Law***

In 2018, significant amendments were made in the companies' law regime, particularly concerning the Joint-Stock Companies (JSC) and Limited Liability Companies (LLC). The changes included new requirements on how to record the articles of association and matters concerning the authorization of director decision-making.

#### ***iii. KSA Bankruptcy Law***

In 2018, the KSA Bankruptcy Law was issued to help a bankrupt debtor reorganize his financial position and resume activities. The law establishes a framework of protection against bankruptcy for individuals, tradesmen, and foreign and local companies.

#### ***iv. New Professional Companies Law***

In 2020, a revised version of the Professional Companies Law introduces some key changes. The non-KSA companies will now be able to form a professional company within the Kingdom.

The New Professional Companies Law addresses many of the issues that were challenging in the past and provides several novel features, including major changes in terms of shareholdings, activities and succession. Different professional activities can be merged into one company to foster innovation and enhance competition. This innovation aims to have a great impact on the market in terms of the variety and sophistication of services and, on the competition.

#### ***v. Revisions to the Negative List***

The “Negative List” lists the group of sectors where foreign entities are barred from investing. The sectors which have been removed from the Negative List are Road transport; Real estate brokerage; Audio-visual services; and Recruitment and related services.

#### ***vi. New Saudi Tender and Procurement Law***

This law ensures that the procurement decisions by government agencies are not influenced by personal interest, and the government can now choose between the RFP model and the invitation to bid.

#### ***vii. New Cloud Regulations***

The Cloud Computing Regulatory Framework (CCRF) is wide-reaching in scope as it applies to the cloud computing services being provided to residents of KSA, and to any security breaches of data that are stored or processed within KSA.

#### ***viii. Value Added Tax (VAT)***

The Government of the KSA announced that the VAT rate would increase to 15 percent from the current 5 percent, effective 1 July 2020.

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*“An investor without investment objectives is like a traveler without a destination.”*

*–Anonymous*

ix. **The adoption of the International Standard Industrial Classification (ISIC4)**

MISA has adopted the ISIC4 for the issuance of new Foreign Investment Licenses as the ISIC4 provides a list of detailed activities to be chosen depending on the proposed investment sector.

x. **FinTech Experimental Permit Instructions**

The Capital Market Authority (CMA) can issue a limited number of FinTech permits (or “ExPermits”), which would enable the holder to use the CMA FinTech Lab for testing a proposed product or service.

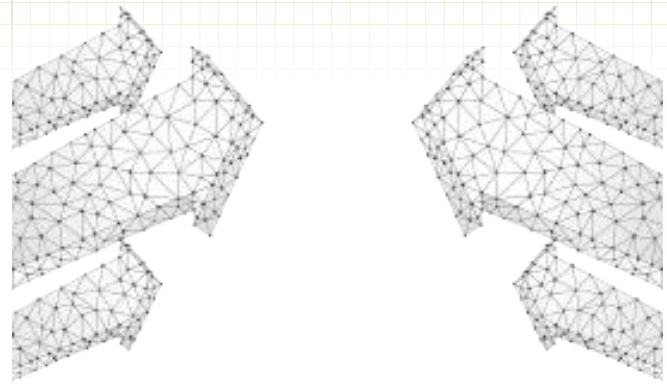
**IV. What restrictions does the KSA impose on doing business with certain countries or jurisdictions?**

Currently, the ban on doing business with Israel under the Israel Boycott Law issued under *Royal Decree Number M/28 dated 25/6/1382H* is in place. Since 2017, when there was a ban imposed on doing business with Qatar and is also still in place.

**V. Does the KSA grant incentive to the investors?**

The KSA offers multiple incentives to investors who establish their business in the KSA in the form of advancing loans or granting affordable rent and financial support on recruiting manpower. The loan availed from the Saudi Industrial Development Fund by the manufacturing and industrial entities, are primarily for setting-up factories in the KSA, recruiting and training Saudis, and shipping their products regionally. The loans provide low rates with long-term payment plans.

The Human Resource Development Fund provide support to businesses recruiting Saudis by paying up to 50 percent of the monthly wages of the employee to foster the recruitment of Saudi talents.



The Industrial Cities Authority established multiple locations around the KSA and prepared the facilitates for factories to be built and operate. Such locations offer rent as low as SAR1 per square meter. Furthermore, there are no exchange control or currency regulations that interfere with doing business in the KSA.

**Business Vehicles**

**VI. What are the most popular forms of business vehicle used in the KSA, their main registration and reporting requirements? What are their management structure and key liability issues?**

- i. Limited liability company (LLC);
- ii. Joint-stock company (JSC), which can be a private or a publicly listed JSC;
- iii. Branch of a foreign LLC or JSC;
- iv. Branch having a temporary commercial registration to perform a government-mandated project (TCR); and
- v. Technical Scientific Services Office (TSO).

**Registration**

**Trade name:** The new local company's trade name is registered with the Ministry of Commerce and Investment (MoCI).

**Foreign investment license:** Applications for foreign investment licenses are to be submitted to the MISA. After payment of fee as per the MISA regulations, it takes about 15 to 20 days to obtain the license.

**Limited Liability Company**

To register an LLC, the company must submit articles of association (AoA) and commercial registration (CR). For CR, an address, telephone and fax numbers are required. The company must then:

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***"If people like you, they'll listen to you,  
but if they trust you, they'll do business with you."***

***-Zig Ziglar, author, salesman,  
and motivational speaker***

- i.* Submit the draft AoA to the MISA for approval, have a notary public notarize the AoA following approval and publish the AoA.
- ii.* Submit a letter of support from MISA addressed to MoCI, to appoint non-Saudi managers.
- iii.* Subscribe to the Chamber of Commerce as well as add the company managers' signatures to the Chamber of Commerce registry.

The cost of registering an LLC is SAR 3,900 payable to the MoCI and the Chamber of Commerce and Industry. The process of registration takes about 15 to 20 days.

The LLCs must be managed by a single general manager, two general managers, or a board of a minimum of three managers, where certain matters shall be reserved solely for the shareholders. The shareholders may decide the appointment of the company's managers.

In an LLC, the company matters are within the shareholders' control, which can be delegated subsequently to a general manager or the board of managers. Shareholder decisions can be passed by a simple majority vote (51 percent). However, amending the AoA requires a supermajority vote (75 percent); and changing the nationality of the company or raising the capital require a unanimous vote (100 percent).

### **Joint-Stock Company**

To register a JSC, the company must:

- i.* Have a drafted AoA;
- ii.* Complete the CR; and
- iii.* Submit the request to MoCI to approve the draft AoA and by-laws and have a notary public notarize the AoA following approval.

The MoCI issues the first resolution approving the formation of the company. The MoCI issues the second resolution approving the proceeding with completion of formation and the by-laws of the company. The company must:

- i.* Publish the AoA, by-laws as well as the Ministerial Resolution; and
- ii.* Subscribe to the Chamber of Commerce and add the director's signatures to the chamber registry. The registration cost is about SAR 60,000 payable to the MoCI, and the Chamber of Commerce and Industry. The registration process takes about 60 days.

In a JSC fully managed by the board of directors, the members of the board are specifically named by the founders during the formation assembly meeting. Following the expiry of the board's term, it will be by nomination and voting of the ordinary general assembly.

In a JSC, all day-to-day company matters are within the control of the board of directors, operative under the control and selection of the ordinary general assembly.

Amendment of the company's bye-laws is reserved solely to the extraordinary general assembly while the other matters affecting the stockholders directly are reserved to the ordinary general assembly, such as increasing financial liabilities of the stockholders personally, changing the nationality of the company or relocating the company's headquarters.

For registering a TSSO, the company must complete CR and submit a request to MoCI to issue the CR. The branch must subscribe to the Chamber of Commerce and must add the branch's or office managers' signatures to the chamber registry. The costs are SAR 3,200 per year payable to the MoCI and the Chamber of Commerce and Industry, and it takes about seven days to complete the registration.

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***"Fortunes are built during the down market  
and collected in the upmarket."***

***-Jason Calacanis,  
Founder of LAUNCH Ticker***

Municipality license: The company is obligated to select the office location as well as provide the location map, pictures of the office, office banner containing the company name in Arabic and CR number along with copies of the following:

- i.* Building permit for the office building.
- ii.* Civil defense permit for the office building.
- iii.* Lease agreement.
- iv.* Ownership deed of the office building.

The cost of the license shall depend on the size of the office and the size of the banner. It costs approximately SAR 500 to SAR 1,500 annually and takes about ten days for the issuance.

The appointment of a full-time Saudi Government Relations Officer (GRO) must be made before sending the details to the Ministry of Labor (MoL). The Saudi GRO must visit the MoL in person for activating the file. MoL requires the following:

- i.* Details and copy of the municipality license.
- ii.* Details of the authorized Saudi representative.

The GRO can have a full-time role with the company and must be registered as the Saudi GRO. It takes about ten days for this completion.

Social insurance and Wassel (Saudi post) address: Registering with the General Organization for Social Insurance and for a Saudi post address is mostly done online. The company social insurance is activated by adding at least one Saudi employee.

The companies must collect their mail from the nearest post office, or the companies may choose to pay an annual fee to enjoy the services to deliver to the company's location. An active MoL file number is required. It costs SAR 1,000 per year. Both Social insurance and Wassel address typically take about two days each.



**Zakat and income tax:** Registration with the General Authority of Zakat and Income Tax (GAZT) may be done online. The certificate is issued electronically and typically takes about 10-20 days.

**Bank account.** An authorized signatory, either non-Saudi under the sponsorship of the new entity, or a Saudi holding the valid Power of Attorney (PoA) to execute bank transactions, is required to activate a bank account. This can be done within 20 days.

#### **The Reporting Requirements include:**

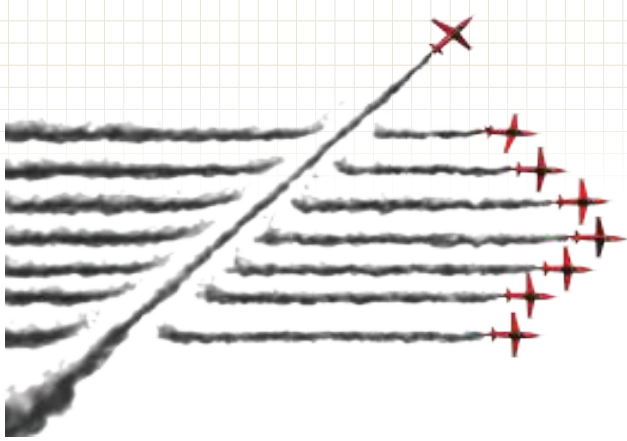
- i.* Annual filing of audited financial statements with the GAZT within three months of closing the fiscal year.
- ii.* Monthly reporting and settling of VAT with the GAZT.
- iii.* Monthly filing of payroll confirmation with the MoL in compliance with the Wage Protection System.

#### **Share capital**

The Foreign Investment Law (the "FI Law") states the minimum capital requirements to be fully paid up by the foreign investor at incorporation and to be deposited in a local bank under the name of the investor's new entity or branch in the KSA.

- I.** Trading license (with a Saudi partner) requires that the shares held by the foreign shareholder amount to a minimum of SAR 20 million and not exceeding 75 percent of the total paid-up share capital. The Saudi participation must form a minimum of 25 percent, a minimum of about SAR 7 million, making the total capital about SAR 27 million fully deposited into the company's local bank account on incorporation.

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*“What do you need to start a business?  
Three simple things: know your product better than anyone,  
know your customer, and have a burning desire to succeed.”*

*- Dave Thomas,  
Founder of Wendy's*

- II. Trading license (100 percent foreign-owned) requires that the foreign capital shareholding must be a minimum of SAR 30 million.
- III. Licenses for TSOs and branches holding temporary commercial registration to perform a government-mandated project (TCRs) are exempt from registering and fully paying up the capital.
- IV. The licenses for Services; Specialized services; construction and contracting; and Industrial, require registering a fully paid-up capital but have no minimum capital requirement (can be 100 percent foreign-owned).

#### **SAGIA annual membership and license fee:**

- I. For trading with a Saudi partner; for trading 100 percent foreign-owned; or for TSO, the annual membership fee is SAR 10,000 for the first year and then SAR 60,000 for the following year. The annual license fee is SAR 2,000.
- II. For Industrial and Agricultural, the annual membership fee is SAR 10,000 for the first year and then SAR 90,000 with the annual license fee being SAR 2,000.
- III. For TCR, the annual membership fee is SAR 10,000, and the annual license fee is SAR 2,000.
- IV. For the Services; or Specialized services, the annual membership fee is SAR 10,000 for the first year and then depending on the service provided, SAR 60,000 or SAR 90,000. The annual license fee is SAR 2,000.
- V. For Contracting and Construction, the annual membership fee is SAR 500,000 for the first three years and then another SAR 500,000 for the second three years, and then it goes down. The annual license fee remains the same, SAR 2,000.

The KSA law permits investors to inject their shares into the share capital by making in-kind contributions, such as real estate or equipment, provided that the contributions are duly evaluated by a licensed professional company to assess the accurate value of the contributions at the time of deposit.

#### **Rights attaching to shares**

The automatic rights include:

- I. Attending shareholders' meetings and voting on resolutions.
- II. Right of First refusal to purchase an exiting shareholder's shares.
- III. Appointing or removing the board members.
- IV. Receiving dividends, financial statements and directors' report.
- V. Have access to the records of the company.

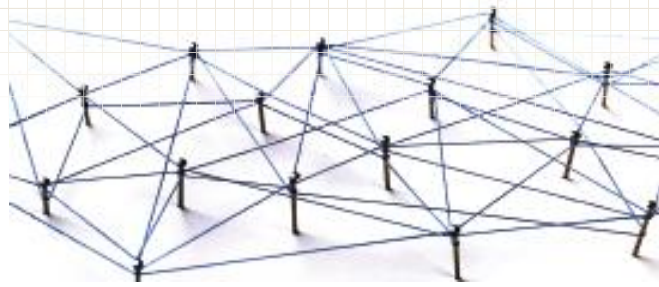
#### **Liability**

Managers and directors are liable to the company, the shareholders and to third-parties where their acts involve:

- I. Breach of fiduciary duties.
- II. Abuse of power.
- III. Acting in contrast to the AoA.
- IV. Submitting incorrect data or information to local authorities and third-parties.
- V. Using the company for fraudulent purposes or illegal acts.
- VI. The directors not separating their personal interests and the company's interests.
- VII. Gross negligence or/and Wilful misconduct.
- VIII. The directors were encumbering the company with obligations, despite knowing that the company cannot fulfil such obligations.

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In an LLC and JSC, the parent company's liability is limited by the shares or stocks which the parent company owns in its subsidiary.

In a branch, the parent company is liable for all liabilities of the Saudi-based branch because it is considered as part of the parent company and not a separate legal entity. This also applies to branches holding temporary commercial registration to perform a government-mandated project and TSOs.

### Employment and the Labor Law

#### VII. What regulates the employment and the termination of the employment?

The *Labor Law, issued under Royal Decree Number M/51 dated 23/8/1426H*, and amended by *Royal Decree Number M/24 dated 12/5/1434H* and *Royal Decree Number M/46 dated 5/6/1436H*, regulates employment relationships.

The *Labor Law* covers redundancies and mass layoffs by allowing the employers to terminate employees as part of a restructuring exercise.

Under the *KSA Labor Law*, the employment contract shall be terminated:

- i. When both parties agree to terminate it, provided that the employee's consent is in writing;
- ii. When the term specified in the contract has expired, unless the contract has been explicitly renewed as per the Labor Law in which case it shall remain in force until the expiry of its term;
- iii. At the discretion of either party for the indefinite term contracts;
- iv. When the employee attains the age of retirement unless the two parties have agreed on continuing the employment. For a fixed-term employment contract which extends beyond the retirement age, it shall terminate at the end of its term; and
- v. Force majeure

*"A big business starts small"*

*- Richard Branson*

#### VIII. How must the employment contract be drafted?

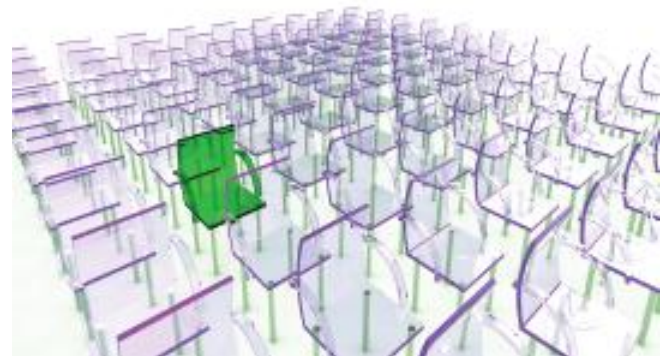
The employment contract is legally required to be written and signed and must include the main terms, for instance, the job title, contract duration and renewal, a probation period, the working hours and days as required by the Labor Law, the non-disclosure and non-compete clauses along with the wages and leave allowances.

Where certain terms are not specified in the written employment contract but are protected by the Labor Law, will be considered as part of the employment contract. Where the parties have agreed to terms that are in violation of the Labor Law, such terms will be considered invalid and unenforceable.

#### XI. What are the requirements for foreign employees?

The foreign employees being Non-Saudi employees must obtain a work permit from the MoL and a residency permit from the General Directorate of Passport. Employees must have a valid employment relationship in the KSA and must be under the sponsorship of their employer. However, a Non-Saudi having a Saudi mother will not require a work permit and will only require a residency permit, under the sponsorship of the mother.

Citizens of the Gulf Cooperation Council countries also do not require a work permit and only require a residency permit.





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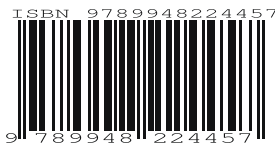
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