

The Road to Saudi Vision 2030: A Glimpse into the Saudi Capital Markets

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As part of its Vision 2030, the Kingdom of Saudi Arabia ('KSA') has launched its 'Financial Sector Development Program' which seeks to develop the financial sector as a diversified and efficient financial services sector underpinned by three main pillars, one of which is the objective of developing an advanced capital market.

Indeed, whilst the KSA is noted for having the second largest proven oil reserves in the world, Vision 2030 recognises the importance of reducing the country's dependence on the energy sector by encouraging economic diversity and foreign investment.

To support this, the KSA has enthusiastically adopted new laws and regulations in order to attract investors to participate in its capital markets. Such new rules and regulations will assist the Saudi capital markets in general but they will also specifically facilitate the proposed Initial Public Offering ('IPO') of Saudi Aramco, where the anticipated listing of five percent of its shares is estimated to raise \$100 billion, which would make it the largest IPO in history in the event that it proceeds.

Although the KSA is well known for its strength in the energy sector globally and its banking activities, the Saudi capital markets are arguably the deepest and most liquid in the Middle East. The Saudi Stock Exchange, the Tadawul, is the largest stock exchange of the Gulf Cooperation Council ('GCC') countries offering trading platforms for equities, Islamic bonds, exchange-traded funds and mutual funds. The Tadawul is currently the sole stock exchange in the KSA and is under the supervision of the Saudi Capital Markets Authority ('CMA') which reports directly to the Prime Minister.

During the course of the past two years, the CMA and the Tadawul have issued a number of regulations, in order to realise the objectives of Vision 2030 and build on the success of its equity capital markets. This also reflects the requirements of the Transition and Activation of Responsibilities Project which is designed to activate the Tadawul's responsibility for supervising and regulating certain aspects of the Capital Markets Law. The Tadawul is now responsible for supervising and regulating the listing of securities and continuous disclosures (regarding timing, format and the mechanism of disclosure) of issuers and market participants, while the CMA is in charge of regulating offers of securities and continuous obligations.

In this article, we shall briefly shed light on some of the interesting legal and regulatory changes that were introduced to the Saudi legal and regulatory financial services regime as part of realising the Financial Sector Development Program objectives.

The Offering Rules

On 27 December 2017, the CMA issued the new Rules on the Offer of Securities and Continuing Obligations ('Offering Rules'). These Rules address the offering of securities in the KSA, being: (a)

the issuing of securities; (b) inviting the public to subscribe for securities or the direct or indirect marketing of securities; and (c) any statement, announcement or communication that has the effect of selling, issuing or offering securities. In addition, any offer of securities to the public in the KSA must also comply with the Listing Rules issued by the Tadawul.

The focus of the Offering Rules is the promotion of transparency and the assurance that sufficiently detailed and appropriate disclosures are made to the public to enable investors to make an informed decision as to whether or not to invest. For example, when conducting an IPO, the Offering Rules require the inclusion of certain mandatory information about the issuer to be included in the prospectus when submitting an application to register shares, including a directors' statement to assume full responsibility for the accuracy of information set out in the prospectus. This statement gives potential investors the comfort that reasonable diligence has been exercised when extracting/retrieving the required information for the purpose of the prospectus.

Also, in order to promote transparency and a fully informed market, issuers are under an obligation to make certain disclosures on an ongoing basis. For example, an issuer is under an obligation to disclose material developments which: (a) are not known to the public; (b) may affect the assets and liabilities or financial position or the general course of business of the company or any of its subsidiaries; or (c) may affect the price of the listed securities or affect the issuer's ability to meet its commitments with regard to listed debt. Material information would comprise, for example, any losses equal to 20 percent of the issuer's net assets according to the latest financial statements or any disputes where the value involved is equal to or more than five percent of the net assets of the issuer according to the latest financial statements.

Moreover, in order to avoid unexpected leakage of confidential information, an issuer is always under the obligation to take reasonable measures to manage the disclosure of material information and developments before disclosing them to the public.

The Listing Rules

The Tadawul published its revised Listing Rules on 22 October 2018, which follow international standards, for example, on takeovers and delisting. To address market requirements, the Listing Rules include specific provisions relating to reverse takeovers and demergers, including valuations, announcement of takeovers and conditionality.

To promote liquidity, the Tadawul requires a minimum value of shares to be listed. The expected aggregate market value of all the shares to be listed, at the date of listing, should be at least SR 300 million and a minimum of 30 percent of shares must be publicly available.

The Listing Rules also address the requirements of minority shareholders. The CMA can suspend the trading of securities or cancel their listing, if, amongst other things, the announcement of a reverse takeover contains insufficient information about the transaction. This avoids the situation where a strategic investor or a majority shareholder might have more access to information about the transaction and, hence, are in an advantageous position compared to other individuals that would be dragged into a takeover without having adequate information to be able to participate thereon.

Corporate Governance

One of the key lessons learned from the 2008-2009 global financial crisis was the importance of

adopting corporate governance best practices. Regulators are aware that adequate corporate governance rules are required to ensure appropriate reporting, accountability and the management of conflicts of interest by issuers. Such rules need to follow international best practice but to be effective require: (a) proper enforcement of the rules; and (b) a change in the mindset of issuers to ensure that corporate governance is not just a 'tick-box' exercise but a way of organising and running the company (a mindset shift).

The CMA's new corporate governance rules were issued on 13 December 2017 and address shareholders' rights, including matters relating to general assembly meetings, the composition and functions of board committees and their relationship with the board of directors. Also, the corporate governance rules regulate the formation of the board of directors, its responsibilities and competencies, how it undertakes its activities as well as the avoidance of conflicts of interests, given that the board of directors is expected to act in the best interests of the issuer and not itself or shareholders it may represent.

Members of the board are not only under a duty to disclose conflicts of interest but, also, the board must annually evaluate the extent of the board members' independence and ensure that there are no situations or circumstances that may affect his/her independence.

In addition to the above, issuers are under a statutory duty to maintain a conflict of interest policy. In this context, the new corporate governance rules set out minimum standards and information that must be included under such policies, such as the requirement to adopt clear procedures addressing situations when a company transacts with a related party, including notifying the CMA and the public of the related party transaction, in the event the transaction is equal to or exceeds one percent of the company's total revenues in its last annual audited financial statements.

Conclusion

Saudi Arabia has made promising and positive steps towards modernising and strengthening its capital markets through developing its securities laws and regulations. This should assist the prospects of a diversified and effective financial services regime as aspired to in Vision 2030.

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