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The Middle East Periodic Bulletin

Winter 2017

New Investment Funds and REIT Regimes in Saudi Arabia

Sukuk in Turkey; The Story So Far and Future Prospects

Benefits of Joint Ventures in the Dubai International Financial Centre

The Libyan Frontier of Islamic Banking and Finance

Saudi Arabia – PPP in Education Sector

Amendments to Foreign Fund Private Placement Exemptions in the UAE

Foreword

Welcome to the Winter 2017 issue of *measure*, King & Spalding's Middle East and Islamic Finance practice group periodic newsletter. Against the backdrop of the significant political and economic events and challenges of 2016, we look forward to 2017 and review recent developments in the legal landscape of the region. In this issue:

- James Stull and Nabil Issa examine the new investment funds and REIT regimes which came into effect in Saudi Arabia in November 2016;
- Rizwan Kanji and Hamed Afzal discuss the evolution of the *sukuk* market in Turkey, particularly in the context of recent enabling tax legislation, and prospects for the market going forward;
- Osama Audi and Nabil Issa examine some of the key benefits to establishing a joint venture in the Dubai International Financial Centre as compared to other regional jurisdictions;
- Andrew Metcalf and James Weir look at the prospects and challenges for Islamic finance in Libya against the backdrop of the Islamic Banking law which came into effect in early 2015;
- Leroy Levy discusses the potential for public private partnerships to be used as a tool to fund Saudi Arabia's education sector; and
- James Stull and Dora Chan discuss recent amendments to the foreign fund private placement exemptions in the United Arab Emirates.

We are also pleased to announce the further growth of our team in the region, with Zeeshan Dhar joining us as Counsel in the International Arbitration group based in our Dubai office. We hope you find this issue useful and informative and we look forward to helping you keep abreast of further developments. In the meantime, as ever, we welcome your comments and feedback.

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This Issue

04 Investment Funds

Amendments to Foreign Fund Private Placement Exemptions in the UAE

07 Debt Capital Markets

Sukuk in Turkey; the story so far and future prospects

10 Corporate

A few reasons why regional joint venture and shareholder arrangements should be structured through the DIFC

15 Islamic Finance

The Libyan Frontier of Islamic Banking and Finance

18 Public Private Partnerships

Saudi Arabia - PPP in education sector

21 Investment Funds

New Investment Funds and REIT Regimes in Saudi Arabia

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Amendments to Foreign Fund Private Placement Exemptions in the UAE

In August 2016, the Emirates Securities and Commodities Authority (**SCA**), the federal securities regulator of the United Arab Emirates (**UAE**), adopted new investment funds regulations (the **2016 Fund Regulations**), which repealed the prior funds regulations which were adopted in 2012 and amended in 2013 (the **2013 Regulations**), clarified the formation process for the establishment of locally domiciled funds and introduced significant changes to the marketing of foreign domiciled investment funds in the UAE. The 2016 Fund Regulations impose substantial hurdles and costs for managers seeking to promote foreign funds in the UAE and have generally been subject to negative feedback.

Managers wishing to market foreign funds onshore in the UAE now have far fewer options: they can register the fund with SCA and enter into a distribution arrangement with a locally licensed placement agent, engage in reverse solicitation (where the investor inside the UAE initiates the transaction) or rely on a private placement exemption when offering to sovereign entities (which is the lone exemption remaining from the 2013 Regulations). Funds established in a free zone inside the UAE, including funds established in the Dubai International Financial Centre (**DIFC**) or the Abu Dhabi Global Market (**ADGM**), are considered by SCA to be foreign funds.

However, it is widely expected that SCA will issue further clarification regarding additional exemptions, potentially reintroducing the private placement exemptions set out in the 2013 Regulations and introducing additional exemptions for certain other classes of investors, such as multilateral institutions. SCA has not confirmed the timing for the issuance of the clarification or the specific terms and requirements of any additional exemptions.

Further, it is important to note the 2016 Fund Regulations do not apply to foreign funds wishing to offer in the DIFC or ADGM. Marketing of foreign fund interests and other securities in these free zones is subject to separate regulations and must be registered with the financial services regulator in the respective free zone without exception.

The 2016 Fund Regulations impose substantial hurdles and costs for managers seeking to promote foreign funds in the UAE and have generally been subject to negative feedback.

Background: 2013 Funds Regulations and Exemptions

The 2013 Regulations introduced the first set of codified fund private placement exemptions in the UAE. Under the 2013 Regulations, foreign funds that were privately placed with the following categories of investors in the UAE were exempt from registration with SCA:

(a) investment portfolios owned by federal or local governmental agencies;
(b) institutions or entities whose purpose is to invest in securities, provided that such institutions are acquiring the fund interests for their own account; and
(c) investment managers with discretionary management authority.

The 2013 Regulations were generally viewed positively as they permitted foreign managers to approach certain types of institutional investors without engaging a local distributor or engaging in a lengthy registration process.

SCA also had adopted certain informal "tolerated" practices including offerings without registration if the foreign manager (i) was marketing to existing clients of the manager and (ii) was relying on engaging in reverse solicitation where the investor initiated the query. It is unclear whether the first "tolerated" exemption will continue to be permitted. The second "tolerated" exemption has been codified in the 2016 Fund Regulations as described below.

Requirement for Distribution by an SCA-licensed Placement Agent

The 2016 Fund Regulations provide that foreign funds may be promoted in the UAE only if:

(a) the foreign fund is registered with SCA; and
(b) the foreign fund is distributed through a SCA-licensed placement agent,

unless the fund can qualify for a limited private placement exemption or rely on reverse solicitation.

The 2016 Fund Regulations provide that SCA shall issue a decision within 30 business days of the submission of the registration application. A foreign fund's registration expires on 31 December each year and a renewal application must be submitted at least one month before expiry of the registration. Pursuant to SCA Board Decision No. 10 of 2016, the fee payable on the initial registration application is AED 35,000 (approximately US$9,500). Thereafter, a fee of AED 7,500 (approximately US$2,050) is payable on each annual renewal application.

Reverse Solicitation

As mentioned above, one positive development in the 2016 Fund Regulations is the express ability of foreign managers to offer funds in the UAE under reverse solicitation where an investor initiates the interaction. Reverse promotion is defined as the following scenario: *"an initiative made by an investor in the [UAE] submitting an application to offer or buy specific units of foreign mutual funds out of the [UAE], which is not based on promotion by the foreign fund, its promoters or distributors of its units, provided this is substantiated by the concerned entity".*

It is expected that this will become the primary manner through which managers offer foreign funds unless SCA reintroduces additional private placement exemptions. It is critical that a foreign fund seeking to rely on the reverse promotion exemption must keep proper records in order to prove the offering of the concerned securities was initiated by the UAE investor.

Government Agency and Other Exemptions

The 2016 Fund Regulations exempt the promotion of foreign funds to federal or local governmental agencies and any companies wholly owned by such an agency from the requirement to use an SCA-licensed placement agent. Therefore, foreign managers can continue to market foreign funds to and visit sovereign entities based in the UAE and other government-related investors.

The following are also exempt from the operation of the 2016 Fund Regulations:

(a) funds established by federal or local governmental agencies or companies wholly owned by such an entity;
(b) the accumulation of money for the purposes of investment in a joint bank account;
(c) the conclusion of group insurance agreements;
(d) social security programs;
(e) employee incentive programs; and
(f) investment plans associated with insurance contracts unless such investments or collected money are directed from such plans to funds.

Conclusion

While the 2016 Regulations do provide clarity regarding the offering process for funds in the UAE, the loss of foreign fund private placement exemptions greatly increases the challenge for foreign funds that wish to fundraise in the UAE. The introduction of the reverse solicitation exemption is a positive development; however, unless SCA issues the expected clarification and reintroduces the broader exemptions, foreign managers and issuers may reconsider the marketing of their products onshore in the UAE.

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Sukuk in Turkey; the story so far and future prospects

The *sukuk* market in Turkey has evolved substantially over the last few years. The evolution has been comparatively quick and helpful. We will review some of the key milestones in the development of the market and, going forward, the key challenges and prospects for the market to further grow and evolve.

The story so far

Sukuk was introduced to the Turkish market in 2010, when the Turkish participation bank, Kuveyt Türk Katılım Bankası A.Ş. (**Kuveyt Türk**), undertook a U.S.$100 million debut issuance, which it listed on the London Stock Exchange. Given the lack of legislative infrastructure to facilitate *sukuk* issuances at the time, the transaction relied on numerous tax and regulatory exemptions by Turkish authorities.

This successful issuance led to the Capital Markets Board of Turkey (**CMB**) adopting a proactive approach to develop the legal infrastructure in Turkey to foster the growth of the *sukuk* market. This resulted in the CMB issuing a communiqué in April 2011 (the **CMB Communiqué**) which provided the regulatory framework for the establishment of asset leasing companies (**ALCs**). The CMB Communiqué provided that such companies would be able to issue and sell "rental certificates" (i.e., *sukuk*) utilising lease (i.e. *ijara*) based structures. The omnibus bill 2011, Law number 6111 followed in February 2011, and provided for the various tax and levy exemptions applicable to ALCs and *sukuk* cashflows. These changes prompted Kuveyt Türk, through KT *Sukuk* Varlık Kıralama A.Ş., an ALC incorporated in Turkey pursuant to the CMB Communiqué, to issue its second benchmark *sukuk*.

These issuances prompted further *sukuk* issuances by other leading participation banks in subsequent years and, in September 2012, Turkey issued its first sovereign benchmark *sukuk*.

Further legislative reform followed, most notably through the Lease Certificates Communiqué (Serial No. III/61.1) in June 2013 (the **Revised Communiqué**). The Revised Communiqué allowed, among other things, ALCs to undertake multiple issuances and introduced a broader range of approved structures for *sukuk* issuances. The Revised Communiqué prompted a spate of further *sukuk* issuances from the various participation banks shortly thereafter and in following years.

To date, up until year end 2015, international *sukuk* issuances by private institutions out of Turkey have raised more than US$5.7 billion[1]. In addition, the sovereign issued eight *sukuk* between 2011 and September 2015, with an approximate total value of US$7.7 billion.

Corporate issuance gap

Whilst the Turkish *sukuk* space has seen considerable growth, this growth has been limited to issuances by participation banks and the sovereign. Among the key challenges in creating a deeper capital market is encouraging Turkish corporates to issue *sukuk*. As of the date of this article, despite apparent drivers such as the large infrastructure funding gap in Turkey and the growth of the Islamic institutional investor base, only a small number of Turkish corporates have issued domestic *sukuk* and none have issued *sukuk* internationally. There are a number of factors which have arguably resulted in the lack of corporates issuing *sukuk*, some of which are discussed below.

ALC regulatory framework

The regulatory framework governing the formation and ongoing operation of ALCs renders such entities unlike special purpose vehicles incorporated in offshore markets (such as the Cayman Islands) for the purpose of issuing *sukuk*.

Firstly, under the Revised Communique, only certain limited entities are permitted to incorporate an ALC, which include financial institutions, certain intermediary institutions and companies which have been assigned a long-term investment grade credit rating. Whilst corporates which are not rated may, as a technical matter, arrange for a financial institution to incorporate an ALC on their behalf or arrange to use an existing ALC set up by a financial institution for the purposes of issuing their *sukuk*, there has been a general reluctance on the part of some financial institutions to offer these services (due to, for example, uncertainties around the requirement to consolidate the ALC's assets with those of the entity establishing it and issues around insolvency remoteness).

In addition, the operation of ALCs is heavily regulated by the CMB; for example, the CMB's consent is required for a number of matters relating to an ALC (including any amendment to the ALC's articles and where there is a transfer of shares granting management or voting privileges), there are prohibitions on an ALC undertaking certain activities (including engaging in any activities other than those indicated under its articles of association) and certain corporate governance and reporting requirements apply to an ALC on an ongoing basis. In relation to corporate governance, the CMB provides that an ALC must have at least three board members, one of which must be an independent board member who satisfies the CMB's independency criteria, with certain board decisions requiring the vote of such board member.

Whilst the Turkish *sukuk* space has seen considerable growth, this growth has been limited to issuances by participation banks and the sovereign.

These requirements are much more onerous and burdensome compared to the equivalent regimes in other jurisdictions in which special purpose vehicles can be incorporated for structured finance and/or *sukuk* transactions, such as the Cayman Islands. Consequently, many originators in Turkey (including corporates) have felt that the cost and administrative burden of using an ALC under the existing framework to issue *sukuk* has been unduly high.

Tax disadvantages

To foster growth in the *sukuk* market in Turkey, the CMB has over the past several years reformed applicable tax legislation to create a "level playing field" for *ijara sukuk* structures, so that:

- Pursuant to the Corporate Tax Law (Law No 5520), any capital gains derived from the sale of an asset portfolio by an originator to an ALC, and vice versa, were made exempt from corporate tax;
- Pursuant to the VAT Law (Law No. 3065), the delivery of *sukuk* to holders was made exempt from value-added tax (VAT), as was the transfer of assets to an ALC and the subsequent leasing of those by an ALC and transfer back to the originator;
- Pursuant to the Charges Law (Law No. 492), the sale of an asset portfolio was made exempt from applicable land transfer fees, such as the title deed registry fee;
- Under the Income Tax Law (Law No. 193), any *sukuk* with a maturity of five years or more was made exempt from withholding tax in respect of income earned by the *sukuk*holders; and
- Under the Stamp Tax Law (Law No. 488), stamp duty exemptions were applied on documents covering the transfer and lease of assets between an originator and an ALC.

The above exemptions applied mainly to *ijara sukuk*, and remained silent on the applicable tax treatment of other *sukuk* structures. There was also concern about the application of the exemptions to *ijara sukuk* itself, including in relation to the scope of the stamp duty exemption.

To overcome these issues and to further encourage corporate issuances, the Turkish Tax Bill Regarding Improvement of Investment Environment (the **Omnibus Bill**) was introduced in August 2016. Pursuant to the Omnibus Bill, the Stamp Tax Law, the Value Added Tax Law and the Law on Charges were amended to grant stamp tax exemption to all *sukuk* transaction documents, VAT exemption to all types of *sukuk* transactions, and exemption from duties to be levied on all *sukuk* transactions involving the establishment of security, mortgage, pledge and other similar transactions.

Asset eligibility

As with other Islamic finance structures, in the context of *sukuk*, returns to *sukuk*holders must originate from underlying assets or ventures. The returns must also be *Shari'ah*-compliant and, accordingly, cash flows used to pay *sukuk*holders must flow from *Shari'ah*-compliant assets and/or ventures. Whilst, according to *Shari'ah* principles, only 33⅓ per cent. of the issue amount of the *sukuk* will need to be supported by tangible assets for the *sukuk* to be tradeable in the secondary market at a premium or discount, finding sufficient eligible assets still presents a significant problem for some corporates. This is particularly the case given that both from a *Shariah* perspective and as a matter of Turkish law (by virtue of the Revised Communiqué) all such assets underlying the *sukuk* are required to be free of any encumbrances (such as mortgages or other security interests).

Path forward

The tax reforms introduced under the Omnibus Bill have brought much needed clarity to originators, particularly corporates, looking to issue *sukuk* in the Turkish market. The numerous stamp tax, VAT and duty exemptions, which now apply to all types of *sukuk* structure transactions, are likely to help create a level playing field for originators compared with the conventional funding space, and it is hoped that this will encourage corporates to come to market.

Nevertheless, challenges remain, particularly given the highly regulated legal framework applicable to ALCs. For example, the cost, administrative burden and control issues around corporate governance requirements applying to the formation and ongoing operation of an ALC may continue to prove too onerous for many Turkish corporates looking to issue *sukuk*.

Despite this, given the strong demand for alternative finance in the Turkish market (particularly to fund the country's growing infrastructure funding requirements) and the willingness on the part of the Turkish regulators and authorities (including the CMB and Borsa Istanbul) to make Turkey a regional hub for Islamic finance, the outlook for the deepening of the *sukuk* market in Turkey seems positive. However, in our view this will require continued dialogue and feedback amongst all market participants, including regulators, banks, corporates, law firms others to ensure an enabling environment is created in Turkey to foster the development of the *sukuk* market.

1 IIFM Sukuk database

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Corporate

A Few Reasons Why Regional Joint Venture and Shareholder Arrangements Should Be Structured Through the DIFC

Introduction

Parties seeking to enter into joint ventures or other shareholder arrangements in the member states of the Gulf Cooperation Council are often left wondering which, if any, of the often complex shareholder arrangements agreed in the relevant joint venture or shareholder agreement (the **JV Agreement**) and entrenched in the constitutional documents are actually capable of being enforced in a timely manner if a counterparty fails to abide by the terms of such JV Agreement. In this article we set out some of the key benefits to establishing a joint venture in the Dubai International Financial Centre (**DIFC**) as compared to other regional jurisdictions as well timing and cost considerations.

Regional joint ventures often lack an enforceable mechanism to enable parties to swiftly force defaulting counterparties to restructure their arrangements or, in a worst-case scenario, to force such defaulting counterparties to sell their shares in the joint venture at a pre-agreed exit price (which can be at fair market value or, depending on the negotiated terms, significantly less than fair market value). In addition, many regional corporate structures are not ideal from the perspective of raising debt and equity financing. This article addresses each of those issues by comparing regional structures with a company limited by shares established in the DIFC.

Joint venture structures

This section is split into three parts:

(i) In the first part, we set out issues relating to the flexibility to implement capital structures for the joint venture which include, amongst others, features such as warrants, convertible debt, options, multiple share classes and employee incentive plans. We also generically compare and contrast onshore structures, which are typically proposed as joint venture vehicles and DIFC vehicles, and consider the ease with which the key provisions, which could be included in the relevant JV Agreement.

(ii) The second part sets out the typical timing and cost limitations to setting up onshore (or in most freezones in the UAE) as compared to the DIFC. The limitations set out in the first section relate predominantly to the relatively time consuming and expensive incorporation process. While these may be less of a concern to some parties, they should be highlighted to potential joint venture partners who may have experience in more developed jurisdictions where these issues do not arise but with little or no experience undertaking complex joint ventures in the region.

(iii) The third and final section sets out some typical joint venture terms to which parties should give careful consideration prior to entering into and negotiating the JV Agreement. While the list is not, by any means, meant to be exhaustive, it does set out the key issues relating to set-up/funding, control and exit.

1. Features relating to fundraising and capital structure

The first set of issues relate to the establishment of a sophisticated and flexible capital structure for a joint venture company. The availability of such arrangements can give comfort to parties providing debt and equity funding that their interests are protected and the terms of their funding arrangements are easily enforced. While these features are quite common in many jurisdictions, as far as we are aware, the DIFC (and the Abu Dhabi Global Markets) are the only jurisdictions in the region which provide flexibility to implement these provisions. It should be noted that a few other regional jurisdictions may offer a handful of these features (e.g. a party can register a pledge over the shares of an 'on-shore' UAE or Saudi Arabian limited liability company though the method to enforce such a pledge in unclear) but none offer the full suite of options available in the DIFC.

Amongst the features which, generally speaking, are available in the DIFC are the following:

(i) Viewed as GCC national: depending on the specific activity/sector in which the joint venture company is intending to operate, DIFC entities which are wholly-owned by GCC nationals are viewed as GCC national for purposes of foreign ownership restrictions in many regional jurisdictions and can have more favourable tax treatment than off-shore jurisdictions (in some cases, even if partially owned by GCC nationals).

(ii) Conversion of debt into equity: a sophisticated investor or private equity firm may seek to investment in a joint venture company, in whole or in part, by way of a convertible debt instrument. This would be undertaken when an investor provides financing to the joint venture company as a loan at an agreed rate of return, but the financing becomes convertible into equity in the joint venture company (sometimes automatically, other times upon election of the investor). The choice between debt and equity funding, and the election to convert (or not) reflects the choice between the relative priority and certainty of loan repayments when distributions are made as well as liquidation versus the enhanced upside potential of an equity interest. Thus, it is critical for investors to be able to easily convert the amount owed as debt into equity. The regulatory regime in the DIFC does provide such flexibility however this is not available in most 'onshore' jurisdictions as well as other free zones.

Regional joint ventures often lack an enforceable mechanism to enable parties to swiftly force defaulting counterparties to restructure their arrangements or, in a worst-case scenario, to force such defaulting counterparties to sell their shares in the joint venture at a pre-agreed exit price.

The availability of warrants to a debt or equity financier can typically reduce borrowing costs or can otherwise act as an inducement to sweeten transaction terms.

(iii) Multiple classes of shares: multiple classes of shares will give the joint venture company the ability to offer different classes of investors different rights depending on when they invest in the joint venture life-cycle. For example, certain investors may request distribution and/or liquidation preferences which, in the present case, are not easily entrenched in the constitutional documents of most 'onshore' jurisdictions in the region or free zones save for the DIFC (and the Abu Dhabi Global Markets), but which are quite commonly entrenched in the constitutional documents for entities established in other jurisdictions which are commonly used to structure investments such as Delaware and the Cayman Islands.

(iv) Warrants: investors will often agree a "pre-money" valuation (plus an agreed premium) for shares in the vehicle into which they are investing. Such a valuation will typically be the basis for the price at which an investor would have the right to exercise the warrant for the company to issue additional shares at such valuation. The availability of a warrant would give the investor the ability to buy such newly issued shares at the pre-agreed valuation at the time the initial investment appreciates in value above the pre-agreed exercise price.

The availability of warrants to a debt or equity financier can typically reduce borrowing costs or can otherwise act as an inducement to sweeten transaction terms. While warrants are quite common in many jurisdictions, they are not typically utilized in the region as, if the issuer or any of the shareholders in the issuer resist the exercise of the warrant, it would be quite challenging and time consuming for the warrant holder to enforce the terms and receive the additional shares. That being said, the process and ability to enforce a warrant in the DIFC would be relatively straightforward in comparison.

(v) Options: investors take a degree of risk when they make their initial investment in the joint venture. Such investors may find such risk more acceptable if, upon the occurrence of certain events or at agreed trigger points, they have an easily enforceable right to buy additional shares (i.e. a call option) in the joint venture from other investors or to sell their shares to another party (i.e. a put option), in each case, at a pre-agreed price. Unfortunately, in the present legal environment in most regional jurisdictions, the process for a party to enforce an option over shares is uncertain at worst and very time-consuming at best. Such enforcement would, however, be relatively straightforward in respect of a joint venture vehicle established in the DIFC.

(vi) Drag-along and tag-along rights: an investor in a joint venture may be relying upon the expertise or reputation of a promoter (or other investors) when making their investment decision. Accordingly, it would be understandable if such an investor would not want to continue with their investment if the promoter exits the joint venture. A tag-along right would give such an investor the right, but not the obligation, to sell their shares in the joint venture on the same terms as the promoter when the promoter exits the joint venture, thereby reducing the risk that investors induced into investing in the joint venture because of the reputation or expertise of a promoter are not forced to continue with the investment if such promoter is no longer a shareholder.

As a joint venture would have a minimum of two shareholders and perhaps many more, a drag-along right would typically be granted to a key financial shareholder or the promoter of the project to enable them to have the ability to force other shareholders to sell their shares in the joint venture to a third party on the same terms as the exiting financial shareholder or promoter. At this time, the inclusion of drag-along and tag-along rights is not easily enforced in most regional jurisdictions save for the DIFC.

(vii) Employee stock options: the joint venture may not be able to pay large salaries required to attract the most talented individuals. In order to be able to recruit the best talent, the joint venture may be willing to attract talented employees to accept a lower salary in exchange for shares in the joint venture vehicle at a future point. Historically, in the

region, employees have not been able to enforce such stock option plans. A mechanism through which employees can obtain shares in a joint venture and have such structure be easily enforceable is available in the DIFC. The availability of such stock options will make it easier for the joint venture to recruit and retain talented individuals.

(viii) Security interests: in the DIFC, a statutory register of mortgages/security interests exists which allows security interests to be registered with the regulatory authority and a clear process to quickly enforce such mortgages/security interests. While such a register may exist in certain 'onshore' jurisdictions the ability to enforce such a pledge or mortgage is untested and questionable.

2. Timing and cost considerations

One of the key issues which joint ventures generally face when setting up in the region (including in nearly all free zones) is the time-consuming and expensive incorporation process. While regional parties have grown accustomed to dealing with these issues, to the extent that a party enters into joint ventures with counterparties (including debt or equity financiers) with little to no experience in the region, these issues should be highlighted at the outset.

Amongst the key cost/time impediments are the following:

(i) Restrictions on commercial activities: companies established in free zones (including financial free zones such as the DIFC) are typically only permitted to undertake commercial activity within the relevant free zone and not 'on-shore'. Accordingly, while a DIFC Ltd, may be established as the joint venture holding company, the joint venture company may not, presently, be licensed to undertake commercial activities on-shore. This is easily resolved by setting up a further subsidiary on-shore to undertake the relevant commercial activity while the joint venture vehicle maintains its jurisdiction in the DIFC flexible legal environment. There is, of course, additional cost and time associated with setting up multiple vehicles as opposed to a single vehicle.

(ii) Documents for incorporation: a large number of documents are typically required for incorporations including legalized and attested constitutional documents of the parent entity. The process to arrange such legalized and attested documentation can be time consuming (taking a number of weeks to complete) and is costly when compared to many other jurisdictions (e.g., the Cayman Islands or Delaware). We understand that the DIFC has recently made moves to reduce the requirement for legalized and attested documents in some circumstances.

(iii) Governmental and regulatory approvals: government/regulatory approval is required to incorporate an entity. In addition, government/regulatory approvals are typically required prior to incorporation or changes to shareholders, directors or the articles of association of 'on-shore' entities. To some extent, this is less of an issue in the DIFC. That being said, if the joint venture company is incorporated in the DIFC, the joint venture would need to deal with the regulatory and governmental approvals in order to establish an 'onshore' entity capable of undertaking commercial activities 'onshore'.

(iv) Office space: companies limited by shares established in the DIFC are required to lease office space in the DIFC. We understand there may be some exceptions in relation to this requirement for the recently announced Intermediate SPVs which are discussed in greater detail below.

(v) VAT: we understand that the provision of services in the UAE will soon be subject to the recently announced VAT regime which we understand will be rolled-out in 2017. It is not clear if services provided by a joint venture company to its subsidiaries or by joint venture shareholders to the joint venture company. Accordingly, when the UAE implements the VAT regime, further analysis will need to be done with tax advisors to determine if the proposed VAT framework will provide for the possibility of "VAT groups". If not, intercompany transactions between affiliates of the same group will likely be subject to VAT. This applies equally to all structures.

(vi) Intermediate SPVs: while the use of the DIFC as the jurisdiction of incorporation of a joint venture company provides flexibility in terms of capital structure as well as a robust common-law legal environment and independent court system each of which are based on English law, the primary limitation of the DIFC is the cost associated with setting up and maintaining a presence within the free zone. The recently announced, low-cost DIFC corporate forms, such as Intermediate SPVs, have limitations attaching to their use and the corporate forms which are the most flexible (e.g., companies limited by shares) are relatively high cost as they must lease office space in the DIFC and pay annual commercial license fees of US$12,000.

The use of Intermediate SPVs could, in particular, be useful as our understanding is that they will have the full flexibility to undertake

commercial activities without a requirement to lease additional office space in the DIFC. That being said, the DIFC have stated that Intermediate SPVs will only be available to entities which have a substantive presence in the DIFC and which maintain "control" over such Intermediate SPV. Accordingly, a joint venture partner would need to be established in the DIFC to meet the requirement for a substantive presence. Finally, the DIFC have stated that the entity with a substantive presence in the DIFC will need to maintain "control" over the Intermediate SPV. It is not clear if negative control (e.g., veto rights over fundamental matters) would be considered sufficient to meet this requirement.

3. Typical joint venture terms

There are quite a few variations on joint venture structures. Key issues which should be discussed at the outset and which will impact the ability of counsel to tailor the JV Agreement to the commercial terms agreed by the joint venture partners are the following:

(i) Agreeing on a business plan and budget: the interests of the parties in the joint venture will vary depending on their respective contributions and expectations. For example, if a party does not contribute equity or assets it should either, not hold an interest in the joint venture or hold only a minor interest equivalent to the value of its 'sweat-equity' contribution. In addition, if a party is seeking only a financial return from its interest in the joint venture, such a party could have minimal voting rights but should maintain limited (if any) veto rights over fundamental matters which would materially impact its rights (e.g. capital increase or decrease, liquidation, etc.).

Such contributions and the manner in which they are made should be set out in a detailed business plan which will be appended to the joint venture agreement. Any material deviation from the business plan must be approved by an agreed threshold of the shareholders.

(ii) Control and reserved matters: the manner in which the joint venture will be controlled and the level of such control (including reserved matters which will require the approval of JC Group) should be setout in detail in the joint venture agreement with, amongst others, a detailed list of reserved matters, rights to appoint directors, quorum and voting thresholds.

(iii) Exit: the manner in which each shareholder in the joint venture sells their shares and the timing and terms of any such sale will need to be agreed in the joint venture.

Conclusion

To protect their rights, investors should consider the flexibility offered by the DIFC to establish their joint venture arrangements and should retain experienced counsel who understand both complex documentation and structures and local law implications which can significantly impinge on the ability to enforce the key terms of such documentation or to implement the optimal joint venture structure.

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The Libyan Frontier of Islamic Banking and Finance

Context

In early 2015, Libya's Islamic Banking Law came into effect. The Islamic Banking Law was adopted during a fleeting lull between the Libyan revolution and the current resurgence of conflict and instability. Despite the civil strife, Libya's commercial banks and finance sector looked promising at the time and had already attracted outside investors, including institutions from Qatar and Jordan. Even now, with the Islamic Banking Law on the books, widespread interest in *Shari'ah*-compliant financial reform and Libya's hydrocarbon potential still able to draw in risk-acceptant investors, Libya may yet be the new frontier for Islamic banking and finance.

The Law

The implementation of the Islamic Banking Law is off to a rocky start. Libyan banks are not lending, and their money is sitting with the Central Bank, which is facing its own host of problems. A main cause of the lending inertia is the impact of the Islamic Banking Law.

The Libyan banking system is governed by Law No. 1 of 2005, as amended by Law No. 46 of 2012 and Law No. 1 of 2013 on Islamic Banking. Article 1 of the Islamic Banking Law sets out the following ban on interest: "Interest on deposits and loans in all civil and commercial transactions between natural and legal entities shall be prohibited." Article 1 further stipulates that "[a]ll usurious interest, whether evident or concealed, earned from such transactions shall be invalidated on an absolute basis." The Islamic Banking Law also provides that "concealed usurious interest shall include the charging by the creditor of a commission or benefit, of whatever type and nature; if it is proven that no actual and legitimate benefit or service has been provided by the creditor in return for obtaining such commission or benefit." Finally, Article 5 of the Islamic Banking Law establishes a broad scope for the law by providing: "All concerned entities shall be obligated to regulate and reorganize all its civil, commercial and banking transaction to be compliant with the Islamic *Shari'ah* law."

The Problem

As noted, the Islamic banking law includes a categorical ban on interest. This sweeping proscription upends a basic component of conventional Libyan banking. At the time the Islamic Banking Law was adopted, the IMF noted (as have other critics) the likelihood that the law "could interrupt commercial bank lending until a new Islamic banking framework is put in place." The prediction has proven accurate. The limited time frame for converting to interest-free banking combined with the limited capacity of Libyan banks to adapt to the Islamic Banking Law's requirements have ground Libyan banking to a near-halt. Since the Islamic Banking Law's implementation, Libyan banks appear to be engaging mostly with public sector entities in transactions related to or funded by oil. Of the scant

lending that does occur, only a fraction goes to the private sector.

The central issue with the Islamic Banking Law is that it raises a host of questions for which there are few answers. The questions include: What is to be done about existing loans? Would contemporary Islamic finance products comply with the Islamic Banking Law? Can transactions with individuals and entities outside Libya that include interest proceed or be enforced?

Public pronouncements of officials as reported in the press have only muddled the law's requirements and added confusion. Industry commentators have argued that, at the very least, Libyan authorities must provide clear guidance to the banking sector and extend the deadline for compliance with the Islamic Banking Law. Many hope that the law will be repealed or change.

Other Economic Issues

In addition to the challenges posed by the Islamic Banking Law, the banking system itself is strained. Banks in Libya simply do not have the current capacity, the business models, the knowledge base, or the human resources needed to comply with the current law or easily adopt new contemporary Islamic finance models. Testimony in a recent Libyan Investment Authority court case against J.P. Morgan by witnesses for the Libyan sovereign wealth fund provides a clear reminder of the underdeveloped banking environment: "[B]anking in Libya had fallen well behind standards in the rest of the world by 2004. Large payments were still undertaken in cash, there were no credit or debit cards, very little use of the internet and poor telephone coverage." Another witness "described the situation in Libya when she arrived there in July 2008 as 'like the "wild west"' where the normal rules of commerce and standard business operating procedures simply did not exist."

The banking system must also grapple with political and legal issues. Old and new political divisions shift and overlap underneath the fractured political mantle of current governance. Genuine property rights are also a knot in financial sector progress. Clear and enforceable property rights are essential to domestic banking and finance, but are largely absent in Libya.

> The implementation of the Islamic Banking Law is off to a rocky start. Libyan banks are not lending, and their money is sitting with the Central Bank, which is facing its own host of problems.

Learning from and Leveraging Global Islamic Finance Experience

While critics generally concur that the Islamic Banking Law is a problem and the banking system needs reform, there is hope that Islamic banking and finance could prove to be a boon to rebuilding and reshaping a dysfunctional banking sector. For guidance, Libya may look to leading examples of other countries that have tackled state implantation of *Shari'ah*-based banking and finance.

During the last few decades, while Libya endured Qaddafi's distortion of the economy and civic life, contemporary Islamic banking and finance was being tried, tested, and developed around the globe. It has competed with other forms of finance in boom years and weathered hard times. Islamic finance has developed in sophistication in both the public and private sectors, in a variety of markets, and across borders to compete and complement as a global financial alternative. Bahrain, for example, has one of the highest concentrations of Islamic financial institutions and was one of the first jurisdictions outside of the G10 to impose Basel capital rules and international accounting standards.

Kuwait is another leading example from the GCC. Kuwait's Islamic Banking Law was passed in 2003 as an amendment to the Kuwait Central Bank and banking regulations law after broad debate. Since its adoption, Kuwait has been able to harmonize compliant and non-compliant banking. Many of the legal provisions for Kuwaiti Islamic banking and conventional banking are similar to one another. The main distinguishing features of Kuwait's Islamic Banking Law are in Articles 93 and 100, which place the issue of what constitutes *Shari'ah* compliance and non-compliance largely in the hands of *Shari'ah* boards. The law otherwise permits banking activity for Islamic banks like conventional ones, provided that they do not contradict Islamic *Shari'ah*. Kuwait Central Bank regulations allow Islamic banking to earn a "return" instead of the "interest" charged by conventional banks. Kuwait's utilization of the expertise and role of *Shari'ah* boards alongside flexible regulation demonstrates that Libya's current approach is not the only path to Islamic banking.

Economic Potential

Despite clear obstacles, the substantial assets and capitalization of Libyan banks and the potential of

The current Islamic Banking Law attempts unrealistically to wipe the slate clean without consideration of the externalities on bank lending and the fragile economy such an approach imposes.

petrodollars place Libya in a position to move from behind the curve. The years preceding the revolution saw a shift in Libya's international relations, which improved financial relations with the world and oil exports fueling steady bank performance. Libya's commercial banks grew from assets of 14.5 billion LYD in 2003 to 65.4 billion LYD by 2010 and a capital adequacy ratio of 17.3 per cent, according to Central Bank data and IMF reports. The revolution of course had a negative impact on the financial sector, but the banking sector assets have fared well, especially during a window in 2012 when oil exports resumed and provided some stability. As the IMF noted, "[a]lthough the conflict will have caused asset quality to deteriorate, the systemic impact should be modest in light of the liquidity buffer provided by banks' substantial reserves, along with limited claims on the private sector and the implicit government guarantee of loans to stateowned enterprises."

Moving Forward

To move forward, Libya cannot ignore political and economic realities. The current Islamic Banking Law attempts unrealistically to wipe the slate clean without consideration of the externalities on bank lending and the fragile economy such an approach imposes. Given this, it is probable there will be some modification of the Islamic Banking Law. However, a complete repeal of the law is unlikely, and some kind of Islamic finance law will probably remain a key feature in Libya's banking. Considering the immense ground that the Islamic Banking Law needs to cover, some have argued that the Islamic Banking Law should be implemented more gradually, by allowing banks to open Islamic banking windows and thereby enabling experience and expertise to evolve. But even if that were now the requirement, instituting *Shari'ah*compliant banking in Libya would still take time, effort, and expertise, all of which Libya does not currently have in abundance.

On the positive side, Islamic finance in Libya can provide much needed principles of, and institutional support for, reform while simultaneously garnering broader credibility for the financial sector among a skeptical population. Libya can also draw on the lessons and expertise developed in other jurisdictions in implementing an Islamic banking system. With hard work and support, Libya may yet be a new frontier in Islamic banking and finance. It will not be easy, but Libya has demonstrated a capacity and willingness to change. Libya could benefit not only from the investment that may come with an engagement with global Islamic banking and finance, but also from the reform based on bedrock principles that call for social good through investment.

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Saudia Arabia's New Finance Minister Faces Questions Over Implementing Vision 2030 In Education Sector

The education sector is seen as fundamentally important to the future success of the Kingdom and the country's ability to compete internationally with the best of the best.

Saudi Arabia recently appointed Mohammed al-Jadaan as the country's new finance minister. Al-Jadaan has reinforced his commitment to the country's Vision 2030 initiative, which was revealed earlier in 2016 to serve as a "road map" for developing the Kingdom's economic and infrastructure during the next 15 years.

One of the major planks of Saudi Arabia's Vision 2030 economic reform programme is education. The education sector is seen as fundamentally important to the future success of the Kingdom and the country's ability to compete internationally with the best of the best.

Al-Jadaan will have to look at a number of issues when assessing how best to deliver on the education investment needed to satisfy the Vision 2030 goals. At present, the Kingdom funds around 80 per cent of education directly, but it is likely that more private sector involvement, both in constructing and financing schools, will be needed.

The PPP Option

One option is public private partnerships (PPPs), which have been used around the world as a means of fulfilling government education policy. Some of these projects have been a resounding success. Others have not.

The starting point of any discussion on the implementation of PPPs in the education sector is public policy. The policy framework sets the key parameters for the government and private sectors and is the instrument through which both the government and private sectors can be held accountable for the success or failure of the PPP scheme.

Shifting the capital expenditure school-building burden from the government to the private sector is a key policy feature of the Saudi government, but it is clear that other objectives are equally important. A review of Saudi Arabia's National Transformation Program (NTP) provides interesting insights into what the government intends to achieve. The NTP reveals eight strategic objectives for education, namely:

- Providing education services for all student levels
- Improvising recruitment, development and training of teachers
- Improving the learning environment to stimulate creativity and innovation
- Improving the curriculum and teaching methods
- Improving student values and core skills
- Enhancing educational systems to address national development requirements and labour market demands
- Developing creative financing methods
- Increasing private sector participation

The real question is whether PPPs work in the education sector and will be a success in Saudi Arabia. It is worthwhile taking a tour of the global PPP education market at this point. Europe, by far, has been the pioneer in the education PPP sector over the past 15 years. European countries have closed more deals than the rest of the world put together by a factor of at least three. The United Kingdom has been the leader within Europe, followed by France and then Germany. The Americas are next in the rankings, with 20 projects in Canada, 13 in the U.S. and at least one in Mexico. After that is Asia, followed by Africa.

When the projects in these jurisdictions are analysed a number of trends can be identified. The table below sets out some of the key features, together with their advantages and disadvantages.

Key Questions

The fundamentally important question is which of the above approaches should be adopted by a host government embarking on PPP in the education sector for the first time. At one end of the spectrum, the government could decide to grant a PPP concession on the basis that all of the above features are combined into a single project and outsourced to a single private sector developer.

Structure	**Outsourcing infrastructure**	**Outsourcing management**	**Outsourcings supporting services**	**Outsourcing professional services**	**Outsourcing teaching**
Description of Services	• School building • Financing capital works • School maintenance	• Finance • HR • Leadership	• Catering • Cleaning • Security • Transportation	• Teacher recruitment • Teacher training • Quality certification	• Teaching children
Advantages	• Increases in number of schools • Allows existing schools to be renovated • Avoids government capital expenditure	• Allows schools to focus on teaching • Leads to private sector innovation	• Allows schools to focus on teaching • Cost savings	• Allows schools to focus on teaching • Innovation • Higher standards	• Improvement in teaching standards • Teaching provided in rural/remote areas
Disadvantages	• Achieving quality • Achieving value for money	• Defining suitable KPIs • Achieving value for money	• Accountability • Defining KPIs	• Accountability • Defining suitable KPIs • Achieving and maintaining high-quality teaching	• Accountability • Defining KPIs • Achieving and maintaining high-quality teaching

The Kingdom will have to decide how it wishes to proceed with its education PPP program and what that programme will look like.

The developer would be in charge of building schools; financing school building; administration and finance; catering, cleaning and transportation; teacher training and recruitment; and the teaching of children.

The education of the child population of a country is an intrinsically sensitive and delicate issue. Governments cannot afford to get it wrong by first, deciding to outsource to the private sector through a PPP and second, adopting the wrong PPP structure. The consequences are potentially dire. For that reason, it is fairly unusual to see PPP projects in the education sector covering such an expansive scope. The determining factor is often a country's lack of fiscal flexibility, combined with a crumbling education infrastructure and a willingness amongst politicians to take a risk on the private sector. In other words, the government has no choice.

If such sweeping projects are to succeed, the interests of the public and private sectors must be closely aligned and reflected in the terms of the PPP agreement. This has proven to be an incredibly difficult task. Successfully allocating risk so that the public sector obtains value for money in the provision of PPP services while the private sector is fully incentivised with appropriate returns on its investment has generally been elusive.

Unless the host government has no choice, it is arguable that the better approach is to limit the role of the private sector to school construction (including the financing of that construction) and facilities management. The interesting piece is facilities management. This can be packaged in an expansive manner or in a more limited fashion. The expansive approach includes "soft facilities management", for example, the support services referred to in the table above: cleaning, catering, transportation and security. The more limited approach is often referred to as "hard facilities management" and typically includes building maintenance, energy management and life cycle renewal.

The distinction between soft facilities management and hard facilities management proved to be extremely controversial in the context of the PPP programme in the United Kingdom. The politically charged national debates culminated in the cancelling of the public finance initiative and the introduction of a new scheme called "PF2". The conclusion was that PPP projects were best structured on a hard facilities management basis and that soft facilities management did not achieve the value for money that the UK government had originally anticipated.

Each country, of course, is different, and it could be argued that the United Kingdom had its own unique circumstances. Nonetheless, the choice of the type of facilities management – soft or hard – is a critical threshold question for any government embarking on a PPP in the education sector.

The Kingdom will have to decide how it wishes to proceed with its education PPP program and what that programme will look like. The Kingdom has a significant advantage in that it has no shortage of success stories in closing multibillion-dollar infrastructure deals. Almost all of these deals have been in the industrial sector: petrochemicals, power and water, to name a few. Many of these deals were project financed on a build-own-operate (BOO) basis and fall into the same conceptual ballpark as a PPP project. However, social infrastructure is different, and the achievement of value for money should be an imperative. A number of key threshold decisions will have to be made, but considering that hundreds of PPP deals in the education sector have been closed globally, the Kingdom is in a uniquely informed position to guide the sector to success.

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Investment Funds

New Investment Funds and REIT Regimes in Saudi Arabia

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EDITED VERSION
This article has been edited to comply with our Editorial Guidelines, which include UK spelling and grammar, and specific house styles for consistency.

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The Saudi Arabian economy, while strong and stable relative to other countries in the region, has entered a period of transition. In early 2016, the country's leadership adopted a national transformation plan – 'Vision 2030' the aim of which was to modernise and diversify the economy. In particular, Vision 2030 focuses on increasing employment, particularly in the private sector. There will also likely be continued investment by the private sector in the retail, power, renewables, transport, education and healthcare sectors.

The financial services sector in Saudi Arabia is undergoing a period of transformation. The Capital Market Authority (**CMA**), which regulates the financial services and asset management industries in Saudi Arabia, has long sought to encourage asset managers and investment banks to grow assets under management by tapping retail markets and international investors. The CMA also wants to encourage managers to develop products which can be accessed by the Saudi public in order to encourage individuals to invest their income in the Saudi domestic market.

As such, throughout 2016 the CMA has released numerous regulations covering the establishment of new corporate vehicles, the IPO process and foreign investment in Saudi Arabia and has promised a complete revamp of existing financial services regulations. Two regulations in particular are pivotal for asset managers looking to raise Saudi Arabia targeted funds: the amended investment fund regulations (the **New Funds Regulations**) and the real estate investment traded funds instructions (the **REITF Regulations**).

After a consultation period, the New Funds Regulations were released in May 2016 and became effective on 6 November 2016. The New Funds Regulations govern the formation, offering and operations of all private and public investment funds in Saudi Arabia, except publicly offered real estate funds, which are governed by the Real Estate Investment Funds Regulations. The issuance of the New Funds Regulations was long expected as the CMA had publicly acknowledged for years that new regulations were in progress.

In August 2016, the CMA released draft REITF Regulations, which provide for certain public real estate funds to be listed on the Saudi Arabian Stock Exchange (**Tadawul**) as real estate investment traded funds (**REITFs**). These REITF Regulations were initially subject to a consultation period, after which final regulations were adopted 24 October 2016. The REITF Regulations allow managers to list certain public real estate funds on the Tadawul; previously, the

only listed funds in Saudi Arabia are exchange traded funds. The first REITF was listed in November 2016, with a number of additional REITFs expected to be approved and listed in early 2017.

Both new regulations provide opportunities to investment banks, private equity firms and asset managers to expand their product offerings and access additional investor bases.

Investment funds regulations

In May 2016, the CMA issued draft New Funds Regulations to replace the previous funds regulations issued in 2006 (the **2006 Regulations**). These New Funds Regulations became effective on 6 November 2016. The CMA intends the New Fund Regulations to provide clarity and to encourage more managers to launch funds. These regulations have been a long time coming. It has been public knowledge for years that the CMA has intended to revamp the 2006 Regulations in order to codify unwritten practices of the CMA, to address problems of investor protection that arose during the financial downturn and to cover the launch of a diverse range of new funds, many of which were not contemplated by the 2006 Regulations.

The processes for launching a private fund remains essentially unchanged, although the required documentation has been detailed, particularly regarding real estate funds. The process for launching a public fund, which has been opaque in the past, has been expanded, with managers required to prepare an information memorandum, the form of which is set out in the New Funds Regulations. The information memorandum contains much greater disclosure requirements than the 2006 Regulations.

There are a number of other provisions of interest. First, the fund manager may not restrict investors of certain nationalities unless the approval of the CMA is obtained. The CMA has indicated that the only restrictions it will apply will be to restrict those private real estate funds which invest in the cities of Mecca and Medina to Saudi Arabian nationals only. Otherwise, all investment funds would be open to foreign investment, regardless of the underlying investments. This is a significant change as it was often considered a grey area whether foreign investors could invest directly into CMA regulated funds or if such investors would be prohibited or would have to register through a lengthy process with the Saudi Arabian General Investment Authority (**SAGIA**).

Second, all funds must have an independent custodian; accordingly, the role of the custodian

Both new regulations provide opportunities to investment banks, private equity firms and asset managers to expand their product offerings and access additional investor bases.

has been expanded so that they control cash flow. Previously, independent custodians were required only for public funds and real estate funds. This new requirement potentially adds significant costs to the fund, though the CMA has determined that the heightened protection for investors outweighs the costs.

Third, administrators, advisers and certain other corporate service providers performing activities in relation to a fund investing in Saudi Arabia must be licensed by the CMA. Previously, many Saudi Arabian managers had outsourced certain functions to advisers and service providers sitting offshore. Such third parties will only now be permitted to provide services to CMA funds if the funds are investing outside of Saudi Arabia.

Fourth, the fund manager and its affiliates are not entitled to vote any units they hold in an investment fund under the new Regulations. Previously, the fund manager was treated equal to other third-party investors in the fund.

Fifth, unitholders are also afforded statutory rights under the New Funds Regulations. Now the manager must obtain the consent of the unitholders prior to making material changes to the fund's documentation, such as changing the strategy or the risk profile or significantly increasing fees and expenses, which would reasonably be expected to cause the unitholders to reconsider participation in the fund. Further, the fund manager must schedule and hold an annual unitholders meeting. The 2006 Regulations provided no such unitholder protections, nor did it provide for any unitholder meetings.

Finally, the fund manager may be removed by a supermajority vote of the unitholders and the process for replacing the fund manager has been clarified under the New Funds Regulations. The 2006 Regulations, by comparison, were silent on

this issue which created a grey area due to the nature of a CMA fund. A CMA fund is a contract between the manager and the investors. It had been widely assumed that if the manager was removed the contract would become void, and as such, the fund would be terminated. The CMA has now introduced the procedure pursuant to which a replacement manager could be introduced and the fund could continue to remain in existence following the removal of the initial manager.

Real estate investment traded funds instructions

The REITF Regulations contemplate the listing of REITFs on the Tadawul and are meant to focus on developed properties that generate periodic income. At least 90 percent of the REITF's net profits must be distributed annually to the unitholders.

REITFs must be closed-ended funds with a nominal value per unit of SAR 10 at the time of the initial offering. The minimum amount to be raised in the REITF's initial offering is SAR 100m and each REITF must include at least 50 unitholders from the public. The road show for the REITF is not to exceed 14 days.

The REITF manager must be a licensed CMA authorised person. The REITF manager is required to appoint both an independent custodian and a licensed property management company. The custodian is to ensure that it segregates its assets from those belonging to the REITF and from the assets of its other clients.

At least 75 percent of the REITF's investments must be in developed assets generating periodic income. REITFs are not to invest in vacant land, but may invest up to 25 percent of the fund's assets in real estate development or the redevelopment of properties. The REITF Regulations allow for up to 25 percent of a REITF's assets to be invested outside Saudi Arabia. At least 75 percent of an REITF's assets must be identified prior to launching the REITF and the CMA will require evidence of binding agreements in relation to the pre-identified income generating properties. The REITF Regulations permit the underlying assets to have leverage and for the concerned lender to record the property in the name of a subsidiary of such lender. Leveraging, however, should not exceed 50 percent of the total assets value of the REITF.

In our experience, the CMA is initially focusing on encouraging various private Saudi Arabian real estate funds to utilise the REITF route as an exit from their existing portfolios and provide liquidity to their investors. It is widely expected that many CMA managers will take advantage of the new regime and the REITF Regulations will further spur the real estate market in Saudi Arabia.

Conclusion

Over the past few years, the CMA has been focused on issuing new regulations and new products to help spur the domestic market and foreign investment into Saudi Arabia. The issuance of the new Funds Regulations and the REIT Regulations are consistent with these aims. The Fund Regulations provide further clarity to local managers who are seeking to tap domestic and international markets. The REIT Regulations introduce a highly anticipated new product which provides investors liquidity and makes it easier for retail investors to participate. Both have been welcomed, as they provide clarity and allow for new products to be offered by managers.

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endnotes

About our Middle East Practice

King & Spalding has been advising clients in the wider Middle East region for more than 30 years and is recognized for its expertise in Islamic finance, corporate finance, debt capital markets, infrastructure projects, energy, international arbitration, real estate and construction, international trade, mergers and acquisitions, and private equity. Our Dubai, Abu Dhabi and Riyadh offices are home to a team of internationally qualified lawyers who are consistently recognized by independent directories for being market leaders in their fields of expertise. Our clients in the Middle East include some of the most high-profile oil & gas, energy and power companies, banks and finance houses, and significant investors and multinationals. Our team has won numerous awards for our ground-breaking deals. In reference to King & Spalding, *Chambers Global* mentions the firm "remains a heavy hitter in the region, as evidenced by the quality of its lawyers and deals".

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