

SAUDI ARABIA | 16 December 2015

## New Saudi Companies Law Approved

2015 has seen a number of interesting legal developments in Saudi Arabia, particularly from a foreign investment perspective. As well as the approval of the new Companies Law 1437H/2015G (the “**NCL**”), which will be of interest to local enterprises and foreign investors alike, this year has seen the enactment of rules that permit qualifying foreign financial institutions to trade in shares listed on the Tadawul and the announcement that the 25% local ownership requirement for retail and wholesale businesses wishing to sell, distribute and market their products directly in the Kingdom will be removed.

These developments suggest that a key priority for the Kingdom is the implementation of a more foreign investor-friendly regulatory framework that facilitates the injection of foreign know-how and foreign capital into the Kingdom, which is not unexpected given:

- the economic challenges presented by low oil prices and the uncertainty as to when prices may be expected to recover; and
- the Kingdom’s interest in diversifying its oil-dependent economy and facilitating the development of new local industries and new employment opportunities for the local population.

Although the NCL has been almost a decade in the making and pre-dates the oil price slump, the timing of the recent approval of the NCL may be viewed as another example of the Kingdom looking to enhance the regulatory environment for foreign investors at a time when foreign investment has a potentially important role to play in maintaining economic stability in the Kingdom.

### New Companies Law

The NCL is a significant overhaul of the existing Companies Law in the Kingdom. The NCL is a law more closely aligned with global best practice in corporate law and governance and reflects the Kingdom’s responsibilities as a member of the World Trade Organisation, as well as the establishment of the Saudi Arabian General Investment Authority (“**SAGIA**”) and the Capital Markets Authority (the “**CMA**”), among others.

The NCL will come into force on 2 May 2016, being 150 days after its publication in the Official Gazette, which occurred on 4 December 2015. Implementing regulations for the NCL will be issued by the Minister of Commerce and Industry and the CMA in due course.

As discussed further below, the NCL changes the position under the existing law in a number of respects that should assist foreign investors and address a number of concerns previously raised by local lawyers, however, it should still be noted that foreign investors remain subject to the regulations of SAGIA, including the Foreign Investment Law and its implementing regulations. We will be interested to see whether these regulations are updated in line with the NCL.

## Key Changes Regarding Joint Stock Companies

- **Minimum number of shareholders:** reduced from five to two, although if owned by a government-related body or if it has share capital of SAR 5 million or more, a joint stock company may be incorporated with a single shareholder.
- **Minimum capital requirements:** decreased from SAR 2 million to SAR 500,000 for closed joint stock companies.
- **Restrictions on number of members of the board of directors:** not less than three and not more than 11.
- **Corporate Governance:**
  - general assembly meetings may be convened using modern communication methods;
  - introduction of cumulative voting system for the election of members of the board of directors;
  - general assembly of shareholders must establish an audit committee to supervise the company's business, with executive board members not eligible for audit committee membership; and
  - the position of the chairman may not be combined with any other executive position.
- **Debt and Convertible Debt Issuance:** joint stock companies may issue sukuk and other debt instruments and these may be converted into negotiable shares.
- **Dealing in Shares:** joint stock companies are permitted to purchase or mortgage their shares.

## Key Changes Regarding Limited Liability Companies

- **Minimum number of shareholders:** reduced from two to one. This is a helpful development for foreign investors as it reduces the burden that establishing a limited liability company with two shareholders presents.
- **Conversion to a Joint Stock Company:** if the number of shareholders in a limited liability company exceeds 50 for reasons other than as a result of an inheritance or provisions of a will, the company must be converted to a joint stock company within one year, otherwise the company will dissolve by operation of law.
- **Statutory Reserve:** contributions to the statutory reserve are no longer required once the reserve has reached 30% of the share capital. Previously, the requirement was 50%.
- **Losses exceeding 50% of share capital:** the shareholders of a limited liability company will no longer be personally liable if the company's debts exceed 50% of the company's share capital—instead, if the General Manager or the Board does not call a meeting of the shareholders or the shareholders do not resolve to continue operating the company or dissolve it, the company will dissolve by operation of law and the shareholders will not be personally liable. Under Article 180 of the existing law, the shareholders are jointly and severally liable for the debts of the limited liability company if no decision is made in these circumstances and any interested party may request the dissolution of such limited liability company. This change is therefore significant for shareholders of limited liability companies and may remove the need for shareholders to rely on waivers by creditors of such limited liability companies of their rights under Article 180.

## Temporary Commercial Registration

The NCL introduces the concept of “Temporary Commercial Registration” for foreign companies entering into contracts with government entities and provides that the registration certificate will expire upon completion by the foreign company of its obligations under the applicable governmental contract.

The NCL does not, however, provide any guidance on the forms of companies, the activities or the percentage of ownership that may be held by a foreign investor, which means that for the purpose of establishing business operations in the Kingdom, a foreign investor (being an entity with non-GCC shareholding) will still need to comply with the Foreign Investment Law and its implementing regulations.

## Holding Companies

The NCL now recognises the existence of a limited liability company or joint stock company as a “holding company” although such a company must have the word “holding” in its name and none of its subsidiaries are permitted to hold shares in such company.

We will issue a new update in due course following the release of the NCL implementing regulations. In the meantime, if you wish to discuss the NCL, a potential investment in Saudi Arabia or Saudi Arabian law generally, please feel free to contact one of our key people below.

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This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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