

# Special Economic Zones In The Kingdom Of Saudi Arabia

Fadi Daher

f.daher@tamimi.com

The purpose of this article is to provide a general overview of the establishment of the Economic Cities (ECs) under the authority of the Saudi Arabian General Investment Authority (SAGIA) and information on key issues including land ownership and employment issues. The article also discusses implications of ECs and the specific incentives offered by SAGIA and the establishment of business operations in ECs.

For reasons that will become clear below, we note that many areas of the applicable regulations to ECs are uncertain, evolving or subject to change.

## ECs sites and objectives

The following are the ECs that are at the development stage:

1. King Abdullah Economic City (KAEC) is located mid-way between Makkah and Madinah and the commercial hub of Jeddah. It encompasses some 168-180 square kilometres, equivalent to around 65 percent of the total area of the emirate of Ajman in the UAE or about the size of the Principality of Liechtenstein. From residential complexes to resort district, KAEC seeks to establish itself as a regional transshipment center. It will comprise a seaport expected to be among the world's largest on completion.
  2. The Knowledge Economic City (KEC), situated in Al-Madinah, aims to be a regional hub for the knowledge and information market. The investment cost of the city will amount to around Twenty Five Thousand Million Saudi Riyals, creating some 20,000 job opportunities.
  3. Prince Abdulaziz bin Mousaed Economic City (PABMEC) is in Hail, 720 kilometres north of Riyadh, and is slightly smaller in land size than KAEC, covering an area of 156 square kilometres. The project cost is approximately Thirty Thousand Million Saudi Riyals or \$8 billion. PABMEC is earmarked as a land-based transport and logistics and touristic centers.
  4. Jazan Economic City (JEC) is intended to become another all-inclusive city similar to KAEC. JEC is some 725 kms. south of Jeddah and will have its own desalination plant and a power plant generating 4,000 MW of electricity. It will cover an area of 100 square kilometres or two-thirds of the entire city. Jazan is industrial in nature and will attract the investors accordingly.
- SAGIA is the regulator of the ECs in KSA.

## SAGIA status and authority

SAGIA was created under the Foreign Investment Act (FIA) in April 2000. The FIA significantly amended the foreign investment framework in the Kingdom of Saudi Arabia (KSA).

SAGIA issues licenses to foreign investors for foreign capital investment in permitted business activity in KSA, whether permanent or temporary.

Pursuant to a recommendation of the Supreme Economic Council in June 2006, by a decision of the Council of Ministers, SAGIA was specifically granted the responsibility for all activities relating to the ECs.

Before this date SAGIA was already active in the promotion of the ECs. For example, in November 2005, SAGIA entered into an agreement with Emaar Properties, under which it agreed to take certain actions to facilitate the development of KAEC. Further, with respect to PABMEC in May 2006, SAGIA signed an agreement with a regional investment holding company for the development of the project.

Generally, based on the above, SAGIA has the authority to issue licenses for the development of the ECs. The license issued by SAGIA allows the Master Developer (MD) to establish and carry out investment projects in connection with the relevant EC. SAGIA license includes the cost of the project. A MD will usually establish a Project Company (PC) to undertake the development of an EC.

The authority of SAGIA regarding ECs appears to be implicitly recognized under Saudi law. We are not aware of the publication by SAGIA of any special act or regulations applicable to the special ECs in KSA. However, we have been informed that the Economic Cities Agency at SAGIA has finalized the draft of the Economic Cities Act and legal code but has not approved it or disclosed it yet.

## **Land Ownership and Development in ECs**

### **Rights and Obligations of SAGIA and License holder**

The rights and obligations of the parties (SAGIA and MD) are covered in contractual arrangements for development. In principle, MD will enter into a Master Developer Agreement (Agreement) with SAGIA. Key obligations of a MD include the development and operation of EC and committing-on behalf of PC (under formation) - to undertake an initial public offering. As part of the private sector participation in KSA's economic growth the PC will be required to offer 30% of its issued share capital to the retail.

Under the Agreement, SAGIA generally assumes certain obligations with respect to the facilitation of EC project's development, conferring any special status on EC required for the project, and facilitating governmental and other approvals and other required actions. SAGIA will, for example, commit to facilitate (a) the registration of all foreign owned companies and other entities established in the ECs, (b) the registration of all land title deeds in the name of foreign entities established in ECs and (c) the issuance of licenses and other regulatory approvals allowing for industrial land usage within the ECs, including district cooling, warehousing, logistics and industrial park distribution ...etc.

### **Project Land Ownership in ECs**

Generally, the following chain of ownership structure has been used in some of the ECs by SAGIA: the land for the EC is acquired by the MD -chosen by SAGIA- from a governmental entity, local authority or other party that owns the land. The terms of such acquisition may vary on a case-by-case basis, for example, as to price. The MD will then transfer title to the land to the PC, for example, by an in-kind contribution on its formation. The PC will in turn transfer the land to investors under a long-term lease or develop the land for sale to third parties or retain ownership of the land and manage the developed property or enter into strategic partnerships, alliances or joint ventures for the development of components of the EC.

Similar model was contemplated by SAGIA for the MD of KAEC and PABMEC.

Note that under Royal Decree number M/15 dated 11/03/1424 (H.) corresponding to 13/05/2003 (G.), ministries, governmental agencies and other authorities (including SAGIA) may appropriate real estate for public interest purposes, subject to fair compensation being paid and such acquisition being for a project expressly contemplated in the government budget. Therefore, the land may remain in the ownership of the SAGIA but be managed by MD. In such case, there should be a clear agreement between MD and the SAGIA giving PC the ability to convey title/ownership rights to third party purchasers.

### **Rights of property ownership**

Real estate ownership in KSA for companies and individuals which are non GCC /Saudi nationals is mainly covered by the Foreign Investment Law and the Law of Non-Saudis Proprietorship and Investment of Real Estate issued by the Royal Decree 15 dated 17/4/1421H (Foreign R/E Ownership Law).

With regard to GCC Nationals Royal Decree No 4 dated 12/7/1415/H and Executive Rules (GCC R/E Ownership Law).

One of the issues is that foreign ownership of KSA property must be linked to a particular project and is not a general right.

The GCC ownership law provides that GCC nationals can own real estate in the Kingdom of Saudi Arabia ("KSA") in the following circumstances:

1. In the case of a company that is wholly owned by GCC nationals:
  - The property is allocated for the needs of the licensed business activity and determined by the competent authority;
  - The size of the property is appropriate for the needs of the licensed activity in KSA as determined by the competent authorities;
2. In the case of an individual who is a GCC national:
  - The individual (unless determined otherwise by the competent authority) owns no more than 3000 square meters;
  - The property is owned as a residence for himself and his family;
  - Is naturalized and may be the subject of a stipulation by the competent authority that at least 5 years has elapsed before they have the right to own property.
  - If the GCC national is licensed to undertake a profession or business in KSA then the restrictions in the case of a company wholly owned by a GCC national apply.

The Non-Saudi Proprietorship Law entitles foreign investors to own real estate in KSA which is required for:

- the conduct of their professional, technical or economic activities,
- private residences for housing employees of a licensed project,
- residential use by individuals with normal legal residency status, or
- property development which the total cost of the project (both land purchase and construction cost) must be at least SR 30 million and invested within 5 years from the date of purchase of the land.

Even the smallest minority interest held by a non-GCC (or foreign) national will be sufficient to make a corporate entity "foreign", thus triggering the requirement for a SAGIA license.

At this stage, instead of designating areas for possible foreign ownership in the nature of free zone jurisdictions and investment zones, KSA has left the licensing of sites to the discretion of SAGIA and simply stipulated two areas where there is a prohibition on foreigners acquiring real estate, namely land within the city limits of Mecca and Al Medina Al Munawara.

### **Property lease/ownership and deed formalities**

In terms of real estate ownership in ECs, 100% foreign landownership is allowed in the ECs except for KEC in Al Medina Al Munawara. Once the investor has completed all commercial agreements with the EC developers regarding land lease and/or ownerships, the Smart Service Center (SSC) will facilitate the official property lease/ownership and deed formalities required.

Documentation requirements include the following:

- Individual Identification Set and Company Identification Set ;
- Original lease and or property sale contract(s) (between investor and city developer); and
- Copy of original contract(s). However, foreign Muslims may rent property in KEC in Al Medina Al Munawara for renewable terms of no more than two years.

### **Employment issues**

With respect to the ECs and employment matters, SAGIA offers a one-stop shop/fast track government immigration centre for ECs to deal with prompt approval and processing of visas, easing of application of labour law requirements, overseas recruitment and renewal of visa and work permits. Since the

development of an EC is considered a private project, employing Saudi citizens will be required .

The amount of information available from SAGIA on this subject is very limited.

However, we note that in the ECs, a more liberal regime will apply to employment issues than in the normal Saudi environment. However, Saudization requirements would still apply in ECs.

Further incentives offered by SAGIA:

**SAGIA offers the following incentives to investors in ECs:**

- One stop-shop/fast track government servicing centre for the city to deal with document processing, planning approvals, building permits and approvals from municipalities.
- One stop-shop/fast track government business registration centre for the city to deal with registration of businesses, incorporation of companies, approval, issue and renewal of trade and commercial licenses, approval, issue and renewal of industrial licenses and monitoring of conditions to comply with environmental guidelines.
- Within the ECs, the creation of an attractive business environment for both domestic and international businesses with respect to exemption from import duties, ownership of land and property, taxation, employment, immigration and land use.
- Each EC may choose to have a bounded zone within its designated area which may comprise an industrial zone.

**Foreign investment restrictions in the ECs:**

An understanding of foreign investment restrictions in ECs requires some background on the applicable foreign investment framework in Saudi Arabia. See generally the creation of SAGIA under the FIA discussed above.

**Negative List**

A negative list has been issued by SAGIA for some business activities that are prohibited to foreign investment. These include manufacture of military materials, equipment and explosives, oil exploration and production, services related to security, real estate brokerage, and land transportation services (excluding trains), among others. The Kingdom is currently reducing the sectors that are not open to foreign investors: retailing, telecommunications and insurance have already been removed from the list.

In a change from the previous investment law, the FIA allows foreigners 100% ownership of certain projects, as well as property required for the project itself or for housing company personnel (with the exception of real estate in Mecca and Al Medina Al Munawara-see above). Under this scheme, foreign investors are allowed to retain the same incentives, privileges and guarantees given to national companies other than taxation.

For example, projects that are 100% foreign-owned are eligible for loans from the Saudi Industrial Development Fund. Investors are also able to hold investment licenses in more than one type of activity. The law has also brought significant changes to the previous sponsorship regulations. Under the new scheme, foreign investors and their non-Saudi employees may be sponsored under a new licensed firm.

Foreign investments are protected by law and may not be confiscated wholly or partially without a court order. Moreover, such investments may not be subject to expropriation wholly or partially except in the public interest in return for equitable compensation.

SAGIA will provide all Government services through its Smart Service Center (SSC) operations. SAGIA is in the process of establishing SSC centers within the ECs offering enhanced services to investors, until the EC SSC centers are completed, all investors wishing to establish in the ECs will be serviced (60/24/7) through

existing SSC's located in all major cities within KSA. The SSC currently offers more than 128 government services and is continuously enhancing its basket services. SSC ensures a fast-track and hassle-free process for establishing a company in ECs.

#### Foreign investments – general

Generally, a license will be required from SAGIA for any such investment.

The conditions for SAGIA granting a foreign investment license include the following:

- The investment activity to be licensed should not be on the negative list – see above;
- The intended product of the company should comply with Saudi rules and regulations and other applicable laws of the European Union or the United States of America and certain other conditions;
- The applicant should be a natural person or corporate entity that intends to invest in the Kingdom;
- The foreign investor should not have been convicted in the past for substantial violations of the provisions of the FIA;
- The foreign investor should not have been convicted in the past for financial or commercial violations whether in the Kingdom or in other countries; and
- The grant of a license should not result in the breach of any international or regional agreement to which the Kingdom is a party.

Most of the above conditions are fulfilled by foreign investors relatively easily.

Foreign investors are also required to submit a declaration stating non-availability of a residency permit in KSA over the last two years. In cases where the investor has held a residency permit in KSA, a letter approved by the last investor's sponsor must be submitted stating the sponsor's non-objection to the return of the investor to KSA for the purpose of investment.

#### Corporate structures in use in ECs

An investor may choose one of several forms of business when establishing business operations in the ECs. The following are the common legal forms used in ECs:

- Branch;
- Limited Liability Company (LLC);
- Joint Stock Company (JSC); and
- Technical Scientific Services Office (TSO).

#### **Establishment process- Step by Step- at SSC**

The establishment of an investment vehicle in the ECs in whatever form will inevitably involve a number of common steps, including:

- Step 1. Obtain an investment license from SAGIA;
- Step 2. Approval of the entity's trade name and location ;
- Step 3 Obtaining Labor Office File Number (File 700);
- Step 4. Resident Manager: Obtain Residency Permit/Iqama;
- Step 5. Physical premises: Obtain Property Ownership Deed/Lease contract;
- Step 6. Approval of draft articles of association (or a Ministerial resolution for a branch);
- Step 7. Notarizing and Publishing the articles of association (Companies only);
- Step 8. Depositing the entity's paid-up capital in a local bank and issuing bank certificate;
- Step 9. Commercial Registration from the Ministry of Commerce;
- Step 10. Chamber of commerce and industry membership registration;
- Step 11. Labour Office registration;
- Step 12. Tax registration;

Step 13. Registering employer and employees for the General Organisation of Social Insurance (GOSI) contributions; and

Step 14. possibly, the role of specialised authorities/agencies such CITC or Ministry of Information.

The above entire process is serviced on a fast-track basis through SSC.

[Al Tamimi & Company's KSA office](#) is focusing on setting up foreign companies in Special Economic Cities and is currently providing legal assistance for the Master Developer of King Abdullah Financial District (KAFD).

Our KSA office is involved in the revision of all rules and instructions regulating the KAFD and most agreements and contracts between MD and other developers, contractors and companies intended on having a presence in the KAFD, such as banks and financial institutions.