

Saudi Arabia: Registration of security interests

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Background

Historically it has been difficult for financiers to register security interests over all types of asset classes in the Kingdom of Saudi Arabia ("KSA") other than in respect of specific categories of property like marine vessels, aircraft, automobiles, real estate, certain types of company shares and intellectual property.

This inability to register a security interest created by (what many Western jurisdictions would term) a "fixed charge", "floating charge", "pledge", "lien", "mortgage" or even title retention provisions like what is commonly referred to as a Romalpa Clause, has meant that financiers found difficulty in gaining comfort lending against many types of assets available in the ordinary course of a borrower's business.

As a consequence, businesses (particularly small to medium enterprises) would often be faced with situations where they were unable to sufficiently leverage off all their available assets which in turn meant that raising finance was problematic. In such situations it is understandable that financiers would require personal guarantees from business owners as well as other security that ultimately results in borrowers paying a higher cost for finance.

Recognising the importance small to medium enterprises have to the national economy, in 2004 the Ministry of Finance introduced a supporting initiative known as the "Kafalah Program". This program is managed by the Saudi Industrial Development Fund under the auspices of the Ministry of Commerce and Industry. The program provides participating banks with guaranteed repayment of up to eighty percent of a qualifying loan provided to small to medium enterprises. It is hoped that being able to register security interests will further enhance the effectiveness of this program and also facilitate lending to all businesses.

Commercial Mortgage Law

The Commercial Mortgage Law was issued by Royal Decree No. (M/75) on 1 January 2004 and its Implementing Regulations issued by Ministerial Resolution No. 6320 dated 4 August 2004 (together the "Commercial Mortgage Law").

The Commercial Mortgage Law essentially defines a commercial mortgage as the pledging of a movable asset (but not money) as security for a debt that is considered commercial in nature, in relation to the provider of the security. Therefore the security provider may either be the actual debtor or guarantor of a debtor.

The Commercial Mortgage Law originally contemplated the establishment of a Unified Centre for Lien Registration ("UCLR") that was to be maintained by the Ministry of Commerce and Industry and where security interests could be registered. However, the concept has never really progressed to its full potential. A brief start up period occurred in 2011, where for about six months the Saudi Arabian General

Investment Authority ("SAGIA") established and maintained the UCLR following an agreement with the Ministry of Commerce and Industry.

Unified Centre for Lien Registration -operational again

The UCLR has recently become operational again under SAGIA. The practical effect of this means that security interests over moveable assets can now be registered.

Assets Capable of Being Registered

The Commercial Mortgage Law provides for security over moveable assets granted to a creditor with respect to commercial debts provided that the amount of the secured debt or maximum limit is specified in the relevant security agreement.

In general terms, the assets to be secured must be:

- in existence (i.e. not future assets);
- in the possession of the debtor;
- owned by the debtor and capable of being disposed of by the debtor;
- (tradable, with details stated in the relevant security agreement; and
- identifiable without ambiguity.

It is important to note that the application form for registration of the secured asset with the UCLR contemplates registration of the following:

- "Individual Items" that can be uniquely identified (for example, cars, boats, airplanes, serial-numbered equipment); and
- "General Collateral" that does not have any unique identifying characteristics (for example, inventory and accounts receivable).

Process of Registration

Once the relevant security agreement has been entered into, a copy of the signed instrument should be lodged at the UCLR if there is no other more appropriate registering agency for the particular security interest.

The UCLR contemplates dual security registrations in circumstances where there is another registering agency for the particular asset category (like marine vessels, aircrafts, automobiles etc. mentioned previously). In these situations evidence of the existing registration must also be supplied to the UCLR.

In all cases, the above documents must be submitted together with a completed registration application form signed by the relevant creditor and debtor.

In general terms, the application form for new registration requires the following information to be supplied:

profile of the debtor which must be supplied with a copy of the debtor's identification document – like a commercial registration certificate;

- profile of the creditor;
- presenter information (that is, information of the individual who submits the application form to the UCLR);

- details and description of the collateral; and
- proof of authorisation to act – the names and signatures of the individuals authorised to act on behalf of the debtor and creditor.

Practical aspects of registration are yet to become clear. For example, whether English language documents can be registered without first being translated to Arabic and if there is a requirement for KSA company signatures to be attested at the Chamber of Commerce before being in a form that is acceptable to the UCLR. **Effect of Registration**

It is difficult to make a definitive determination on how effective the register will be and what the detriment is for failing to register. An overall assessment can be made such that registration would be evidentially beneficial in respect of a security interest and that failure to register could conceivably have dire consequences should there be a later registered security interest for that same asset. For example, take a situation where the same secured asset is subject to competing claims by numerous creditors – in these circumstances registration could make the difference with a bona fide first in time registered interest having a priority claim.

It will also be interesting to see how KSA courts deal with situations akin to a common law lien where a creditor is in possession of an asset that becomes subject of a creditor priority dispute.

Searching the Register

Only manual 'in-person' searches are currently available, although it is hoped that over time and with further development, electronic search capabilities will be introduced.

Enforcement

Generally speaking, to enforce a commercial mortgage over moveable assets requires application before a competent KSA court, after providing at least three days notice to the debtor. On satisfaction of a claim, the court will order the sale (in full or part) of the assets subject of the security. Ordinarily the sale will be by way of public auction.