

The CMA's New Rules on the Ownership of Foreign Strategic Investors in Companies Listed on Tadawul

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In an effort to further attract foreign investment in the KSA, the Capital Market Authority ('CMA') issued the Instructions for the Foreign Strategic Investors Ownership in Listed Companies ('FSI Instructions') in June 2019. The FSI Instructions remove the foreign ownership limitations contained in the Rules for Qualified Foreign Financial Institutions Investment in Listed Securities ('QFI Rules'), with regard to persons qualifying as foreign strategic investors.

The QFI Rules

KSA has traditionally restricted foreign investment in Saudi securities. Until 2015, when the QFI Rules were introduced, it was not possible for foreign persons to directly invest in securities listed on the Saudi Stock Exchange (Tadawul). Instead, foreign investors were only able to invest in listed securities through swap agreements entered into with CMA authorised persons (i.e. entities authorised by the CMA to engage in securities business in the KSA).

Since 2015, it has been possible for qualified foreign investors ('QFIs') to directly invest in securities listed on Tadawul and exercise all rights associated with them. The QFI Rules set out the procedures, requirements and conditions for QFIs to invest in listed securities and specify the obligations of QFIs as well as the obligations of authorised persons assessing them.

In order for a foreign (i.e. non-GCC) entity to qualify as a QFI, it must be a financial institution having a legal personality and must fall in any of the following categories:

- banks;
- brokerage and securities firms;
- insurance companies;
- government and government related entities;
- investment funds;
- any other financial institution considered eligible by the CMA.

The financial institutions mentioned above must be incorporated in a jurisdiction applying regulatory and monitoring standards equivalent to those of the CMA or acceptable to it.

Furthermore, with the exception of governments or government related entities, the foreign financial institution must have assets under management or custody of at least SAR 1,875,000,000 (or an equivalent amount) – although the CMA may reduce such assets.

In order to obtain the qualification, the foreign entity must file an application with an assessing authorised person (which is an authorised person licensed to conduct ‘custody’ or ‘dealing’ activities). Such authorised person will assess the application in accordance with the procedures and criteria set out in the QFI Rules.

In terms of investment restrictions, the QFI Rules stipulate the following:

- a QFI may not own more than 10 percent of the shares or convertible debt instruments of a listed issuer;
- the maximum proportion of shares or convertible debt instruments in any listed issuer that may be owned by all foreign investors – in all categories, whether resident or non-resident, excluding foreign strategic investors pursuant to the FSI Instructions – is 49 percent;
- limitations set out in the constitutional documents of the listed companies or any instructions issued by the competent supervisory or regulatory authorities as well as any other legislative limitations on foreign ownership in joint stock companies must also be adhered to.

The FSI Instructions

The QFI Rules do not apply in relation to foreign strategic investors (‘FSIs’). A FSI, pursuant to the FSI Instructions, is a foreign legal entity that aims to own a ‘Strategic Shareholding’ in Tadawul listed companies. ‘Strategic Shareholding’ is a direct ownership percentage in the shares of a listed company, through which it is intended to contribute in promoting the financial or operational performance of the listed company.

In order for a FSI to own a Strategic Shareholding in a listed company it must:

- be established or licensed in a country that applies regulatory and supervisory measures similar to those applied by the CMA or acceptable to it;
- have a client account with an authorised person and an account with the Securities Depository Centre; and
- meet any other requirements or conditions as the CMA may require.

Given that the QFI Rules do not apply to FSIs, the ownership restrictions set out in the QFI Rules (including the 49 percent maximum limit) will not be relevant to FSIs. However, investments of a FSI will still be subject to the following restrictions:

- the limitations set forth in the constitutional documents of the listed company or any instructions issued by the competent regulatory and supervisory authorities;
- other legislative limitations on foreign ownership in joint stock companies (for instance foreign investors may not currently acquire shares in companies investing in the development of the Holy Cities of Makkah

and Madinah); and

- the FSI may not dispose of any of the shares it owns in accordance with the FSI Instructions within a period of two years after the date of acquiring such shares.

It is worth noting that the Listing Rules of Tadawul specify a minimum 30 percent float requirement for shares listed on the main market and a minimum 20 percent float requirement for shares listed on the parallel market (unless the CMA permits lower percentages). On this basis, it seems that the maximum holding limit for a FSI in any issuer listed on the main market is 70 percent of the shares and 80 percent of the shares in any issuer listed on the parallel market - subject always to any other applicable limitations as mentioned above.

Other issues to consider

Industry-specific regulators (e.g. in the area of telecommunications) may be required to provide their approval before a strategic investment is made in a listed company under their supervision. Furthermore, the General Authority for Competition may be required to assess and approve a transaction involving the shares of a listed company where this would result in an economic concentration.

Moreover, the CMA's Merger and Acquisition Regulations provide that the CMA has the right to require an investor acquiring over 50 percent of a given class of listed shares carrying voting rights, to make a mandatory bid for all shares of the same class in the target.

Conclusion

By introducing the QFI Rules in 2015 and the FSI Instructions in 2019, KSA has taken significant steps towards reducing regulatory obstacles to foreign investment in KSA listed companies. A testament to the continuous efforts of KSA to modernise its stock market is the recent debut of Tadawul in the emerging markets indexes of FTSE Russell, S&P Dow Jones and MSCI. It is expected that these developments will further boost foreign investment in the Saudi market.

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