

Finance Companies Law in the Kingdom of Saudi Arabia

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Since these laws are largely related to the real estate finance industry, many call them the real estate finance laws. This article discusses the developments that have occurred in the finance environment generally and it also discusses the key points in relation to finance companies.

Finance Environment:

To date there appears to be little changes in the manner of providing finance in Saudi Arabia. Most of the finance products are provided by Saudi banks have remained as they were before the new finance laws were introduced. However, lease finance and the structure of Murabaha (a method of Islamic financing) seem to be the most popular financing techniques used.

Finance Companies:

Following the issuance of finance laws, only a small number of finance companies have been incorporated. Most of these are real estate finance companies and ones which provides lease finance along with small and mid-size project financing.

Legal Environment:

In order to carry out a finance business, a license must be obtained from the Saudi Arabian Monetary Agency ("SAMA"). This is a pre-requisite before incorporating any entity that is to engage in the provision of financing, whether it be real estate finance or micro-finance activities.

The form of the legal entity must be a closed joint stock company; as a consequence, there must be at least five founding shareholders.

Unlike limited liability companies which are usually managed directly by its owners, a joint stock company is managed by a board of directors which is elected by the company shareholders in a general assembly.

Similar to banking and insurance activities, SAMA also has conservative policies towards the finance industry. For example, the approval of SAMA is required in order for the company to be incorporated and then SAMA maintains a supervisory role over transactions and contracts the finance company is involved in. Also, SAMA must approve the appointment of the directors of the board and senior executives, as well as the actual products to be issued by the finance company.

Further, the supervision of SAMA extends to limiting the maximum amount that the finance company can provide as a finance; restricting the finance company from entering into certain transactions; and determining the minimum security that the finance company should obtain.

The Law on Supervision of Finance Companies (Royal Decree No. M/51 dated 13/8/1433 H(2 July 2012 G) provides that the finance company can be licensed for one or more types of finance activities. The types of

finance are:

- real-estate finance
- productive assets finance
- small and medium enterprises finance
- credit card finance
- consumption finance
- micro finance.

However the Implementing Regulations of the Law on Supervision of Finance Companies provides that neither a real estate finance company nor a micro finance company can carry out more than one finance activity.

The license to be issued by SAMA should specify the type of finance(s) the company intends to provide and may limit the finance company to run its business within a specific geographical territory in the Kingdom. The license should be for five years renewable.

Finance Company Capital:

The share capital of finance companies varies according to the finance type practiced. For example, the capital of micro finance companies must not be less than ten million riyals (USD 2.7m), the capital of real-estate finance must not be less than two hundred million riyals (USD 53m), while other types of finance companies practicing other activities (except for the real-estate finance company and the micro finance company) must have a capital of not less than one hundred million riyals (USD 27m).

Under the Law on Supervision of Finance Companies it seems that a finance company may not fully be owned by foreign investors. However, the law does not specify the maximum limit of such foreign ownership although after considering the case in banks and insurance companies it is likely that the percentage may not exceed 49% of the company shares.

Requirements for Incorporating Finance Companies:

There are various requirements to incorporate a finance company, most importantly:

- Filling out a license application form approved by SAMA
- Providing a copy of the finance company articles of association and bylaws in line with SAMA's template.
- Providing a description of the finance company structure including the main departments and the main functions of each department.
- Completing a Form of Appropriateness stipulated by SAMA for each shareholder and each director.
- Providing a feasibility study.
- Providing a business plan.
- Providing a bank guarantee of an amount equal to the maximum amount that the company is intending to carry for finance activities.
- Providing a copy of the proposed arrangements with third parties.

The template of the articles of association and bylaws proposed by SAMA are almost the same as the ones current issued by the Ministry of Commerce and Industry except that SAMA's versions indicates that there must an executive committee within the board of directors of the finance company.

The incorporation of a finance company must start with SAMA approvals before being forwarded to the other regulatory authorities such as the Ministry of Commerce & Industry and the Saudi Arabian General Investment Authority in cases where there is non-GCC shareholding in the finance company.

SAMA is required to respond to the license applicant within sixty days of an application being submitted. The response could be positive, negative or requesting further matters to be provided or further

clarifications. If the response is positive, the applicant must complete the incorporation of the finance company within six months from the issue date of SAMA's preliminary approval, although this may be renewable for another period of no more than six months.

The development and regulatory regime of the finance industry in the Kingdom is still in its early stages and it may take a decade to have a more mature industry, bearing in mind that the law provides that each finance company must have a Shari'ah committee to ensure that the company operates its business in compliance with Shari'ah. As a result there is likely to be differing opinions issued by these Shari'ah committees acting for the various finance companies.

Also, the formation of the judicial committee mandated with resolving disputes arising out of the finance contracts or the violation of finance laws is yet to be formed. It is likely to take a considerable period of time to set the principles governing the settlement of finance disputes.