

## NEW RULES FOR FOREIGN INSTITUTIONAL INVESTORS IN SAUDI LISTED SHARES

By Paul C. Homsy

Partner, Eaton & Van Winkle LLP ([www.evwn.com](http://www.evwn.com))

Saudi Arabia, after several years of consideration, has allowed foreign institutional investors to directly own publically listed shares on the Tadawul, the Saudi stock exchange (see the Rules for Qualified Foreign Financial Institutions Investment in Listed Shares (“Rules”)) issued by the Capital Markets Authority of Saudi Arabia pursuant to Resolution Number (1-42-2015), dated (15/7/1436 H) corresponding to May 4, 2015, issued pursuant to the Saudi Capital Markets Law. Prior to the Rules, foreign institutional investors could only invest in listed Saudi equities through swaps or a limited number of exchange traded funds.

The Rules contain five main provisions governing the investment by foreigners in Saudi listed stocks as described below:

1. Authorized limits on ownership by foreigners – Qualified foreign investors (“QFI”) and clients of qualified investors are entitled to full ownership rights in listed shares including the right to trade in such shares. QFIs are defined as a foreign investor which is registered with the Saudi Capital Markets Authority (“CMA”), the governing body for the Saudi stock exchange. Each QFI together with affiliates and clients which are approved by the CMA, may own up to 5% of the total listed shares of any issuer. An approved client of an approved QFI, together with its affiliates, may not own more than 5% of the listed shares of an issuer.

Total foreign ownership through swaps, QFIs or approved clients of QFIs may not exceed 49% of the total listed shares of an issuer. Multiple QFIs together with their approved clients may not own more than 20% of the listed shares of any single issuer. Total share ownership by QFIs and QFI clients may not exceed 10% of the market value of any single issuer including shares owned by swaps.

The foregoing restrictions are to be interpreted together with any limitations on foreign ownership found in the issuer’s governing documentation.

2. Qualifications for approved QFI and an approved client of an approved QFI – The Rules allow for both approved QFIs and approved clients of QFIs to purchase shares. However, it appears that approved clients of approved QFIs may only purchase and sell shares through an approved QFI and not directly. QFIs must enter into a “QFI assessment agreement” under which it appoints an “assessing authorized person” to review the application for approval and submit such application on behalf of the QFI (and its client) to the Saudi Capital Markets Authority (“CMA”). Authorized persons are covered by the Authorized Person’s Regulations and typically include Saudi companies licensed by the CMA to buy and sell securities.

A QFI must satisfy the following conditions to become a qualified QFI:

- a) Must be a bank, brokerage, or securities firm, a fund manager, or an insurance company;
- b) Must be licensed or regulated by a regulatory body that meets the standards of the CMA;
- c) Must have at least approximately \$5 billion of AUM which may be reduced to approximately \$3 billion of AUM at the CMA's discretion;
- d) Must have at least 5 years of securities investment experience.

An approved QFI cannot invest on behalf of its clients unless the client has been approved by the QFI. The client must be a financial institution that meets each of the above requirements of an approved QFI or an investment fund that is incorporated in a jurisdiction that satisfies the CMA's standards. Such client cannot be an approved QFI in its own right nor an approved client of another QFI.

3. Registration Procedures – The QFI must submit an application on the CMA's form to an assessing authorized person ("AAP"). The QFI must also submit an application to the AAP for any client it intends to invest on behalf of. The QFI must also authorize the AAP to submit the application to the CMA. The AAP must review the application for completeness and accuracy, compliance with the Rules, and must ensure that any applicant meets the preconditions described in the Rules.

When and if the AAP has received all necessary information and documents from any applicant and has accepted the applicant's application, the AAP must notify the CMA. The AAP must also supply the CMA with various information such as the identity of any applicant's affiliates, details of any criminal or regulatory sanctions, or any civil or criminal penalties or settlements made by or assessed against the applicant in the last 5 years.

The CMA must notify the AAP without delay when it has received all required applications and documents. The AAP's decision to approve the application becomes final once 5 days have passed since the CMA has notified the AAP that it has received a complete application unless it notifies the AAP that it rejects the application within said five day period. The CMA may extend this period by notification to the AAP.

Once the AAP's acceptance of the application becomes final, the CMA will register the applicant as an approved QFI. The AAP must then notify the QFI that it accepts the QFI as a client for dealing activities and the parties must sign a copy of the QFI assessment agreement which must be supplied to the CMA. Conversely, the AAP must notify the applicant if it rejects the application or the CMA decides to override the AAP's approval of the application.

4. Commencement of Trading by QFI – The QFI can start trading in listed shares once it holds a client account, holds an account with a "Depository Center", and has satisfied any other conditions imposed by the CMA.

A QFI cannot trade for any clients unless each of them has been approved by the AAP or the CMA. The approval and disclosure requirements by a QFI for an investment fund client are less than for non-investment fund clients.

5. Ongoing Disclosure and Compliance Requirements – QFIs and QFI clients are subject to ongoing compliance and disclosure requirements. QFIs must submit their annual reports and consolidated accounts to their AAP and must notify them of any material changes to the information upon which the QFI was registered with the CMA. The QFI must also notify the AAP immediately of any criminal or regulatory proceedings against it or its client or of any restructurings, material changes, and the like.

The Rules are a major development for Saudi Arabia and the global investment community. The Tadawul is the largest stock exchange in the Arab World and its most liquid market. The Tadawul contains more than 160 listed companies with a total market capitalization of over \$500 billion and has a daily trading volume of over \$2.4 billion. By opening the Tadawul to foreign investors, the Saudi Government hopes to achieve several objectives, including inclusion of the Tadawul in the MSCI index thereby increasing the exposure of Saudi listed companies to a greater level of market research and coverage, and enhancing market efficiency and transparency.