

## The merger of commercial companies in the Saudi Arabian Stock Exchange (*Tadawul*) and its impact on the rights of Foreign Direct Investment (FDI) in the Saudi system

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### Abstract

This work focuses on the rights of Foreign Direct Investment (FDI) in Saudi Arabia when a merger occurs between two or more commercial companies in the Saudi Arabian Stock Exchange (*Tadawul*). This article aims to give a comprehensive and critical review of the new Saudi Arabia Companies Law 2015 and also the Foreign Investment Law 2000, and the extent to which these laws provide protection for foreign investors in Saudi Arabia. The article is divided into eight sections, as follows. The first provides an overview of FDI in Saudi Arabia; the second discusses the concept of the merger of commercial companies according to the Saudi Companies Law 2015; the third section examines common types of merger of commercial companies in Saudi Arabia, while the fourth considers the regulatory framework of such mergers; the fifth section examines the regulation and supervision of FDI in Saudi Arabia; the sixth goes on to discuss the means of settlement of foreign investment disputes in the country; the seventh section considers the legal challenges facing FDI in the country; and in the final section a summary is provided.

**Keywords:** Foreign Direct Investment, *Shariah*, Saudi Arabia, *Tadawul*, SAGIA, Capital Market Authority.

### Introduction

At present, many countries rely on attracting capital from abroad, which is called Foreign Direct Investment (FDI). FDI contributes to economic growth by increasing total capital accumulation in the host economy. It has been recognised that maximising the benefits of FDI for the host country can be significant, including technology spillovers, human capital formation support, enhancement of a competitive business environment, contribution to international trade integration and improvement of enterprise development. Moreover, further than economic benefits, FDI can help the improvement of environmental and social conditions in the host country by relocating modern technology and leading to more socially responsible corporate policies.<sup>1</sup> Therefore, all developing and developed countries alike seek to provide the appropriate environment to attract FDI. The Kingdom of Saudi Arabia (KSA) is one of those countries that has been seeking economic diversification since the 1970s. According to the United Nations Conference on Trade and Development (UNCTAD),

<sup>1</sup> Selma Kurtishi-Kastrati, 'The Effects of Foreign Direct Investments for Host Country's Economy', *European Journal of Interdisciplinary Studies* (2013) 5 (1) 26; Hira Arain, Liyan Han, Li Zhang, 'Effects of Information Systems and Technology on Foreign Direct Investment in Developing Countries', *International Journal of e-Education, e-Business, e-Management and e-Learning* (2017) 7 (2) 146.

Saudi Arabia is a large host country to foreign direct investment (FDI) where the volume of FDI reached about \$200 billion by the end of 2014.<sup>2</sup> Recently, Saudi Arabia in its Vision 2030 decided to change its development strategy so as to become less dependent on oil revenues by focusing on FDI as one of the most important factors of real and comprehensive economic development.<sup>3</sup> The KSA thus embarked upon various legal and policy reforms and also the provision of facilities, information, incentives and legal advice to improve the investment climate in the country. One of the most important issues for foreign investors in the KSA is the availability of an adequate legal framework which facilitates the establishment and operation of their business and provides them with adequate protection for their investments.<sup>4</sup>

### 1.1 Research Problem

In the KSA, there are some laws related to FDI such as the Foreign Investment Law, Companies Law and Commercial Court Law. These laws do not include Articles for the protection of foreign investors in the case of a merger of commercial companies in the Saudi Arabian Stock Exchange (*Tadawul*). In addition, there is no court specialised in the settlement of commercial disputes. Therefore, the main research problem is the absence of regulatory policies for FDI in the case of a merger of commercial companies in *Tadawul* under the current Saudi laws.

### 1.2 Research Questions

The main question of this article is: *To what extent do Saudi regulations provide adequate legal protection for foreign investors in the case of a merger of commercial companies in the Saudi Arabian Stock Exchange (Tadawul) in the Kingdom of Saudi Arabia?* In order to answer this research question, the following sub-questions are formulated:

- a. What are the common types of merger of commercial companies in the KSA?
- b. What is the regulatory framework for Foreign Direct Investment (FDI), and?
- c. What is the regulatory framework for the merger of commercial companies in the KSA?
- d. What are the challenges facing FDI in the KSA from a legal point of view?

### 1.3 Research aims

The primary aim of this article is to examine whether the current Saudi laws provide adequate legal protection for foreign investors in the case of a merger of commercial companies in the Saudi Arabian Stock Exchange (*Tadawul*) in the Kingdom of Saudi Arabia. However, there are additional aims, which are as follows:

- a. To discuss and analyse the basic laws of Foreign Direct Investment (FDI) in Saudi Arabia.
- b. To determine the legal challenges that face Foreign Direct Investment (FDI) in Saudi Arabia from the legal point of view.
- c. To identify dispute resolution mechanisms needed for the protection of Foreign Direct Investment (FDI) in Saudi Arabia.

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<sup>2</sup> See the official website of Saudi Vision 2030, available at: <https://www.chathamhouse.org/sites/files/chathamhouse/publications/research/2017-07-20-vision-2030-saudi-kinninmont.pdf> [Accessed 10 December 2017].

<sup>3</sup> Ibid.

<sup>4</sup> Faisal Alkahtani, Legal protection of foreign direct investment in Saudi Arabia (Newcastle University 2009) 1.

## 1.4 Research Methodology

The selected methods for this article are a critical literature review and a critical analysis. The first step will be an in-depth critical literature review to cover all different forms of commercial companies in Saudi Arabia through reviewing the books, laws and regulations. The next step will be to review the academic journals and reports which are concerned with the actual practices of Foreign Direct Investment (FDI), and also to understand the mechanism of the merger of commercial companies in the Saudi Arabian Stock Exchange (*Tadawul*) in Saudi Arabia. In addition, the critical literature review will cover the Saudi Arabian General Investment Authority (SAGIA) and the Capital Market Authority (CMA) as the authorities who are responsible for the regulation and supervision of FDI practices in Saudi Arabia and the merger of commercial companies in *Tadawul* in order to determine the legal challenges that face FDI in the case of the merger of commercial companies in *Tadawul* in the current Saudi laws, from the legal point of view.

## 2. An Overview of FDI in Saudi Arabia

A foreign investor has been defined by the Saudi Foreign Investment Law, issued by Royal Decree No M /1 dated 10 April 2000,<sup>5</sup> as a natural person who is not of Saudi nationality or a corporate person whose partners are not all Saudi. According to the 2017 World Investment Report published by UNCTAD, Saudi Arabia is the third largest FDI recipient in Western Asia, after Turkey and the United Arab Emirates. In 2016, FDI inflows fell by 8.5% compared to the previous year, reaching USD 7.45 billion, the lowest since 2014<sup>6</sup> which means that FDI flows to Saudi Arabia have followed a downward trend during five recent years.

FDI is seen as one of the most effective ways to diversify the economy and provide employment for younger generations. The Saudi Government welcomes FDI, due to the ability of FDI to transfer technology, employ and train the national workforce, foster economic development and enhance local raw materials. Once Saudi Arabia became a member of the WTO in 2005, the foreign investment climate in the Kingdom substantially improved. From an investor's point of view, the country's strong points are economic stability, the large local market with a high spending power, significant increase in population, sound infrastructure and a well-regulated banking system, and all of these are considered decisive factors for foreign investors.

According to the Saudi law on foreign direct investment, foreign investors are now allowed to invest in all sectors of the economy in Saudi Arabia, except for specific activities on a negative list. This list includes the industry and service sectors, real estate investment in Mecca and Medina, some sub-sectors in printing and publishing, audiovisual and media services, land transportation services excluding inter-city transport by trains, and upstream petroleum.

Foreign investment in public companies listed on the *Tadawul* is one of the permitted

<sup>5</sup> See the official website of the Bureau of Experts at the Council of Ministers, available at: <https://www.boe.gov.sa/ViewSystemDetails.aspx?lang=en&SystemID=50&VersionID=60#search1>, [Accessed 28 October 2017].

<sup>6</sup> See the official website of Lloyds Bank, available at: [https://www.lloydsbanktrade.com/en/market-potential/saudi-arabia/investment?&accepter\\_cookies=oui](https://www.lloydsbanktrade.com/en/market-potential/saudi-arabia/investment?&accepter_cookies=oui), [Accessed 28 October 2017].

and preferred activities for foreign investors. Joint stock companies are considered the preferred form for foreign investors because a foreigner is not allowed to conduct business in Saudi Arabia as a sole proprietor, unless the individual is operating a branch of a foreign company.

### **3. The Concept of a Merger of Commercial Companies according to the Saudi Companies Law (2015)**

According to the Saudi Companies Law, a merger is defined as the combining of one or more companies with another existing company or by combining two or more companies to establish a new company. Therefore, all rights and obligations of the merged company shall be transferred to the merging company or the company resulting from the merger after completing merger procedures and registering the company in accordance with the Law. The merging company or the company resulting from the merger shall be considered a successor company of the merged company to the extent of assets transferred thereto, unless agreed otherwise in the merger contract.<sup>7</sup>

In the new Companies Law, the Saudi regulator addressed some provisions related to the merger of companies. For example, a merger shall not be valid except after valuation of the net assets of the merged and merging companies, if the consideration for the share or shares of the merged company or part thereof is a share or shares in the merging company. In all cases, the decision on the merger shall be issued by each company that is a party thereto, in accordance with the condition prescribed for amending the articles of incorporation of the articles of association of such company. In addition, a partner who owns shares in the merged and merging companies may vote on the merger decision only in either company.<sup>8</sup>

### **4. Common Types of Merger of Commercial Companies in Saudi Arabia**

In general, there are three common types of mergers in Saudi Arabia. Firstly, a horizontal merger. This is defined as a merger or business consolidation that occurs between firms that operate in the same space, as competition tends to be higher and the synergies and potential gains in market share are much greater for merging firms in such an industry. This type of merger frequently occurs because of larger companies attempting to create more efficient economies of scale, such as the November 1998 merger of Daimler-Benz AG of Germany and Chrysler Corporation of the United States.<sup>9</sup>

The second type is a vertical merger, and this can happen in two ways. The first is when one firm acquires another firm which produces raw materials used by it. For example, a tyre manufacturer acquires a rubber manufacturer, a car manufacturer acquires a steel company, a textile company acquires a cotton yarn manufacturer. The second form of vertical merger happens when one firm acquires another firm

<sup>7</sup> Companies Law 2015, Art. 191 (A) and 192.

<sup>8</sup> Companies Law 2015, Art. 191 (A – B - C).

<sup>9</sup> Ziad Ahmed al-Qurashi, Saudi Commercial Law (Dar Hafiz Ltd 2017) 150.

which would help it come closer to the customer; for example, a consumer durable manufacturer acquiring a consumer durable dealer, or a fast-moving consumer goods (FMCG) company acquiring an advertising company or a retailing outlet.<sup>10</sup> The third type is a conglomerate merger. This refers to the combination of two firms operating in industries unrelated to each other. In this case, the business of the target company is entirely different from that of the acquiring company. For example, a watch manufacturer acquiring a cement manufacturer, a steel manufacturer acquiring a software company. The main objective of a conglomerate merger is diversification of risk.<sup>11</sup>

## 5. The Regulatory Framework of the Merger of Commercial Companies in Saudi Arabia

The merger of commercial companies in the *Tadawulis* is regulated and supervised by the Capital Market Authority (CMA) under the Mergers and Acquisitions Regulation, issued by the Capital Market Authority Board approved on 3/10/2007. The CMA was established under Article 4 of the Capital Market Law (CML), issued by Royal Decree No. M/30 dated 2 July 2003, to regulate and develop the capital market activities in Saudi Arabia including commercial companies in the *Tadawul*.<sup>12</sup>

The basic objectives of the CMA are to create an appropriate investment environment through issuing the required rules and regulations, reinforcing the transparency and disclosure standards of all listed companies, boosting confidence, and protecting investors and dealers from illegal acts in the market.<sup>13</sup> The CMA is empowered under Article 5 of the CML<sup>14</sup> to issue the required rules and regulations to create an environment that is conducive to the growth of investment activities in Saudi Arabia.<sup>15</sup>

The CMA has issued a decision to adopt the rules governing the investment of qualified foreign<sup>16</sup> financial institutions in listed shares. The new decision allows a

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<sup>10</sup> Ibid.

<sup>11</sup> Ibid.

<sup>12</sup> See the official website of the Capital Market Authority (CMA), available at: <http://www.cma.org.sa/En/AboutCMA/CMALaw/Pages/CH2Article4.aspx> [Accessed 24 October 2017].

<sup>13</sup> See the official website of the Capital Market Authority (CMA), available at: <http://www.cma.org.sa/En/AboutCMA/Pages/default.aspx> [Accessed 24 October 2017].

<sup>14</sup> The Capital Market Law (CML) was issued by Royal Decree No. M/30, dated 31/07/2003, to regulate and develop the Saudi financial market through improving the development of procedures that would reduce the risks related to securities transactions. The CML gives the Capital Market Authority broad powers to regulate the issuance of securities, as well as to monitor them and dealings in them. In addition, the CML protects citizens and investors in Securities from unfair and unsound practices or practices involving fraud, deceit, cheating or manipulation. The CML seeks to achieve transparency, fairness and efficiency in Securities transactions.

<sup>15</sup> Kabir Hassan and others, *Islamic Capital Markets: Products and Strategies* (John Wiley & Sons 2011) 102.

<sup>16</sup> The foreign investor qualified in accordance with the decision of the Capital Market Authority Board is the foreign investor registered with the Capital Market Authority in accordance with the rules of investment in listed securities.

foreign investor to own a maximum of 5% of each listed company as long as the foreign investment in each company does not exceed 20%. The decision sets the maximum percentage that foreign investors are entitled to acquire from the market at 10%.

## 6. The Regulation and Supervision of FDI in Saudi Arabia

In Saudi Arabia, FDI is governed and regulated by the Saudi Arabian General Investment Authority (SAGIA) under the Foreign Investment Law enacted by Royal Decree No. (M/1) dated 19/04/2000, and its Implementing Regulations issued by the Board of Directors' Resolution No (1/20) dated 23/06/2002. Therefore, SAGIA is the sole authority responsible for promoting FDI, for the approval of investments, for supporting and providing hands-on assistance to existing and prospective investors, and for the collection of data on investment declared by the newly established foreign companies.<sup>17</sup>

SAGIA's duties include formulating government policies regarding investment activities, proposing plans and regulations to enhance the investment climate in the country, and evaluating and licensing investment proposals. In addition, SAGIA issues licences to prospective investors through SAGIA's Investor Service Centre (ISC) which offers detailed information on the investment process, provides licences and support services to foreign investors, and coordinates with government ministries to facilitate investment. According to SAGIA, the ISC must grant or refuse a licence within five days of receiving an application and supporting documentation from the prospective investor.<sup>18</sup>

In addition, SAGIA works to foster and promote investment opportunities across the economy, particularly in energy, education, transportation, health, life sciences, and knowledge-based industries. It offers a number of incentives in order to attract foreign investors to the KSA. Among them are 100% foreign ownership of property and companies in certain industries, lower minimum capital requirements, no restriction on repatriation of capital, tax incentives if the company is registered in certain economic cities located in the less developed provinces of KSA and the ability for foreign investors to sponsor foreign employees.<sup>19</sup>

As a result, there have been some encouraging decisions for foreign investors by SAGIA, such as the fact that in many sectors foreign investors are no longer required to take local partners and that foreign investors may own real estate for company activities. They are allowed to transfer money from their enterprises outside the country and can sponsor foreign employees, provided that Saudisation quotas are met. The minimum capital requirements to establish business entities range from zero to SR 30 million (\$ 8 million) depending on the sector and the type of investment.<sup>20</sup>

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<sup>17</sup> See the official website of the Bureau of Experts at the Council of Ministers, available at: <https://www.boe.gov.sa/ViewSystemDetails.aspx?lang=en&SystemID=50&VersionID=60#search1>, [Accessed 24 October 2017].

<sup>18</sup> See the official website of the Saudi Arabian General Investment Authority (SAGIA), available at: <https://www.sagia.gov.sa/en/pages/default.aspx>, [Accessed 10 December 2017].

<sup>19</sup> Ibid.

<sup>20</sup> Ibid.

## 7. Means of Settlement of Foreign Investment Disputes in Saudi Arabia

One of the most important issues for foreign investors is the availability of an adequate legal framework for them in Saudi Arabia which facilitates the establishment and operation of their business in Saudi Arabia and provides them with adequate protection for their investments. However, there are concerns which have arisen amongst foreign investors. These concerns mainly stem from a sense of legal uncertainty and unpredictability of the laws and dispute settlement systems relating to FDI in Saudi Arabia, including where relevant *Shariah* which is fundamental to the Saudi legal system.<sup>21</sup>

According to Article Thirteen of the Saudi Foreign Investment Law, disputes arising between the government and the foreign investor in relation to its investments licensed in accordance with this Law shall, as far as possible, be settled amicably. Failing such settlement, the dispute shall be settled according to the relevant laws. Secondly, disputes arising between the foreign investor and its Saudi partners in relation to its investments licensed in accordance with this Law shall, as far as possible, be settled amicably. Failing such settlement, the dispute shall be settled according to relevant laws without prejudice to agreements to which the Kingdom of Saudi Arabia is party.<sup>22</sup>

Referring to the Article above, it can be seen that the Saudi Foreign Investment Law refers to three means of dispute resolution – amicable settlement, formal settlement and settlement to which Saudi Arabia is a party – depending on the agreements. In addition, there is a committee, composed of at least a chairman and two members, to be named the Investment Disputes Settlement Committee. The committee is not included in the Foreign Investment Law, but is mentioned in the Implementing Regulations of the Foreign Investment Law.<sup>23</sup>

According to Article Twenty-six of the Implementing Regulations of the Foreign Investment Law:

The Board of Directors shall form, subject to Article Thirteen, paragraph 2 of The Act, a committee composed of at least a chairman and two members to be named The Investment Disputes Settlement Committee. This committee shall consider the disputes arising between the Foreign Investor and his Saudi partners in respect of a licensed investment under The Act. The committee shall work to settle the dispute amicably. In case an amicable settlement could not be reached, the dispute shall be settled through arbitration according to the Arbitration Act and its executive rules issued by Royal Decree No. (46) Dated 12.7.1403 H. This committee is the competent body to consider the dispute as stipulated in the Arbitration Act.<sup>24</sup>

It is clear that the text of Article Thirteen of the Foreign Investment Law is in its entirety ambiguous enough to give the executive authority (Saudi Arabian General Investment) the right to constitute a quasi-judicial committee for the settlement of investment disputes to cover the apparent deficiencies in the law which did not

<sup>21</sup> Faisal Alkahtani, Legal protection of foreign direct investment in Saudi Arabia (Newcastle University 2009) 7.

<sup>22</sup> Foreign Investment Law 2000, Art. 13 (A – B).

<sup>23</sup> The Implementing Regulations of the Foreign Investment Law 2002, Art. 26.

<sup>24</sup> Ibid.

provide a clear means of amicable settlement of disputes on the one hand, and where the mechanism through which disputes can be resolved is not specified on the other hand.

Therefore, we believe that the Saudi regulator should reconsider the formulation of Article Thirteen of the Foreign Investment Law by adopting conciliation, mediation and arbitration as a means of resolving any dispute relating to foreign investment except for disputes governed by agreements to which the Kingdom is a party. This is because the formulation of the Article did not give the investor a guarantee in the case of dispute. Laws that protect the investor are the most important attraction of foreign capital. Therefore, it is important to review the system of foreign investment in Saudi Arabia as well as the judicial system, which is the cornerstone, where the owners of capital do not invest their money until after making sure that the judge's ruling on the dispute is based on the law and not on his personal judgement. In addition, we do not see a need to distinguish between the disputes to which the government is a party and those that arise between investors and their partners or between investors and other national institutions or citizens who have contracted with the investors.

With regard to Article Twenty-six of the Implementing Regulations of the Foreign Investment Law, it is to be hoped that the executive authority consider the legislative pyramid<sup>25</sup> or the legislative hierarchy where it is not permissible to form a committee that has not been mentioned by the Foreign Investment Law. It may be useful in this regard to refer here to a precedent registered by the decision of the Board of Grievances No. 1 / T of 1981 in a case dated 20/12/1979, where the principle was established by the Chamber that "The executive regulations that may be issued by the executive authority are regulations based on laws enacted by the competent authority."<sup>26</sup> Such regulations shall be limited by detailed rules for their implementation and may not be added to, modified or exempted from implementation, unless the law itself shall have been suspended; nor is it permissible to add any new provision to such regulations that is not provided by the law".<sup>27</sup>

## 8. Legal Challenges Facing FDI in Saudi Arabia

FDI in Saudi Arabia is still in its formative stage and faces a number of legal challenges that need to be addressed to enable it to continue its rapid expansion. These important legal challenges facing the FDI in Saudi Arabia are identified as follows:

The first legal challenge facing FDI in Saudi Arabia is an absence of coordination between the Foreign Investment Law 2000 and the Companies Law 2015 in Saudi Arabia with regard to the merger of commercial companies in the *Tadawul*. The foreign investor may contribute to a listed company in the *Tadawul* but a problem

<sup>25</sup> The legislative pyramid refers to the arrangement of legal rules or legislative instruments from top to bottom in accordance with the authority that issues them, and with the necessity of adhering to this arrangement. The legislative pyramid, which includes the constitution, the law and the regulations, also contains international treaties, according to the legal systems of each country.

<sup>26</sup> A 'competent authority' is a person or organisation that has the legally delegated or invested authority, capacity, or power to perform a designated function.

<sup>27</sup> See the official website of the Board of Grievances, available at: <https://www.bog.gov.sa/ScientificContent/JudicialBlogs/Pages/default.aspx>, [Accessed 15 November 2017].

arises when the company he has merged with is merged into another company. When reviewing the relevant laws such as the Foreign Investment Law, the Companies Law and the Commercial Court Law, there are no legal articles that protect the foreign investor in the case of the merger of the commercial company to which he has contributed, where the Foreign Investment Law and its executive regulations and the Commercial Court Law did not address the merger in all their articles. As for the Companies Law, it addressed the merger in Part Eight under the title of Company Transformation and Merger in two chapters concerning Article 187 to 193. Chapter One talked about the transformation of companies, and the second chapter was about the merger of companies. All the articles in Chapters One and Two in Part Eight of the Companies Law did not address the foreign investor in the case of the merger of commercial companies and how such an investor can be protected in accordance with the Saudi law.

It is recommended to amend Articles 187-193 of Chapter One and Two in Part Eight of the Companies Law in order to cover a wider range of foreign investor issues, such as the merger of commercial companies and how foreign investors can be protected in accordance with the Saudi law. In addition, it is necessary to coordinate between all laws and regulations related to foreign investment by the Ministry of Commerce and Investment so as to avoid conflict between them. The recommendation is that the Foreign Investment Law is considered the basic law for foreign investment and then the Companies Law. The current Foreign Investment Law needs some articles to be added to cover disputes over foreign investment in the case of the merger of commercial companies in the *Tadawul* in Saudi Arabia.

The second legal challenge is multiple authorities. Generally, SAGIA is considered the authorizing body for issuing investment licences to foreign investors and coordinating with other pertinent government agencies under the Foreign Investment Law. Its objective is to achieve economic growth by creating a pro-business environment, providing services to investors and fostering investment opportunities in key sectors of the economy, including energy, transportation, ICT, and knowledge-based industries.<sup>28</sup> SAGIA is the supervisor of foreign investment in normal circumstances, but when the merger is of two commercial companies, the jurisdiction will be transferred to the Capital Market Authority (CMA).<sup>29</sup>

The functions of the CMA are to regulate and develop the Saudi Capital Market by issuing the required regulations and rules for implementing the provisions of the Capital Market Law. It also regulates and monitors the work and activities of parties subject to the control and supervision of the Authority.<sup>30</sup> The basic objectives of the CMA are to create an appropriate investment environment through issuing required

<sup>28</sup> See the official website of the Saudi Arabian General Investment Authority (SAGIA), available at: <https://www.sagia.gov.sa/en/pages/default.aspx>, [Accessed 18 November 2017].

<sup>29</sup> The CMA was established under Article 4 of the CML, issued by Royal Decree No. M/30 dated 2 July 2003, to regulate and develop the capital market activities in Saudi Arabia. The CMA is as an independent authority directly linked with the Prime Minister, and it has financial and administrative autonomy. It is governed by a board of five full-time members appointed by the King under Royal Decree.

<sup>30</sup> See the official website of the Capital Market Authority (CMA), available at: <http://www.cma.org.sa/En/AboutCMA/CMALaw/Pages/Ch2Article5.aspx>, [18 November 2017].

rules and regulations, reinforcing the transparency and disclosure standards of all listed companies, boosting confidence, and protecting investors and dealers from illegal acts in the market.<sup>31</sup> The CMA is empowered under Article 5 of the CML to issue the required rules and regulations to create a conducive environment for the growth of investment activities in Saudi Arabia.<sup>32</sup>

It is clear from the above that there are two independent authorities, SAGIA and CMA, that are specialised in the case of the merger of two commercial companies where a foreign investor has shares in one of them. This conflict of jurisdiction will cause concern to foreign investors about the legal environment in which they will invest their money. The problem of conflict of jurisdiction entails the issuance of conflicting judgments, as well as the expenses incurred by the foreign investor, repetition of the proceedings, waste of time, and presenting the same case to two authorities or two courts at the same time, which leads to an increased burden on the judiciary without justification. This is in the case of a conflict of jurisdiction between two independent authorities of the disputes settlement committees. However, if the conflict of jurisdiction is between the *Shariah* courts and the courts of the Board of Grievances or any other body, there is a legal regulation in this regard.

The Saudi Law of Judiciary 2007 has assigned the task of adjudicating jurisdiction between the *Shariah* courts and the courts of the Board of Grievances or any other body to a committee headed by a member of the Supreme Council of the Judiciary. The law provides for the formation of a committee consisting of three members: a member of the Supreme court chosen by the president of the court, a member of the Board of Grievances or the other body chosen by the president of the court or the head of the authority, and a member of the full-time judges who are members of the Supreme Judicial Council. This member is to be chosen by the President of the Council and shall be the Chairman of this Committee. The Committee is also competent to adjudicate the dispute arising in connection with the execution of two contradictory final judgments, one issued by a *Shariah* court and the other by a court of the Board of Grievances.<sup>33</sup>

The recommendation in this regard is the adoption of a unified authority dealing with issues of foreign investors. The Saudi Arabian General Investment Authority (SAGIA) is considered to be the responsible authority for all matters related to foreign investment in Saudi Arabia in order to avoid conflict of jurisdiction between SAGIA and other authorities such as the CMA. SAGIA should coordinate with the relevant authorities to resolve all disputes related to foreign investment.

The third legal challenge is that there are no specialised commercial courts to look into commercial issues including foreign investor issues in Saudi Arabia. Currently, the Investment Disputes Settlement Committee in the Ministry of Commerce and Investment, which is composed of at least a chairman and two members, is responsible for looking into issues related to foreign investor disputes.<sup>34</sup> The problem

<sup>31</sup> See the official website of the Capital Market Authority (CMA), available at:

<http://www.cma.org.sa/En/AboutCMA/Pages/default.aspx>, [18 November 2017].

<sup>32</sup> Kabir Hassan and Mervyn Lewis & Michael Mahlknecht, *Islamic Capital Markets: Products and Strategies* (John Wiley & Sons 2011) 102.

<sup>33</sup> Law of the Judiciary & Law of the Board of Grievances 2007, Art. 27.

<sup>34</sup> See the official website of the Saudi Arabian General Investment Authority (SAGIA), available at:

is that this committee, known as a quasi-judicial committee, does not have binding force to implement the provisions or the decisions issued by it, and its decisions are not conclusive because it is not a *Shariah* court. In addition, it is linked with the Board of Directors of the Ministry of Commerce and Investment, and as such is not an independent judiciary.

Initially, the Board of Grievances took over the task of adjudicating commercial cases from the beginning of 1998 by issuing Royal Decree No. 63 dated 23/07/1987 and Cabinet Resolution No. 241 dated 23/06/1987, and the powers of the commercial dispute resolution bodies have been transferred to the Board of Grievances since the beginning of the fiscal year (1998). To date, this task has been carried out until the completion of the process of removing the commercial and commercial appeals chambers of the Board of Grievances to the *Shariah* public courts. Royal Decree No. (10827) dated 02/12/2016 approved the removal of the Department of Commercial Courts in the Board of Grievances from the general judiciary on 21/09/2017, in order to establish Commercial Courts.<sup>35</sup>

Under Article Twenty-Two of the Law of the Judiciary and the Law of the Board of Grievances issued by Royal Decree No. M/78 dated 1 October 2007, the Commercial Court shall be composed of specialised chambers. Each Chamber shall be composed of one or more judges, as determined by the Supreme Judicial Council.<sup>36</sup>

According to Article Thirty-five of the Law of Procedure Before *Shariah* Courts, issued by Royal Decree No. M/1, dated 25 November 2013, Commercial Courts will have jurisdiction overall original and corollary commercial disputes between merchants; lawsuits filed against a merchant due to his original commercial activities or an activity related thereto; disputes between partners in partnerships; all lawsuits and violations relating to commercial laws, without prejudice to the jurisdiction of the Board of Grievances; lawsuits of bankruptcy and imposition of interdiction on bankrupt persons and removal thereof; and other commercial disputes.<sup>37</sup>

As a result of the above, there are two issues: the first is that the commercial courts have not yet started their functions since the Law of the Judiciary issued in 1 October 2007, although the Minister of Justice has consistently promised to open three primary commercial courts in the three main cities of Riyadh, Jeddah and Dammam. This delay would not help promote a business climate built on trust nor expedite the resolution of commercial disputes by foreign investors.

The other issue is that the Law of the Judiciary and the Law of Procedure Before *Shariah* Courts did not address the issue of commercial disputes related to foreign investors and therefore the legal challenge remains that in the case of opening commercial courts in Saudi Arabia, these courts will not consider the cases of foreign investors because it is not within their jurisdiction under the Law of the Judiciary and the Law of Procedure Before *Shariah* Courts.

The recommendation is to establish specialised commercial courts to look into commercial issues, including foreign investor disputes in Saudi Arabia, taking into

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<https://www.sagia.gov.sa/en/pages/default.aspx>, [Accessed 18 November 2017].

<sup>35</sup> Ibid.

<sup>36</sup> Ibid.

<sup>37</sup> Law of Procedure Before *Shariah* Courts 2013, Art. 35.

account that such courts could benefit from the current committee (the Investment Disputes Settlement Committee in the Ministry of Commerce) for its experience throughout the previous period. In addition, the jurisdiction of such commercial courts should include foreign investor issues with their jurisdiction to avoid any conflict of jurisdiction.

The final legal challenge is that where an amicable settlement could not be reached to settle a dispute arising between a foreign investor and others, the dispute should be settled through arbitration according to the Arbitration Act and its executive rules issued by Royal Decree No. (46) Dated 24/04/1983.<sup>38</sup> The challenge here is that the rules of arbitration in Saudi Arabia are governed by Islamic law (*Shariah*) for several considerations.

According to the famous rule, “agreements must be kept”, which is considered a basic principle of both civil and international law, conventional arbitration adopts the principle of the freedom of the parties to choose the law applicable to the subject of arbitration and therefore adopts this rule, whilst in Saudi Arabia, the arbitrator is committed to the implementation of the provisions and rules of *Shariah*. According to Article 1 of the Basic Law of Governance, the Kingdom of Saudi Arabia is a fully sovereign Arab Islamic State; its religion is Islam and its constitution is the *Quran* and the *Sunnah*.<sup>39</sup> In addition, Article 7 reaffirms that the government derives its authority from the *Quran* and the *Sunnah*, both of which govern all administrative regulations of the state.<sup>40</sup> The Basic Law of Governance confirms that the state’s role is to protect the principles of Islam and to enforce its *Shariah*.<sup>41</sup> Article 67 of the Basic Law of Governance stipulates that the legislative authority shall have the jurisdiction of formulating laws and rules in accordance with the principles of Islamic *Shariah*.<sup>42</sup> The problem is not in Islamic law or *Shariah* but lies in that there are four Sunni schools of jurisprudence represented by four Imams: Imam Abu Hanifa, Imam Malik ibn Anas al-Maliki, Imam Muhammad ibn Idris al-Shafi’i and Imam Ahmad ibn Hanbal.<sup>43</sup> Each of these schools derives its provisions from the evidence of the primary sources, which are the *Quran* and *Sunnah*, in accordance with the rules and principles of Islamic jurisprudence. Generally, there is agreement among the scholars of the Islamic faith and the primary sources. However, there are different views among them in the secondary sources, such as commercial transactions and Islamic commercial jurisprudence known as *fiqh al-muamalat*.<sup>44</sup>

Based on the above, judges and arbitrators in Saudi Arabia are committed to follow *Shariah* law, but the problem is that there are several different views in Islamic jurisprudence, especially in commercial transactions and therefore the judges and arbitrators may judge according to each one’s particular doctrine, while another arbitrator judges according to another doctrine and this undoubtedly creates hesitation for foreign investors, and leads to the justification that the legal environment

<sup>38</sup> The Implementing Regulations of the Foreign Investment Law 2002, Art. 26.

<sup>39</sup> Basic Law of Governance 1992, Art. 1.

<sup>40</sup> *Ibid.*, Art. 7.

<sup>41</sup> *Ibid.*, Art. 23.

<sup>42</sup> *Ibid.*, Art. 67.

<sup>43</sup> Hans Visser, *Islamic Finance: Principles and Practice* (Edward Elgar Publishing Limited 2009) 15.

<sup>44</sup> Abdur Rahman Doi, *Shariah: The Islamic Law* (Ta Ha Publishers Ltd 1984) 85.

for foreign investment in Saudi Arabia needs to be codified, especially in matters of commercial transactions. Therefore, it is necessary to provide a stronger legal framework for settling the disputes of foreign investors in Saudi Arabia in order to avoid judgments that are issued by judges and arbitrators according to their personal readings of Muslim texts, especially since there are several different Islamic doctrines. In addition, the absence of a clear and legal codification of the provisions of Islamic law in matters of transactions leads to the justification for excluding the application of *Shariah* in the international community. The following is an example of a case which shows that English courts do not consider *Shariah* principles in commercial transactions disputes:

In *Shamil Bank of Bahrain v Beximco Pharmaceuticals Ltd (2004)*, the facts of the case are summarised as follows. The Shamil Bank entered into a *murabaha* agreement with Beximco whereby Beximco agreed to purchase commodities from the bank on the basis of deferred payments, which previously the bank had purchased on its behalf. The applicable law in the case of a dispute arising is English law but with a condition precedent that the *murabaha* agreement must be consistent with the principles of *Shariah*. The agreement contained the following choice of law provision:

*"Subject to the principles of the Glorious Shariah, this Agreement shall be governed by and construed in accordance with the laws of England."*<sup>45</sup>

When the defendant (Beximco) failed to make payments under the agreement, the bank claimed the amount outstanding through the High Court in London and applied for a summary judgement under the agreement. The defendant argued that the obligations on them were enforceable only if valid under both *Shariah* and English law. Beximco argued further that the *murabaha* arrangements were merely a disguise for an interest-bearing loan, which is prohibited and unenforceable under *Shariah*.<sup>46</sup> According to the judge in the first instance, English law does not recognise *Shariah* law as a valid source of law to govern a commercial contract in the sense that Islamic financial contracts could not be governed by Islamic law in the UK even if so specified in the contract. The judge further held that there was no scope for the *Shariah* law to apply as there could not be two separate systems of law governing a transaction. Further, it would be impossible for an English secular court to apply religious principles in determining a dispute. The Beximco appeal was rejected by the English Court of Appeal because the 1980 Rome Convention on the Law Applicable to Contractual Obligations allows only one system of law, from a particular country, to govern a contract. The appellate court held that the reference to the "Glorious *Shariah*" in the governing law clause was merely intended to reflect the Islamic religious principles according to which the Bank held itself out as doing business, and thus it was not a system of law to displace English law.<sup>47</sup>

The recommendation here is the adoption of legal codification of the provisions of Islamic law in matters of transactions in order to protect the rights of foreign investors in Saudi Arabia where the codification of the provisions of *Shariah* will not

<sup>45</sup> Rodney Wilson, *Legal, Regulatory and Governance Issues in Islamic Finance* (Edinburgh University Press 2012) 32-33.

<sup>46</sup> Julio Colon, 'Choice of Law and Islamic Finance', *Texas International Law Journal* (2011) 46 (3) 414.

<sup>47</sup> *Ibid.*

allow judgments to be issued based on independent reasoning (*Ijtihad*) or personal readings of Muslim texts by judges or arbitrators taking into account when codifying Islamic law that there is no conflict with the UNCITRAL Model Law on International Commercial Arbitration because foreign investors favor applying arbitration instead of national laws.

### Conclusions

This article has provided a background of the Foreign Direct Investment (FDI) in Saudi Arabia, its inception, concept and mechanism, practices, challenges and dispute resolution mechanisms. It also reviewed the common types of merger of commercial companies in Saudi Arabia and its regulatory framework. This article has discussed and examined whether the current Saudi laws provide adequate legal protection for foreign investors in the case of the merger of commercial companies in the Saudi Arabian Stock Exchange (*Tadawul*) in Saudi Arabia. It has also analysed the basic laws of Foreign Direct Investment (FDI) in Saudi Arabia. The last section analysed the obstacles and challenges that face FDI in Saudi Arabia from the legal point of view, and their possible solutions.

The researcher found that the Foreign Investment Law, the Companies Law and the Commercial Court Law do not provide adequate legal protection for foreign investors in the case of the merger of commercial companies in the *Tadawul* in Saudi Arabia. The researcher also found that there are no Articles in the Foreign Investment Law, Companies Law and Commercial Court Law that protect foreign investors in the case of the merger of commercial companies in Saudi Arabia. It also found that there are two independent authorities, SAGIA and CMA, that specialise in the case of the merger of two commercial companies where a foreign investor has shares in one of them. The researcher further found that there are no specialised commercial courts to look into commercial issues including foreign investor issues in Saudi Arabia, and currently the Investment Disputes Settlement Committee in the Ministry of Commerce and Investment is responsible for looking into issues related to foreign investor disputes. Finally, the rules of arbitration in Saudi Arabia are governed by Islamic law (*Shariah*) for several considerations.

The researcher recommended that Articles 187-193 of Chapter One and Two in Part Eight of Companies Law should be amended in order to cover a wider range of foreign investor issues, such as the merger of commercial companies and how foreign investors can be protected in accordance with Saudi law. It is recommended that a unified authority should be adopted that deals with issues of foreign investors, instead of having two independent authorities. The recommendation in this regard is to adopt SAGIA as the only authority that is responsible for all matters related to foreign investment in Saudi Arabia. The researcher recommended that a specialised commercial court should be established to look into commercial issues, including foreign investor disputes in Saudi Arabia. The final recommendation is to adopt the legal codification of the provisions of *Shariah* in matters of transactions in order to protect the rights of foreign investors in Saudi Arabia.

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