

# **Investment Laws in Saudi Arabia: Restrictions and Opportunities**

**By**

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## DECLARATION

“I, Hussain Naser Agil, declare that the PhD thesis entitled “Investment Laws in Saudi Arabia: Restrictions and Opportunities” is no more than 100,000 words in length including quotes and exclusive of tables, figures, appendices, bibliography, references and footnotes. This thesis contains no material that has been submitted previously, in whole or in part, for the award of any other academic degree or diploma. Except where otherwise indicated, this thesis is my own work”.

Signed.....

Date.....

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## **Abstract**

The Kingdom of Saudi Arabia follows the holy *Qur'an* as its Constitution, and virtually every sphere of human activity is governed by the *Shariah*. Owing to the particular nature of the tenets of *Shariah*, several forms of business activity are held to be illegal and forbidden, including anything that pertains to gambling, pornography and alcohol. Moreover, the *Shariah* has its own code with regard to loans and investments, and the charging or paying of interest are both prohibited.

Foreign direct investment (FDI) is almost universally regarded as significant for the growth of an economy. Nations vie with one another to attract FDI from multinational corporations. Numerous studies have suggested a link between FDI and the growth rate of the GDP or gross domestic product of a nation. Globalisation has caused a marked degree of homogeneity in the world economy and the Kingdom of Saudi Arabia offers various business opportunities to foreign investors. However, the intricacies of the workings of the *Shariah* need to be clearly understood by overseas investors.

In this thesis, an attempt is made to study the investment climate of the KSA, and to explore the various key factors of the *Shariah*, the desirability of FDI for development, the forces of globalisation, and the mechanisms by which the KSA can uphold its laws as well as profit from an increasing infusion of funds by overseas investors. The research yields several interesting insights into various aspects of the KSA investment climate, and concludes with a series of recommendations that are designed to reconcile the apparently conflicting interests and pressures.

## **ABBREVIATIONS INDEX**

ADR – Alternative Dispute Resolution Mechanism

DLA- Defense Logistics Agency

EU – European Union

FTA – Free Trade Area

GCC – GULF Corporation Council

ICSID – International Centre for Settlement of Investment Disputes

IFC – International Finance Corporation

IAs – International Investments Agreements

KSA – Kingdom of Saudi Arabia

H - Hijri (Arabic Calendar)

MENA – Middle East and North Africa states

MIGA – Multilateral Investment Guarantee Agency

OPIC – Overseas Private Investment Cooperation

SAMTCO - Saudi Arabia Maritime Tankers Co

SAGIA – Saudi Arabian General Investment Authority

SATCO – Saudi Arabia Maritime Tankers Co

SEC – Saudi Electricity Company

ECT - Energy Charter Treaty

SNCC – Saline Water Conversion Corporation

TSOS – Technical and Scientific Offices

UNCTAD – United Nations Conference for Trade and Investment

RD - Royal Decree

IWWPs - Independent Water and Power Projects

SABIC - Saudi Arabian Basic Industries Corporation

SIDF - Saudi Industrial Development Fund

CMA - Capital Markets Authority

ICT - *Information and Communication Technology*

TSOs - Technical and Scientific offices

SR- Saudi Riyal

\$ - United States Dollars

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## **Chapter 1: Introduction:**

In the KSA legal system, the constitution of the Kingdom of Saudi Arabia is the Qur'an, which is the Book of God. In other words, the laws governing aspects of life in the country are based on the basic tenets of Islamic principles. According to the Islamic faith, equality and fairness should be applied in all aspects of life. Therefore, any business transaction in the Kingdom follows Sharia law, including investments by foreigners in the Kingdom. As a matter of fact, laws governing all forms of investments are promulgated as subordinate laws to the constitution. This law recognises Qur'an and Sunnah, which are the basis for the governing of business transactions in the Kingdom.<sup>1</sup>

Sharia law prohibits certain forms of investment that may be contrary to the Islamic faith. It is therefore obvious that investors are prohibited from engaging in any business activity that involves gambling, pornography and alcohol. Furthermore, the Sharia law prohibits any investment that charges interest because it is believed that the risk should be distributed equitably between the investors and the public because profit should be shared equally. All these factors affect investments in the Kingdom of Saudi Arabia.

### ***1.1 A study of investment climate in Saudi Arabia- Opportunities and Restrictions***

Saudi Arabia is one of the more sought-after investment destinations in the Middle East. It belongs to the Gulf Corporation countries, most of which are producers of oil. The country has also attracted foreign investments in various sectors such as the construction industry and other

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<sup>1</sup>Yahya Al-Samaan, *The legal protection of foreign investment in the Kingdom of Saudi Arabia* (Dar Al Andalus Publishers, 2000), at 7.

industries that are not prohibited by the government. In the last few years, the country has received investments from foreigners worth billions of dollars which have enabled the Gross Domestic Product (GDP) to change significantly. The change in attitude of foreigners regarding investment in Saudi Arabia is driven by the government policy to reduce restrictions affecting investments.<sup>2</sup>

Saudi Arabia, indeed, increasingly has become more open to international trade. As a consequence, the country has become more dependent on international trade. Thus, according to the WTO 2012 International Trade Review, “Saudi Arabia is, increasingly, a net importer of services, with a deficit averaging around US\$50,000 million per year during 2005-10”.<sup>3</sup>

The influx of foreign investments is also impressive. Thus, in the period between 2005 and 2010, Saudi Arabia became the eighth biggest recipient of FDI in the world. This happened partially due to the opening up of additional industries such as petrochemicals, gas and telecommunications to foreign investments. Also, the country established four economic cities and special economic zones with favourable investment conditions.<sup>4</sup>

However, some restrictions still exist. Saudi Arabia has restrictions on the types of investments that foreigners can make in the Kingdom. These restrictions have led to having classes of investments that can be made by foreigners. Members of the Gulf Cooperation Council receive the same preferential treatment as the citizens of the Kingdom of Saudi Arabia, while those outside the Council are restricted from investing in certain sectors. It is obvious that these

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<sup>2</sup> Disputes within National & International Spheres’ *Journal of King Abdulaziz University: Economics and Administration* (2000), at 4.

<sup>3</sup> WTO (2012). *Trade Policy Review: Saudi Arabia*. WT/TPR/S/256 <  
[http://www.wto.org/english/tratop\\_e/tpr\\_e/tp356\\_e.htm](http://www.wto.org/english/tratop_e/tpr_e/tp356_e.htm)>

<sup>4</sup> Ibid

restrictions focus on investments that contravene the Sharia law. Foreigners can only take up investments that are not on the prohibited list. Most of these investments that are restricted are considered to be of national importance.<sup>5</sup>

As noted in Saudi Arabia, a foreign investor can take advantage of many investment opportunities. After the global financial crisis and a European crisis, most foreign investors have started to realize the importance of the prohibition of *riba* in Sharia law and invested in banking. The demand for economic goods is also increasing in the Kingdom of Saudi Arabia because the country is developing fast. Therefore, citizens require products to satisfy their wishes and needs.<sup>6</sup> There is a need for housing and other infrastructure in the Kingdom of Saudi Arabia, thus creating opportunities for investment in the construction industry. The telecommunication and financial sectors are other areas in which foreigners are permitted to invest. Furthermore, the law has allowed foreigners to undertake gas exploration, be involved in the petrochemical industry and pipeline services, and as mentioned previously, banking. This means the Kingdom is opening up investment opportunities for foreigners, especially those with technical know-how.<sup>7</sup>

Although in the Kingdom of Saudi Arabia investments are vetted, 80% of all investments are owned by foreigners because the majority of the citizens are slow to take up the opportunities. This represents a good investment opportunity for a foreigner who is interested in a growing and responsive economy. The good investment infrastructure, supported by the

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<sup>5</sup> Al-Samaan, above n 1 at 7.

<sup>6</sup> Mary Hallward-Driemeier, 'Do Bilateral Investment Treaties Attract FDI? Only a bit...and they could bite'. *World Bank, DECRG*, (June 2003), at 3.

<sup>7</sup> Al Ghazzawi, Belal, and Buxton, Meriel, The European, and Middle Eastern arbitration review. (*Global Arbitration Review*, 2001), 2-10.

business environment, has made the country more attractive to foreigners and has spurred economic growth.

Various laws protect investments in Saudi Arabia. Sharia law and any subordinate laws in the country require people to protect property, and these laws are applied consistently; thus, property is protected. In cases where a dispute arises from investment, arbitration is given priority and if it fails, the courts are given an opportunity to settle the dispute. Arbitration is based on the local arbitration laws or the ICSID. The arbitration laws empower foreign investors to demand the insertion of a clause that will show how investment disputes are resolved. Any investor who enters into a contract of exchange, gratuity, safe custody, security, partnership or consolidation is able to protect his interests using arbitration clauses. If an investor does not demand the inclusion of such clauses, he is allowed to use other means of redress as provided by the law. Hence, Sharia law protects foreign investments because it does not discriminate against anyone - it protects both foreigners and locals.<sup>8</sup>

These rights are guaranteed for as long as the investor interests are in existence in Saudi Arabia. It has long been recognised that if foreign investors are not protected, they will lose their investments and leave the country, thereby slowing down economic growth which is not in the national interest. Before an investor makes an investment, his rights and privileges are explained to him and he is made aware of the procedure that will be followed to settle disputes.<sup>9</sup>

In case there are problems, such as disputes between business persons which could involve a foreign investor and a local partner, these are resolved by the application of the basic

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<sup>8</sup> Nancy Turck, Disputes resolution in Saudi Arabia, *Journal of International Law*, (1988) at 14.

<sup>9</sup> John Kline and Rodney Ludema, *'Building a Multilateral Framework for Investment: Comparing the Development of Trade and Investment Accords'*, (2008).



law of the Kingdom if no other law was specified in the contract. Investments in Saudi Arabia are considered beneficial for both the investor and the country because laws protect an investor from losing his investment(s). The economy of the country is also doing well; therefore, people have money for the purchase of products or services that are offered. If the economy is performing poorly, then there will be no market for some of the goods that are offered by foreign companies and their investment opportunities will decrease.<sup>10</sup>

Any dispute between a business person from an Islamic country and a local businessperson can be resolved amicably without the involvement of an arbitrator. Rarely do such cases or rather, such disputes, end up in court. However, disputes arising from investments between foreign investors and local business persons are resolved by arbitrators chosen by the foreign investors. If this process fails, the court will take over the handling of disputes.<sup>11</sup>

The most interesting dispute is the one which arises between a foreign investor and the government. If the dispute cannot be resolved by the ICSID, which is an international investment arbitration body, then the foreign investor is given the opportunity to choose both a local legal representative and an arbitration process that he deems to be fair. The government recognises the arbitration process as a means of settling disputes as long as the disputes relate to investments that can be resolved through arbitration. This is the surest way of amicably resolving disputes without encroaching on the investors' time and money. However, government-to-business person disputes are affected by various factors that impede their effectiveness. This has led most

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<sup>10</sup> Al-Samaan, above n 1.

<sup>11</sup> Daniel Vielleville and Baiju Vasani. Sovereignty over natural resources versus rights under investment contracts: which one prevails? *Transnational Dispute Management*, (2008).

investors to include clauses relating to an arbitration process when entering into contracts with the government of Saudi Arabia.<sup>12</sup>

The ICSID may play an important role in dispute resolution in Saudi Arabia. However, it is involved in resolving disputes that are not related to oil because the Kingdom of Saudi Arabia has excluded the oil disputes from the authority of the ICSID and this is made clear in the Royal Decree no. M8 Dated 22/03/1994H which creates a level playing field for both foreign investors and the Saudi government. Foreign investors use this body when they feel aggrieved and it is seen as being open and flexible in the resolution of disputes.<sup>13</sup> However, what might be of interest to contemporary research is the extent to which KSA's legal framework for dispute resolution and the protection mechanisms for foreign investors is based on Shariah. As the KSA continues to attract foreign trade and improve its trade environment as a catalyst for foreign investment growth, many of its trade laws have to include new factors other than those embodied by Islamic jurisprudence. In other words, while the KSA has in the past predominantly framed its laws based on the Qur'an, it now has to consider parameters for the governing of trade other than those attractive to a predominantly Muslim community. The national objective of being a preferred foreign investment destination comes with its responsibilities and obligations that are sometimes overarching to the sovereign determinations of a state.<sup>14</sup>

To Lee, globalisation is the interactive product of culture, technology and economics to enable the compression of time (so that everything is done faster), of space (blurring traditional geographic boundaries) and of cognition (creating awareness of the globe as one and as a

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<sup>12</sup> 'Disputes within National & International Spheres', above n 2.

<sup>13</sup> Marie-France Houde, *'Relationships between International Investment Agreements'*, Organization for Economic Co-operation and Development (2005) at 2-22.

<sup>14</sup> Cynthia Weber, *'International Relations Theory: A Critical Introduction'* (New York: Routledge, 2005), at 7- 64.

whole).<sup>15</sup> According to Waltz, globalisation is the interdependence of nations, societies and communities. He argues that with globalisation, “people, firms, markets matter more; states matter less”, as economic considerations become the main driver when states are making decisions.<sup>16</sup> From this perspective, nations increasingly become more interdependent, whereby most decisions (especially in regards to trade laws, communication and governance) are made as a collective response of all those in the economic field (or those who want to be in the collective field), and not as individual responses of separate states.<sup>17</sup>

Foreign investment flows are based on the internationalisation theory, where markets for both firms and nations are established across borders. In the contemporary world, globalisation has, in part, increased the manner and intensity of trade across geographical borders. Saudi Arabia has in the last few decades embraced globalisation, and in so doing, has proceeded to create a market for Shariah-compliant firms and non-Shariah compliant firms. The present study will seek to explore the ways in which popular views regarding the theory of globalisation are reflected in the transformation (or lack of it) of the Kingdom of Saudi Arabia as it markets itself as the prime destination for foreign investments in the Middle East.

For those who, like Waltz, subscribe to the ‘homogeneity’ school of globalisation, there is a belief that a state loses its individual sovereignty to the collective. For instance, Waltz argues that any nation that wishes to join the international market (or world market) must necessarily be

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<sup>15</sup> Kelly Lee, “*Health Impacts of Globalization: Towards Global Governance*.” In *Making Sense of Global Health Governance - A Policy Perspective*, ed. Kelly Lee, Kent Buse and Suzanne Fustukian, at 24. (New York: Palgrave Macmillan, 2002).

<sup>16</sup> Kenneth Waltz, “*Globalization and Governance*” *Political Science and Politics* 32, no. 4, (1999): at 693.

<sup>17</sup> *Ibid* at 694.

prepared to wear the ‘golden straightjacket’.<sup>18</sup> This golden straightjacket refers to the sets of national policies that are enforced in all member states and include balanced budgets, openness of national market to international trade and investment, economic deregulation, free-trade market liberation and currency stabilization.<sup>19</sup> Several conditions are imposed on nations that want to join the international trade.

Scholars argue that globalisation is primarily concerned with the economy and trade in- and/ or out-flows, KSA for instance may prefer to follow Islamic guidelines for their trade laws and to apply Qur’anic requirements to their investment law protocols; however, globalisation will impose a more collective approach on the governance of trade and investment. As Waltz argues, oftentimes, a group of international investors, lenders and regulators assume the decision-making role in regards to what each country must enforce if it is to receive international investments or be allowed to invest internationally, and by so doing become a player in the global economy.<sup>20</sup>

This assertion is of significance to the present study in that, as the country continues to adopt a globalized stance in trade, the KSA’s legal framework for dispute resolution and protection of foreign investors might have to be based on international investment laws rather than on its domestic preferences. Globalisation of a state’s trade and investment rarely takes into consideration the members of a particular state government, the local culture and/or religion, or the local philosophical aspirations. Rather, the concerns of globalisation in a particular state

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<sup>18</sup>Ibid at 694.

<sup>19</sup> Ibid at 695.

<sup>20</sup> Ibid, at 695.

relate to ‘stability, predictability, transparency, commonality, standardisation and the ability to transfer and protect private property’.<sup>21</sup>

Apart from giving up the individual state to the collective, another important aspect of globalisation is homogeneity. Labonte and Schrecker define globalisation as the “process of greater integration within the world economy through movements of goods and services, capital, technology and (to a lesser extent) labour, which lead increasingly to economic decisions being influenced by global conditions”, ultimately leading to a “global marketplace”.<sup>22</sup> According to these scholars, globalisation describes the manner in which people, businesses and nations are increasingly becoming interdependent and connected across national borders consequent to increased economic integration, advances in communication technology, increased and better travel, and cultural diffusion.<sup>23</sup>

In agreement with the foregoing assertions, Waltz contends that globalisation imposes homogeneity of interest rates, prices, products and terms of business on member states, and further points out that the world is rapidly moving to perfect homogeneity as globalisation continues to expand. It is thus predictable that the Kingdom of Saudi Arabia in its quest to become the best foreign investment destination in the Middle East, has established or is progressively establishing an investment climate that is homogeneous with that of many other internationalized economies in regards to the opportunities and the protection of both local and foreign investments.

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<sup>21</sup> Ibid at 694.

<sup>22</sup> Ronald Labonte and Ted Schrecker, “Globalization and social determinants of health: Analytic and strategic review paper”. *Globalization Knowledge Network Report*. (Ottawa: Institute of Population Health, 2006), at 3.

<sup>23</sup> Ibid at 3.

Nonetheless, KSA may yet be unreceptive to the homogeneous trade and investment laws predominant in the West. This is because Saudi Arabia is still largely and predominantly Islamic in its culture, governance and economy. The theory of globalisation contends that commonality in trade and investment leads to homogeneity in culture. A globalized economy has a very high level of transparency, which in turn transfers transparency ideology (oftentimes defined from the perspective of the West) to the local political and social realms as well. According to Waltz, the socio-political and economic environment sees “latecomers imitate the practices and adopt the institution of the countries which have shown the way”.<sup>24</sup> This means that non-Western countries which are only now attempting to play an active role in international trade have to adopt and assimilate the conventional policies and practices of their western counterparts who have been at the forefront of international trade for decades. It is of interest to the present study to investigate the extent to which the Kingdom of Saudi Arabia has implemented homogeneous investment policies and practices typical of the West.

It is variously argued that globalisation for most late comers to the international trade fraternity (including most of Asian, African, South American and Middle East nations), the policy is to “either adopt our common laws or you remain out of the loop” or in other words “change your laws to correspond with ours or we will not trade with you”. For instance, Waltz argues that, “states are differentiated from one another not by function but primarily by capability”.<sup>25</sup> This means that successful entry into the arena of international trade depends on the capacity to change, to adopt and to adapt homogeneity, since “if a country cannot adapt, they

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<sup>24</sup> Waltz, above n 16, at 695.

<sup>25</sup> Ibid, at 698.

cannot be welcomed into the global community leading to a larger poverty gap, less investment, less technology and ultimately, a stagnant economy”.<sup>26</sup> It is this latter aspect of globalisation that has emerged as most controversial.

According to Robinson, globalisation implies the emergence of two processes namely, the replacement of protectionist state economies with capitalist production and free-market trade practices through specialization, and the internationalisation of production processes to create an integrated common market.<sup>27</sup> This scholar argues that these two processes have led to the integration of national economies to an extent that the most ideal political, economic and social state a country can attain is having uniformity of results with those of other nations, and in reality these results are defined and set by the US and its European allies within the circle of ruling elites. To give the elite group of nations optimal power and influence, globalisation has meant “the elimination of state intervention in the economy and the regulation by individual nation states over the activity of capital in their territories”.<sup>28</sup>

Not all scholars, however, perceive globalisation as negatively as Robinson does. There are those who advocate the benefits and advantages of globalisation. Some scholars believe that globalisation promotes world peace as nations become interdependent, thereby reducing the propensity for conflict.<sup>29</sup> This proponent perspective holds that through shared trade and trade policies, globalisation enables weaker nations to benefit from the advanced economies, thereby reducing the poverty gap and developing their economy. Countries are able to buy what they do

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<sup>26</sup> Ibid, at 699.

<sup>27</sup> William Robinson, “Globalization, the World System, and ‘Democracy Promotion’ in US Foreign Policy”, *Theory and Society*, 25, no. 5 (1996), at 622.

<sup>28</sup> Ibid at 634.

<sup>29</sup> Weber, above n 14 at 55-64.

not have locally and to sell their produce to international markets, and consequently increase their capacities, revenues and living standards.

On the other side of the debate, there is a school of thought that argues the evil of globalisation. The opponents of globalisation maintain that it leads to the domination of weaker states by those with a greater international presence and economic muscle. As Polanyi unequivocally states, “*it is a dangerous delusion to think of the global economy as some sort of ‘natural’ system with a logic of its own, rather it is, and always has been, the outcome of a complex interplay of economic and political relations*”.<sup>30</sup> This school of thought believes that states are losing their sovereignty to the international community, which would be a good thing were it not for the fact that the international community endorses the will of a few powerful western nations.

To its detractors, globalisation is nothing but westernization (what has also been referred to as McDonaldization which is the imposition of western values, western culture and western laws on the ‘lesser’ nations as the maxim of civilization, development and economic progress). This corresponds to the view of William Robinson, a notable scholar, who argues that economic globalisation simply refers to the process of spreading capitalism from the West to the rest of the world.<sup>31</sup> Subscribing to this perspective, Waltz argues that contemporary globalisation is not the mere increase of international interdependence “but growing domination, inequality and pacification of norms regarded as inferior, in the relation of Southern and Northern states”.<sup>32</sup>

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<sup>30</sup> Karl Polanyi, *The Great Transformation*. (Boston: Beacon Press, 1944), at 3 - 4.

<sup>31</sup> Robinson, above n 27, at 619.

<sup>32</sup> Waltz, above n 16, at 699.



Further, Robinson argues that at the beginning of the 1980s following the end of the Cold War, the US had to change its foreign policy from authoritarian regime implantation in less developed nations to promoting democracy, good governance and economic development.<sup>33</sup> This necessitated the growth of international institutions with clearly-defined mandates.

Unfortunately, in the creation of these institutions, an elite group of nations emerged measured by their capitalist muscle, economic strength, availability of aid money and free market principles. This elite group formed the foundation on which globalisation was built. Robinson claims that the US and allied nations foresaw globalisation as an instrument that could be leveraged to continue their dominance by enforcing a political and economic hegemony that would elevate their position in the hitherto bi-polar divide of nations.<sup>34</sup>

Robinson's argument is also seconded by Weber who states that:

*The modernisation and development tradition emerged during the Cold War as the West's economic, political, social, and cultural response to the management of former colonial territories. ... The dilemma facing Western scholars and practitioners of international politics was twofold. First, they hoped to theorize ideas and then implement policies that would transform newly independent colonies into politically developed sovereign nation-states. But these theorists – the bulk of whom were from the USA – were not interested in so-called "Third World states" achieving development according to just any model. Rather, the only acceptable model of development was through liberal processes of politics, economics, and socialization, and the only acceptable model of a*

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<sup>33</sup> Robinson, above n 27, at 621.

<sup>34</sup> Ibid, at 619.

*fully developed state was a Western liberal capitalist, so-called “First World state. (consequently), ... modernisation and development tradition was consciously conceived as a Western (and predominately US) alternative to Marxist and (neo)-Marxist strategies of development espoused by so-called “Second World states” like the then Soviet Union”.*

It is debatable whether the KSA in its quest to open its domestic market to international investors has adapted and adopted the homogeneous policies and practices that govern the contemporary globalized trade. As will emerge in subsequent discussions in this dissertation, the KSA has, to a certain extent, internationalised its trade and investment policies and practices. This can be observed in the number of bilateral treaties and trade agreements that it has accepted as a signatory. However, the country is yet to attain international homogeneity in other areas important to international trade and investment. For instance, there are numerous domestic laws being enforced by the Saudi government that are in conflict with international trade laws. A good example of such laws is the arbitration law which has not changed. The theoretical foundation and insights borrowed from the theory of globalisation will be used extensively in the subsequent discussions.

## ***1.2 Statement of a problem***

The Kingdom of Saudi Arabia markets itself as the best destination for foreign investments. At the same time, the country applies laws that may discourage potential investors, especially those who may not understand Sharia law. The complex nature of this system may not be very appealing to foreign investors. Foreign investors who choose to invest in the KSA need to understand the various restrictions that may be placed on matters such as advertising.

With an increase of foreign investments in the Kingdom of Saudi Arabia, it could be difficult to differentiate between appropriate and inappropriate activities. One complication that might arise is the nature of investment that Sharia law forbids. If a foreign investor decides to make an investment in the Kingdom of Saudi Arabia, it may be much more difficult to tell the difference between activities which are considered acceptable under Sharia law, and those which are forbidden. This may seem simple on the surface. However, the difference between acceptable and unacceptable practices can influence the very nature of the returns and recouping of investment sums if one overlooks the religious basis of the transaction.

Another problem is the distinction between official statements and laws and Royal Decrees in the Kingdom. There are instances where Royal Decrees are made to protect the investments of the people of Saudi Arabia and this could present a problem to foreign investors. The investors may have difficulties in understanding which laws supersede the other Royal Decrees and official statements. This requires the investor to be aware of this legal structure before making investments in Saudi Arabia. To avoid any type of risky situations caused by failure to understand the cultural differences, all parties involved in a particular transaction are responsible for clearly highlighting what the investment will consist of and the consequences of deviating from the official government statement or Royal Decree.

Preferential treatment is given to foreign investors who come from Gulf States. This is intended to protect the interests of the Gulf States' agreement to co-operate. However, this may be seen as discriminatory towards other foreign investors with enough capital to invest in the country. It is evident that the main purpose of preferential treatment is to limit the number of

non-Gulf States foreign investors. Gulf States may enter with other investors into silent partnership contracts.

These domestic issues in Saudi Arabia have a global impact in today's world. How the Kingdom of Saudi Arabia governs and administrates its trade and investment is pivotal in determining Foreign Direct Investment inflows and outflows. Foreign investors prefer or trust their investments to be in stable, liberalised and standardised markets rather than in protectionist states. Similarly, Saudi investors are able to invest in global markets only to the extent that the local legal infrastructure allows and enables them to do so. Advocating that scholars should develop a fitting theoretical framework capable of facilitating the analysis of the new global system as well as the nation-states incorporated within this novel concept, Clark argues that only a holistic approach can enable contemporary globalisation scholars to study the international system. This system, Clark argues, should necessarily "treat globalisation and the states not as mutually exclusive, but as mutually reinforcing" where any national circumstances are seen as having repercussions on and implications for the global arena.<sup>35</sup>

This means that, in this age, it is not enough to analyse the trade policies and investment environments of independent states without providing a contextual comparison with the current and potential trading partners of such a state.<sup>36</sup> Globalisation is moving states towards homogeneity and it is important for the present study to analyse the Saudi investment environment not only from a national perspective, but also from a global one. The study will adopt Clark's theoretical approach to globalisation where the concept of globalisation and

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<sup>35</sup> Ian Clark, *Globalization and International Relations Theory* (Oxford: Oxford University Press, 1999), at 42 - 68.

<sup>36</sup> Weber, above n 14 at 40-67.

international relations is drawn from “the fundamental unit of analysis” of the globalized or non-globalized state.<sup>37</sup> In this approach, by analysing the policies and practices of an individual state, such as in trade and investment, a scholar can aptly define the standings of such a state within the full spectrum of globalisation. It is hoped that by evaluating the KSA’s investment environment, the study will be able to determine where the country stands in the international trade arena, of which foreign direct investment is a major component.

#### ***1.4 Importance of the research***

The findings of this thesis are expected to contribute to the literature by providing foreign investors and academics with insights that will assist them to understand the various types of investment to be made in Saudi Arabia, laws governing operations, conflict resolution, and protection of foreign investment. Foreigners intending to make investments in Saudi Arabia should therefore be aware of these issues and how to deal with them. The thesis will act as an incentive to potential foreign investors who are intending to invest their money in Middle East to invest in Saudi Arabia. By using the theory of globalisation, the study enables its findings and conclusion to be relevant to a global audience of investors. As Saudi Arabia strives to attract greater FDI inflows, the findings of this study will play an important role in guiding those within and outside the KSA on the way forward. It is hoped that the study will also help the KSA government and relevant stakeholders to reform and strengthen the local economy so that it becomes a friendly investment destination.

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<sup>37</sup> Clark, above n 35, at 56 – 61.

## ***1.5 Assumptions***

### **1.5.1 Specific Assumptions**

The assumption of this research is that all foreign investors are subject to Sharia laws. A trend that is becoming prevalent in the Kingdom of Saudi Arabia is the preferential treatment of those businesspersons who directly carry out business with the government. It is assumed that this practice will continue; whilst those trading directly with Saudis are treated normally. Arbitration is the best method of resolving conflict between investors and the government or investors and the locals. Apart from the ICSID, Sharia law can be applied to assist in arbitration.

## ***1.6 Methodology***

### **1.6.1 Forms of Investigation**

The biggest challenge in this study was to find the most reliable and appropriate method for obtaining answers to the research questions. Firstly, primary and secondary sources were investigated, some of which related to international dispute resolutions while others dealt with the laws linked to the Saudi Arabian investment climate. The investigation covered literature on Sharia law, the ICSID, and bilateral and multi-bilateral agreements.

It is of course vital that the researcher find relevant literary sources that could support the implicative discussion that the researcher hopes to create, especially in connection with the topic at hand. Although literary sources such as previous reports and relevant researches are helpful, nevertheless, a more direct investigation of the matter would provide a sounder basis for

understanding. To create a more effective approach to validating the researches' implicative results, it is important to undertake an actual evaluation process.<sup>38</sup>

### **1.6.2 Structure of the Thesis**

**Chapter 1** introduces the topic and states the problem. The chapter presents the theoretical background upon which the present study is based, namely the theory of globalisation. This helps to provide a context from which the study's aims and objective are drawn, as well as qualify what the study hopes to achieve. Thereafter, the chapter describes and justifies the chosen research method and summarizes the research outcomes.

**Chapter 2** analyses the Sharia law that is used in the Kingdom of Saudi Arabia, demonstrating how it relates to the constitution and laws of governance. In particular, it covers the role of Islam in the law-making process in the Kingdom of Saudi Arabia. It further discusses how Islamic Sharia influences investments of a country, and how the law affects foreigners investing in the country. It considers how Sharia law is applied to reduce investment risks as well as other investments made in the Holy Cities of Medina and Mecca.

**Chapter 3** covers classes of foreign investment that are made in Saudi Arabia and the preferential treatment that each class of investor is accorded in this country. It explains the criteria that are used in classifying foreign investors and describes the various types of investors, these being Saudi-Arabian or non-Saudi-Arabian, Arab investors or non-Arab investors, and

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<sup>38</sup> J. W. Creswell, *Qualitative Inquiry & Research Design: Choosing Among Five Approaches*. (London: Sage Publication Inc, 2007).

investors from Gulf cooperation states.<sup>39</sup> In essence, this chapter clarifies the different classes of investors.

**Chapter 4** explains the various dispute resolution processes that exist in the KSA and also explores the most common one among the investors doing business in the KSA.

**Chapter 5** concentrates on the history of arbitration in Saudi Arabia; it covers various events and Acts of law that have led to the current arbitration process in Saudi Arabia. The chapter presents a history of arbitration in Saudi Arabia and its beginnings in 1954 when oil exploration started. Later in 1963, the government signed a number of protocols to govern the disputes between foreign investors and the government. However, this chapter indicates that in the Kingdom of Saudi Arabia, arbitration law and its implementation rules were passed in 1983 and 1985. The 1983 arbitration law was vague, and in 1985 the shortcomings of the 1983 Act were amended. The chapter shows how arbitration Acts have complied with Sharia law.

**Chapter 6** covers the free trade agreement between various regions and Saudi Arabia; it also examines the bilateral trade agreement between Saudi Arabia and various countries such as the Philippines, Arab states, European states and African states. It extensively covers arbitration and the various laws used to resolve disputes.

**Chapter 7** deals with the international centre for settlement of investment disputes and the Kingdom of Saudi Arabia laws. It explains how arbitration law and foreign investment law are applied to resolve disputes, the purpose of international treaties, and the application of the

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<sup>39</sup> *Economic Agreement between the GCC States*, Adopted by the GCC Supreme Council (22nd Session; 31 December 2001) in the City of Muscat, Sultanate of Oman; see also '*Economic Unity Agreement among States*' the Arab League, Cairo, A.R.E (February 2003).



national centre for settlement of investment disputes in the Kingdom. The structure of laws applied to governing investments is discussed at length. The chapter also provides a brief overview of the globalisation theory and how it applies to Saudi's status in dispute resolution policies. This section also reviews the globalisation theory in the light of bilateral trade agreements and how such agreements govern dispute resolution and foreign investment protection. Hence, the chapter helps to determine the extent to which Saudi Arabia has globalized its market in a bid to attract and retain investment inflows.

**Chapter 8** covers the protection of foreign investors and their rights. The chapter clearly explains how oil investment disputes are resolved in the country so as to avoid conflict of interests. It also explains the weaknesses of the country's current dispute-resolution laws.

**Chapter 9** concludes the thesis with recommendations based on the various issues explored in the chapters. Of importance is that the dissertation provides a theory-backed conclusion. The theory of globalisation is utilised to place the study's findings in context such that literature-based evidence is evaluated against the evidence generated by this study. The concluding chapter summarizes the findings of this study and examines the implications of these findings as a basis for the proposed recommendations.

### ***1.7. Conclusion***

Foreign investors are protected by both foreign investment laws and international laws in Saudi Arabia. The government has recognised arbitration as the quickest and the easiest way to resolve conflicts between businesspersons and the government or businesspersons and businesspersons. This can be observed by the fact that foreigners account for 80% of Saudi Arabia's investment opportunities.

## Chapter 2:

### Sharia and Investment

#### 2.1 Overview

The foundation of all laws in the KSA is the Constitution (Qur'an and Sunnah). The constitution is the Book of God (Qur'an) as well as the Sunnah – traditions from His Messenger Peace Be upon Him. The Saudi constitution is also referred to as the Islamic Sharia Law because it (Islamic Sharia law) comprises the Book of God and the Sunnah. As expected, this constitution forms the basis of the Kingdom's system of governance. This fact is reflected in the Kingdom's serving King, who promised that the Qur'an and Sunnah would be the constitution under his leadership. Basically, the constitution endorses equality and fairness in all spheres of life.<sup>40</sup>

From the constitution, subordinate laws such as the Saudi Basic Law of Governance (promulgated in March 1992) have been applied in the business sector. These subordinate laws help to reinforce the constitution by addressing areas that are not clearly addressed by the constitution – they merely clarify and expound on the constitution. For example, Article 1 of the Basic Law provides that the Book of God and the Sunnah will form the basis of governance in the Kingdom.

This chapter will examine the foundation of all laws (related to investment matters only) which can be promulgated in the KSA. For this purpose, it will investigate the extent to which

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<sup>40</sup> Custodian of the two Holy Mosques King Abdullah Bin Abdul-Aziz, '*To the people of Saudi Arabia*', <<http://www.mofa.gov.sa/ServicesAndInformation/news/TwoHolyMosquesSpeeches/Pages/NewsArticleID38513.aspx>>, (Transulation with Aurther).

the Islamic Sharia law influences investment activities between foreign investors and the Saudi government – the various latitudes (if any) as well as the inherent restrictions imposed on foreign investors.

## **2.2 Introduction**

Though the scope and nature of governance systems among Islamic states significantly differ across the Arab world, one thing stands out clearly: they are incorporated within the provisions of the Islamic Sharia law. Governance in Saudi Arabia is entirely based on the provisions of the Islamic Sharia law. Consequently, it is assumed that all the citizens are Muslims and therefore should abide by the Sharia law principles which in this case may include praying five times a day, paying taxes, and upholding other requirements related to dogma.<sup>41</sup>

Nonetheless, to accommodate persons not of Islamic faith, the Kingdom established the Basic Law (a secular law) that succinctly stipulates the responsibilities of both the state and the citizens vis-à-vis the obligations imposed by Islamic Sharia law. Hence, it is arguable that Islamic Sharia law is the mother law (the Saudi constitution), and that all other laws should reflect the letter and spirit of the Book of God and the Sunnah. Therefore, being a secular and by extension, a subordinate law, the Basic Law just like other secular laws such as the Foreign Investment Law, merely reflects what is contained in the constitution. This is because, although the Kingdom is committed to instituting secular legal and social reforms, such reforms should be carried out within the provisions of the Holy Book and the Sunnah. This argument derives its

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<sup>41</sup> Saudi Basic Law of Governance art 6,11, Royal Order A/91 (27 Sha'ban 1412H – 1 March 1992), (*Umm al-Qura Gazette No. 3397 2, 1992*).

impetus from the Saudi Minister of Foreign Affairs, HRH Prince Saud Al-Faisal when reacting to pro-secularization demands allegedly being pushed by interested investors. He agreed that although the Kingdom ought to embrace a number of reforms so as to achieve its goals of being the investment destination of choice in the MENA (Middle East and North Africa) region, he cautioned that such reforms should be widely accepted by the people and, most importantly, that they should be gradual and realistic in order to have the greatest impact. In the KSA, such reforms should be pro-Islam. This is because, according to Prince Saud Al-Faisal, Islam is not only a religion but also a way of life for Muslims. He maintained that for the vast majority of Muslims, religion is not the basis of a theocratic rule, but rather a necessary moral check on the misuse of power by governments while providing Muslims with a sense of community, or '*Ummah*' in Arabic. Religion is vital to the unity and cohesiveness of Muslim societies.<sup>42</sup> Based on the Basic Law, the KSA has since enacted a number of investment-related secular codes such as the Foreign Investment Law, Arbitration Law, Capital Market Law, Companies Regulations, Zakat Regulation, and Real Estate Regulation, among others. These laws indicate the Kingdom's commitment to embracing economic diversification. Moreover, the government has entered into international investment agreements as part of its long-term goal of being the desired investment destination in the MENA region. Moreover, when addressing the European Policy Centre Brussels in Belgium on February 19, 2004, the Saudi Foreign Affairs Minister, Prince Saud Al-Faisal hinted that the Saudi government has put in place strong judicial, social, political and economic measures aimed at enlarging the scope of investment activities in the region. He said:

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<sup>42</sup> Minister of Foreign Affairs HRH Prince Saud Al-Faisal, *address to the European Policy Centre Brussels*, (Belgium February 19, 2004). Accessed from [http://www.saudiembassy.net/files/PDF/Saud\\_Speech\\_EPC\\_2.19.04.pdf](http://www.saudiembassy.net/files/PDF/Saud_Speech_EPC_2.19.04.pdf)

*Judicial reforms are of paramount importance. They include new regulations covering judicial procedures and the establishment of the Independent Public Prosecution Authority. Our regulatory reforms include more than twenty-five new legislations on foreign investments, insurance, financial markets, taxes, and control of money laundering and other fiscal irregularities. New and effective measures are being introduced to eliminate corruption. Our economic restructuring reforms include the establishment of regulatory agencies to accelerate privatization in the fields of communications and information technology, water and electricity, the establishment of industrial and technological zones, and financial markets. Saudi Arabia is actively seeking to join the World Trade Organization, and has successfully completed many rounds of bilateral negotiations including an agreement with the European Union.*<sup>43</sup>

Arguably, these agreements and measures are secular. Thus, they are tailored in accordance with the Basic Law. So, it is imperative to note that the implementation of the Basic Law as well as the range of investment-related codes do not in any way undermine the enforcement of the Islamic Sharia laws. This is because they are entirely drawn from the Islamic Sharia law. Article 1 of the Basic Law states:

*The Kingdom of Saudi Arabia is a fully sovereign Arab Islamic State. Its religion shall be Islam and its constitution shall be the Book of God and the Sunnah (Traditions) of His*

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<sup>43</sup> Ibid.

*Messenger, may God's blessings and peace be upon him (PBUH). Its language shall be Arabic and its capital shall be the city of Riyadh.*<sup>44</sup>

This article underscores the fact that all laws (including the Basic Law) were enacted to enhance the ease of engagement between the state and its people on one the hand and foreign nationals on the other. They are subordinate to the Book of God and the Sunnah (the Saudi Constitution). This fact is also set forth in Article 9 of the Basic Law which clarifies that the Saudi society is tailored around the values of the Islamic creed.<sup>45</sup> This article states:

*The nucleus of Saudi society is the family and its members should be brought up on the basis of the Islamic creed and its requirement of allegiance and obedience to God, to His Messenger and to those in authority; respect for and implementation of laws, and love of and pride in the homeland and its glorious history.*<sup>46</sup>

Furthermore, Article 48 of the Basic Law provides that the enforcement of these values should be done in accordance with the Islamic Sharia Law as provided for by the Book of God and the Sunnah as well other laws that are not in conflict with the Book of God and the Sunnah.<sup>47</sup> Arguably, this is chiefly because the Kingdom is under obligation to protect and uphold the tenets of Islam as provided by the Book of God and the Sunnah and as reflected in Article 23 of

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<sup>44</sup> Saudi Basic Law of Governance art1, above n 39.

<sup>45</sup> Ibid art 9.

<sup>46</sup> Ibid art 9.

<sup>47</sup> Ibid at art 48.

the Basic Law. This Article stipulates that, “*The State shall protect the Islamic creed, apply its Sharia, enjoin the good and prohibit evil, and carry out the duty of calling to God.*”<sup>48</sup>

This is achieved by engaging prominent personalities such as ministers, renowned Islamic scholars, and close members of the King’s family. These people are members of prominent councils such as the Council of Ministers which is chaired by the King himself. Also, there is the Shoura Council, an advisory body whose task is advice the King on legal and governance matters and to scrutinize annual reports submitted by ministries. In his annual speech to the Shoura, King Abdullah expressed his satisfaction with the Council for playing a pivotal role in the country’s investment agenda. He said,

*The participation of the Shoura Council in formulating program of economic and social reform in the Kingdom has increased over the past few years through its regulatory, supervisory and advisory role.*<sup>49</sup> *The participation of the Shoura Council, a monarchical body whose body comprises of the most religious personalities, the majority of whom come from the King’s family enhances the chances of fully implementing the supreme constitution.*

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<sup>48</sup> Ibid art 23.

<sup>49</sup> ‘Speech by King Abdullah’, *opening of activities of Shoura's fourth Year for the Fourth Session.*  
<<http://www.mofa.gov.sa/sites/mofaen/ServicesAndInformation/news/KingOfficialSpeeches/Pages/NewsArticleID76857.aspx>>

## **2.3 The Saudi Constitution (Sharia law) and the Basic Law of Governance**

### **2.3.1 Sources of the Islamic Sharia**

The Book of God and the Sunnah shape the law (Islamic Sharia) that cannot be challenged by any secular legislation enacted by Muslim states.<sup>50</sup> Thus, in a bid to supplement the teachings of the Book of God, like all other Muslim nations, the Kingdom utilises the personal experiences and/or teachings of the Prophet Mohamed in the Sunnah.

Together, the Holy Qur'an teachings and the Sunnah are the two most important (primary) sources of the universal Islamic law conventionally referred to as the *Sharia law*.<sup>51</sup> Also, Sharia law comprises content drawn from secondary sources such as precedents and/or teachings unanimously consented to by acknowledged Muslim scholars popularly known as Ulama.<sup>52</sup>

The central premise behind the Islamic Sharia law is that it is perceived by Muslims as a true reflection of God's will. Therefore, the Islamic Sharia occupies a very salient position among the national constitutions (whether secular or otherwise) promulgated throughout all Muslim nations.<sup>53</sup>

### **2.3.2 Relationship between the Saudi Constitution and the Basic Law of Governance**

The Saudi constitution comprises the Book of God (Qur'an) and the Sunnah (Islamic Sharia). Even so, in order to engage the Saudi citizens and residents alike, the Kingdom in March

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<sup>50</sup> Saudi Basic Law of Governance art 1, above n 39.

<sup>51</sup> B.G Weiss, *The Spirit of Islamic Law*. (Alta Mira Press, 2006) at 17.

<sup>52</sup> J.M Otto, *Sharia and National Law in Muslim Countries: Tensions and Opportunities for Dutch and EU Foreign Policy*, (Amsterdam University Press, 2008) at 7.

<sup>53</sup> Ibid.



1992 through the Royal Decree No. (A/91) 27 Sha'ban 1412H – 1 March 1992 established the Basic Law of Governance that was published in Umm al-Qura Gazette No. 3397 2 Ramadan 1412H - 5 in March 1992.<sup>54</sup> It is arguable that the Basic Law is subordinate to the constitution and that the letter and spirit of the law (Basic Law) entirely conforms to the Book of God and the Sunnah. The need to comply with the Holy Book and the Sunnah is also supported by Article 48 of the Basic Law which clarifies that when handling all types of cases, the Saudi courts can apply the provisions of the Islamic Sharia or other laws (such as the Basic Law of Governance, commercial law) only as long as they are in conformity with the Book of God (Qur'an) and the Sunnah. This Article states that:

*The courts shall apply to cases before them the provisions of Islamic Sharia, as indicated by the Qur'an and the Sunnah, and whatever laws not in conflict with the Qur'an and the Sunnah which the authorities may promulgate.*<sup>55</sup>

While the Islamic Sharia is considered to be an entirely religious (Islamic) law, the Basic Law of Governance is considered as secular but drawn from a religious (Islamic) law. Therefore, no conflict between the two should exist. After all, the Kingdom cannot establish a law that contravenes its constitution (Islamic Sharia) because it will not be enforced. This is because the King who is the custodian of the Two Holy Mosques, and by extension, the custodian of the Islamic Sharia laws, has vowed to protect the Book of God and the Sunnah. Part of this protection entails not enacting laws that contravene the teachings of Islam. This can be seen in King Abdullah's speech to the citizens of the Kingdom in 2005 when he said:

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<sup>54</sup> Basic Law of Governance art 1, above n 39.

<sup>55</sup> Ibid at art 48.

*In my leadership, I will take the Qur'an and the Sunnah as my constitution and the Islamic Sharia as my way of life. I will protect the value of life as required by the Islamic Sharia laws through the protection of basic human rights and serve all the Saudi citizens equally and rightfully.*<sup>56</sup>

Hence, it is arguable that the Basic Law alongside other secular legislations which have since been enacted were meant to offer guidance on the provisions of the Islamic Sharia on matters of governance, economic principles, rights and duties of the Saudi citizens and residents, as well as to the authorities of the state, particularly to non-Muslims who may find it hard to understand the enforceability of the Islamic Sharia law.

These facts derive their impetus from Articles 7 and 8 of the Basic Law which provide that the Islamic Sharia law (as derived from the “*Book of the Most High and the Sunnah of His Messenger*”)<sup>57</sup> shall form the basis of the Saudi system of governance.<sup>58</sup> Article 7 of the law stipulates that:

*Governance in the Kingdom of Saudi Arabia derives its authority from the Book of God Most High and the Sunnah of his Messenger, both of which govern this Law and all the laws of the State.*<sup>59</sup>

On the other hand, the Kingdom is obligated to apply the Basic Law (a derivative of the Islamic Sharia law) in all areas of governance except in very extreme instances when the

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<sup>56</sup> Bin Abdul-Aziz, above n 38.

<sup>57</sup> Basic Law of Governance art 8, above n 39.

<sup>58</sup> Ibid at art 7, 8.

<sup>59</sup> Ibid at art 7.

Kingdom is involved in warfare or during any other form of emergency.<sup>60</sup> Even in these circumstances, the stipulated regulations allowing exceptions should be strictly adhered to.<sup>61</sup>

This article stipulates that:

*Without prejudice to the provisions of Article 7 herein, no provision of this Law may be suspended except on a temporary basis, in the manner set forth under the Law, at the time of war or during a declared state of emergency.*

It is clear that this article specifically underscores the inherent uniformity that exists between these two legal frameworks. Neither framework prejudices or compromises the other. To explain further, while Article 7 of the Basic Law clarifies that the Islamic Sharia law is the core pillar of governance, this article (Article 82) stresses that the applicability of the letter and spirit of the Basic Law and by extension, the Islamic Sharia, should not be compromised.

Apart from the notion of inherent uniformity between the Islamic Sharia law and the Basic Law, it is also important to highlight that the influence of Islamic Sharia law is felt in all the economic realms. This is because it gives specific guidance on all matters that fall under these three core aspects of governance. As an example, it is stipulated in Article 17 of the Basic Law that all investment-related matters be handled within the provisions of the Sharia law and that any changes should be determined by the relevant authorities. This article (17) stipulates that:

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<sup>60</sup> Ibid at art 82 .

<sup>61</sup> Ibid.

*Property, capital, and labour are basic constituents of the economic and social structure of the Kingdom. They are private rights which fulfil a social function in accordance with Islamic Sharia.*<sup>62</sup>

In accordance with the spirit and the letter of the Basic Law, it is clear that apart from providing guidance on the investment climate in the Kingdom, this article serves to underscore the importance of the Saudi constitution given that Article 7 of the Basic Law states that the Kingdom is governed by the Qur'an and Sunnah,<sup>63</sup> and that, as explained earlier in this chapter, Article 82 of the law clarifies that Sharia law shall be deemed to be operational unless extreme circumstances prevail such as war or a state of emergency.<sup>64</sup>

Perhaps the magnitude of the Islamic Sharia law's leverage on the Basic Law can be better seen in Article 1 of the Basic Law. As mentioned earlier, Article 1 stipulates that Saudi Arabia is a fully sovereign Islamic state.

This article is self-explanatory in that the Qur'an and Sunnah, which as explained earlier in this chapter are the two primary sources of the Sharia law, are the officially recognised basis for the Saudi constitution. The appointment of the relevant authority should be entirely based on the Book of God and the Sunnah. All person shall pay allegiance to the Book of God and the Sunnah. Specifically, this requirement is also supported by the fact that Article 5 of the same law mentions that the Kingdom is entirely a monarchy, run by male descendants of the founding family, that is, the Abd al-'Aziz ibn 'Abd ar-Rahman al-Faysal Al Sa'ud family. Therefore, it

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<sup>62</sup> Ibid at art 17.

<sup>63</sup> Basic Law of Governance art 7, above n 39.

<sup>64</sup> Ibid at art 7.

should be noted that although the appointment of the Crown Prince (the King's successor) is the prerogative of the King,<sup>65</sup> Article 5(b) stipulates that:

*Allegiance shall be pledged to the most suitable amongst them to reign on the basis of the Book of God Most High and the Sunnah of His Messenger (PBUH).*<sup>66</sup>

This is an indicator that the relationship between the Islamic Sharia and the Saudi Basic Law is perpetual because the appointment of persons to the highest executive authority in the Kingdom (the Kingship) is carried out in accordance with the Islamic Sharia provisions. In addition, the fact that the appointees are always male descendants of the Kingdom's founding family underscores the argument that there is little chance of compromising the letter and spirit of the Islamic Sharia "traditions". This is because comparatively, monotheist regimes are better positioned to maintain the status quo than polytheist regimes since the former are bound by a single religious ideology while the latter are bound by multiple religious ideologies which may end up diverting the regime into secular ends.<sup>67</sup>

The King, as overall ruler of the Kingdom, is the symbol of sovereignty and the embodiment of the Sharia law. The fact that all legislations are either ratified by the King himself or in collaboration with the Council of Ministers affirms this. Moreover, one of the popular methods of enacting new legislations in the Kingdom is through the issuance of Royal Decrees which originate from the King and/or the Council of Ministers which he chairs in his

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<sup>65</sup> Ibid at art 5(c).

<sup>66</sup> Ibid at art 5(b).

<sup>67</sup> A. Koster and A.K. Meijers, *Religious regimes and state formation: perspectives from European ethnology*. (State University of New York Press, 1991) at 85-87.

capacity as the Prime Minister. The King's authority is further supported by Article 6 of the Basic Law that demands the Saudi citizens' and residents' allegiance to the King as stipulated in the Book of God and the Sunnah.<sup>68</sup>

#### ***2.4 The Role of Islam in KSA***

Ever since Saudi Arabia was founded in 1932, there have been conscious efforts from the ruling family to uphold and protect the Islamic Sharia principles. The various legislations and agreements that have since been enacted in the Kingdom provide clear evidence of such efforts. For instance, the promulgation of the Basic Law may have been perceived as the turning point (from a Sharia law-state to a secular state) for the Kingdom, but unfortunately this was not the case. Instead, while worded succinctly, the Basic Law spelled out the civil rights and obligations of Saudi's citizens and residents.

It should be noted that although the Kingdom has gained some credibility in enacting "secular" legislations to govern most investment activities, it has never done so on family and private/personal matters.

Other instances that confirm the gradual process of Islamising the Kingdom include the continued use of Hanbali school jurisprudence in interpreting the Sharia laws especially when handling family and personal matters that do not have their respective "secular" legislations.

The notion of Islamising the KSA is embodied by the Muslims' belief that Allah's teachings are universal and do not discriminate between Muslims and non-Muslims simply

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<sup>68</sup> Basic Law of Governance art 6, above n 39.

because according to Verse 142 of the Qur'an Surah 2 (Baqarah), Allah belongs to all the people living in both the "east and the west".<sup>69</sup>

Furthermore, part of Verse 143 Surah 2 (Baqarah) provides that true believers in the teachings of the Prophet Muhammad should embrace a monotheist lifestyle as directed by the Book of God (Qur'an). Basically, this verse clarifies that the strict adherence to Prophet Muhammad's teachings and fellowship of Allah's Covenant form the fundamental prerequisites for a just nation. This is because Allah never lets the prayers of His believers go to waste as He is "... *the Most Merciful towards mankind*".<sup>70</sup>

Also, Verse 27 of Surah 2 (Al Baqarah) of the Holy Qur'an prohibits Muslims from engaging in activities that flout Allah's teachings.<sup>71</sup> In this regard, the King who is the embodiment of the Islamic Sharia law in the Kingdom is under obligation to enforce the Sharia-based constitution as part of the broader obligations to Allah's Covenant so as to avoid the wrath of God. Precisely, verse 27 Surah 2 (Baqarah) of the Holy Qur'an stipulates that:

*Those who break Allah's Covenant after ratifying it, and sever what Allah has ordered to be joined (as regards Allah's Religion of Islamic Monotheism, and to practice its legal laws on the earth and also as regards keeping good relations with kith and kin), and do mischief on earth, it is they who are the losers.*<sup>72</sup>

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<sup>69</sup> Holy Qur'an, Surah Number 2 Verse 142.

<sup>70</sup> Ibid.

<sup>71</sup> Ibid Verse 27.

<sup>72</sup> Ibid.

Arguably, this verse forms the basis of the Islamic Saudi Basic Law given that it clearly cautions Muslims against defying Allah's Covenant. In the same way, it serves as a caution against the veering off from the spirit of constitutionalism among those entrusted with the day-to-day implementation of the Saudi constitution. The duty to comply with the Book of God as well as with the King's authority is further set forth in Article 6 of the Saudi Basic Law which calls upon Saudi citizens and residents alike to respect the institution of the Kingship on the very basis that it is formulated within the Islamic Sharia provisions (Qur'an and Sunnah). In particular, Article 6 of the law stipulates:

*Citizens shall pledge allegiance to the King on the basis of the Book of God and the Sunnah of his Messenger, and on the basis of submission and obedience in times of hardship and ease, fortune and adversity.*

When read together, Articles 1, 5, 6, 7, 8 and 82 of the Basic Law clearly indicate that the Saudi Basic Law is not only derived from the Islamic Sharia, but that its wording and general spirit are a true reflection of the Book of God and the Sunnah. A close association between the Saudi Basic Law and the Book of God and the Sunnah can be seen from the fact that the process of implementing the constitution is the responsibility of the executive authority (King, Council of Ministers, and the Shoura Council) headed by a monarch who is appointed in accordance with the Book of God and the Sunnah. Furthermore, the spirit of the constitution as set out in Article 23 of the law (Basic Law of Governance) stipulates that the Kingdom has only one core mission, which in this case is to “*protect the Islamic creed, apply its Sharia, enjoin the good and prohibit*



*evil, and carry out the duty of calling to God*” according to the Book of God and the Sunnah.<sup>73</sup>

Moreover, it is imperative to note that the King and the various sets of governing councils are required to uphold the dignity of the Saudi citizens and residents and by extension, accord them the basic human rights as demanded by the Islamic Sharia.<sup>74</sup>

From a different perspective, it can be argued that Sharia law has a deep-seated history in the Saudi system of governance. This is because well before the Basic Law was established, the Kingdom relied only on the Sharia law when handling all matters of governance. Perhaps this was possible because the Kingdom was predominantly Muslim and the number of foreign nationals doing business or even residing in the Kingdom was relatively small then compared to the current situation.<sup>75</sup> Also, based on the fact that the “secular” law (Basic Law) was established only as recently as March 1992, about sixty years after the Kingdom was founded, it can be argued that the Islamic Sharia law directly influences overall governance of the Kingdom.

#### **2. 4. 1 Application of the Islamic Sharia Law in the KSA**

Saudi Arabia can be regarded as a religious (Islamic) state among the Arab world countries. This is because it is home to the two holy Islam sites, Mecca and Medina. Hence, this places entirely on the Kingdom the core responsibility of ensuring that these two holy sites are kept secure and holy. To this end, and as Article 24 of the Basic Law provides, the Kingdom is committed to not only upholding the values of Islam but also to protecting the Two Holy

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<sup>73</sup> Saudi Basic Law of Governance art 23, above n 39.

<sup>74</sup> Ibid at art 26.

<sup>75</sup> Saudi Arabia has been using Sharia law to address all the various judicial areas ever since it was founded back in 1932. Even after the promulgation of the Basic Law, Sharia courts continue to rely heavily on the revisions of the Qur'an to make rulings.

Mosques of Mecca and Medina. Most importantly, the Kingdom endeavours to ensure that Muslims from all parts of the world fulfil their major and minor pilgrimage obligations as well as visiting the Prophet's Mosque. Article (24) stipulates that:

*The State shall maintain and serve the Two Holy Mosques, and provide security and care to those who travel to them as to enable them to perform Hajj (Major Pilgrimage), 'Umrah (Minor Pilgrimage), and Ziyarah (Visit of the Prophet's Mosque) in ease and tranquillity.*<sup>76</sup>

In interpretation, it is arguable that one of the most obvious and effective ways of protecting the two holy sites is by the enactment of new laws that restrict foreigners (non-Muslims) from owning real estate and/or carrying out investment activities within the two cities.<sup>77</sup> These restrictions are legitimate given that the Kingdom is normally regarded as the epitome of Islamic faith by virtue of being the host to these Two Holy Mosques. For this reason, though foreign investors (non-Muslims) can physically visit the two cities with great ease but not within Al-Haram borders (Holy Mosques borders), they cannot own real property (unless as provided by Article of Real Estate Regulation) or even carry out investment activities in the two cities.<sup>78</sup>

Even so, this provision should not be interpreted as a sign of bad governance. It is only meant to protect and uphold the values of Islam, which entails keeping the Two Most Holy

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<sup>76</sup> Saudi Basic Law of Governance art 24, above n 39.

<sup>77</sup> Saudi Real Estate Regulation, Article 1, reg M/22.

<sup>78</sup> Ibid.

places free from any form of transgressions by non-Muslims. This was emphasized by King Abdul in his 2008 speech to the Shoura Council annual meeting. He said,

*“From here, I address every citizen saying: When I advise you and myself to fear Allah and to be vigilant on having among us neither oppressor nor oppressed neither depriver nor the deprived, and neither strong nor weak. We are all beloved brothers in one homeland where we adhere to bonds of our religion, sacrifice our lives for it, adhere to the unity of nation and do not hear appeals of ignorance age whether they put on dresses of sectarian, regional or tribal extremism. Your strong unified state will remain (Allah willing) stronger than any challenges. All at home and abroad must be aware that the period of chaos and dissension eliminated by the founder late King Abdulaziz Al-Saud (May Allah bless his soul) has gone without return. With the help of Allah, this period will only be a memory that enhances concepts of morality and affiliation to this nation; an affiliation that estimates difficulties and transforms them into determination, will and change.”<sup>79</sup>*

Arguably, this official statement by King Abdullah served to dispel any fears among foreign investors who are non-Muslims and may be having doubts regarding the dark history that is characterized by civil strife and bad governance. Furthermore, this statement served to instil

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<sup>79</sup>King Abdullah, above n 47.

confidence in foreign investors given that the Kingdom lacks a formal codified legal framework.<sup>80</sup>

The lack of a formal codified legal framework means that Sharia law is directly applied in the Kingdom, particularly in those areas that lack existing secular legislations. The application of the Islamic Sharia law in Saudi Arabia is largely based on the Hanbali School of jurisprudence. This school is by far the most conservative, particularly in matters of doctrine. Also, this school gives significant consideration to teachings and precedents unanimously supported by acknowledged Muslim scholars.<sup>81</sup>

Nonetheless, in instances where this school has no specific provision for a particular legal situation or even if the application of the existing provisions are suspected to cause public outcry, other schools of jurisprudence may be applied with ease.<sup>82</sup> As a result, the following schools are the most likely to be applied in Saudi Arabia: Maliki, Shafei, and Hanafi. However, the reliance on Hanbali, Maliki, Shafei, and Hanafi schools of jurisprudence has over time been overtaken by events starting from the time when the Saudi Basic Law was established.<sup>83</sup>

Similarly, with the steady growth in investment activities in the Kingdom over recent years, there has been growing pressure from investment partners, particularly those from the western world, for the Kingdom to develop a formal legal system to facilitate mutual engagement between foreign investors and government agencies. This has resulted in the

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<sup>80</sup> G.L. Roberts, *Sharia Law and the Arab Oil Bust: Petrocurse or Cost of Being Muslim?* (Boca Raton, Florida, 2003) at 59.

<sup>81</sup> Ibid at 61-62.

<sup>82</sup> Ibid.

<sup>83</sup> J. Wynbrandt and F.A. Gerges, *A Brief History of Saudi Arabia* (2<sup>nd</sup> ed.). (InfoBase Publishing, 2010) at 90.

issuance of a number of Royal Decrees, enactment of investment related legislations, and the ratification of international investment agreements. However, it should be noted that these Royal Decrees, local legislations and international agreements were issued in conformity with the Islamic Sharia principles as they are only meant to supplement the Islamic Sharia law and not to replace it.

The enactment of Sharia-compliant laws has been possible because the Kingdom has upheld the values of the Islamic Creed as well as strictly adhering to the Basic Law.

#### **2.4.2 Conclusion**

In conclusion, there is no doubt about the extent to which the Islamic Sharia law impacts on matters of governance in the KSA. Tellingly, the Sharia law has a greater impact in Saudi Arabia than in any other Arab/Muslim nation. This is because the Kingdom follows the Hanbali school of jurisprudence which is by far the most conservative on matters of dogma. In addition, the Kingdom has to strictly enforce the Sharia law as part of its religious obligation to protect the Two Holy Mosques of Mecca and Medina. For that reason, it is arguable that the only practical way to fulfil this obligation is by enforcing Sharia-compliant laws that restrict the movement of persons in these two holy sites. Though non-Muslims are not barred from freely entering these areas, they cannot carry out any investment activities near them.

As recently as March 1992, Saudi Arabia established the Saudi Basic Law. As expected, this law entirely reflects the Islamic Sharia principles. Also, other secular legislations have since been enacted to help address specific areas that may not be directly addressed by the Book of God, the Sunnah, or even the Basic Law such as those touching on investment matters involving

foreign nationals (non-Muslims) and the Saudi government. Again, it is important to note that these secular legislations fully conform to the Islamic Sharia doctrines.

## ***2.5 The Islamic Sharia Law and Investments***

The Islamic Sharia law is very accommodating towards investment activities as long as these do not contravene the conventional Islamic financing structures; that is, they do not involve unethical purposes, unfair exploitation and/or unjust enrichment, uncertainty, or even speculation.<sup>84</sup> At first glance, one might think that restrictions imposed by the Sharia law will discourage investors. However, a closer look at restrictions suggests that they provide stability to the financial system, and thus, in fact attract investors. For instance, Sharia law does not tolerate speculation. On the one hand, this restriction does not allow investors to operate in a certain way. On the other hand, this provision discourages misconduct, thereby making the financial system more stable. Hence, Saudi Arabia is one of the most desired investment destinations in the whole of the MENA region.<sup>85</sup> Ideally, the positive investment climate is a culmination of a series of pro-investment legislations and agreements that have been enacted in recent years.<sup>86</sup>

Because these legislations and agreements were enacted with the sole purpose of providing detailed explanations of the provisions of the Islamic Sharia law, it becomes clear that all investment matters carried out within the Kingdom are entirely in accordance with the Book of God and the Sunnah.<sup>87</sup> This is because, as Article 14 of the Basic Law provides, the Saudi

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<sup>84</sup> H. Smith. Saudi Arabia investment guide 2010. (*Al-Ghazzawi Professional Association*, 2010) at 34.

<sup>85</sup> Saudi Arabia Investment Climate, < [www.the-saudi.net/.../investment-climate.htm](http://www.the-saudi.net/.../investment-climate.htm) - *United States*>.

<sup>86</sup> Saudi Arabia Investment Guide, 3-4, <<http://www.cityscapeintelligence.com/saudi-arabia-investment-guide-2009/2010?>>

<sup>87</sup> Saudi Basic Law of Governance art 14, above n 39.

government reserves the right to issue directives and/or laws aimed at protecting the exploitation and development of all forms of wealth (i.e., property, capital and labour).<sup>88</sup>

Additionally, this provision is supported by Article 17 of the law which, as explained earlier, allows both material and human capital to play a salient role in the fulfilment of the Kingdom's religious obligations.<sup>89</sup> Moreover, in compliance with the Book of God and the Sunnah, the Saudi government perceives all forms of national wealth (property, capital, and labour) to be sacred. Consequently, any investment activities that result in the award and/or receipt of "*Riba*" (interest) are prohibited under the Islamic Sharia law as it constitutes "*haram*" (acquisition of wealth by unethical means).<sup>90</sup> Therefore, foreign investors should acquaint themselves fully with the Islamic financial structures so as to differentiate what constitutes "*haram*" from what constitutes legal exchange of assets for productive purposes according to the Islamic Sharia law.

From a different perspective, it can be argued that the Sharia law as applied in the Kingdom is not sensitive to foreign investors (particularly those who do not profess Muslim faith), given that the government rarely consults foreign entities when establishing social and economic policy frameworks. This is because the Kingdom's leadership, embodied in the King, is obligated to honour only the Supreme Constitution (Book of God) and, by extension, the values of Islam. This notion was emphasized in an official statement made by King Abdullah

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<sup>88</sup> Ibid at art 14.

<sup>89</sup> Ibid at art 17.

<sup>90</sup> Roberts, above n 78 at 60-61.

when he emphasized the importance of consultation between the Kingdom's leadership and the citizens (not foreigners) at the Shoura Council's 2008 annual meeting. He said:

*When your government draws its policies and develops its programs, it takes into account the public interest, senses the needs of citizens and addresses any problem or phenomenon emerging in the Saudi society. Therefore, it has established a number of government commissions and departments as well as private associations concerned with the affairs and interests of citizens, including (National Commission for Protecting Integrity and Fighting Corruption), (General Commission for Housing) and (Consumer Protection Association).<sup>91</sup>*

This indicates that even the international investment agreements that the Kingdom enters into with other countries are meant to enhance the quality of life of its citizens. For instance, FDIs help to ensure a smooth supply of essential goods, services, capital and labour that cannot be sourced from within the Kingdom.

### **2.5.1 Investment Activities by Foreigners**

In what can be interpreted as efforts to exploit, protect and develop the God-given wealth with which the Kingdom is generously endowed, Saudi Arabia has set out a number of regulations that limit the number of investment activities in which nationals of other countries can engage. This is pursuant to Article 3 of the Saudi Foreign Investment Law which stipulates that *"The council shall have the authority to issue a list of activities excluded from foreign*

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<sup>91</sup> King Abdullah, above n 47.



*investment.*”<sup>92</sup> Some of these sectors considered sensitive to national security and sovereignty include “... *oil exploration, drilling and production, ... manufacturing of military equipments, devices and uniforms, manufacturing of civilian explosives, catering for military sectors, insurance services, ... real estate investment in Mecca and Medina, ... [and] real estate brokerage, ...*.”<sup>93</sup>

Dr. Abdul Rahman Al-Tuwaijri, the Secretary-General of the Supreme Economic Council of Saudi Arabia, expressed his full support for this provision when he was fielding questions from journalists. He said:

*The SEC has revised the list of economic sectors in which foreign investment will not be allowed, thus allowing foreigners to invest in new areas, ... the SEC opened new economic sectors for foreign investment in line with the Custodian of the Two Holy Mosques King Abdullah’s reforms aimed at strengthening the economy, attracting more foreign investment and enhancing private sector participation.*<sup>94</sup>

Even so, Dr. Al-Tuwaijri clarifies that bans on foreign investment within the precincts of the two Holy Cities of Mecca and Medina will continue to operate as always as part of the Kingdom’s obligation to keep the Two Holy places pure. He said, “... *restrictions on real estate*

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<sup>92</sup> Foreign Investment Law art 3, Royal Decree No M/1 5, 10 April 2000.

<sup>93</sup> Saudi Negative List: (*Activities excluded from Foreign Investment*), <<http://www.cgijeddah.com/cgijed/comm/business/negative.htm>>

<sup>94</sup> *Kingdom opens more economic sectors for foreign investments* (March 26, 2007). <<http://www.saudiembassy.net/archive/2007/news/page576.aspx>>

*investment in Makkah and Madinah would continue without change. The same is the case for tourist orientation and guidance services related to Haj and Umrah.*”<sup>95</sup>

In interpretation, the decision to bar foreign investors from engaging in some investment activities while allowing them to invest in others, can be perceived as conforming to the letter and spirit of the Islamic Sharia law as reflected in Article 14 of the Basic Law as well as other articles in Part Four of the Basic Law. More specifically, Article 14 of the law stipulates that:

*All God’s bestowed wealth, be it underground, on the surface, or in national territorial waters, on the land or maritime domains under the State’s control, all such resources shall be the property of the State as defined by the Law. The Law shall set forth the means for exploiting, protecting, and developing such resources for the benefit, security, and economy of the State.*<sup>96</sup>

Pursuant to this article, the Saudi government is obligated to enforce strict measures to protect, extract, develop, and equitably distribute national wealth among its citizens and/or residents. To achieve this, the Kingdom utilises the Islamic Sharia principles as provided in Article 9 of the Basic Law. This article partly provides for:

*(...) obedience to God, to His Messenger and to those in authority [as well as] respect for and implementation of laws, and love of and pride in the homeland and its glorious history.*”<sup>97</sup>

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<sup>95</sup> Ibid.

<sup>96</sup> Saudi Basic Law, above n 39 at art 14.

<sup>97</sup> Ibid at art 9.

Nevertheless, this provision should not be interpreted as an impediment to foreign investment as Article 18 of the law clarifies that the Kingdom is committed to enhancing a healthy investment climate by protecting and upholding the sanctity of private property. Specifically, Article 18 stipulates that:

*The State shall guarantee private property and its inviolability. No one shall be deprived of his property except for the public interest, provided that the owner is fairly compensated.*<sup>98</sup>

Basically, this article (18) underscores the fact that the Kingdom is not only committed to protecting and upholding the sanctity of its national wealth, but it is also determined to achieve this goal by making concerted efforts to encourage investment activities and the private ownership of property. No doubt this is a very progressive provision that increases the number of direct foreign investments in the Kingdom.

In what can be interpreted as an attempt to align its legal framework with the Islamic Sharia, particularly in regard to the sanctity of the national wealth,<sup>99</sup> the Kingdom through Article 1(e) of the Saudi Foreign Investment Law outlines strict regulations that determine who can qualify as a foreign investor.<sup>100</sup> Moreover, pursuant to Article 15 of the Basic Law which stipulates that, “*No concession is to be granted and no public resources of the country are to be exploited except pursuant to a law,*” the Kingdom through Article 2 of the Foreign Investment

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<sup>98</sup> Ibid at art 18.

<sup>99</sup> Saudi Basic Law, above n 39 at art 16, 17.

<sup>100</sup> Above n 91, stipulates that foreign investors should be natural persons from other countries or corporate entities whose partners are not of Saudi nationality.

Law demands that foreign investors should be strictly vetted by the Board of Directors of the Saudi Arabian General Investment Authority (SAGIA).<sup>101</sup>

Anyone who meets the prerequisite legal capacity requirements as well as other regulations as stipulated by legislations and agreements will be granted a permit. Nevertheless, so as to allow for fairness as provided in Articles 20 and 22 of the Basic Law and as outlined in Article 2 of the Foreign Investment Law, the Board is obligated to act on an application within a thirty-day period. If this period elapses without the application being substantially scrutinized, then the Board must issue a licence.<sup>102</sup> In this regard, it is arguable that the legal capacity for foreign investors is limited only to those sectors that are open to foreign investors.

While still conforming to the tenets of the Islamic financing system, the Saudi Foreign Investment Law grants a wide range of privileges and rights to foreign investors.<sup>103</sup> These privileges and rights are accorded fairly to all classes of foreign investors except in the case of those whose countries have got existing mutual investment agreements with the KSA, such as investors from the GCC and Arab League countries who are accorded preferential treatment.<sup>104</sup> Some of the privileges and rights accorded to foreign investors include, but are not limited to, the following: acquisition of immovable property for purposes of developing the licenced investment activity as well as settling their staff,<sup>105</sup> unlimited access to statistical and other pertinent

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<sup>101</sup> Saudi Basic Law, above n 39 at art 15; Foreign Investment Law, above n 91 art 2.

<sup>102</sup> Saudi Basic Law, above n 39 at art20,22; Foreign Investment Law, above n 91.

<sup>103</sup> Smith, above n 83 at 34-35.

<sup>104</sup> Economic Unity Agreement Art 1, the Arab League, Cairo (A.R.E Feb. 2003A); Economic Agreement above n 37, Art 3.

<sup>105</sup> Foreign Investment Law, above n 91 art 8.

investment related information,<sup>106</sup> and repatriation of the proceeds of their investments, among others.<sup>107</sup>

There are significant distinctions between investment activities by Saudi investors and those of foreign investors. This is pursuant to the Saudi Basic Law which clearly stipulates that the Saudi government should be committed to upholding and protecting the Islamic creed as stipulated in the Book of God and in the Sunnah. Although there is no express regulation that provides for the preferential treatment of foreign investors, it is clear that the existing mutual agreement between Saudi Arabia and the GCC countries as well as the other between the Kingdom and the Arab League nation states, accords investors from these two predominantly Muslim regions preferential treatment in terms of the nature and scope of the investment activities that can be undertaken, or even the physical locations where such investment activities can be carried out.

For more illustration, pursuant to Article 1 of the *Economic Unity Agreement among States of the Arab League*, nationals of contracting states are accorded a wide range of preferential treatments spanning economic, social and cultural realms. This article provides for a number of preferential treatments which may include, but are not limited to, the following:

*“Freedom of personal and capital mobility ... Freedom of exchange of national and foreign goods and products ... Freedom of residence, work, employment and exercise of economic*

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<sup>106</sup> Ibid at art 10.

<sup>107</sup> Ibid at art 7.

*activities ... Freedom of transport, transit and use of transport, ports and civil airports, and, ... Rights of possession, bequeath and inheritance.”*<sup>108</sup>

In this regard, it can be argued that foreign Muslim investors may enjoy more privileges than their non-Muslim counterparts from outside these two regions. Nevertheless, the tenability of this argument is limited only to the extent that the majority of foreign investors in the Kingdom originate from GCC and Arab league areas.

On the other hand, regarding foreign investors from the GCC countries, similar preferential treatment is accorded to them. This is pursuant to Article 3 of the *Economic Agreement between the GCC member states*, whereby host nations (Saudi Arabia) are obligated to accord preferential treatment to citizens of other GCC states as if they were their own citizens in the following sectors: “*Movement and residence ... Work in private and government jobs ... Pension and social security ... Engagement in all professions and crafts ... Engagement in all economic, investment and service activities ... Real estate ownership ... Capital movement ... Tax treatment ... Stock ownership and formation of corporations ... Education, health and social service.*”<sup>109</sup>

### **2.5.2 Investment in the Two Holy Cities (Mecca and Medina)**

Article 3 of the economic agreement between the GCC states covers a wide area of investment sectors, some of which are listed in the Saudi Negative List. For example, foreign investors are not allowed to own or invest in immovable property within the precincts of the Two

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<sup>108</sup> Economic Unity Agreement, above n 103.

<sup>109</sup> Economic Agreement, above n 37, art 3.

Holy Cities of Mecca and Medina.<sup>110</sup> In what can be interpreted as efforts to uphold and protect the provisions of the Islamic creed and the sanctity of places considered holy by Muslims, foreign investors are not allowed to carry out any investment activities within the precincts of the two Holy Cities of Mecca and Medina.<sup>111</sup> In addition, they are not allowed to own immovable property within the precincts of these two Holy Cities unless there are special circumstances provided for in Article 1 of the Real Estate Regulation, for example, through succession, in instances where ownership is by dedication or even through a two-year renewable leasehold.<sup>112</sup> This provision does not, however, bar them from physically entering the two cities on private and/or other personal activities apart from investment activities.

Part of Article (1) states:

*Non-Saudi nationals may not, other than by succession acquire the right of ownership, servitude or usufruct to real property within the limits of Mecca and Medina; the acquisition of the right to ownership, if coupled with “wakf” (dedication) of the property executed in accordance with the Sharia rules to ascertain specified Saudi party is excluded from such provisions, provided that the deed of dedication provides that the supreme Council of Dedications shall have the right of supervision over the property dedicated.*

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<sup>110</sup> Saudi Negative List, above n 92.

<sup>111</sup> Saud Basic Law, art 24, above n 39. It provides that the Saudi Government is committed to protecting the Two Most Holy Mosques of Mecca and Medina. This means foreign investors who are not Muslims cannot carryout investment activities in these two regions. See also Article I of the Real Estate Regulation (N. 2340 of 21/7/1390 AH). Even so, there is an exception on GCC and Arab League nationals courtesy of the existing mutual agreements between the two regions and Saudi Arabia.

<sup>112</sup> Real Estate Regulation, above n 75 at art1.

*However, a non-Saudi national may lease real property for a fixed period not exceeding one year; the term of the lease may be extended for a term or terms which does not exceed one year.*

It is important to note that investors from GCC and Arab League countries can acquire immovable property and carry out investment activities within the precincts of Mecca and Medina courtesy of the existing reciprocal agreements between the two regions and Saudi Arabia.<sup>113</sup> On the other hand, other foreign investors cannot carry out investment activities within the precincts of these Two Holy Mosques.

Although Article 1 of the Real Estate Regulation does not bar non-Muslim foreigners from physically entering the two Holy Cities, the constitution of the Kingdom ensconced in the Book of God (Qur'an), verse 28 of Surah Al-Touba states that "after this year (ninth year of the prophet Mohammed's migration) do not let non-Muslims come near the Sacred Mosque". This clearly means that non-Muslims are forbidden under any circumstance to physically enter the Holy Cities with boundaries of the Mosques (Alharm)<sup>114</sup>.

### **2.5.3 The Role of Sharia Law in Minimizing Investment Risks in KSA**

The Islamic Sharia doctrines provide for a risk-free investment climate through the enforcement of a number of contractual regulations. In mitigating investment risks, the Sharia law pursues the following measures which totally prohibit engagement in deals that may result in the loss of capital by one party. Regarding the prohibition of payment of interest – any

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<sup>113</sup> Economic Unity Agreement, above n 103 at art1.

<sup>114</sup> Holy Qur'an, Surah 9 (Al-Touba) Verse 28.



contractual obligation which entails the payment of interest is considered as an act of *haram*. This helps to discourage investors from engaging in risky investment activities. However, interest payment is allowed in investment activities that guarantee returns, such as the “exchange or ownership of shares.”<sup>115</sup> The permit to apply interest to operations that involve exchange or ownership of shares is based on the Islamic law concept that while money is not a factor of production, and thus cannot be valued as something that can definitely produce interest, this concept is not true for some assets. The core of *riba* is that it “represents a cost that is borne for the hope that the project succeeds, and such behaviour is consistent with ... the tendency to gamble”.<sup>116</sup> Thus, one may observe that the motivation behind the *riba* prohibition is to prevent operations that are based on mere reliance on chance. However, if the operation *guarantees* the return, interest payment is allowed. The difference is that in the first case, there is no guarantee on return by virtue of the “gambling” character of the operation, and in the second case, there is no “gambling”, but rather there is certainty about the return.

Investment activities that involve speculation are also prohibited by the Sharia law. This provision normally targets risky investment dealings such as gambling but allows for “genuine commercial risk-taking or investment in business enterprises”.<sup>117</sup> Also, business dealings that are

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<sup>115</sup> Smith, above n 83 at 35.

<sup>116</sup> Iqbal, Munawar, and David T. Llewellyn, eds. *Islamic banking and finance: New perspectives on profit sharing and risk*. Edward Elgar Publishing, 2002, 27

<sup>117</sup> Ibid.

uncertain in their returns are also prohibited by the Sharia law. Moreover, any business contracts which result in the enrichment of one party are also considered as illegal.<sup>118</sup>

Overall, one may observe that in Saudi Arabia, Sharia law has a positive impact on the local investment market by reducing the number of risks and/or disputes faced by foreign investors and the Saudi government agencies.

#### **2.5.4 Conclusion**

Under the Sharia law, the Saudi government is obligated to protect and uphold the sanctity of the God-given national wealth. One way of achieving this is by instituting Sharia-compliant regulations that allow for the fair and full exploitation as well as equal distribution of the national wealth. To achieve this, the Kingdom has put in place stringent regulations for vetting foreign investors before commencing on investment activities in the Kingdom. For example, anyone meeting the basic requirements for registration as a foreign investor is accorded some significant rights and privileges to ensure smooth engagement. Thus, foreign investors from the GCC and Arab League regions are accorded preferential treatment courtesy of the existing reciprocal agreements between their countries and Saudi Arabia. On the other hand, so as to enhance the sanctity of the Two Holy Cities of Mecca and Medina, foreign investors (except GCC and Arab League nationals) are not allowed to engage in any investment activities within the precincts of the two Holy Cities of Mecca and Medina.

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<sup>118</sup> Ibid.

## **2.6 The Islamic Sharia Law: Saudi Investment Climate**

Under the Islamic Sharia law, the Saudi government is obligated to provide a friendly investment climate that allows for a level playing field among foreign and local investors.<sup>119</sup> To achieve this, the Kingdom provides a range of regulations that ensure that foreign investors and their investments are entirely protected from arbitrary appropriation and/or possession by the state except for extreme situations when there is clear public need for such.<sup>120</sup> In a speech to the European Policy Centre Brussels, Belgium February 19, 2004, the Saudi Minister of Foreign Affairs opined that in the Kingdom, such regulations and/or reforms should not be perceived as a panacea for challenges that continue to be faced in the country as

*(...) a reform is not a mere slogan or a field for risky experimentation. It is an ongoing process where adaptability and continuity are essential. Within this framework Saudi Arabia is trying to evolve and adopt reforms rather than imposing them from above, taking into account the diverse views of its people, while maintaining the unity of the country and the cohesion of its society.*<sup>121</sup>

The minister further clarified that in order for these reforms to be effective, they must achieve three main goals. These goals are:

- 1. That the reforms contemplated shall address the specific needs of the community.*
- 2. That the reforms meet with popular approval and consent as much as possible.*

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<sup>119</sup> Saudi Basic Law, above n 39 art 1; Foreign Investment Law above n 91 art 6.

<sup>120</sup> Saudi Basic Law, above n 39 art 18.

<sup>121</sup> Al-Faisal, above n 40.

*3. That the reforms take into consideration the due process and cause no drastic social upheavals and unnecessary hardship.*<sup>122</sup>

It is arguable that most of the reforms instituted in the Kingdom have achieved these three goals. This is because they have increased the number of privileges accorded to foreign investors while simultaneously increasing the administrative services provided by the government to foreign investors. For instance, under the Capital Market Law, the Saudi government is obligated to establish a stock exchange market capable of facilitating a smooth, fair and efficient trading of securities within the Kingdom.<sup>123</sup> In addition, under the Foreign Investment Law, the Saudi government is obligated to provide statistical data as well as other pertinent investment-related information to foreign investors so as to facilitate smooth and quick growth.<sup>124</sup>

On the other hand, foreign investors are expected by the host states to fulfil and/or show intent of fulfilling several basic requirements before commencing investment activities.<sup>125</sup> These requirements may comprise the acquisition of the minimum capital set for the particular investment sector in question, and fulfilling of the requirements on the acquisition of immovable property for setting up the licensed activities among other pertinent requirements.<sup>126</sup>

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<sup>122</sup> Ibid.

<sup>123</sup> Saudi Capital Markets Law, art 1.

<sup>124</sup> Foreign Investment Law, above n 91 art 10.

<sup>125</sup> Ibid art 2.

<sup>126</sup> Foreign Investment Law, above n 91; Saudi Real Estate Regulations; Saudi Company Law; Saudi Capital Markets Regulations above 75.

Under the Saudi Foreign Investment Law, foreign investors are expected to meet the legal capacity requirements,<sup>127</sup> invest only in those sectors not featured in the Negative List,<sup>128</sup> incorporate their investments either as joint ownerships or as wholly owned entities,<sup>129</sup> and most importantly, abide strictly by the Real Estate Regulations as regards the ownership of immovable property for the smooth operation of the licensed activity or even for housing of their staff.<sup>130</sup>

## **2.6.1 Obligations**

### **2.6.1.1 Saudi Government Obligations**

Saudi Arabia has emerged as the most favoured investment destination among MENA countries in recent years.<sup>131</sup> This is because the Kingdom has put in place necessary investment infrastructures that accord to both foreign and local investors almost similar privileges. As a result, the country is ranked number four globally for promoting a free fiscal climate and number seven for putting in place a highly rewarding tax regime.<sup>132</sup> The Kingdom scores high rankings for other factors such as labour (7<sup>th</sup> globally), reforms of business climate (world's fastest reforming practices), and registration of property (1<sup>st</sup> globally) among other pertinent investment climate information.<sup>133</sup>

It should be noted that Saudi Arabia is a relatively new state, founded only in 1936.<sup>134</sup> Therefore, its achievements as described above indicate that the Kingdom has continuously fulfilled its obligations as a host country. No doubt this is in line with Verse 143 Surah 2

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<sup>127</sup> Foreign Investment Law, above n 91 art 1, 2; Saudi Negative List above n 92.

<sup>128</sup> Foreign Investment Law above n 91 art 3.

<sup>129</sup> Ibid art 5.

<sup>130</sup> Ibid art 8.

<sup>131</sup> 'Saudi Investment Climate' <<http://www.sagia.gov.sa/en/Investment-climate>>

<sup>132</sup> Ibid.

<sup>133</sup> Ibid.

<sup>134</sup> A. Madawi. *A History of Saudi Arabia*. (UK: Cambridge University Press, 2002).

(Baqarah) of the Book of God which gives guidance on the importance of honouring one's obligations. The verse holds that:

*Thus We have made you [true Muslims -- real believers of Islamic Monotheism, true followers of Prophet Muhammad and his Sunnah (legal ways)], a Wasat (just) (and the best) nation, that you be witnesses over mankind and the Messenger (Muhammad) be a witness over you. And We made the Qiblah (prayer direction towards Jerusalem) which you used to face, only to test those who followed the Messenger (Muhammad) from those who would turn on their heels (i.e. disobey the Messenger). Indeed it was great (heavy) except for those whom Allah guided. And Allah would never make your faith (prayers) to be lost (i.e. your prayers offered towards Jerusalem). Truly, Allah is full of kindness, the Most Merciful towards mankind.*<sup>135</sup>

In interpretation, this verse emphasizes the need to honour one's obligations. In this regard, the Saudi government is obligated to provide, among other things, necessary investment-related information,<sup>136</sup> ensure corrupt-free regulatory bodies, facilitate adequate social amenities, provide an efficient stock exchange market, protect an investor's property, and vet foreign investors before issuing investment licences.<sup>137</sup>

It should be noted that these obligations are applicable only to those investment activities and/or sectors allowed to foreign investors. In this regard, the state is not under any obligation to provide critical information regarding the oil sector to foreign investors given that no foreign

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<sup>135</sup> Holy Qur'an, Surah 2 (Baqarah) Verse 143.

<sup>136</sup> Foreign Investment Law above n 91 art 10.

<sup>137</sup> Ibid art 2.

investor is allowed to invest in the Saudi oil sector. Moreover, the scope of this chapter revolves around the investment activities between foreign investors and the Saudi government.

### **2.6.1.2 Foreign Investors Obligations**

These obligations are based on the Sharia guidelines, since their provisions pertain to investors' practices in the Kingdom of Saudi Arabia. Consequently, they are designed in a manner that the foreign laws that bind Saudi Arabia and other trading partners are observed, but also comply with the Sharia laws. In return for the wide range of rights and privileges accorded to them, licensed foreign investors are expected to honour the set regulations governing investment activities within the Kingdom as provided for by Article 15 of the Foreign Investment Law which stipulates that,

*“The foreign investor shall comply with all laws, regulations and directives in force in the Kingdom of Saudi Arabia, as well as international agreements to which the Kingdom is party.”*<sup>138</sup>

Some of the obligations include the timely and regular payment of the set taxes pursuant to Article 14 of the Foreign Investment Law which provides that

*“All foreign investments licensed under this Law shall be treated in accordance with applicable tax provisions and amendments thereto in the Kingdom of Saudi Arabia.”*<sup>139</sup>

In addition, foreign investors are obligated to cooperate with Saudi government agencies during the inspection of their business or even during any other activity. Other obligations

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<sup>138</sup> Foreign Investment Law above n 91 art 15.

<sup>139</sup> Ibid art 14.

include the observation of the Sharia-based social regulations meant to ensure a just nation pursuant to Article 6 of the Saudi Basic Law which categorically states that the Saudi citizens as well as residents who might be investors are required to abide by the Holy Qur'an and the Sunnah.<sup>140</sup>

From these discussions, one core generalisation can be made: Saudi Arabia protects its public wealth which according to Article 16 of the Basic Law is God-given. Article (16) stipulates that “*Public property has sanctity. The State shall protect it, and citizens and residents shall safeguard it.*”<sup>141</sup>

Apparently, part of the powers of protecting this public property entails entering into mutual agreements with other states so as to enhance the maximum and beneficial exploitation as well as the exchange of surplus goods, services, capital, and labour. This is understandable given that a nation state cannot provide all its own goods, services, capital and labour necessary to sustain its population. By entering into these mutual agreements, the Kingdom demonstrates its willingness to share/exchange its national wealth with other nations. Even so, the amount of its national wealth that the Kingdom shares and/or exchanges with other nations differs from one state to another or even from one region to another.

## **2.9 Conclusion**

This chapter has presented an analysis of the impacts of the Islamic Sharia law on investment activities between foreign investors and the Saudi government. For this purpose, it

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<sup>140</sup> Saudi Basic Law, above n 39 art 6.

<sup>141</sup> Ibidart16.



has examined all investment-related laws which have been established in the KSA. In addition, it has investigated the various obligations that the state owes to foreign investors.

It has been argued that the Islamic Sharia law is the supreme law in Saudi Arabia. This is because Saudi Arabia is officially a sovereign Muslim state structured according to the Book of God and the Sunnah. In connection to this, the chapter has argued that Saudi Arabia is one of the most conservative Muslim nations in the world given that it utilises the Hanbali school of jurisprudence in the application of the Islamic Sharia laws. Moreover, the fact that the Kingdom is home to the two most Holy Cities of Mecca and Medina makes it the epicentre of the Muslim faith.

On matters of investment, the chapter has argued that the local laws governing the vetting, registration and operation of investment activities in the Kingdom are a true reflection of the Islamic Sharia laws. Pursuant to the strict Islamic financing structures, these laws also help to reduce risks associated with normal investment activities. From a different perspective, these Sharia-compliant laws also help to create different categories of foreign investors, in this case, Muslim, Arab, GCC and Arab League investors.

Lastly, the chapter has extensively discussed the sensitive issue of sovereignty from a Sharia law perspective. Thus, the chapter holds that Sharia advocates the full sovereignty of the people and the nation.

## Chapter 3: Classes of Foreign Investors in Saudi Arabia

### 3.1 Overview

Foreign Investment Law perceives foreign investors as citizens of other nations pursuing investment activities within the KSA.<sup>142</sup> This is quite a general description of the non-Saudi investors given the diverse bilateral and multilateral agreements that the KSA has entered into with other nations pertaining to investments, some of which provide for the preferential treatment of non-Saudi investors from specific countries and/or regions. This preferential treatment permits different classes of foreign investors to carry out investment activities according to whether these activities are permissible and the modalities surrounding such investments. As evidenced in the Foreign Investments Code, foreign investors are not given total freedom to operate business as are local investors; instead, they are limited in terms of business and activities in which they are permitted to engage, and are left to the policing of some professional agencies. In this regard, it is arguable that the nationalities and/or regions of the investors determine the allocation of such investments. For example, pursuant to the agreement among the Gulf Cooperation Council (GCC) states, the KSA should accord preferential treatment to GCC states investors, similar to that given to Saudi nationals.<sup>143</sup> In the same way, pursuant to the agreement signed by all member states in the Arab League, the KSA is duty-bound to preferentially treat Arab League states investors chiefly in the areas of agriculture, industry and internal trade.<sup>144</sup> In this regard, this chapter is intended to carry out an extensive

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<sup>142</sup> Foreign Investment Law above n 91.

<sup>143</sup> Economic Agreement above n 37, art 3.

<sup>144</sup> Economic Unity Agreement, above n 103.

scrutiny of a wide range of laws, agreements, and Royal Decrees that have since been enacted to control the investment climate in the Kingdom of Saudi Arabia. Therefore, KSA promotes foreign investments but has reservations as defined by the laws and policies (secular and religious) on foreign investment, which restrict foreign investments to some extent to the advantage of local investors.

### **3.2 Introduction**

A general overview on the Saudi investment climate shows that over the years it has changed in terms of the range of accommodations accorded to foreign investors.<sup>145</sup> Ideally, as described in the previous chapters, this is courtesy of a range of ambitious plans the Kingdom has embarked on to market itself as the friendliest country within the Middle East and North Africa (MENA) region.<sup>146</sup> SAGIA is responsible for changes as it has been at the forefront of instituting best investment strategies in the Kingdom. According to the organization's networks and operations manager, Hassan Al Duham, this is part of the Kingdom's core objectives.

*SAGIA's objective is to create the best business strategy for achieving our vision of promoting direct investment into the Kingdom of Saudi Arabia and we are always looking at ways to leverage economies of scale and synergies.*<sup>147</sup>

This statement is strengthened by the deputy custodian of the Two Holy Mosques, Prince Sultan Ibn Abdulaziz Al Saud when expressing his gratitude to the SAGIA chief, Al-Dabbagh

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<sup>145</sup> Saudi Arabia Investment Guide above n 85.

<sup>146</sup> Saudi Arabia Investment Climate above n 84.

<sup>147</sup> 'SAGIA reduces costs with Cisco WeBex offered in partnership with stc in the Kingdom' (Dec. 13, 2010). <<http://www.sagia.gov.sa/en/sagia/media-centre/news/sagia-reduces-costs-with-cisco>>.

for overseeing a period of improved business climate in the Kingdom. The results from the World Bank placed the Kingdom at position 11<sup>th</sup> globally as one of the most friendly investment destinations. He said:

*'We thank you for the exerted efforts. We wish you further progress in light of the comprehensive developmental progress patronized by the Custodian of the Two Holy Mosques. King Abdullah Ibn Abdulaziz Al Saud.'*<sup>148</sup>

Again, it is demonstrated in Chapter 3 that the Kingdom has achieved this by signing mutual agreements (bilateral and multilateral) with other countries, establishing a series of legislations, and issuing Royal Decrees that outline various rights and privileges enjoyed by both Saudi and foreign investors.<sup>149</sup> It can be argued that the impetus for these legislations, Royal Decrees, and agreements, has been the poor performance of state-owned corporations as well as the rapid increase of the demand for critical goods and services occasioned by the increasing population.<sup>150</sup> For example, as a result of poor performance by the Saudi national electricity generating and transmitting company, the Saudi Electricity Company (SEC), the country effectively opened the transmission of electricity to foreign investment by removing it from the Negative List (list of investment activities barred from foreign investment).<sup>151</sup> Consequently, this led to the private sector owning as high as 60% of the Independent Water and Power Projects

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<sup>148</sup> 'Deputy Custodian Hails SAGIA's Role in Improving Investment Environment in Kingdom' (Dec. 5, 2010). <<http://www.sagia.gov.sa/en/SAGIA/Media-centre/News/Deputy-Custodian-Hails-SAGIAs-Role>>.

<sup>149</sup> Saudi Arabia Investment Guide above n 85.

<sup>150</sup> Norton Rose Group, 'Arbitration in the Middle East' (July 2008), at 13, <<http://www.nortonrose.com/knowledge/publications/pdf/Arbitration%20manuals/Middle%20East/file25752.pdf?lang=en-gb>>.

<sup>151</sup> Ibid.

(IWWPs), with the government maintaining 30% through the Saline Water Conversion Corporation (SWCC), and the remaining portion going to the SEC.<sup>152</sup>

Following the issuance of the *Royal Order 7/B/12661 at 17/03/1424H* in May 18, 2003 by His Royal Highness, the Saudi King, to all government agencies requiring them to revise the existing laws governing their mandate so as to adjust them to multilateral and bilateral investment treaties that the KSA had ratified,<sup>153</sup> as many as fifty-five investment-related laws “and their implementing rules” have since been enacted.<sup>154</sup> Some of these laws include the Commercial Law which is also popularly referred to as the Law of the Commercial Court, Capital Market Law, The Charter of the Saudi Arabian Monetary Agency, Foreign Investment Law, Law of Commercial Papers, Companies Law, banking Control Law, Cooperative Insurance Companies Control Law, and Anti-Money Laundering Law, among others.<sup>155</sup> For instance, the Anti-Money Laundering Law, ratified in August 2003, is one of the world’s most effective and powerful legislations governing Anti-Money Laundering according to FTAF (Financial Task Action Force).<sup>156</sup> This Law is highly significant at it minimizes the possibility of any money syndicates being established that would otherwise be used to negatively manipulate their investments.

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<sup>152</sup> Norton Rose above n 149, at 15-16.

<sup>153</sup> Royal Order 7/B/12661, 17/03/1424H .

<sup>154</sup> F Al Malki, ‘The development of commercial laws in Saudi Arabia’. (*Law Update*, 2003), 23.  
<[http://www.tamimi.com/files/.../Commercial\\_Laws\\_in\\_KSA\\_Jul08.pdf](http://www.tamimi.com/files/.../Commercial_Laws_in_KSA_Jul08.pdf)>.

<sup>155</sup> Ibid.

<sup>156</sup> Royal Order above n 152.

As a matter of fact, in a bid to align itself with the prevailing international investment trends, the Kingdom in 2000 enacted the Foreign Investment Law.<sup>157</sup> This law can be billed as the most explicit legislation in the history of the KSA commercial legislations in terms of defining who foreign investors are, the range of investment activities allowed to such foreign investors, the licensing requirements for investing in the Kingdom, as well as the terms and conditions governing the actual investment process.<sup>158</sup> By extension, multilateral agreements such as those between the GCC and the Arab League nations help to clarify the range of preferential treatments accorded to investors from different countries and/or regions, in this case the GCC and Arab League regions, respectively.<sup>159</sup> The Cooperation Council for the Arab States of the Gulf (GCC) is a regional organization consisting of six Gulf countries: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates. The GCC was created in May 1981. Its main objectives are to enhance coordination, integration and inter-connection among its Member States in different spheres. All the GCC member states are members of the Arab League; and Qatar, Saudi Arabia, Kuwait and the United Arab Emirates are the prominent members of OPEC.

Basically, the essential purpose of these legislations, Royal Decrees, and agreements was/is to enhance the ease of access to investment opportunities for both Saudi and non-Saudi investors (Arab and non-Arab, Muslim and non-Muslim, and GCC and non-GCC) pursuant to the tenets of the then envisaged 10 x 10 goal of becoming one of the top ten most economically competitive countries by the year 2010.<sup>160</sup> In fair terms, this was an ambition whose realization

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<sup>157</sup> Foreign Investment Law, above n 91.

<sup>158</sup> Ibid.

<sup>159</sup> Economic Unity Agreement, above n 103.

<sup>160</sup> SAGIA, (2010) [www.sagia.gov.sa](http://www.sagia.gov.sa), above n 146.

was wholly dependent on the Kingdom's ability to create more competitive investment opportunities for both Saudi and non-Saudi investors.<sup>161</sup> Among the envisaged changes was the ambitious petrochemicals production expansion plan that hinged entirely on the ability of the country to reduce some of the existing barriers to foreign investment.

Pursuant to this ambitious expansion plan, the Saudi Aramco made explicit plans that sought to offer new competitive contracts to foreign investment ventures particularly in the exploration and development of upstream oil and gases.<sup>162</sup> According to Al-Dabbagh, the SAGIA chief has moved through the ranks to occupy a prime position in the ease-of-doing-business rankings globally between 2005 and 2009. He said that over the years, SAGIA's main aim has been to

*(...) position Saudi Arabia among the top 10 most competitive nations by 2010 through the creation of a pro-business environment, a knowledge-based society, and by developing new, world-class "Economic Cities." He said, "The Kingdom's ranking improved from 67th among the 135 countries in 2005 to 38th in 2006, to 23rd in 2007, to 16th in 2008, and to 13th now in 2009."*<sup>163</sup>

Evidence gathered from the International Finance Corp. shows that SAGIA has achieved this overarching aim. This is because the Kingdom's reputation has improved over the years to now rank among the most friendly business destinations. This institution indicated that the

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<sup>161</sup> Saudi Arabia Investment Guide above n 85.

<sup>162</sup> Norton Rose above n 149, at 12.

<sup>163</sup> M.G.A Khan, 'Top world figures due at GCF 2010'. (Arab News, 2010).  
<<http://archive.arabnews.com/?page=6&section=0&article=127541&d=19&m=10&y=2009>>

Kingdom occupied position 16 globally in a report released in 2008, an improvement from position 67 in 2004. When breaking the good news to stakeholders, Al-Dabbagh stated:

*“We are only three positions away from achieving our 2010 goal ... In 2008, the United Nations Conference for Trade and Investment (UNCTAD) report had ranked Saudi Arabia as the 14th biggest recipient of FDI in the world, and the largest recipient in the Middle East and Africa; ahead of Turkey and South Africa...”<sup>164</sup>*

Actually, in 2010 the Kingdom of Saudi Arabia did realise its main goal. According to the *United Nations Conference for Trade and Investment (UNCTAD) 2010* report, the Kingdom of Saudi Arabia (KSA) still received the most FDI inflows in 2010, which amounted to \$28 billion US Dollars. Egypt came second with \$6 billion, and Qatar third with \$5.5 billion US Dollars. Lebanon, for its part, maintained fourth place, albeit with a slight increase from \$4.8 billion in 2009 to \$5 billion in 2010, while the United Arab Emirates (UAE) was ranked fifth with \$4 billion approximately.

Tellingly, because of these legislations, Royal Decrees, and agreements that empower institutions such as SAGIA, the gap between Saudi investors and their foreign counterparts has significantly narrowed in terms of the privileges they enjoy.<sup>165</sup> As a matter of fact, acting on the need to increase the foreign direct investments in the Kingdom as part of the envisaged 10x10 goal, the Saudi government increased the number of investment activities in which foreigners

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<sup>164</sup> Ibid.

<sup>165</sup> Saudi Arabia Investment Climate above n 84.



could be involved.<sup>166</sup> For instance, it has allowed internationally owned companies to explore downstream gas sites and permitted a wide range of activities in the petrochemicals sector.<sup>167</sup> Other sectors opened to foreign investment include: insurance, mobile telecommunication, education, and pipeline services.<sup>168</sup> In addition, the KSA government has also tried to woo foreign companies already doing business in the Kingdom to expand their existing activities to include these newly-opened investment opportunities.<sup>169</sup> This expansion of investment opportunities for foreigners can be interpreted as an indirect attempt to blur the lines between the different classes of investors in the KSA (Saudis and non-Saudis). The creation of the International Centre for Settlement of Investment Disputes (ICSID) in 1996 set up a forum to handle disputes involving foreign investors, which has been successful to date.<sup>170</sup>

Essentially, these legislations, Royal Decrees, and agreements, as well as their accompanying implementing rules have directly impacted on making the KSA a relatively friendly destination for foreign direct investments (FDI). In fact, they demonstrate the Saudi government's commitment to opening up new investment opportunities that initially were considered unfeasible due to inherent risks or the lack of technical know-how. Most importantly, the laws underscore the Saudi government's commitments to reducing the list of investment activities not allowed to foreign investors and wholly or partly relinquishing some of the state-

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<sup>166</sup> SAGIA above n 146.

<sup>167</sup> Saudi Arabia Investment Guide above n 85.

<sup>168</sup> Ibid.

<sup>169</sup> Ibid.

<sup>170</sup> 'Investment, ICSID and climate change: turning obstacles into opportunities', 2009, at 1-7 <<http://ecologic.eu/soef/ineg/downloads/Marshall.pdf>>.

run corporations to private investors.<sup>171</sup> Consequently, it can be stated that these regulations have undoubtedly contributed toward making the KSA one of the top rated places to do business, at position 13 overall, out of the 181 countries studied by the World Bank in 2009.<sup>172</sup>

These legislations, Royal Decrees, and agreements have achieved this in a number of ways that include: the creation of state agencies such as the SAGIA, Saudi Arabian Monetary Agency (SAMA), and The Royal Commission for Jubail and Yanbu, Saudi Arabian Basic Industries Corporation (SABIC), the Saudi Industrial Development Fund (SIDF), Shoura Council, and Capital Markets Authority (CMA), among others.<sup>173</sup> No doubt, it is these state agencies that are responsible for the enhancement of the

*...rapid and sustainable economic growth by creating a pro-business environment, providing comprehensive services to investors and fostering investment opportunities in key sectors of the economy, including energy, transportation, information and communication technology (ICT) and knowledge based industries.*<sup>174</sup>

The Shoura Council, which works as an advisory body to the King on matters of governance, has continued to make a strong impact in a number of areas. Its advice to the King on various matters of interest to the Kingdom has resulted in successful decisions being made. While addressing the Shoura annual meeting held in 2008, King Abdullah commended the Council for being steadfast in its duties. He stated:

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<sup>171</sup> 'Legal considerations for new investors in Saudi Arabia', (February 2010) at 1, <<http://www.hazzawilawfirm.com/.../Legal%20considerations%20for%20new%20investors.pdf>>

<sup>172</sup> Ibid.

<sup>173</sup> Saudi Arabia Investment Guide above n 85.

<sup>174</sup> Ibid.

*You continued your noble acts when you announced adding cost of living allowance to the salaries of government employees and retirees with a cumulative rate of 5% for three years in addition to that the government will bear 50% of port fees, passport fees, traffic licence fees and vehicle ownership transfer fees and residence permit renewal fees for house workers as well as the 10% increase in allocation for social security and other feasible decisions that reflect the state's keenness to alleviate the wave of price rises.*<sup>175</sup>

Secondly, these regulations have helped the country to achieve its primary goal of becoming the leading economy in the Middle East and North Africa (MENA) region and ranking among the top ten investment destinations by the year 2010<sup>176</sup>. This has been done by incorporating the private sector in the process of economy enhancement, particularly in wooing potential foreign investors to form joint investment ventures.<sup>177</sup> Thirdly, the Kingdom has also invested heavily in the development of critical infrastructure such as the opening up of new investment cities and development of road networks, railways, airports, water desalination and power (electricity) production, as well as “the expansion of oil production and refining capacity.”<sup>178</sup>

In order to effectively implement the Royal Order 7/B/12661 at 17/03/1424H which required all government agencies to revise laws so as to enhance FDI and social empowerment among the citizens, pro-business structures have been put in place. In his statement to the annual

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<sup>175</sup> King Abdullah, above n 47.

<sup>176</sup> SAGIA, above n 146.

<sup>177</sup> Saudi Arabia Investment Guide above n 85.

<sup>178</sup> Ibid.

Shoura meeting,<sup>179</sup> King Abdullah expressed his satisfaction with the council's efforts to identify key areas of development and propose plans to address them. These efforts have culminated in the establishment of a number of institutions such as the

*(...) establishment of King Abdullah University for Science and Technology, building industrial cities, planning to develop education, increasing number of scholarships, offering thousands of educational jobs, exempting the deceased from real estate fund premiums, supporting health and social services, compensating livestock owners, increasing barley subsidy, giving amnesty for prisoners of public right in addition to sending assistance to a number of Arab and Islamic countries, including Palestine, Lebanon, Sudan, Mauritania and Bangladesh.*<sup>180</sup>

Certainly, a combination of these three strategies has paid huge dividends within a very short period of time. In fact, an economy-wide overview indicates that between 2004 and 2007, the country's FDI outlay increased from US\$2 billion to US\$18 billion.<sup>181</sup> The following section discusses the case of Saudi Arabia, which has strong commercial laws in support of foreign investment and is therefore a suitable ground for such investments.

### ***3.3 Categories of Investors***

Basically, the KSA distinguishes between two broad investor classes, namely, Saudi and non-Saudi investors. This broad distinction is used to specify the type of investments which can

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<sup>179</sup> Shoura is a working council that comprises prominent personalities whose main responsibilities are to provide critical advice to the executive.

<sup>180</sup> King Abdullah, above n 47.

<sup>181</sup> Saudi Arabia Investment Guide, above n 85.

be undertaken as well as any associated restrictions and benefits. This means that regulations and benefits are different for the various groups of investors. Hence, it is important that investors understand these variations in order to comply with relevant requirements and understand the benefits to which the different classes of investors are entitled.

### 3.3.1 Saudi Investors

According to regulation 3(f) of the Saudi Arabian Nationality Regulations, a Saudi national is any person who resides within the boundaries specified as follows:

*“The Kingdom of Saudi Arabia includes the territories, territorial waters and the air space under the Saudi Arabian sovereignty, as well as vessels and airplanes, carrying the Saudi Arabian flag...”<sup>182</sup>*

However, that person needs to fulfil the following nationality requirements as provided by Regulation 4 of the same law.<sup>183</sup> First, that person should be either an “indigenous ... of the land” or should have been, “an Ottoman national on 1332 H” which is formally recognised as starting from “1914G.”<sup>184</sup> Again, in the case of the Ottoman nationals, it is clearly provided that if such subjects, “were born on the territories of the Kingdom of Saudi Arabia [,] and ... [as long as they] were residing therein ...[as of the issuance of] 1332 H, [formally interpreted as] corresponding to 1914 G. and who [in this case] continued to reside in these territories till

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<sup>182</sup> Saudi Arabian Nationality Regulations, reg 3(f), Resolution No (4), dated 25/1/1374.

<sup>183</sup> Ibid.

<sup>184</sup> Ibid, at reg 4(A).

22/3/1345 H without acquiring, any other nationality before this date,” they are Saudi nationals.<sup>185</sup> Lastly, a Saudi national is:

*...any person who was not an Othman subject ... [but] was residing in the territories of the Kingdom of Saudi Arabia ... [as of the issuance of] 1332 H, [formally interpreted as] corresponding to 1914 G...[provided that their residency] in these territories extended up to 22/3/1345 H without acquiring any foreign nationality before this date.”*<sup>186</sup>

Saudi investors (investments owned by Saudi nationals and joint ventures with at least 25% Saudi capital) are given immunity from unnecessary competition by the Ministry of Industry and Electricity, particularly in serving the local market.<sup>187</sup> This was evidenced by the unification of ten electrical companies under the name ‘Saudi Electrical Company’ with the aim of competing with the private investors who had an interest in electricity generation. This support included a tax waiver on imported raw materials and technological advice, and a guaranteed market through the use of a production and importation quota system.<sup>188</sup> Even so, such support is accorded only to companies that produce high quality products and that cover a large (major) segment of the local market.<sup>189</sup> The government also collaborates closely with such investors to ensure that their products are of high quality, thereby gaining the upper hand over

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<sup>185</sup> Ibid, at, reg 4(B).

<sup>186</sup> Ibid, at reg 4(C).

<sup>187</sup> Saudi Arabia Investment Climate above n 84.

<sup>188</sup> Ibid.

<sup>189</sup> Ibid.

foreign investors. Again, Saudi investors are allowed to sell their products at prices higher than those manufactured or imported by foreign investors.<sup>190</sup>

Figures collected between 2004 and 2006 show that Saudis owned only 20% of the total financial equity of the 2, 280 licensed joint ventures. Again, the results showed that Saudis have been very slow in taking up investment opportunities in both the service and industrial sectors. Specifically, figures showed that of the 928 licensed projects in the industrial sector, the Saudis accounted for only 25.4 % and a mere 6.4% of the 1, 347 licensed projects in the service sector.<sup>191</sup> Again, of the six licensed agricultural projects, Saudis had only 22.2%.<sup>192</sup>

It is not surprising that the Saudi economy is greatly influenced by foreign investors. For instance, based on empirical data collected between 2004 and 2006, foreigners accounted for 80% of the overall equity of the 2, 280 licensed joint ventures concentrated in the industrial and service sectors.<sup>193</sup>

### **3.3.2 Non-Saudi Investors**

“Non-Saudi investor” is a collective term that is used to refer to investors from other countries – GCC, Arab, non-Arab, Muslim, non-Muslim, etc. Article 1(e) of the Saudi Foreign Investment Law defines foreign investors as naturally existing persons who are nationals of other countries.<sup>194</sup> The article provides this by succinctly stipulating that a

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<sup>190</sup> Ibid.

<sup>191</sup> Anthony Shoult. *Doing business with the Saudis (3<sup>rd</sup> ed.)*, (GMB Publishing, 2006), at 38.

<sup>192</sup> Ibid.

<sup>193</sup> Shoult, Above n 190.

<sup>194</sup> Foreign Investment Law, above n 91 art 1(e).

*“Foreign investor [is] “[a] natural person who is not of Saudi nationality or a corporate person whose partners are not all Saudi.”<sup>195</sup>*

In extension, Article 1(f) and 5 (1) (2) further defines foreign investment as any form of capital investment jointly or wholly owned by foreign nationals as long as it is within the provisions of the Saudi investment laws. Article 1(vi) considers a foreign investor as a non-Saudi national or an investment in which partners, or all owners are foreigners to Saudi Arabia. Article 5 requires that the owner be a licensed foreigner described by the definition provided by Article 1(vi) above.<sup>196</sup> Actually, the law is flexible regarding the exact limit of such assets but does list a few categories of such assets. These are contained in Article 1(g) of the Foreign Investment Law, which stipulates that:<sup>197</sup>

*... For purposes of this Law, foreign capital shall mean, for example, but not limited to, the following assets and rights so long as they are owned by a foreign investor.*

- 1. Cash, securities, and negotiable instruments*
- 2. Foreign investment profits, if invested to increase capital, expand existing projects, or establish new ones.*
- 3. Machinery, equipment, furnishings, spare-parts, means of transport and production requirements related to the investment.*
- 4. Intangible rights, such as licences, intellectual property rights, technical expertise, administrative skills, and production techniques.*

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<sup>195</sup> Ibid.

<sup>196</sup> Ibid art 1(f), 5(1)(2).

<sup>197</sup> Ibid art 1(g).



Basically, except in extreme (special) cases, all non-Saudi investors are treated according to the provisions of the Foreign Investment Law and several other Saudi commercial laws meant to reinforce the provisions of the Foreign Investment Law, 2000. For instance, even after fulfilling the requirements outlined above, foreign capital investment activities must meet all the vetting and licensing requirements according to Article 2 of the same law before commencing operation.<sup>198</sup> Perhaps this is a prerequisite measure meant to ensure they do not contravene the set regulations regarding the types of investment activities permitted to foreigners.<sup>199</sup> Precisely, Article 2 of the Foreign Investment Law stipulates that:

*Without prejudice to the provisions of the laws and agreements, the authority shall issue a licence for foreign capital investment in any investment activity in the Kingdom, whether permanent or temporary. The authority shall act on the investment's application within thirty days of the submission of all the documents required by the regulations. If the specified period lapses without the authority acting on the application, it shall issue the required licence to the investor. If the authority rejects the application within the prescribed period, the decision must be justified, and the party whose application has been rejected shall have the right to appeal such decision according to laws.*<sup>200</sup>

In extension, before beginning any operation, foreign investors are expected to assume either of the two broad categories of business ownership in order for them to qualify according to

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<sup>198</sup> Foreign Investment Law, above n 91 art 3.

<sup>199</sup> Ibid.

<sup>200</sup> Foreign Investment Law, above n 91 art 2.

the requirements set by the licensing authority.<sup>201</sup> This is pursuant to the provisions of Article 5 of the same law which stipulates that

*“Foreign investments licensed under the provisions of this Law may be in either of the following forms: (1) Firms jointly owned by a national and foreign investor, and; (2) Firms wholly owned by a foreign investor.”*<sup>202</sup>

Moreover, for purposes of taxation, such firms may fall within one of the following business ownership types: they may be “[a] joint stock company, a limited liability company, or a company limited by shares...”<sup>203</sup> Again, non-Saudi investors can apply for temporary commercial registration (see Article 2) if the activities to be undertaken are short-term. These activities can include the franchising of consumer-oriented investments activities, distribution arrangements through established Saudi outlets or even opening up distribution outlets in the KSA, technical and scientific offices (TSOs) of foreign companies for technology-intensive activities, and setting up branches of foreign companies to represent foreign owned organizations within the KSA.<sup>204</sup>

Non-Saudi investors incorporated as joint investment companies as per the provisions of the April 9, 2000 Foreign Investment Law, enjoy several incentives (provisions) which include access to reliable statistical data regarding the Saudi development plans, modern infrastructural facilities in the newly-modelled investment cities, exemption from company tax for joint

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<sup>201</sup> Ibid at art 5.

<sup>202</sup> Ibid.

<sup>203</sup> New Income Tax: The Law. ch 1 art 1 cl 9.

<sup>204</sup> Saudi Arabia Investment Guide, above n 85, at 6-7.

ventures with at least 25% Saudi capital for 10 years starting from the incorporation date, preference for state procurement, and higher industrial loans with flexible repayment plans.<sup>205</sup>

Even so, it seems that the Foreign Investment law establishes only a general division between Saudi and non-Saudi investors, but fails to delineate the different categories of foreign investors. However, given the large number of countries that the KSA collaborates with on investment matters, either through bilateral or multilateral agreements, it is quite obvious that different categories of foreign investors receive completely different treatment under the existing Saudi investment laws. For instance, as will be further elaborated later on in this chapter, investors from Gulf Cooperation Council states are accorded the same treatment as are their Saudi counterparts,<sup>206</sup> while investors from the Arab League countries are given preferential treatment particularly in the realms of “agriculture, industry, and internal trade”.<sup>207</sup> Hence, it is essential to point out that although “non-Saudi investor” is a general term referring to investors from other nationalities and/or regions, there are special provisions that govern how these investors are treated.

### **3.3.3 Arab Investors**

For purposes of investment, the KSA considers Arab investors to be nationals and/or investment entities owned by nationals of the “Arab League,”<sup>208</sup> contracting states.<sup>209</sup> The ‘Unified Agreement for the Investment of Arab Capital’ in effect among the Arab nations, signed in 1980

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<sup>205</sup> Saudi Arabia Investment Climate, above n 84.

<sup>206</sup> Economic Agreement, above n 37, art 3.

<sup>207</sup> Economic Unity Agreement, above n 103 art 2.

<sup>208</sup> “Arab League” is a regional organization made up of Arab countries from North Africa and Middle East.

<sup>209</sup> Economic Unity Agreement, above n 103.

is given backing in Chapter VI to help handle disputes among the Arab League countries.<sup>210</sup>

Even so, for purposes of investment within the KSA, such persons are generally recognised as Arab League nationals and not as Muslims or even as Christians. In this case, neither Muslims nor Christians are accorded special preference, one more than the other, in terms of the investment activities in which they can engage or even the amount of capital they must deposit with the Saudi foreign investment licensing authority prior to the actual incorporation of the investment activities.<sup>211</sup> The central premise behind the consolidation of the contracting states' economies is to create the most favourable methods of utilizing the natural resources, thereby enhancing future economic prosperity. This is defined in the Economic Unity Agreement, under Chapter III, Article 14.<sup>212</sup>

Moreover, Article 1 of the *Economic Unity Agreement among States of the Arab League* grants nationals of contracting states a significant amount of immunity ranging from economic and social to cultural privileges. It stipulates that:<sup>213</sup>

*A Complete economic unity shall be established among the states of the Arab League. It shall guarantee for these states and their nationals in particular the following freedoms and rights on equal footing: (1) Freedom of personal and capital mobility; (2) Freedom of exchange of national and foreign goods and products; (3) Freedom of residence, work, employment and exercise of economic activities; (4) Freedom of transport, transit and*

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<sup>210</sup> 'OECD: Evolution of International Investment Agreements (IIAS) in the MENA Region' (2010), at 7, <<http://www.oecd.org/dataoecd/52/26/46581917.pdf>>

<sup>211</sup> Economic Unity Agreement, above n 103 Preamble; Foreign Investment Law above n 91.

<sup>212</sup> Economic Unity Agreement, above n 103 Preamble at ch III art 14.

<sup>213</sup> Economic Unity Agreement, above n 103 at art 1.

*use of transport, ports and civil airports, and; (5) Rights of possession, bequeath and inheritance.*

The provisions of this article should be interpreted literally. In this regard, it is clear that the five core freedoms stipulated in the article are to be accorded to the nationals of these states, whether they are Muslims or non-Muslims. After all, the Preamble to the agreement states that the underlying factor behind the league is the “natural and historical links among them,” and not religion.<sup>214</sup> Moreover, Article 2(5) of the same law provides the guidelines that the contracting states should adhere to so as to achieve a strong and unified economic growth.<sup>215</sup> It states, in part, that in order to achieve the envisaged unity, the contracting states should streamline all the:

*...policies related to agriculture, industry, and internal trade; and unification of economic legislation in a manner that would guarantee equivalent conditions for all nationals of the contracting countries working in agriculture, industry, and other professions.*<sup>216</sup>

Even so, pursuant to the provisions of Article 15 of this agreement (Economic Unity Agreement among States the Arab League), contracting states, in this case the KSA, are granted the authority to enter into other agreements with specific members of the Arab League for purposes of strengthening the objectives of economic prosperity. Article 15 stipulates that

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<sup>214</sup> Economic Unity Agreement, above n 103 Preamble.

<sup>215</sup> Ibid art 2(5).

<sup>216</sup> Ibid.

*“Any two or more of the contracting parties may conclude economic agreements that aim at realizing broader unity than that provided for under this agreement.”*<sup>217</sup>

In this regard, the KSA is a signatory to the GCC, an organization that encompasses five other Arab League members to which it accords more freedom than that enjoyed by the Arab League contracting states. Members of GCC are treated as nationals in terms of their investments and operate under unified labour rules, among other preferential benefits, which Arab League member states may not enjoy. As a matter of fact, as will be elaborated in the next section, investors from GCC states are treated in the same way as are KSA nationals – they are not subject to the income tax law.<sup>218</sup>

### **3.3.5 Gulf Cooperation Council (GCC) Investors**

GCC investors are nationals from the GCC states, namely, Bahrain, Kuwait, Oman, Kingdom of Saudi Arabia, United Arab Emirates, and Qatar running investment activities in the KSA. Pursuant to the provisions of the Economic Agreement between the Gulf Cooperation Council States (The Economic Agreement), ratified in 2003, investors from these five nations are accorded the same privileges as Saudi nationals under Article Two, “the International Economic Relations”.<sup>219</sup> In essence, the Preamble of the Economic Agreement outlines the need for the GCC states to forge strong and closely harmonised economic, financial, and monetary ties

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<sup>217</sup> Ibid art 15.

<sup>218</sup> Economic Agreement above n 37, art 3.

<sup>219</sup> Economic Agreement above n 37, art 3.

capable of propelling the region into the international economic elite' league.<sup>220</sup> The Preamble reads in part:

*... Pursuant to the GCC Charter which calls for closer ties and stronger links among Member States; and In the light of reviewing the economic achievements attained since the inception of the Council, including accomplishments attained by the Economic Agreement signed in 1981 ...and Seeking to achieve advanced stages of economic integration that would lead to a Common Market and an Economic and Monetary Union.... and Desiring to enhance the economy of the GCC Member States in the light of recent global economic developments which require further integration ... and Responding to the aspirations and expectations of GCC citizens towards achieving Gulf citizenship, including equal treatment in the exercise of their rights to movement, residence, work, investment, education, health and social services...*<sup>221</sup>

In affirming the provisions of the Preamble, Article 3 of the Economic Agreement stipulates that GCC member states should accord nationals of other GCC states equal treatment as if they were their own citizens, an indicator that such investors are not subject to the foreign capital investment law.<sup>222</sup> Such treatment should cover all economic realms including the payment of taxes as well as ownership of real estate near the two Holy Cities of Mecca and Medina in the case of the KSA. For instance, the Foreign Capital Investment Code dictates that joint ventures with 51% GCC capital must be accorded the duty-free export privileges when

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<sup>220</sup> Ibid at, Preamble.

<sup>221</sup> Ibid.

<sup>222</sup> Economic Agreement above n 37, art 3.

exporting to other GCC countries. However, only those joint ventures that have invested more than 51% of non-Saudi capital are to be accorded such preferential treatment.<sup>223</sup>

Interestingly, the agreement stipulates that such treatment should be accorded without bias and/or discrimination. The article provides that:<sup>224</sup>

*GCC natural and legal citizens shall be accorded, in any Member State, the same treatment accorded to its own citizens, without differentiation or discrimination, in all economic activities, especially the following: (1) Movement and residence (2) Work in private and government jobs (3) Pension and social security (4) Engagement in all professions and crafts (5) Engagement in all economic, investment and service activities (6) Real estate ownership (7) Capital movement (8) Tax treatment (9) Stock ownership and formation of corporations (10) Education, health and social services.*

In fact, Article 31 of The Economic Agreement also seems to affirm the nationalistic sentiments underlying the notion of “Saudisation,”<sup>225</sup> whereby Saudi nationals are expected to enjoy the fruits of economic development (employment opportunities, investment profits, improved infrastructure, etc.) more so than foreigners.<sup>226</sup> The laws do not specifically explain what happens when an investment involves a GCC and non-GCC compliant partner. So preferential treatment becomes difficult even when the two partners have unequal investment shares (say, 60% and 40%).

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<sup>223</sup> Saudi Arabia Investment Climate, above n 84.

<sup>224</sup> Economic Agreement, above n 37, art 3.

<sup>225</sup> “Saudisation” is used colloquially to refer to the notion that all prime sectors of the Saudi economy should be occupied by the Saudis. It may also be used to indicate Saudi nationalism.

<sup>226</sup> Legal considerations above n 170, at 2.



More specifically, in reference to the exclusivity granted to GCC nationals, Article 31 states that:

*“No Member State may grant to a non-Member State any preferential treatment exceeding that granted herein to Member State ... [or] conclude any agreement that violates provisions of this agreement.”*<sup>227</sup>

In addition, investors from the GCC states can legally run business activities in the KSA and still receive the standard treatment accorded to Saudi nationals such as access to investment opportunities listed on the Negative List. For example, investors from the United Arab Emirates can operate investment activities in the KSA and have the same privileges as Saudi nationals even if they are living in the UAE. This has been one of the most attractive methods of establishing business entities in the KSA, where GCC investors can establish off-shore fund companies in a GCC country, most preferably Bahrain, as a way of evading the rigorous Saudi licensing procedures. Bahrain does not have stringent licensing processes that investors find cumbersome, making it a suitable place for GCC investors. Such fund companies are then used to acquire other investment opportunities in the KSA as long as they are formally recognised by the Bahrain Central Bank. As expected, this form of business ownership is available only to GCC investors operating in Bahrain, not in the KSA.<sup>228</sup>

On the issue of taxation, investors from GCC countries are exempted from paying income tax but not zakat (an obligatory charitable donation) courtesy of their treatment as Saudi

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<sup>227</sup> Economic Agreement, above n 37, art 31.

<sup>228</sup> Saudi Arabia Investment Guide, above n 85, 11.

nationals.<sup>229</sup> This is in accordance with Article 3(8) of the Economic Agreement between the GCC States which, as explained above, provides for taxation treatment of GCC states investors similar to that of their Saudi counterparts.<sup>230</sup> In this regard, as part of the preferential treatment accorded to them, nationals of GCC states, whether running limited liability companies, joint stock companies, or even other forms of companies, are exempted from paying income tax, but not zakat. This stipulates that:

*"ALL Saudi companies and persons: male, female, adults, minors or legally incompetent, are subject to zakat after completion of one year under the provisions of Islamic Jurisprudence starting from 1/1/1370 H (corresponding to 13/10/1950)"<sup>231</sup>.*

As seen above, the Arab League agreement does not distinguish between Muslims and non-Muslims despite the fact that Saudi Arabia's secular laws have to be Sharia-compliant. The question, therefore, is whether members of other countries are given special status when investing in the KSA due to their religious status.

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### **(iii) Does the law of foreign investments classify the investors based on their religion?**

The question is whether Muslim investors, say from Australia, who extend their investments within the KSA are subject to the various laws governing foreign investments.<sup>232</sup> Two possible solutions can be envisaged. The answer at first glance appears to be obvious.

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<sup>229</sup> Economic Agreement, above n 37, art 3 (8); Zakat is an obligatory charitable donation.

<sup>230</sup> Ibid.

<sup>231</sup> Ministerial Resolution of the Zakat By-Law art 1, Res 393, (6/8/1370 H).

<sup>232</sup> Economic Agreement, above n 37, art 3.

Muslim investors originating from Australia are subject to laws governing foreign investment when they extend investments to the KSA because they are non-residents, and are therefore regarded as foreigners.<sup>233</sup> This implies that they are expected to comply with the various laws which control foreign investments.

In accordance with the KSA's foreign investment laws, all individuals who originate from other nations irrespective of being Muslims or non-Muslims are usually treated equally; hence, they are usually subject to the various laws which govern aspects of foreign investment.<sup>234</sup> This is in line with the spirit of the Economic Unity Agreement among states belonging to the Arab League where religion does not play a role at all.

The investment laws are usually aimed at ensuring that the KSA realizes its desired objectives and goals which require a steady inflow of expertise and technology. All individuals from outside the KSA – except where special agreements are in place - are therefore treated the same, irrespective of their religious leanings.<sup>235</sup>

Although Saudi Arabia is considered as a Muslim nation, it treats Muslims from other nations as foreigners and they are bound by similar rules which bind other individuals regarded as foreign investors.<sup>236</sup> In this case, individuals regarded as foreign investors are not categorised

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<sup>233</sup> 'Doing Business in the Kingdom of Saudi Arabia', (Al Swailem Consulting Group, 2011), <<http://www.agn-waa.org/pdf/DoingBusinessInKingdom.pdf>>

<sup>234</sup> Muhammad Al-Jasser and Muhammad Banafe Ahmed. "Monetary policy transmission mechanism in Saudi Arabia", (BIS Papers No. 35, 2011).441, <[www.bis.org/publ/bppdf/bispap35u.pdf](http://www.bis.org/publ/bppdf/bispap35u.pdf)>

<sup>235</sup> *Ibid.*

<sup>236</sup> Foreign Investment Law, above n 91.

into any differentiating groups, to which varying laws are applied; rather, they are all controlled by the same regulations pertaining to foreign investment.<sup>237</sup>

Although it has been argued that the Sunnah and Qur'an stand out as Saudi Arabia's law references, this was not a sufficient reason to differentiate the way in which individuals from nations other than the KSA are handled. This implies that all investors making foreign investments within the KSA are usually guided by the same laws irrespective of their religious beliefs.<sup>238</sup> Owing to the fact that foreign investors exert a great influence upon the nation's target operations, it is apparent that strict laws have turned out to be necessary for the purpose of ensuring that experienced outcomes do not harm national operations.<sup>239</sup> The laws therefore have been formulated in such a way that they direct the various activities undertaken by foreign investors so that the outcomes benefit the nation.

It is obvious that the investment laws need to strike a balance between two competing factors. First, foreign investors may benefit the nation by improving its economic performance due to their capacity to invest in a productive capacity which could not otherwise be possible within the country.<sup>240</sup> Conversely, competition from foreign activities may cause domestic investments to stagnate and prevent home-grown industries from developing.<sup>241</sup> Due to this, the nation treats all such foreign investors equally and they are usually bound by identical laws irrespective of whether they are non-Muslims or Muslims.<sup>242</sup> The purpose of having strict laws

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<sup>237</sup> Saudi Arabia Investment Guide, above n 85, at 2.

<sup>238</sup> Economic Unity Agreement, above n 103.

<sup>239</sup> Al-Jasser above n 233.

<sup>240</sup> Saudi Arabia Investment Climate above n 84; SAGIA above n 146.

<sup>241</sup> 'Saudi Arabia Advancing your Business' <http://www.sagia.gov.sa>.

<sup>242</sup> Saudi Arabia Investment Guide, above n 85.

irrespective of the religion of individuals is that they all have the capacity to bring about similar outcomes; hence, the need to prevent the occurrence of negative outcomes.

The various laws in this case include regulations regarding foreign investments which were enacted on April 9, 2000 , aimed at regulating the various investment activities within the KSA. It has been found that some of the investment laws apply to all investors whether foreign or domestic.<sup>243</sup> These include the law against money laundering.

As provided for in the Foreign Investment law, Muslim and non-Muslim investors - as long as they do not come from a country that has a preferential economic agreement with the KSA - must comply with the provisions of the Foreign Investment Law. Subject to Article 15, foreign investors are obligated to comply with all other laws set out for purposes of streamlining the investment climate in the KSA.<sup>244</sup> Article 15 stipulates that

*“The foreign investor shall comply with all laws, regulations and directives in force in the Kingdom of Saudi Arabia, as well as international agreements to which the Kingdom is party.”*

Simply put, foreign investors are expected to take up investment activities other than those included in the Negative List.

In return, they are accorded various benefits, including the freedom to repatriate the proceeds from any investment activities and to acquire real estate for purposes of operating licensed investment activities pursuant to the provisions of Articles 7 and 9 of the Foreign

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<sup>243</sup> Legal considerations above n 170, at 2.

<sup>244</sup> Foreign Investment Law, above n 91 art 3.

Investment Law. These Articles provide that licensed foreign investors together with their non-Saudi employees should enjoy a number of privileges such as accessing sponsorship services from the licensed business entities.<sup>245</sup>

The legal basis is articulated in Article 6 of the Foreign Investment Law which states that:

*“A project licensed under this Law shall enjoy all the benefits, incentives, and guarantees extended to a national project, according to laws and directives.”*<sup>246</sup>

However, regarding the payment of taxes, foreign investors are not accorded any preferential treatment in the KSA.<sup>247</sup> As has been explained in the preceding sections of this paper, the only classes of foreign investors accorded preferential treatment in the KSA are GCC states and, to some extent, Arab League nationals.<sup>248</sup> In this regard, other investors are governed by the provisions of Article 14 of the Foreign Investment Law, which stipulates that:

*“All foreign investments licensed under this Law shall be treated in accordance with applicable tax provisions and amendments thereto in the Kingdom of Saudi Arabia.”*<sup>249</sup>

### ***3.4 Classes Based on the Capital Outlay***

While the increasingly positive role of foreign investments in the KSA cannot be overemphasized, foreign investment laws have also been ratified over time, giving foreign

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<sup>245</sup> Foreign Investment Law, above n 91 art 7, 9.

<sup>246</sup> Ibid art6.

<sup>247</sup> Economic Agreement above n 37, art 3; Economic Unity Agreement, above n 103.

<sup>248</sup> Ibid.

<sup>249</sup> Foreign Investment Law, above n 91 art 14.

investors room to determine the kind of organizational frameworks on which their investments will be based (limited by the provisions of the Foreign Investment Code). Due to this, foreign investors in the KSA can decide which business organizational model to utilise depending on the amount of capital they have. In fact, the Saudi government sets specific figures for specific investment structures, with some sectors attracting greater sums of capital than others. This however, depends on the investment class, whether Muslim or non-Muslim.<sup>250</sup> For instance, investors seeking to invest in the industrial and agricultural sectors are expected to invest huge amounts of capital, while those interested in investing in sectors that require higher technological expertise are expected to invest less.<sup>251</sup>

To incorporate and operate a limited liability company, foreign investors from non-GCC countries must have a minimum of USD 133,314.14 before commencing operations.<sup>252</sup> In contrast, for wholly-owned limited liability companies by GCC investors, the KSA licensing authority does not set any minimum amount of capital; however, sometimes the Ministry of Commerce and Industry may set a minimum figure for purposes of convenience in transactions. In most cases, the Ministry may increase the minimum from the set 500, 000 Saudi Riyals (US \$133,372) to one million for industrial and twenty-five million for agricultural projects. Again, the minimum amount may be reduced for subsidized export-oriented investment activities

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<sup>250</sup> Saudi Arabia Investment Guide, above n 85, at 14-16.

<sup>251</sup> Ibid, at 14.

<sup>252</sup> Saudi Company Law, Royal Decree M37,11/03/1983H.

technological-intensive projects to attract potential investors to this sector that has been continually overlooked by the Saudi investors.<sup>253</sup>

On the other hand, for joint stock companies, investors are expected to have a minimum of two million Saudi Riyals (US \$533,490), with this amount increasing depending on the prevailing investment trends as analysed by the Ministry of Commerce and Industry.<sup>254</sup> Again, those joint stock companies that issue shares through public trading must have a minimum of ten million Saudi Riyals (US \$2,667,450), with 25% of this capital paid up front when the company is being formally established and the remaining is paid when the joint stock company is being incorporated.<sup>255</sup> Unlike the limited liability companies where GCC investors are not required to have the minimum amount of capital stipulated by the Ministry of Commerce and Industry, for joint stock companies no such special treatment is accorded to the GCC investors.<sup>256</sup>

On the other hand, foreign investors running business activities through “partnerships limited by shares,”<sup>257</sup> are expected to have at least 1,000, 000 Saudi Riyals before commencing operations.<sup>258</sup> As pertains to investment activities touching on the real estate sector, non-Saudi investors are expected to invest an amount of capital not less than thirty million Saudi Riyals,

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<sup>253</sup> Saudi Arabia Investment Guide above n 85, at 14.

<sup>254</sup> Saudi Company Law, above n 251.

<sup>255</sup> Saudi Arabia Investment Guide, above n 85, at 16; Ibid.

<sup>256</sup> Saudi Arabia Investment Guide, above n 85, at 14-16

<sup>257</sup> “Partnerships limited by shares” are described as those partnerships that have got one “partner who is personally liable for partnership debts to the extent of his personal assets, and at least four shareholders who are responsible for partnership debts only to the extent of their shares in the capital”; Saudi Company Law above n 251.

<sup>258</sup> Saudi Company Law above n 251.



including the amount of money required to purchase the actual land and development expenses.<sup>259</sup>

### ***3.5 How and Why Sharia Classify Investors***

All legislations, agreements, and Royal Decrees issued in Saudi Arabia are reflections of the Islamic Sharia law. In extension, Article 81 of the Basic Law provides that all laws, agreements and Royal Decrees enacted/issued thereof should conform to the Holy Qur'an and the Sunnah for them to be implemented in the Kingdom. This article stipulates:

*The enforcement of this Law shall not prejudice whatever treaties and agreements with states and international organizations and agencies to which the Kingdom of Saudi Arabia is committed.*<sup>260</sup>

In interpretation, this article provides for the harmonization of all the legislations and/or agreements enacted/ratified thereof for the smooth governance and discharge of justice among the Saudi citizens and residents. In this regard, the foreign investors classes discussed in Chapter 4 are Sharia-law-compliant. Therefore, it is correct to argue that the Saudi version of the Islamic Sharia law classifies foreign investors into various categories based on the anticipated mutual benefits.

These classifications are necessary as they are entirely based on the notion of reciprocity in the sense that, as a sovereign state endowed with immense natural resources, the Kingdom is committed to mutually engaging in exploitation/investment activities with like-minded states.

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<sup>259</sup> Saudi Arabia Investment Guide above n 85, 65.

<sup>260</sup> Saudi Basic Law, above n 39 art 81.

Mutual investment activities entail giving the same treatment to Saudi investors as is accorded to investors from states that have existing mutual agreements with Kingdom. However, the existence of these treaties reduces the confidence of investors from regions that are not covered under the treaties. This is because they feel discriminated against in terms of the business opportunities offered to them, and this eventually severs relations with other international trading blocs.

On the other hand, although no existing regulation explicitly classifies foreign investors as Muslims and/or non-Muslims, there are existing regulations that implicitly do so. As established earlier in this chapter, the mutual agreements between GCC and Arab League member states offer Muslim investors more privileges than their non-Muslim colleagues. This is because the majority of Muslim investors in the Kingdom originate from these two regions (GCC and Arab League) and therefore they enjoy preferential treatments not explicitly as Muslims, but implicitly as Muslims from GCC and Arab League regions. Analytically, it can be argued that the main reason behind Sharia law classification of foreign investors is to safeguard and uphold the sanctity of the God-given national wealth which according to Article 17 of the Saudi Basic Law has social significance.<sup>261</sup> In addition, it is also arguable that Sharia law classifies investors into various categories so as to encourage many investment partners to enter into mutual agreements with the Kingdom.

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<sup>261</sup> Saudi Basic Law, above n 39 art 17.

### 3.5.1 Does Classes Make a Difference?

All Saudi commercial laws are expected to be in harmony with each other. Even so, it is important to acknowledge that there are some discrepancies among these laws, particularly in regard to the treatment of investors from different nationalities. For instance, whereas the Foreign Investment Law which delineates the modalities governing the process of investment (foreign investment) provides general regulations, to some extent other commercial laws such as the range of agreements between the Kingdom and other economic partners, stipulate completely different terms.<sup>262</sup> Again, the provisions of the Economic Agreement among the GCC undermines the letter and spirit of the Foreign Investment Law, particularly regarding access to investment activities, access to loan facilities, payment of minimum investment capital, and payment of taxes, among other pertinent provisions.<sup>263</sup> These activities do not fully comply with the teachings of the Qur'an and Sunnah.

Consequently, these discrepancies produce a significant impact in terms of the overall growth of the Saudi economy as they end up placing some investors at a greater advantage than their counterparts, thereby creating imbalance in the way the national resources are shared. Moreover, these discrepancies are a blessing to the Saudi nationals as they get a chance to access foreign markets for their locally manufactured goods. In this case, the GCC countries provide an ample market for Saudi investors, as they can acquire goods from them and also sell their

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<sup>262</sup> Foreign Investment Law, above n 91; Saudi Arabia Investment Guide above n 85, at 14.

<sup>263</sup> Saudi Arabia Investment Climate above n 84.

products to them while still enjoying subsidized prices for key production materials and equipment.<sup>264</sup>

### 3.5.2 Effects of classifying investors

As noted earlier in this chapter and in the preceding chapters, foreigners are allowed to engage only in those investment activities that are not featured on the “Negative List” issued by the Council of Saudi Ministers.<sup>265</sup> For instance, Article 3 of the Foreign Capital Investment Law stipulates that, “[t]he Supreme Economic Council Licenced shall issue a list specifying the types of activities from which foreign investors are excluded.”<sup>266</sup> Essentially, this list comprises at least 22 investments areas spread across the Kingdom’s investment opportunities that are considered the preserve of Saudi nationals and/or Saudi government agencies and are therefore out of bounds to foreigners. More specifically, the investment activities range from “exploration, drilling and production of oil” to educational services, insurance services, retail and wholesale trade, to telecommunication services.”<sup>267</sup>

Even so, acting on the urge to streamline the service sector so as to meet the demands of the rising population the majority of whom is comprised of youth, the Supreme Economic Council has over the years been reviewing this list. An advisor at the Saudi Oil Ministry, Prince Faisal bin Turki strongly supports the review of the list, emphasizing the importance of expanding investments, particularly, in sensitive sectors so as to ensure that the supply of critical goods and services is provided to the citizens at cheap and stable prices. He was addressing a

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<sup>264</sup> Ibid.

<sup>265</sup> Foreign Investment Law above n 91 art 2.

<sup>266</sup> Foreign Capital Investment Law art 3, Res, 11/21, (17/11/1421 H).

<sup>267</sup> Shoult above n 190, at 101.

stakeholders' meeting called by the SAGIA to decide on the best investment strategies that the Kingdom should put in place. He said:

*Why are we importing plastic bags? We need to stop talking about expanding if we are not creating and focusing on local demand," he said. "We need to invest in goods that are sought by the local market and can create jobs locally."<sup>268</sup>*

This review has led, in whole or in part, to the elimination of several investment activities from the list. For instance, foreigners can now legally invest in some critical areas of the telecommunication, educational, publishing, and insurance sectors that have already been cleared for foreign investment by the Council.<sup>269</sup> No doubt, this regular revision of the "Negative List" by the Council is a positive step toward making the Saudi investment environment more equitable and vibrant. Moreover, this can be interpreted as an acknowledgement by the Kingdom that the MENA region and the world in general is a risky place that demands appropriate economic policies capable of ensuring maximum utilisation of resources. This fact has been acknowledged by King Abdullah in his speech during the G-20 meeting in 2008. In his capacity as the custodian of the Two Holy Mosques, the two most critical points in the MENA region and the entire Muslim world, he notes that:

*Our region is not immune to the effects of this crisis, and we in turn shall strive to adopt the economic policies necessary for the continued growth of our economies and to play a constructive role in the global economy.*

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<sup>268</sup> 'Saudi Arabia is seeking foreign investors industrial parks' (March 2011)

<<http://www.sagia.gov.sa/en/SAGIA/Media-centre/News/Saudi-Arabia-is-seeking-foreign-investors>>

<sup>269</sup> Shoult above n 190, at 101.

The regular revision of the “Negative List” has helped the Kingdom to enter into new investment agreements with members of the international community. Moreover, this has helped to broaden the range of privileges accorded to foreign investors.

In regard to protection of foreign investments, the KSA does not restrict the transfer of funds from investment profits to home countries. Foreigner investors, just like their Saudi counterparts, can duly dispose of their investment income in any way they see fit as long as it does not contravene the regulations stipulated by various Saudi commercial laws.<sup>270</sup> In fact, there are no checks on the amount of capital flowing in or out of the Kingdom for payment of debts, profits, dividends, interest payment, etc; however, foreigners are required to part with up to 45% of their total revenue to meet tax obligations for joint venture investments.<sup>271</sup>

### **3.5.3 Can Foreigners Own 100% of Companies in the KSA?**

Basically, the current Saudi commercial codes allow for 100% ownership of companies run by foreign investors whether or not such companies are limited liability entities or even joint stock entities.<sup>272</sup> Even so, there are some reservations about the combinations that some of these regulations allow, most probably pertaining to the espoused national sovereignty values as well as the unique religious (Islamic) and social traditions, which as discussed in the previous chapters, define the Kingdom. For example, it is stipulated in the Basic Law that all matters concerning the smooth governance of the Kingdom are to be referenced from the “Book of God and the Sunnah.”<sup>273</sup>

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<sup>270</sup> Saudi Arabia Investment Climate, above n 84.

<sup>271</sup> Ibid.

<sup>272</sup> Legal considerations above n 170.; Saudi Arabia Investment Guide, above n 85, at 14-16.

<sup>273</sup> Saudi Basic Law of Governance art 1, above n 39 .

One of the restrictions imposed only on foreign investors and those who are not exempt from treaties and agreements is based on the ‘Negative List’. The ‘Negative List’ mentioned in Article 3 states in brief:

*“The council shall have the authority to issue a list of activities excluded from foreign investment.”*<sup>274</sup>

In this regard, Article 1 affirms that regardless of the nature of the foreign investment, a number of laws restrict foreign investment. For instance, for ownership of companies by foreign investors, three issues must be adhered to: the investment must not feature in the “Negative List” that SAGIA (see Section 5 of the 2009/2010 Saudi Arabia Investment Guide) maintains; if in the banking industry, SAMA (Saudi Arabian Monetary Agency) sets the policies and regulations; and if in professional fields like law, the licensing bodies provide the regulations.<sup>275</sup> Essentially, the above and following limitations determine the extent to which foreign investors can own 100% of companies within the KSA. Primarily, the letter and spirit of the particulars of the highly regarded Negative List are adhered to when determining ownership of companies by foreign investors. Based on the fundamental notion behind the contents of the Negative List, it is obvious that foreign investors are not allowed to own even 1% of companies falling within investment sectors highlighted in the list.<sup>276</sup>

As a matter of fact, and as discussed in the previous chapters, investment opportunities in the KSA are carefully vetted and awarded only to the “right” investors. In this regard, whereas

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<sup>274</sup> Ibid.

<sup>275</sup> Smith, above n 83.

<sup>276</sup> Legal considerations above n 170, at 2.

Saudi nationals can operate investment activities in almost all the sectors of the country's economy with the exception of those that are run by state agencies, their foreign counterparts cannot. For instance, according to the provisions of Article 3 of the Saudi Mining Investment Law, some investment activities in the KSA cannot be left in the hands of foreign nationals.<sup>277</sup> These include "...petroleum, natural gas and derivatives thereof, pearls, corals and similar organic marine substances."<sup>278</sup> Others include ownership of real estate within the precincts of the two Holy Mosques of Mecca and Medina.<sup>279</sup>

The Mining Investment Law defines an investor as "*a natural or corporate person, Saudi or non-Saudi, who wishes to be granted specific rights over an area in accordance with this Law.*"<sup>280</sup> Article 3 provides that the authority shall have the right to provide a list of industries from which foreign investors are excluded. Petroleum, natural gas and derivatives thereof, and pearls, corals and similar organic marine substances are the areas from which foreign investors are excluded.<sup>281</sup> It is clear from the provisions of the Foreign Investment Act that investment in the petroleum industry, even in the form of shares, is not allowed. Foreign investment is defined as:

*"Investment of Foreign Capital in a licenced activity under this Act"* and foreign capital as *"money, instruments, securities and commercial instruments; , foreign investment profits if reinvested to increase capital, expand existing investment entities or establish*

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<sup>277</sup> Foreign Investment Law, above n 91 art 1(e) (f), 3, 5 (1) (2).

<sup>278</sup> Saudi Mining investment law art 3, Royal Decree M/47 (20 *Sha'ban* 1425 / 4th October 2004).

<sup>279</sup> Real Estate Regulation for Non-Saudis, Royal Decree 2340 (21/7/1390 AH).

<sup>280</sup> Saudi Mining investment law art 3, above n 277.

<sup>281</sup> Ibid art 1



*new ones; machinery, supplies, spare-parts, means of transportation and production requirements relevant to the investment; legal fights i.e., licences, intellectual properties, technical know-how, administrative skills and production techniques.’”*<sup>282</sup>

The other obstacle to maximum ownership of companies by foreign investors pertains to the autonomy of governance extended to the Saudi banking system.<sup>283</sup> Specifically, the Basic Law empowers the SAMA to regulate, coordinate, draw out, and impose policies relating to the critical processes of licensing as well as monitoring the minting and circulation of money within the Kingdom.<sup>284</sup> Basically, SAMA assumes the functions of conventional central banks as it is also directly responsible for the formulation of all the country’s fiscal policies vis-à-vis global fiscal trends.<sup>285</sup> In fact, because of the unique religious and social traditions which are weaved into the notion of national sovereignty and given impetus by the Sharia-based Basic Law, only a few wholly-owned foreign banking institutions operate in the country, with the majority of these being operated as joint ventures between one or more foreign investment groups and the Saudi government.<sup>286</sup>

Some of these co-owned banking institutions include Saudi American SAMBA co-held by Citigroup (United States), Al Saudi Al Franci co-held by Credit Agricole Indosuez (France), Saudi British co-held by HBSC (United Kingdom), Saudi Hollandi co-held by ABN AMRO (Netherlands), Bank Al Jazira co-held by National Bank of Pakistan, Arab national co-held by

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<sup>282</sup> Ibid art 1

<sup>283</sup> Legal considerations above n 170, at 2.

<sup>284</sup> Ibid.

<sup>285</sup> Saudi Arabia Investment Guide above n 85.

<sup>286</sup> Legal considerations above n 170, at 2.

Arab Bank (Jordan), and Saudi Investment co-owned by JP Morgan Chase (United States) and Industrial Bank of Japan.<sup>287</sup> Perhaps this trend is a result of the SAMA's bold stance not to make public the criteria it uses when vetting potential foreign investors intending to carry out investment activities in the country's partially exploited banking market.<sup>288</sup> A recent banking industry overview shows that most banking institution in the KSA are either 100% owned by Saudis or co-owned by Saudis and non-Saudis at a 60:40 venture ratio, respectively.<sup>289</sup>

The other pertinent caveat regards the regulation of the professional services sectors that require high levels of technical know-how as well as capital outlay. For instance, sectors such as "engineering, architecture, and law" are normally run by their "respective licensing bodies".<sup>290</sup> The reason for such close monitoring is to ensure that locally-trained professionals in these fields and locally-bred investors are given the opportunity to reap the fruits of professionalism, which works towards the realization of the country's envisaged education system goals of producing competitive graduates who are equipped with the necessary skills and knowledge to efficiently take up positions in their country's economy.<sup>291</sup> Again, this caveat may be interpreted as a measure by the Saudi government to safeguard and maintain its rich religious and social traditions.<sup>292</sup> In respect to this goal, foreign investors intending to invest in these fields are

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<sup>287</sup> Adrain E. Tschoegl, *"Foreign Banks in Saudi Arabia: a brief History,"* (Transnational Corporations, Vol.11, No. 2, 2002) at 136.

<sup>288</sup> Legal considerations above n 170, at 2.

<sup>289</sup> Ibid.

<sup>290</sup> Saudi Arabia Investment Guide above n 85, at 1.

<sup>291</sup> Ibid.

<sup>292</sup> SAGIA, above n 146.

required to partner with licensed local investors again, in joint ventures whose ownership rights do not exceed the 60:40 ratio, for Saudi and non-Saudi investors respectively.<sup>293</sup>

### ***3.6 Projects Owned by Foreign Nationals***

According to investment figures collected in 2009, foreign investors hold a significant portion of the KSA investment opportunities. However, in 2008, fifty-one of the 109 cases for arbitration by the ICSID that were resolved favoured the host state, while forty-eight favoured foreign investors, with the other four pending. This may suggest that local investors might in reality be holding a greater portion of investment within the KSA.<sup>294</sup> This is courtesy of the “economic diversification reform” program that the country has pursued over the years that has moved the country to the leading position on the “Ease-of-Doing-Business Index” among the MENA countries.<sup>295</sup> Other countries represented in the Kingdom include Japan, Germany, United Kingdom, France, Canada, Syria, India, Jordan, and Palestine, to name just a few. Empirical evidence gathered between the years 2000 and 2004 shows that foreign investment in the KSA accounts for the majority of the country’s industrial investments at 80%.<sup>296</sup> The United States leads in this category followed by Japan, France, the UK, Canada, Syria, India, Germany, Jordan, and Palestine in the top ten positions.<sup>297</sup> Again, data from this same period shows that foreign investors occupied as much as 80% of the country’s licensed joint ventures, which, as of 2004, stood at 2,280.<sup>298</sup> Curiously, and for no apparent reason, the Saudis have been hesitant

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<sup>293</sup> Saudi Arabia Investment Guide above n 85, 1; Al-Jasser above n 233.

<sup>294</sup> Investment, ICSID above n 169.

<sup>295</sup> SAGIA, above n 146.

<sup>296</sup> Shoult, above n 190, 37.

<sup>297</sup> Shoult above n 190, 38.

<sup>298</sup> Ibid.

about investing in the service sector.<sup>299</sup> Perhaps this has been because of the lack of proper technological know-how or even the risks inherent in the sector in terms of huge capital outlay.

### ***3.7 Conclusion***

This chapter has presented a comprehensive account of the modalities employed in the classification of foreign investors in the KSA. In this regard, it can be generally recapped that the major discrepancies between the various classes of foreign investors in the KSA are: (a) the number of privileges and/or rights accorded to foreign investors in terms of the nature of the investment activities they can undertake; (b) the amount of capital and technical know-how they require; and, (c) the percentage of ownership of investment ventures, among other privileges. For instance, according to the SAGIA, which is the body tasked with the responsibilities of vetting, licensing and coordinating investment activities in the KSA, Saudi investors as well as their GCC states counterparts can undertake any form of investment activity provided they meet the set monetary and technological qualifications. However, non-Saudis cannot engage in activities considered to be sensitive to the espoused values of national sovereignty. On the same note, Arab League investors are accorded preferential treatment, particularly in the realms of agriculture, industry and internal trade.

Even so, it is interesting to note that even as the KSA pursues the two main goals of economic liberalism and “open-market private enterprise policies”, it steadfastly adheres to its unique religious and social traditions.<sup>300</sup> In this regard, the Kingdom strongly delineates what

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<sup>299</sup> Ibid.

<sup>300</sup> Saudi Arabia Investment Climate above n 129.

foreigners can do in terms of investment and what the Saudi nationals can do. For example, pursuant to the provisions of the Negative List, foreign investors are not allowed to undertake investment activities concerning oil and mining in addition to a plethora of other activities considered sensitive to the national sovereignty.

Consequently, it can be concluded that King Abdullah and the Saudi leadership in general are committed to liberalizing the Saudi economy through the execution and implementation of the Kingdom's Islamic Sharia legal framework which provides for equality. Such commitment is affirmed by King Abdullah in his statements. Thus, during the interview with journalists from the Itar Tass News Agency, King Abdullah specifically expressed his desire to leave a legacy in his tenure by not abusing the powers granted to him by the Saudi constitution but by using them for the benefit of every male and female Saudi citizen. He opined that power

*(...) is about trustworthiness and responsibility. It is not only a force, influence or leverage that is used pass a decision, but also the responsibility of how you could draw a link between you and those you govern.*<sup>301</sup>

This indicates that, apart from the provisions of the Holy Book, the King espouses conventional leadership qualities of humility and dedication. For instance, he understands that

*Power is to embody the aspirations of the normal citizen in the street, understand the views of the elites, apprehend the details of the social texture of your society and conceive the relation between your country and people and the culture of the world*

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<sup>301</sup> King Abdullah's Interview, Itar Tass News Agency.  
<<http://portal.mofa.gov.sa/Detail.asp?InNewsItemID=60362/>>

*around you and the world at large. Power is to represent all what others would like you to be.*<sup>302</sup>

Needless to say, these qualities will go a long way to ensure that key decisions are made after serious consideration, particularly those that touch on the rights and privileges enjoyed by foreign investors doing business in the Kingdom.

## **Chapter 4: Dispute Resolution Aspects**

### ***4.1 Overview***

The Kingdom of Saudi Arabia (KSA) has in recent years emerged as one of the leading investment destinations in the world, ranking among the most preferred investment nations in the

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<sup>302</sup> Ibid.

Middle East and North Africa (MENA) region<sup>303</sup> With its numerous investments, the KSA has been able to attract investors not only from the GCC region, but from all over world.<sup>304</sup> The influx of investors to the country has been partly attributed to the versatile nature of its investment opportunities as well as its favourable investment climate, especially in terms of protecting and securing foreign investments.

In the KSA, two main processes have been put in place to offer foreign investors protection in the event of disputes against the government of the KSA or other private businessmen.<sup>305</sup> The first one is the use of litigation where the aggrieved party can take the matter to the courts for determination. However, owing to the constraints of the country's litigation processes, this avenue of dispute resolution has not been favourable to foreign investors. Instead, alternative dispute resolution methods have been commonly used, notably arbitration.<sup>306</sup> However, the choice of method depends on whether the foreign investors are involved in a dispute with the government or with private businessmen. This chapter explains and highlights various aspects of dispute resolution regarding investment disputes. It briefly explains litigation, but most of it is dedicated to alternative dispute resolution avenues, notably arbitration. Finally, the chapter makes a distinction between dispute resolution in disputes involving the government and foreign investors and those between private businessmen and foreign investors.

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<sup>303</sup> SAGIA, 'Investment climate in Saudi Arabia' <<http://www.sagia.gov.sa/Investment-climate/Some-Things-You-Need-To-Know-/Investment-Incentives/>>

<sup>304</sup> H Anthony, *Western Strategic Interests in Saudi Arabia* (London: Croom Helm, 1987) at 26.

<sup>305</sup> Turck, above n 8 at 19-29.

<sup>306</sup> Christian Buhring-Uhle and Gabriele Lars Kirchhof, *Arbitration and Mediation in International Business* (2nd Edition 2006).

## ***4.2 Introduction***

In the KSA, measures have been put in place to ensure that foreign investors, who are often prone to disputes with the government and with other private businessmen, are sufficiently protected from any undue investment losses resulting from disputes. To a large extent, foreign investors in the country are either engaged directly with governmental business projects such as public procurement, or they deal with private businessmen in the country. In the event of disputes, resolution mechanisms and various aspects of these have had to be modified accordingly since doing business with the government calls for different approaches to dispute resolution compared with doing business within the country's private sector. Where a foreign investor is engaged in commercial ventures with the government, the rules of the International Centre for Settlement of Investment Disputes (ICSID) have to be applied because the global body has been charged with the responsibility of ensuring that investments are protected wherever they are. In cases where foreign investors are engaged in business with the private sector, dispute resolution has mainly been by way of Alternative Dispute Resolution Mechanisms (ADR), notably arbitration which is often provided for in contractual agreements from the very beginning. This means, therefore, that regardless of the specific entity with which an investor is doing business – the government or the private sector – the most widely-used mechanisms for resolving investment disputes and thereby offering protection of investments, are litigation and ADR (arbitration is the preferred ADR mechanism, conciliation and mediation are less widely applied in the KSA).<sup>307</sup>

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<sup>307</sup> Shoult above n 190, at 103.



### ***4.3 Dispute Resolution Mechanisms***

Since about 80% of the total investments in the KSA are owned by foreigners, it has become the responsibility of the government to ensure that these foreign investors are protected by law in order to safeguard their investments.<sup>308</sup> Investment growth in any country is almost always accompanied by a corresponding rise in investment-related disputes. Therefore, the effective resolution of investment disputes is a key determinant of a country's ability to not only attract investors but, more importantly, to retain them. This includes both foreign and domestic investors.

While the KSA has provided a fairly cordial business environment for foreign investors, there have been challenges regarding protection occasioned by the fact that some investors engage directly with the government while others carry out their business with private businessmen. It is because of these parallel business operations that the investment environment in Kingdom of Saudi Arabia has significantly changed, owing to government provisions directed at both foreign and local investors. Hence, the effectiveness and success of any dispute resolution mechanism has become largely dependent on whether or not a foreign investor does business with the government or with private businessmen.<sup>309</sup>

As mentioned earlier, dispute resolution in the KSA is mainly undertaken by either litigation or ADR. And of the three commonly-applied ADR mechanisms, arbitration is the most preferred. Foreign investors, as noted before, are always keen to ensure that their investments are

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<sup>308</sup> Turck above n 8 at 24-25.

<sup>309</sup> Ibid.

well protected by the host country's legal framework. Therefore, the definition of a good investment climate in any country must include a description of its investment laws and rules. The government of the KSA has expressed its full support for investment dispute resolution through different channels, but arbitration and conciliation have been the most common. However, support for arbitration by the KSA has been on condition that the process is undertaken within the limits of the country's list of critical investment activities that are open to arbitration; and that the various investments for which arbitration is invoked as a mechanism to resolve disputes are fully licensed as provided for in the Saudi Foreign Investment Law 2000.<sup>310</sup>

Additionally, business dealings between the government and foreign investors are offered protection under Article 26 of the Foreign Investment Law Implementing Rules which defines the manner in which disputes between the two parties can be resolved through arbitration and in accordance with the Royal Decree No. (46) Dated 12.7.1403 H (April 26, 1983). One of the main reasons that the government of the KSA has been enacting the relevant legislations for investment dispute resolution is that, throughout the world, governments keen to increase investments in their country have moved to assure both existing and would-be investors (especially those from foreign countries) of the security of their investments. It is also widely known that the level of foreign investments in any country is almost a direct function of the soundness of that country's investment protection laws. Hence, the KSA can be considered as an investor-friendly nation owing to the fact that it is ranked among the most preferred investment destinations in the MENA region. But much of this high influx of foreign investors to the

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<sup>310</sup> Foreign Investment Law above n 91 art 26, implementation rules.

country can be directly attributed to the fact that the country has in place a very sound legal framework for investment protection.<sup>311</sup>

It is worth noting, however, that getting to this stage where foreign investors are assured of the security of their investments has not been easy. Various procedures and processes have had to be followed, notably the ratification by the KSA of International Investments Agreements (IIAs), which now act as a guarantee to all foreign investors that Saudi law will never be the only legal framework governing the protection of their investments in the country, but that international statutes will also play a very critical role in doing the same, such as the tax agreement with Netherlands that binds the two regions. And since international laws and statutes seek to offer versatile and unified protection of investments, foreign investors from all parts of the world have been readily drawn to the KSA as a result. Apart from the ratification of international treaties, the government of the KSA has also adopted various multilateral and bilateral agreements aimed at encouraging investments between it and other nations and regional blocs, thereby enhancing its ability to amicably resolve investment-related disputes. The most prevalent international binding treaty is the International Investments Agreements (IIAs), which provides guidelines on how the KSA investors relate with other foreign investors. The main approaches used to resolve investment disputes in the KSA are discussed below:

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<sup>311</sup> O Bakhashab, 'Legal Concepts of Saudi Law of Arbitration for Settling Commercial Disputes within National & International Spheres', (*Journal of King Abdulaziz University: Economics and Administration*, 2000) at 153.

### **4.3.1 Litigation**

While litigation is a very important mechanism in the resolution of various disputes arising from investments within the KSA, its application has been overshadowed by ADR owing to the traditional and historical limitations that have come to be associated with it. It is for this reason that this thesis is mainly concerned with the ADR mechanism of dispute resolution, especially arbitration which has been widely applied with high levels of success. As for litigation, it is excluded from this discussion for several reasons, all of which point to it as a second alternative to ADR and so is not a real priority. That aside, litigation is not an entirely appropriate mechanism for resolving disputes involving foreign investors for the following reasons:

1. Language barriers – Litigation is by its very nature a very tedious process which requires that parties to a dispute be able to not only understand each other well but also understand the language of the court officials presiding over their dispute. Many foreign investors are from the European Union (EU) and are essentially English-speakers, but in most local courts, Arabic is used. Given that the foreign investors in the KSA are drawn from different nations across the world, it is highly unlikely that they all understand Arabic which is the main language in the KSA and by extension the official legal language used in all courts in the country.
2. Inconsistencies in Litigation Law – Every foreign investor is always keen to have his investments protected as much as possible. Therefore, whenever disputes related to investment arise, investors expect the legal frameworks of the host nation to provide the necessary instruments to effectively manage the litigation process. One of the most important aspects of law which ought to be considered is the ability of courts to enforce the awards granted to foreign

investors in the same way as local investors.<sup>312</sup> However, many courts in the KSA lack this mandate within their jurisdictions, meaning that even though foreign investors can file their disputes in court for determination, there is no guarantee that the award granted will be enforced. For instance, Australian investors in the KSA cannot have their awards granted in the KSA enforced in their country.

High Costs – Litigation in the KSA is ranked among the most expensive dispute resolution mechanisms. Unless litigants are lucky enough to find a lawyer to take up their case on a contingency fee basis, business litigation is extremely expensive. It can cost thousands of dollars, at a minimum. Legal fees and other related legal costs are prohibitively high in the KSA and foreign investors find this rather intolerable.<sup>313</sup> The cost of conventional litigation measures has resulted in the formulation and development of ICSID which, while geared to produce similar dispute-resolution objectives, does not incur similar financial and psychological costs, and further enable investors to settle disputes amongst themselves. This ICSID mechanism includes arbitration, mediation, and negotiation. The ICSID processes are used to transform the investment environment and implement dispute-resolution roles and procedures for certain types of disputes.

The law protecting foreign investment in the Kingdom of Saudi Arabia is not comprehensive since it does not cover all disputes, resulting in some of them being resolved by international laws.<sup>314</sup> The responsibilities of the Kingdom of Saudi Arabia are to oversee the protection of

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<sup>312</sup> R David, *Arbitration in international trade* (1985) at 42.

<sup>313</sup> William W. Park, 'Treaty Obligations and National Law: Emerging Conflicts in International Arbitration' (58 *Hastings Law Review*, 2006) at 251.

<sup>314</sup> Al-Samaan, above n 1.

investments so that foreigners see this country as a good investment destination. However, the idea of preferential treatment of investors raises questions about the KSA's willingness to protect investments of foreigners when it comes to disputes. Bureaucracy-litigation processes in the KSA can take a very long time to conclude. Trial dates are usually delayed for months and years at a time. Investors may find on the eve of trial that no courtrooms are available and that the matter has been postponed to a date months into the future. This can result in huge legal fees that many investors do not anticipate. It therefore requires a lot of patience and perseverance on the part of the foreign investors to have their disputes resolved in courts. Due to a backlog of cases in the country's court systems, it has been difficult for cases to be expedited as required by many foreign investors.<sup>315</sup> This time-wasting process has meant the overall loss of critical investments.

3. Lack of Credibility in Domestic Courts<sup>316</sup> – Since foreign investments are more often than not very complex in nature, their expedited resolution through litigation has encountered obstacles such as underfunding and general lack of capacity of domestic courts. By filing a lawsuit, investors may expose proprietary information and other business records not only to the other side but also to the public at large. Defence lawyers have an arsenal of tools that they can use to get defendants to answer questions and submit documents. They can also subpoena (a court order) other people and use similar tactics on them. They look for dirty laundry and smoking guns. So many investors try to streamline the affairs of their companies before taking up a law suit. By extension, domestic courts in KSA are almost always overburdened by domestic cases

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<sup>315</sup> G Sayen, 'Arbitration, conciliation, and the Islamic legal tradition in Saudi Arabia' (*U. Pa. J. Int'l Bus. L.*, Vol. 9, No. 2, 1987), at 214.

<sup>316</sup> Turck above n 8

awaiting resolution. An already difficult situation is exacerbated when foreign investment cases are pending.

4. Risks of Partiality – Foreign investors not only in the KSA but in many other jurisdictions have had an inherent tendency to avoid litigation because domestic courts are considered to be biased and inclined to exercise double standards when handling investment disputes. For instance, many investors are seldom satisfied with the final result in any business lawsuit because local laws are those mostly invoked by the courts. Many foreign investors have expressed frustration at the decisions made by domestic courts, accusing them of using laws tailored to favour the local people and the government.<sup>317</sup> Sometimes, political overtones have come to play a critical role in influencing the decisions by courts, some deliberately driven by political interests, determining disputes in favour of the locals so as to punish an investor from a politically unfriendly country.
5. Variations in Litigation Procedures – Courts in the KSA are very different from courts in other countries. In Saudi Arabia, it is common belief that there are two sides to every story, and there is always a good probability that an investor will be counter-sued, which is when the opposing party decides to file a claim against the complainant. This difference becomes more pronounced when one moves away from the Arab world to the Western world and other areas where Arabic customs and practices are hardly known.<sup>318</sup> Hence, foreign investors not used to legal systems that have Islamic law as their foundation will often find litigation the least welcome option for the settlement of their investment disputes.

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<sup>317</sup> Julian Lew, Loukas Mistelis and Stefan Kroell, *Comparative International Commercial Arbitration*, (2003).

<sup>318</sup> Anthony, above n 302.

6. Religious Differences<sup>319</sup> – Perhaps one of the most common reasons why litigation is not a preferred mechanism for investment dispute resolution for foreign investors in the KSA is its close association and links with Islamic practices. As noted earlier, the Qur'an and Sunnah are the supreme law of the KSA; and it is upon this law that all other laws are founded. Since not every foreign investor practises Islam as a religion, the use of Islamic religious principles in litigation procedures has tended to deter these investors from taking this option. For instance, Sharia law is very strict on issues regarding the making of profits. Under Sharia law, all Saudi courts are not obliged to approve any monetary gains to parties that are claiming the loss or possible loss of profits in the days to come. Neither can courts give consent for the payment of interest on amounts that are long overdue. Such issues are definitely undesirable for foreign investors who are in the country to make as much profit as possible.

Owing to these limitations associated with litigation, ADR is the main mechanism of dispute resolution that is being investigated in this thesis, with great emphasis being placed on arbitration. Since arbitration has come to the fore as a preferred mechanism for dispute resolution especially for foreign investors in the KSA, the laws of the KSA require that investors include arbitration clauses in their contracts of investments stating in part that in the event of any dispute between the investor and his partner (government or private businessman), then the dispute will be resolved using arbitration.

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<sup>319</sup> Turck above n 8.



### 4.3.2 Alternative Dispute Resolution Mechanisms

Alternative dispute resolution mechanisms have been implemented for the resolution of investment disputes involving foreign investors. The resolved disputes have involved different parties some of whom were foreign investors suing their local business partners. On the other hand, alternative methods have also been widely used in disputes involving foreign investors suing the governments for practices they felt were breaching international agreements. Three main ones have been used: arbitration, conciliation, and mediation.<sup>320</sup> However, this thesis is mainly dedicated to the discussion of arbitration which has been the most commonly used owing to its special place in the constitution of the KSA. According to Article 1 of the Saudi Arbitration Law, it is up to the foreign investors (parties) to choose any alternative mechanism for resolving their investment disputes when such disputes do arise. Therefore, foreign investors have been given the right to choose how to settle their disputes and by which means. By extension, they can freely include arbitration clauses in their contracts as a safeguard for their investments as they can then have the assurance that their investments will be secured. Article 1 also allows foreign investors to arbitrate their conflicts even if their contracts do not have an arbitration clause. More protection for foreign investors is entrenched in Article 26 of the Implementation Rules of the Foreign Investment Law<sup>321</sup> as well as in Article 13 of the Foreign Investment Law which will be discussed in detail later.<sup>322</sup>

The popularity of arbitration is partly due to its success with Saudi Arabian foreign investors. During the last two decades, arbitration has become of increasing significance in the

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<sup>320</sup> Buhring-Uhle and Kirchhof, above n 304.

<sup>321</sup> Foreign Investment Law, above n 91 art 26.

<sup>322</sup> Ibid art 13.

Kingdom of Saudi Arabia as a means of resolving business disputes. In response to this phenomenon, Saudi Arabia issued its first Arbitration Regulations in 1983 (Royal Decree No. M/46 dated 1983), and its implementation rules by the Council of Ministers Resolution No.7/2021/M dated 8/9/1405 H; corresponding to May 27, 1985 G. Article I of the Regulations provides that "arbitration may be agreed upon in a specific existing dispute. It may also be agreed in advance to arbitrate any dispute arising as a result of the execution of a specific contract." This article therefore validates arbitration generally as a means of dispute resolution and does not limit arbitration to commercial matters. It expressly recognises the validity both of the submission, or agreement to resolve an actual dispute between the parties by means of arbitration, and of the agreement to refer to the arbitration clause in any existing contract. Arbitration has benefits that no other dispute resolution mechanism affords, especially in its application in the context of foreign investment disputes in the KSA. They include the following:

1. Arbitral awards granted in the KSA can be enforced in any other seat.<sup>323</sup> Similarly, courts in the country can enforce arbitration awards granted by other seats, giving investors assurance about their investments regardless of where they are from. According to Article 19 of the Arbitration Law, it is the duty of the authority with jurisdiction to make sure that all disputes are handled in a way that allows aggrieved parties to make appeals. The resolution is required to be reasoned, in writing, and in Arabic. Article XVII of the Regulations provides that "the award document shall include in particular the arbitration document, a summary of the oral statements and documents of the parties, the reasons and text of the award, the date of its issuance, and the signatures of the

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<sup>323</sup> Turck above n 8.

arbitrators. If one or more of them refuse to sign the award, that shall be stated in the award document” If there is sufficient evidence that there is no worthwhile objection coming from either of the parties to the dispute, the authority with the jurisdiction has the obligation of ensuring that in granting the arbitral award, no public policy of the KSA is contravened.<sup>324</sup>

2. Liberty to Choose Arbitrators – One of the commonest and perhaps most important concerns for foreign investors is the ability for justice to be delivered fairly in investment disputes. This has especially been a concern in litigation where judges determine the outcome of the case. In arbitration, all parties to a dispute are represented fairly because each has a part to play in the selection of the arbitrators.<sup>325</sup> Even where the arbitrator is an agency, the parties to a conflict have to agree to it before the arbitral process can commence.
3. Expediting of Arbitral Proceedings – Unlike litigation, arbitration in the KSA’s investment disputes is seen as a rather fast way of resolving disputes. There are no unnecessary delays as far as time is concerned.<sup>326</sup> Since speed is a critical factor in investment dispute resolution, arbitration has been instrumental in helping foreign investors to save a great deal of resources in terms of time and other investments.
4. Comparatively Low Cost – Arbitration is one of the few investment dispute resolution mechanisms in the KSA that can be afforded by almost all parties.
5. Fairness and Efficiency – Every party to a dispute expects that the resolution of the dispute is done in a way that is not only fair but also efficient. Arbitral processes in the KSA stand out for their exceptional efficiency and fairness. This is due to the fact that the arbitrators are

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<sup>324</sup> Law of Arbitration art 19, Royal Decree M/46 (12 *Rajab* 1403 - 25 April 1983).

<sup>325</sup> Turck above n 8.

<sup>326</sup> The Permanent Court of Arbitration, ‘*International Alternative Dispute Resolution: Past, Present and Future*’ (2000).

empowered to order independent investigations and to conduct on-site inspections. They are also authorized to appoint one or more experts to report on technical or other matters and to set these experts' fees and determine which party will pay them. Parties may submit advisory reports on the issues. This has been largely attributed to the fact that the country's arbitration law expressly provide for these issues, requiring that all arbitrators being selected by parties to a dispute must first have a good understanding of both Saudi commercial laws and Sharia law.<sup>327</sup> Given that Sharia law is a main part of the Islamic teachings, all arbitrators strive to adhere to its requirements as much as possible, almost in a similar manner as they would adhere to the very teachings of the Qur'an.

Further legal provision is made to the effect that arbitrators ought to be male and Saudi nationals so that cases of bias are avoided. Most importantly, they ought to be well-versed in the practice of the Muslim faith. Further provision is made in the arbitration requiring that there must be an odd number of arbitrators (almost always three) so that key decisions can be reached by voting. Finally, every person who is selected to act as an arbitrator must have a high level of moral integrity, and not be guilty of having committed *hudoud* crimes at any given time in his life. Close monitoring of arbitral proceedings by competent authorities, by extension, ensures that both parties to a dispute adhere strictly to the provisions and rules of the arbitration process. This has the added advantage of enhancing the chances that both parties will accept the arbitral award at the end of the whole process.<sup>328</sup>

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<sup>327</sup> Sayen, above n 313.

<sup>328</sup> Ibid.

6. Uniformity and Versatility – Arbitration has gone a long way in minimizing discrepancies in litigation laws especially concerning international disputes. This is because it offers all parties a unified law which has to be adhered to by all parties to the dispute.<sup>329</sup> Since foreign investors are wary of litigation because of, among other issues, its use of Saudi and Islamic law, arbitration gives them confidence as they can have their disputes settled fairly away from home just as they would have at home.
7. Promotion of Investment Cooperation – Unlike litigation which has the greatest potential of straining relations between foreign investors and host nations, arbitration has come in handy to not only resolve investment disputes but also, in doing so, promote cooperative coexistence among businessmen.<sup>330</sup> Through arbitration, foreign investors in the KSA have been able to enhance their business relationships with both the government and private businessmen.
8. Arbitral Matters are Clearly Defined – In the KSA, foreign investors are made aware in advance of the areas in which they can arbitrate and the ones in which they cannot invoke arbitration. This makes it very clear to them when and where they can arbitrate, thereby minimizing the costs of having to arbitrarily try out dispute resolution mechanisms. Article 2 of the Law of Arbitration states that:  
  
*“Arbitration shall not be accepted in matters wherein conciliation is not permitted. Agreement to resort to arbitration shall not be deemed valid except by those who have the legal capacity to act.”*

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<sup>329</sup> Lew, Mistelis and Kroell, above n 315.

<sup>330</sup> A Redfern and H Martin, *Law and Practice of International Commercial Arbitration* (London: Sweet & Maxwell, 2004) at 567.

This clause points out that the right to use arbitration as a dispute resolution mechanism is not by any means automatic but the preserve of selected persons that merit its use based on the criteria set by the government of the KSA. This is understandable because, for instance, minors cannot be left to arbitrate in their disputes since they lack the so-called *full Legal capacity* requirement as stipulated by Article 2 of the Arbitration Law Implementing Rules.<sup>331</sup> Additionally, endowment administrators, parents, and guardians of such minors cannot use arbitration except with the consent of the court. Here, the advantage of arbitration is that it cannot be misused as it is applicable only to matters which directly involve the foreign investor while in the KSA.<sup>332</sup> Furthermore, there is a clear delineation by the country's arbitration system between arbitration procedures that are ad hoc and those that are institutional. By extension, a clear distinction is made between arbitration procedures that are national and international; and the difference between arbitration procedures based on clauses and agreements is also clear.<sup>333</sup>

#### **4.3.2.1 Disputes with Government**

As mentioned earlier, the KSA is faced with protecting investors from foreign countries who are doing business with either the government or private businessmen in the country. When disputes involving foreign investors and the government need to be resolved, the former have to go to the ICSID.<sup>334</sup> However, this is only for those foreign investors who do not have investments in the oil sector. For those in dispute with the government and yet have investments in this lucrative sector of the KSA's economy, there is still provision for them to arbitrate. The

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<sup>331</sup> S Ware, 'Arbitration Clauses, Jury Waiver Clauses, and Other Contractual Waivers of Constitutional Rights' (*Law and Contemporary Problems* Vol.67, 2004) at 634.

<sup>332</sup> *Ibid.*

<sup>333</sup> A.H. Al Ahdab, '*Arbitration with Arab countries*' (Kluwer law and Taxation Publishers, 1990) at 594.

<sup>334</sup> Shoult above n 190, at 103.

only limitation here is that Saudi arbitration law as opposed to international arbitration law is applicable. However, if foreign investors investing in the oil sector do not wish to arbitrate using Saudi arbitration law, they can resolve their disputes amicably or by using relevant laws in accordance with Article 13(2) of the Foreign Investment Law:<sup>335</sup>

*Disputes arising between the foreign investor and its Saudi partners in relation to its investments licensed in accordance with this Law shall, as far as possible, be settled amicably. Failing such settlement, the dispute shall be settled according to relevant laws.*

The relevant laws include international investment agreements such as the ICSID, multilateral investment agreements such as those between GCC and Arab League countries, bilateral agreements such as those between the Kingdom and the US, Italy, Philippines, Malaysia, Germany etc., and local investment laws such as the Saudi Arbitration Law and the Foreign Investment Law.<sup>336</sup> This is because, in line with Article 25(4) of the ICSID:<sup>337</sup>

*“Any Contracting State may, at the time of ratification, acceptance or approvals of this Convention or at any time thereafter, notify the Centre of the class or classes of disputes which it would or would not consider submitting to the jurisdiction of the Centre. The Secretary-General shall forthwith transmit such notification to all Contracting States. Such notification shall not constitute the consent required by paragraph (1).”*

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<sup>335</sup> Foreign Investment Law above n 91 art 13.

<sup>336</sup> Turck above n 8.

<sup>337</sup> Yves Fortier, “Arbitrating in the Age of Investment Treaty Disputes”, (The University of Southern Wales Law Journal, 2008) at 31 (1).

This clause effectively means that all investment disputes in the KSA have been duly covered by the ICSID jurisdiction.<sup>338</sup> This excludes those investments touching on the very sensitive areas of the country's economy, notably the oil sector, or as provided for in other laws passed in the country. A good example of such a law is Section 3 of the KSA's Foreign Capital Investment Law which came into force in the year 2000 and which specifically states in part that "matters which have significant impact on the economic and national security policies of KSA ought to be effectively shielded from foreigners as much as possible." Therefore, when they are read together and interpreted, according to Article 25(4) of the ICSID the Royal Decree No., M/8 Dated: 22/3/1394 H) (April 15, 1974), the KSA has the final say in what is submitted to the ICSID jurisdiction and what is resolved at home.<sup>339</sup>

#### **4.3.2.2 Disputes with Saudi Private Businessmen**

According to Article 6 of the Foreign Investment Law of 2000<sup>340</sup>, every investment venture has the right to enjoy the benefits that are due to any national project. It says in part:

*All investment ventures licensed under this Law [Foreign Investment Law 2000] shall enjoy all the benefits, incentives and guarantees extended to a national project, according to laws and directives.*

This article is best understood when it is read alongside Article 3 of the Foreign Investment Law of 2000 that states:<sup>341</sup>

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<sup>338</sup> Shoult above n 190, at 103.

<sup>339</sup> Park above n 311.

<sup>340</sup> Foreign Investment Law above n 91 art 6.

<sup>341</sup> Ibid art 3.



*The Council [Saudi Supreme Council] shall have the authority to issue a list of activities excluded from Foreign Investment.*

With this information, and judging by the so-called Negative List (a listing of the investment activities from which individuals of foreign nationality are barred), it becomes expressly clear that foreign investors have arbitration as the only mechanism to resolve their disputes regarding licensed ventures. They may not, however, present their case to the ICSID owing to the fact that this international body is concerned only with interstate matters or matters pitting one state against individual investors of a different state.<sup>342</sup>

While not much is said regarding how exactly foreign investors in the KSA are to engage in dispute resolution through ADR, something is said regarding arbitration as a mechanism. This is that in undertaking any dispute resolution process, appropriate measures ought to be taken to ensure that prejudice towards other existing arbitration laws and regulations is not in any way reflected. A key law to this effect is Article 13 of the Foreign Investment Law which, among other provisions, explicitly requires that all investment disputes arising from licensed ventures between foreign investors and any of the three entities namely the Saudi government, any of its agencies, and any of its citizens must be settled in a manner that is most friendly.<sup>343</sup> Therefore, the invocation of the relevant laws will have to follow.

In the context of this study, the term “Relevant law(s)” is used to exclusively mean Sharia-based Basic Law. The term “friendly” as used to describe a mechanism or aspect of resolving investment disputes, effectively means arbitration. Therefore, investment disputes

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<sup>342</sup> T. G Nelson, “*History Ain’t Changed: Why Investor-State Arbitration Will Survive the New Revolution*” (2010 Kluwer Law International, The Netherlands), at 555.

<sup>343</sup> Foreign Investment Law, above n 91 art 13.

between foreign investors and Saudi private businessmen can be resolved largely by arbitration because it is the only mechanism that is provided for and supported by most international investment agreements. This means it is the best placed dispute resolution mechanism for such disputes involving private, non-governmental entities and foreign investors. The only disadvantage of arbitration, however, has been that its application is limited only to cases where its basis is international law and where it is aligned with local frameworks of law.

#### ***4.4 Conclusion***

The protection of foreign investors in the KSA is largely by way of ensuring that they can effectively resolve any disputes that arise. And owing to the fact that disputes are unavoidable, especially where commercial activities are undertaken, the government of the KSA has taken drastic measures to ensure that appropriate dispute resolution mechanisms are made available for foreign investors. Disputes between foreign investors and private businessmen are resolved largely by litigation or ADR, with arbitration being the most effective ADR mechanism owing to, among other reasons, its almost universal acceptance internationally. Hence, this thesis has discussed at length the process of arbitration and in particular its benefits to foreign investors operating in the KSA. In disputes between foreign investors and the government of the KSA, the matter is referred to the ICSID unless the disputes involve investments in the oil sector in which case disputes are resolved amicably using relevant laws.

The KSA has become one of the leading investment destinations in the MENA region partly as a result of its concerted efforts to put in place appropriate legal frameworks that can help assure foreign investors of the safety and security of their investments in the country. Such

efforts have included the ratification of international treaties and clauses, and entering into bilateral and multilateral agreements with individual nations and regional blocs to enhance the KSA's ability to effectively handle investment disputes. The result has been that many foreign investors feel increasingly secure and have no qualms about investing in the country.

## Chapter 5: Arbitration

### 5.1 Overview

Arbitration has been found to be an effective means of resolving disputes. According to Ibn Taimiya, a renowned Muslim scholar, “the rule of our contracts is tolerance and validity and one must only forbid or set aside those contracts which are forbidden by virtue of text or qiyas.” Therefore, it is clear that since arbitration is not considered as *Haram* by the Islamic Sharia law, then it should be perceived as *Halal* and, therefore, contracts providing for arbitration should be fully enforced. After all, the Book of God upholds the legitimacy of arbitration in the following words, “*O ye who believe respect your contractual undertakings.*”<sup>344</sup> This chapter attempts to examine the root of arbitration in Saudi Arabia as well as the reasons for its recognition within the legal system. It compares the Act of 1983 with that of 1985 and considers the shortcomings of the Act of 1983. In addition, it discusses the 1963 protocols in relation to the arbitration acts.

The Saudi Arbitration Law officially recognises the validity of arbitration clauses mutually agreed upon by the contracting parties during the time of drafting a contract.<sup>345</sup> Articles 1, 5, and 7 of Arbitration Law allay the prevailing fears about the validity of the arbitration agreements provided for during the process of drafting a contract particularly in contractual agreements where a party, or both of the parties made it clear to exploit such arbitration

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<sup>344</sup> Naheed Maabreh (n.d.). ‘Agreements binding in Saudi Arabia? Three theories revised’, Saudi Arabia Office,16 <[http://www.tamimi.com/files/articles/Riyadh/Arbitration\\_KSA\\_Jul08.pdf/](http://www.tamimi.com/files/articles/Riyadh/Arbitration_KSA_Jul08.pdf/)>.

<sup>345</sup> A. Baamir and I. Bantekas. ‘Saudi Law As Lex Arbitri: Evaluation of Saudi Arbitration Law and Judicial’ (*Arbitrational International*, Chartered Institute of Arbitrators, Vol. 25, No. 2, 2009), at 244.

agreements well before a dispute occurs.<sup>346</sup> Initially (before the Arbitration Law and its Implementing Rules), the Sharia courts were better known for their strong stance in refusing to recognise and implement the provisions of the arbitration clauses in a contract before a dispute arose.<sup>347</sup> Moreover, the courts were adamant about dealing with only the first parties to disputes as long as they are parties to an existing arbitration agreement that is subject to premature dispute resolution terms. In clear terms, the Implementing Rules acknowledged that arbitration clauses in a contract are legally binding on the contractual parties and that it should not be subjected to the problems of new arbitration agreements.<sup>348</sup>

Even so, the Arbitration Law does not encompass all types of investment disputes.<sup>349</sup> In fact, the KSA government and its agencies are not bound by the provisions of the arbitration clauses even if they are embroiled in disputes.<sup>350</sup> However, an exception that allows this is provided in the form of a ministerial authorization from the Council of Ministers and/or a Presidential consent. This is a true reaction to the effects of the ARAMCO case where the KSA government was found guilty of a contract breach and fined accordingly. This prompted the KSA policy makers to formulate legislations that would cushion the government and its entities against future ‘unfavourable’ arbitral tribunal award rulings on disputes between the state or its agencies and foreign entities.<sup>351</sup> This is clearly provided for in Article 3 of Arbitration Law which stipulates:

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<sup>346</sup> Law of Arbitration above n 322, art 1, 5 and art 7.

<sup>347</sup> Baamir and Bantekas above n 343, at 246.

<sup>348</sup> Ahdab above n 331, at 569.

<sup>349</sup> Law of Arbitration above n 322, art 3.

<sup>350</sup> Ibid, art 3 and art 8.

<sup>351</sup> Baamir and Bantekas above n 343, at 248.

*Government bodies may not resort to arbitration for the settlement of their disputes with third parties except after approval of the President of the Council of Ministers. This provision may be amended by a Resolution of the Council of Ministers.*

These provisions were a follow-up to a Royal Decree signed in 1963 that imposed a ban on all forms of arbitration if a KSA government agency, ministry, department, or even its representative is involved in a dispute.<sup>352</sup> Moreover, this is in tandem with the notion of flexibility as provided for the ICSID where the jurisdiction of the convention is limited to only investment disputes that the member states outlined/declared during the ratification of the Convention. In this regard, it is generally agreed that the ICSID provisions and the arbitration instruments provided thereof are applicable only within the limits of these member state declarations; anything outside these declarations is addressed by the host state's domestic legal framework.<sup>353</sup>

Apart from the salient role of enhancing investor protection, this method also helps to create mutual investment opportunities for Saudi-based investment ventures. The Kingdom achieves this by holding talks with other like-minded states. These talks are intended to strengthen trade ties and open up new investment opportunities for foreign investors. For example, talks between the Kingdom and Italy have yielded immense returns in recent years. Moreover, while on a three-day visit in Saudi Arabia, the Canadian Minister in charge of International Trade, Peter Van Loan, expressed his satisfaction with the mutual investment agreement that the two states have since enacted. He said,

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<sup>352</sup> Ibid.

<sup>353</sup> Shoult above n 190, at 112.

*My three-day visit to Riyadh will provide an opportunity to raise and discuss several important subjects with Saudi officials, including full access to the Saudi beef market, cooperation in the agriculture sector, and issues concerning the operation of Research in Motion's BlackBerry services in Saudi Arabia.*<sup>354</sup>

On the other hand, the Kingdom has since instituted talks with the Italian government aimed at opening up mutual investment forums for both countries. These forums span the agricultural and industrial sectors. Dr. Buora, a representative of the Italian Ministry of Agriculture back in 2004 asserted that

*“(...) strengthening the Saudi-Italian relations in the agri-industrial sector will go a long way in boosting the economies of the two countries.”*<sup>355</sup>

The Italian Ambassador, Dr. Armando Sanguini, stated that bilateral trade between Saudi Arabia and Italy will go a long way in instituting strong economic pillars capable of cushioning the two countries in times of economic crises. He reiterated his country's commitment to implementing this bilateral agreement. He said:

*Italy was keen to strengthen the bilateral program with Saudi Arabia, particularly in water and irrigation, fishing and aquaculture systems, collaboration on safety issues*

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<sup>354</sup> 'Canadian minister's visit to Kingdom focuses on trade' (Oct 8, 2010).  
<<http://www.sagia.gov.sa/en/SAGIA/Media-centre/News/Canadian-ministers-visit/>>.

<sup>355</sup> 'Italian officials speeches' <<http://www.ameinfo.com/46331.html>>.

*related to agricultural mechanization and in pursuing common interests in the agri-industrial product sector.*<sup>356</sup>

## **5.2 History of arbitration in the Kingdom of Saudi Arabia**

The history of arbitration law in the KSA is linked to business opportunities of oil and other basic commodities such as copper, agricultural products, fertilisers and petrochemicals. Foreign nations consider Saudi Arabia as a country that meets the investment demands of many Western countries with which it conducts most of its trade. In 1998, for instance, U.S goods accounted for approximately 21% of imports to Saudi, and in the KSA there are about 5.5 million workers from foreign countries.<sup>357</sup>

The Kingdom of Saudi Arabia is arguably one of the best known energy trading centres in the Middle East. It is also ranked as the largest exporter of petroleum.<sup>358</sup> This is due to its existing world oil reserves estimated to be around 20%. Over the years, the Kingdom has improved in terms of its overall oil productivity to occupy the prime position in oil production. Being one of the biggest producers of oil, Saudi Arabia found itself in many commercial disputes that could not be handled by the Sharia, especially cases that involved Western partners who did not understand or follow the Sharia. Arbitration was thought to be the best way to resolve disputes.

Arbitration in the Kingdom of Saudi Arabia started from the early days of oil exploration and was used until the '50s although it was not formalized at that time.<sup>359</sup> However, this changed

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<sup>356</sup> Ibid.

<sup>357</sup> Sayen above n 313, at 34.

<sup>358</sup> Ware above n 329, at 634-647.

<sup>359</sup> Anthony, above n 302.



after the ARAMCO case of 1958.<sup>360</sup> ARAMCO was formed as a result of an agreement between King of Saudi Arabia and a British American concessionaire whereby this company was supposed to conduct oil exploration in Saudi Arabia. They were assigned the Eastern part of the state. Identification of oil took a lot of time, yet only minor traces of oil were discovered. In addition, they did not have any equipment or enough capital to start mining; hence, they had to import these which necessitated more money and time.<sup>361</sup>

In 1954, the Government made an agreement with yet another company, the '*Arabian American Oil Company*' under the leadership of Mr. Aristotle Onassis to engage them in oil transportation. This caused a conflict between ARAMCO and the Saudi Arabian Maritime Tankers Limited. The former company had put in place strategies for oil transportation as they had installed pipelines and signed several agreements such as the trading terms including reduced tariffs on how to oil make available to their clients depending on the amount they have. They were denied their right to transport as per the set contracts with the government.

To resolve their disagreement, ARAMCO initiated arbitration but the Saudi government was dissatisfied with the decision of the arbitral tribunal which ruled in favour of ARAMCO. It developed some hostility towards any arbitration conducted outside Saudi or any that followed non-Saudi law.<sup>362</sup>

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<sup>360</sup> Redfern and Martin above n 328.

<sup>361</sup> E. Lauterpacht and H. Lauterpacht, H. (1960). *International law reports: Saudi Arabia v Arabian American Oil Company*. "State responsibility: Nature and kinds of state responsibility from revocation of, or interference with concessions or concessionary contracts."

<sup>362</sup> Arbitration did not only dissatisfy the government but also the involved party if Saudi Arabia arbitration law was applied for foreign companies. (New York :Skyhorse Publishing) 89 <<http://www.dlapiper.com/arbitration-in-the-kingdom-of-saudi-arabia/>>

According to Zuhur (2005), the 1983 act was devised for business purposes for it deals with ministries related to business. It gave the following outline: The Kingdom's businessmen//or women were to accept the goods that met the standards set by the Government.<sup>363</sup> However, foreign companies and business persons did not always act according to the terms of the arbitration and the government deplored the fact that foreign rules were applied within and outside the country.<sup>364</sup> Foreign traders were to provide a warranty of goods for a year after the conclusion of a deal or a new supplier was selected.<sup>365</sup> Moreover, there was no juridical support or clear procedure for the arbitration process, thereby making the resolution of problems between private parties sporadic at best. Foreign awards were subject to scrutiny by the judiciary and Saudi Arabia's government.<sup>366</sup>

Since then, the Kingdom has ratified a number of local and international laws that have streamlined the process of resolving investment disputes. Plans to put in place an international conciliation centre within the Kingdom are at an advanced stage. Local legal practitioners have been trained as a pre-emptive measure to prepare them for the tasks ahead of the actual opening of the institution that is intended to enhance awareness of the enforceability of international arbitration laws such as the UNCITRAL. When speaking at the conclusion of an awareness seminar for legal experts, the person in charge of overseeing preparations for the conciliation centre, Dr. Fahd Mushabab Aal-Khafir opined that:

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<sup>363</sup> S. Zuhur, S. (2005). Saudi Arabia: Threat, Political Reform, and the Global War on Terror. *Carlisle, PA: Strategic Studies Institute*, at 70 <<http://www.carlisle.army.mil/ssi/pdf/PUB598.pdf>>

<sup>364</sup> F. Rahman and A. Sheikh (2003). 'The Legal Regime of Foreign Private Investment in Sudan and Saudi Arabia'. *New York: Cambridge University Press*, at 104.

<sup>365</sup> Ibid.

<sup>366</sup> S. Thomas, 'The American Review of International Arbitration' (New York: Hans Smit and Juris Publishing, Inc, 2006) at 306.

*The Makkah International Centre for Conciliation and arbitration will be the main headquarters for Afro-Asian arbitration starting March 15 ... [and it] will play a very important role in finding solutions to complex commercial issues.*”<sup>367</sup>

It is expected that this institution will play a core role in streamlining the process of resolving investment disputes through arbitration within the Kingdom. This will have a huge impact now more than at any other time particularly considering that the Kingdom is strengthening its overall investment capacity by opening up new investment sectors and partnering with the international community in risky and sensitive areas such as upstream oil and gas exploration and extraction.

### **5.2.1 1963 Protocols**

The Government accepted the 1983 Act because the state had formerly set up protocols in 1963. The protocol declared that the only applicable law was Saudi law and that government bodies were not allowed to enforce any foreign law to govern relationships between countries.<sup>368</sup> The parties involved had the responsibility of reporting the dispute. An ad hoc panel would listen to the case. If the ad hoc team would not help, a legal team could take over to carry out the process of arbitration.<sup>369</sup>

The 1963 protocols allowed for a solution to be derived from a compromise by either one party or both. If the parties failed, the legal team would come up with a decision on how the arbitration process would be carried out. In addition, they would ensure the protocols they used

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<sup>367</sup> Dr. Fahd Mushabab Aal-Khafir, speech by the Chairman of the organizing committee for setting up an international conciliation centre at the Mecca, (conclusion of a legal practitioners training held in March 2009).

<sup>368</sup> Zuhur, above n 363.

<sup>369</sup> Ibid.

did not permit any international agreements but they would follow what is outlined in their laws especially in matters concerning commercial activities. These protocols also outlined the procedures to follow for activities such as ordering and supplying when trade was being done internationally. Moreover, they gave a few privileges such as reduced tariffs to those nations that favoured Saudi Arabia with trade. In their declaration, the protocols ascertained that all government agencies were to obtain approval from Council Ministries whenever there were disagreements.<sup>370</sup>

The protocols did not allow for any trials. This denied the arbitrators the right to be more informed and the parties had no opportunity to testify or defend their cases accordingly in order to arrive at any solution. The protocols allowed submission of the dispute and arbitrators could choose the rules to follow in resolving the problem. They followed them and agreed on the best way to resolve the problem. Since the arbitrators were not continuously monitored, this could end up in business success, or else failure to appropriately solve the problem.<sup>371</sup> It was after this that the discussed solution was presented to the parties concerned. They were not allowed to question anything but had to accept it as it was.<sup>372</sup> Later, an award was to be made within an interval of one year. This was after a third arbitrator was invited. The award was given out without any input from anyone, and this meant that they were not permitted to challenge the resolution arrived at by the arbitration team.

It was only after this entire process was concluded that the arbitration team calculated the total expenses. Costs were divided equally between the two parties and each would contribute an

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<sup>370</sup> Sayen above n 313, at 78-80.

<sup>371</sup> Rahman and Sheikh above n 362.

<sup>372</sup> G. Bajaj, (2009). 'Arbitration in the Kingdom of Saudi Arabia'. < <http://www.dlapiper.com/arbitration-in-the-Kingdom-of-saudi-arabia/>>

equal amount to meet the total cost. If there were any reasons as to why the cost should not be shared equally, they would agree on the amount that each party would have to pay.

In conclusion, the arbitration process was one that required the procedures to be followed to the mark. The 1963 protocols were very complicated and denied the people several rights such as the right to representation which would help resolve disputes.<sup>373</sup> Therefore, it was necessary to devise a better means of resolving the disputes.

### **5.2.2 1983 Act**

The 1983 Act provided stated regulations which were available to overseas business people and their counsels.<sup>374</sup> Despite the fact that it would take care of the international trade, the Act gave the Government the arbitration protocols that allowed it to control and monitor other fundamental units in like agencies and courts.<sup>375</sup> This Act was implemented because it ensured that both local and international arbitration protocols were stated and favourable to all parties.<sup>376</sup> Article 1 has a unique feature which is not found in any other procedural rules. Parties may resort to arbitration with regard “*to a specific existing dispute*” but also, as traditionally is known under the severability argument, agree beforehand to resolve future disputes through arbitration. The parties could examine their difference before enlisting the aid of one or more intermediaries. If not, the dispute would be presented so that the arbitration act would be used unless there were

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<sup>373</sup> Zuhur above n 361 at 74-79.

<sup>374</sup> Sayen above n 313, at 79-82.

<sup>375</sup> Rahman and Sheikh above n 362, at 72.

<sup>376</sup> However some countries have other alternatives apart from arbitration law. For instance France, see Sayen above n 313.

other production agreements that could be invoked.<sup>377</sup> However, what is not clear is whether an agreement to arbitrate has to be in writing. The act is silent on this issue.

Article 1 states that:

*“It may be agreed to resort to arbitration with regard to a specific, existing dispute. It may also be agreed beforehand to resort to arbitration in any dispute that may arise as a result of the execution of a specific contract.”*<sup>378</sup>

This means that if a dispute exists between two parties which do have a mutual contract, arbitration may be chosen as a method to resolve their differences. However, the parties involved may select arbitration as the process through which their disputes will be resolved before signing the contract. This was a precaution in case a dispute occurred between the parties in the future.

A confirmation was required that it was a real dispute that needed to be resolved. This was to deter the parties from launching an arbitration process in a case that could easily be resolved. After determining that the dispute was valid, they would approach a legal body (the body deemed as competent in dealing with the arbitration) of impartial persons, that is, persons who supported neither side and were therefore positioned to make sound and objective decisions that allowed arbitration. This was in accordance with Article 2 of the 1983 Act:

*“Arbitration shall not be accepted by the law or either of the parties in dispute, in matters wherein conciliation is not permitted. Agreement to resort to arbitration shall not be deemed valid except by those who have the legal capacity to act.”*

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<sup>377</sup> S. Thomas above n 364.

<sup>378</sup> Law of Arbitration, above n 322, art 1 and art 2.

Article 2 resolves the matter of arbitrability. Arbitration is permitted only where conciliation is also permitted. It suggests that the 1983 Act envisaged a two-tiered approach, namely conciliation followed by arbitration. Also, the Article stated the legal capacity as a condition for the validity of the arbitration agreement but failed to specify the legal capacity.

Article 3 includes a notable exception which in effect excludes government bodies from arbitration unless approval from the President of the Council of Ministers has been obtained. In both Acts, this was to be done in accordance with Article 5 of the 1983 Act. At that time, this Act was of great importance albeit with limitations.<sup>379</sup> The limitations affected the application of this Act since boundaries of the actions to be undertaken in case one failed were not defined in the conciliation. These involved cases where parties could not accept the resolution offered to them. Arbitration is restricted to private parties, and government bodies pursuant to Article 3 can resort to arbitration only by a resolution of the Council of Ministers.

In Article 4, the parties to be involved in the arbitration process were required to have appropriate experience. This article is noting only the relevant experience of an arbitrator but fails to note what the experience actually entails. The Act, indeed, also included some articles such as Article 6 as indicated by Sayen in 2003 which were essential in sorting out a conflict.<sup>380</sup> The parties would come together to resolve the disagreement at hand or arrive at a prior agreement to prevent any further disagreement from interfering with the performance of a

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<sup>379</sup> F Vogel, (2000). *Islamic Law and Legal System: Studies of Saudi Arabia*. New York: Brill, at 36.

<sup>380</sup> Sayen above n 313, at 346.

deal.<sup>381</sup> Article 6, however, does allude to an authority which is originally competent depending on the dispute but does not elaborate on the exact character of the authority. It can be assumed that the authority as nominated in Articles 6 and 8 is a relevant Ministry as noted in Article 3. Article 7 indicates that *the legal procedures do not apply where the parties involved in the dispute have agreed to resolve such matters through arbitration before the dispute escalates or the decision is already made to resolve the issue through arbitration.*

Article 8 mentions that *only the clerk of the competent authority allowed to hear the arbitration will be involved in this process* and he will take charge of all notices and notification which must be done in accordance with the law. Article 9 addresses the matter of time. The date set in the arbitration instrument is applied when the arbitration process begins. If this is not fixed, the Article allows 90 days for the award to be issued by the arbitrators. In the 1983 Act, during arbitrations to resolve conflicts, it was difficult to predict the time that the whole process would take. Article 9 gives freedom to both parties and states the dual rule of the court:

*“in this case, any litigant who so desires may submit the matter to the Islamic authority which may decide either to hear the subject matter or extend the time limit for a further period.”*<sup>382</sup>

Initially, some of the arbitrators considered the Islamic law as unsuitable for settling any business disputes as it appeared to be unclear to the parties. It was difficult to elaborate on the issues discussed in the law. In addition, the law did not consider private parties' interests when

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<sup>381</sup> Bajaj above n 370.

<sup>382</sup> Law of Arbitration, above n 322, art 9.



making decisions, and was thus considered to favour the Muslims in the country.<sup>383</sup> Where foreign countries or Christians were involved, the law was rejected.<sup>384</sup> In some cases, such as in disputes involving a bank, the arbitrators are specialized committees formed for this specific purpose. This is done in respect to the signed contract between the parties. There were no specifications based on which authorities would reserve or refuse to carry-out an award.<sup>385</sup>

The court interferes only when it is *deemed* “*as necessary, upon request of the party interested in expediting the arbitration, in the presence of the other party or in his absence, after being summoned to a session to be held for this purpose*”.<sup>386</sup>

This meant that although one party may be comfortable with selected arbitrators, the other may not agree and the jurisdiction could intervene. The number of arbitrators appointed is equal or complementary to the number agreed upon among the parties. The decision in this respect is final. If according to the agreement there were to be five arbitrators, then there must be no more and no less than this number. This is because the decisions made regarding the selection of arbitrators at the beginning had to be respected. Due to lack of restrictions, parties could fail to choose their arbitrators in good time. Moreover, the arbitrators could withdraw or be stopped, which would call for additional time to recruit new ones. Article 10 of 1983 Act states: *Where parties fail to appoint the arbitrators or one party abstains from appointing the arbitrator(s).... or where one*

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<sup>383</sup> Vogel above n 377.

<sup>384</sup> Law of Arbitration above n 322, art 9.

<sup>385</sup> Zuhur above n 361 at 305.

<sup>386</sup> Law of Arbitration above n 322, art 10.

*arbitrator or more refuses to work, or withdraws...the authority which includes judges originally competent to hear the arbitration shall appoint the arbitrator(s)*<sup>387</sup>

This article resolves the matter of selection of arbitrators where the arbitrators are not agreed upon or there is any obstacle preventing selected arbitrators from taking part in the arbitration process; i.e. “*the authority originally competent to hear the dispute shall select the arbitrators.*”

Article 11, defends the arbitrators thus: “*The arbitrator may not be dismissed except by the consent of the parties. The arbitrator so dismissed may claim compensation, if he had already commenced work prior to dismissal, and as long as the dismissal is not attributed to him.*” This meant that if the arbitrator had acted appropriately during the arbitration process, it was not easy to dismiss him. The process was expensive due to the compensation involved when dismissing the arbitrator. Furthermore, in relation to the selection of arbitrators, Article 12 provides room for disqualification of arbitrators. This could be done during the hearing and result in the disqualification of the arbitrators.<sup>388</sup> The arbitrators could be dismissed if they violated the privacy rights or showed subjectivity in decision making. Article 13 is silent on the matter of arbitrators and states only that the arbitration process will continue even after the death of one party with only an allowance of a break of thirty days unless a longer period is agreed upon.

However, according to Article 18, the decisions made by the arbitrators must be filed and handed to the authority within a period not exceeding five days. This Article also gives a chance

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<sup>387</sup> Ibid, art 10.

<sup>388</sup> Central Intelligence Agency. 2009. The World Factbook. 2010. New York : Skyhorse Publishing, at 345.

to the party who is not satisfied with the decisions made by arbitrators a chance to object as indicated by: “*Parties may submit their objections against what is issued by arbitrators to the authority with which the award is filed*” But this is limited to fifteen days as the Article stipulated “*within fifteen days*” and clarified when this period would start and end by stating: “*from the date they are notified of the arbitrators’ awards; failure to do so such awards shall be final*”.<sup>389</sup> So, if no parties have submitted any objection within the stated period, the decision made by the arbitrators becomes final. In the 1983 Act, conclusions of awards were done depending on the majority of arbitrators.<sup>390</sup> It is indicated in Article 15 that arbitrators “*may on the ground of circumstances pertaining to the disputed subject matter extend the period of an award though it may have already been set.*” This means that if the majority decided to extend the dates on reasonable grounds, they may do so. Article 16 also states that the opinion of the majority prevails in the decision-making process concerning the issue of an award.

In regards to Article 19, the authority competent to hear the arbitration can decide to give the go-ahead or object to the issuing of the award if more than one party puts forward an objection within not “*more than 15 days after the notification of the arbitrators award.*” If on further examination it is found that Sharia law has been adhered to, Article 20 notes that any of the parties involved in the dispute can request the authority concerned to issue the order. Therefore, the award takes effect if no objection is submitted to this authority. Article 21 emphasizes the effectiveness of the award issued by the arbitrators.<sup>391</sup> In the 1983 Act, people from other states had little say in the process of arbitration in Saudi Arabia but this was later

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<sup>389</sup> Law of Arbitration above n 322, art 18.

<sup>390</sup> Rahman and Sheikh above n 362, at 45.

<sup>391</sup> Central Intelligence Agency, above n 386.

allowed under universally enforced global conventions<sup>392</sup> which provided uniform and comprehensive rules that could be applied internationally. According to Rahman, this Act had a higher level of impartiality than the previous one.<sup>393</sup>

In conclusion, the Act of 1983 had many weaknesses including time wastage since arbitrators were not thoroughly scrutinized during selection.<sup>394</sup> There were also many inconveniences such as withdrawal of arbitrators. The procedures provided in the Act of 1983 were inadequate and needed to be modified.

### **5.2.3 1985 implementation rules**

This Act contains four chapters, each of which is divided into sections. The chapters are arranged so that one can easily follow the procedure of arbitration. In the 1985 Act, the arbitration process was clarified because it provided room for compromise so that the two parties could reach a consensus. This led to a reduction of further conflicts and allowed commercial relations to proceed, even when a common solution had not been established.<sup>395</sup> Article 5 of the 1983 Act requires that an arbitration tool be prepared with the relevant authority. Failure to prepare the instrument with the authority halts any further progression of the arbitration process. It would take some time before the re-commencement of the whole process. According to Section 17, parties may have representation. As indicated in Chapter II Section 18, the arbitration

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<sup>392</sup> D. Crutcher and Gibson. 'Certificate in Islamic Studies and Islamic Law'. Washington, D.C: University of Pennsylvania, 1986, at 204.

<sup>393</sup> This gave confidence to either party during crisis to come into arbitration with the assurance that there is a defined protocol to be followed. Rahman and Sheikh above n 362, at 345.

<sup>394</sup> A. Asouzu, *International Commercial Arbitration and African States: Practice, Participation and Institutional Development*. New York: Cambridge University Press, 2003, at 56.

<sup>395</sup> Cooperation in trade was made easier and business flourished with reduced barriers. See G Dalaume, (1991). *State Contracts and Transnational Arbitration*. American Journal of International Law, Vol.75, at 68-83.

process may continue even where one party has defaulted, unless this party has not been informed. The Act of 1985 also provides guidelines on how the hearing will be conducted. For instance, Section 22 of Chapter III indicates that “*the defendant party will be the last in making their submission*”. These procedures are probably useful in preventing time wastage.

Due to the weaknesses found in the articles of the 1983 Act, such as lack of clarity regarding the selection of arbitrators and time wastage, the Kingdom had to revise the 1983 Act in order to improve the dispute resolution process. This resulted in the 1985 Act. It was different from the other one since it complied with international arbitration standards, making it easier for arbitrations to be conducted world-wide.<sup>396</sup> The articles of the 1983 Act limited parties to having the arbitration process being conducted in regard to relevant arbitration laws such as Hanbali (*an Islamic legal tradition*) arbitration law.<sup>397</sup> Unlike the previous Act that clearly defined who should arbitrate, this 1985 Act allowed for flexibility regarding who would settle the dispute. It has been argued that the implementation of the 1985 Act was due to the fact that the Government looked at arbitration as a method of advancing justice in cases of dispute and reducing resource (time and money) consumption.<sup>398</sup> Arbitration was seen as inexpensive and quick compared to other existing methods of resolving disputes. This was because the new Act permitted openness and the Government established protocols defining the order to be followed. This involved agreements between arbitrators and the parties to the conflict. Parties would be notified of the progression of the arbitration and could avail themselves of this information. The Act defined the

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<sup>396</sup> Through the act, it was possible to have complete commitment from both parties during arbitrations and provision of evidence materials needed to ensure justice in times of dispute. Rahman and Sheikh above n 362, at 67.

<sup>397</sup> Baamir and Bantekas above n 343, at 9.

<sup>398</sup> Asouzu above n 392.

expected code of conduct, whereby all parties and arbitrators were expected to co-operate for the success of the process. The other process included the case hearing, examination, and records pertaining to the allegations. These would be examined and conciliations would begin. The award would be provided if there were no opposition from either party.

Section 3 of Chapter I stipulated that the intermediary was to be a citizen of Saudi Arabia. The other alternative was a Muslim expatriate. In addition, the arbitrator had to be approved and needed to have knowledge of the set of Sharia laws, business policies, ethnicity and way of life pertinent to the Kingdom.<sup>399</sup> This was in accordance with Section 3, Chapter I of the 1985 Act. This was facilitated by the minister in charge of integrity to ensure fairness. The Minister of Trade was entitled to ascertain that the arbitrators were conversant with business laws according to Section 5 of Chapter I.<sup>400</sup>

In the 1985 Act, the procedures were defined and streamlined, thereby expediting the process and reducing costs, although this required several further amendments. The amendments produced a well-defined procedure for conducting arbitration. In the 1983 Act, the parties were permitted to extend the arbitration date if they so desired or circumstances dictated so, even after informing the arbitrators. This is not so in the Act of 1985 where the date was not to exceed five days after the arbitrators had been informed of this as indicated in Section 10 of the 1985 Act:

*“The arbitration panel shall fix the date of the hearing for consideration of the dispute within a period not exceeding five days from the date in which approval of the arbitration document had been notified to the arbitration panel”.*

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<sup>399</sup> Baamir and Bantekas above n 343, at 9.

<sup>400</sup> Saudi Arabian Arbitration regulation (1985) in Albert Jan van den Berg (ed), *Yearbook Commercial Arbitration Volume XI - 1986*, Volume XI (Kluwer Law International 1986) at 370-377.

The agreement on the date according to the Act of 1985 was to involve an authority such as a mayor or police officer among others, and this had to be in writing and included the time, date and year, and approved in writing according to Section 11 of Chapter II: *“Police or mayors are required to assist the relevant authority in performing its duties within their prescribed jurisdiction”*. Tracing the parties involved was easy as records were kept from the initial stage of the arbitration. The Act of 1983 did not include these procedures.

Chapter I includes sections which elaborate on arbitration approval, the people eligible as arbitrators and the parties that will be involved in the arbitration process. Section 9, Chapter I of the 1985 Act stipulates that all actions taken during the arbitration process must be recorded. This provided evidence to avoid further disputes during arbitration. Section 26 allows any party to provide any verification that can lead to a fair judgment. In addition, the arbitration claim was to be carried out openly according to Section 20. According to Section 19 of the 1985 Act, the summons was to be advertised in the newspapers.

The next chapter explains how the persons concerned can begin the arbitration process and examines the rules by which they must abide. The third chapter of the Act states exactly what is to be done during the process where arbitrators listen to the dispute and understand their claims. It concludes by describing the process of issuing awards, opposition, and executions.

*“Article 9: If parties do not fix in the arbitration instrument a time limit for decision, arbitrators shall issue their award within ninety days from date of the decision approving the arbitration instrument (the court approves the arbitration instrument).”<sup>401</sup>*

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<sup>401</sup> Law of Arbitration above n 322, art 9.

The chapter and section structure of the 1985 Act has made easier to read and comprehend as opposed to the 1983 Act that provides no indication of the content of the articles. The 1985 Act is also much clearer than the 1983 Act. It imposes limits on what is to be done during the arbitration progress stating reasons as to why the procedures are to be done. This can be seen in Section 38 where the board in charge of arbitration has to conduct several examinations and come to an agreement before they award, oppose or execute the commands which have been discussed in order for the arbitration process to be successful. Such awards, commands, and/or oppositions should be in line with the letter and spirit of the Saudi constitution. Generally, being the most current version of the Saudi arbitration law, it is perceived that the 1985 Act is binding on all the stakeholders.

In a speech to differentiate the main differences between binding and non-binding contracts, Dr. Sanhury Abed Elrazaq, a notable Egyptian Muslim jurist who also played a key role in drafting the Egyptian civil code opined that prophet Muhammad taught Muslims to respect any contracts they make whether verbally and/or in writing. He said:

*Muslims must respect their contractual undertakings except those which forbid what is authorized or those which authorizes what is forbidden, because the rule is that the act of disposition of any person must be performed as was agreed, if such person has the capacity to dispose of his property and if the object of the contract is legal.*<sup>402</sup>

As expected, the 1985 Act outlines the authorities on issues that are legal according to the prevailing Saudi constitution (Book of God and the Sunnah). To this end and in quoting Dr.

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<sup>402</sup> Maabrhe above n 342.



Sanhury, it is arguable that this act is entirely binding on both the Saudi government and foreign investors (Muslims and non-Muslims) doing business in the Kingdom.

Clearly, the 1985 Act is different from the other Act in that it uses departments that are quite different from the each other to facilitate the resolution of issues related to them. This allows the process to be conducted fairly. It also uses terms such as ‘arbitration panel’ which are not present in the 1983 Act. This indicates that the Act was modified to improve its efficiency.

Secondly, the needs of business people were given better consideration since they could select specialized committees for the process as in the case of a bank.<sup>403</sup> In the 1983 Act, this is indicated in Article 3. In the 1985 Act, it was done mainly by three ministries as mentioned above (Trade, Integrity and Panel of Grievance). In the case of the 1983 Act, arbitrators were not thoroughly investigated, which meant that some arbitrators lacked the knowledge or experience to be involved in the whole process. Obviously, the arbitration process would be complicated if not all arbitrators were qualified. According to Bajaj (2009), it is was clearly shown in the 1985 Act that arbitrations would take place even if the dispute resolution was not taken care of by the Kingdom’s Authority.<sup>404</sup> Arbitrators were allowed to amend or change long-lasting contracts. They defer to a large extent to the officially authorized opinions concerning disputes, but they do not vacillate or depart from the stated rulings; this is to ensure that they are just and that no dishonest practices are involved in the arbitrations. If arbitrators observe the set rules and regulations, business people will be more likely to accept their interpretations during arbitrations.

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<sup>403</sup> Reduced number of procedures to be followed resulted to an easier and faster means of solving issues. See Asouzu above n 392.

<sup>404</sup> Dalaume above n 393.

They will also be more comfortable with an arbitration process that involves the authorities of a specific institution.

The 1985 Act has certainly helped the Kingdom to advance in its trade affairs both locally and internationally. It allows for a better understanding of the protocols followed during arbitrations. This has further attracted international investment which has promoted the growth of the Kingdom's economy.<sup>405</sup> This is because it has instilled confidence in foreign investors by dispelling fears that the Islamic Sharia legal framework does not embrace amicable resolution of investment disputes. Specifically, it reflects King Abdullah Bin Abdul-Aziz's commitment to uphold the rule of law (Islamic Sharia principles). In his (King Abdullah) speech announcing the death of his predecessor, King Fahd Bin Abdul-Aziz promised to both Allah and the people of Saudi Arabia that under his leadership, equality would be ensured and most importantly, he would uphold the provisions of the Saudi constitution (the Holy Qur'an).

*In my leadership, I will take the Qur'an and the Sunnah as my constitution and the Islamic Sharia as my way of life. I will protect the value of life as required by the Islamic Sharia laws through the protection of basic human rights and serve all the Saudi citizens equally and rightfully.*<sup>406</sup>

Moreover, while acknowledging the magnitude of the task (safeguarding the supreme constitution as well as upholding the tenets of the Islamic Sharia) that lay ahead, King Abdullah expressed his desire to seek guidance from Allah at all times during his tenure. He said:

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<sup>405</sup> This is a clear indicator that the Act did not focus on commercial arbitration processes, but rather on how they could attract international investors who would promote the Kingdom's economic growth rate. Rahman and Sheikh above n 362, at 234.

<sup>406</sup> King Abdullah, above n 47.

*I ask Allah to help me and give me the strength to continue on the way that the great founder of Saudi Arabia had drawn and succeeded him in that way his sons (May their soul rest in peace).*<sup>407</sup>

These promises can be clearly interpreted to mean that they are intended to promote continuity by instilling a sense of confidence in the Saudi citizens and, most importantly, the foreign nationals who might have been uneasy about the commitments of the incoming regime on matters of upholding the rule of law, particularly those laws that touched on dispute resolutions using international legal frameworks such as the ICSID. Hence, it is arguable that there has been a smooth transition of power that is committed to embracing the rule of law as did the founding King who according to King Abdullah, was a

*...good leader and founder of the KSA who had spent the better part of his life doing good deeds and serving his country and defending issues of Arabian and Islamic Nations.*<sup>408</sup>

Tellingly, King Abdullah is equally committed to doing good deeds in the service of his country throughout his reign. Part of these good deeds entails embracing international arbitration agreements and enacting local legislations to implement such agreements.

In its current form, the Act of 1985 serves this purpose of expressing the Saudi government's commitments to implementing international arbitration agreements. This is because it is clear on issues regarding who is to receive information or reports on arbitration procedures from different parties. For instance, if a case involves the state, information is

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<sup>407</sup> Ibid.

<sup>408</sup> Ibid.

reported to the government directors, ministers or the district officers, not delivered to head offices or managers. These specifications are not included in the Act of 1983. Moreover, the Arabic language was declared as the official language to be used during arbitration. Unlike the 1983 Act, the Act of 1985 makes provision for the inclusion of translators in case one of the parties does not speak or understand the Arabic language. The government ratified this Act because it was much better than the 1983 Act, evidenced by the fact that since its implementation, there has been a significant growth in international trade and investment in the Kingdom.<sup>409</sup> Due to the improvement in the arbitration process, economic growth has occurred. Currently, the Kingdom accepts the rules and protocols of international arbitration acts.

In efforts to facilitate business activities in the Kingdom, the Saudi government has instituted a number of legal and economic reforms that help to implement these international arbitration agreements. As expected, these reforms have helped to position the Kingdom in a strategic position among the most friendly investment destinations in the Middle East and North Africa region. While addressing a policy forum in Brussels in 2004, the Saudi Minister for Foreign Affairs, Prince Saud Al-Faisal hinted that the Kingdom is keen on establishing comprehensive reforms so as to create a brighter future. He said:

*Over the past several years, Saudi Arabia has initiated a process of reform that we hope would pave the way for a brighter and enriching future for our people. These reforms are comprehensive in scope, integrated in implementation, and they are to be realised with deliberate speed. We are fully aware that partial, minor, and isolated reforms are not sufficient to meet the challenges, or to develop the opportunities the future holds. Rather,*

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<sup>409</sup> Rahman and Sheikh above n 362, at 234.

*what is needed is a comprehensive reform program that includes political, legal, administrative, economic, and educational components; hence the need for deliberation.*<sup>410</sup>

Tracing the history of arbitration in the KSA, it can be concluded that the Kingdom has indeed undertaken comprehensive reforms, particularly since the first arbitration protocols of the 1963 and 1983 Acts were very ineffective. The enactment of the implementation rules in 1985 was therefore a milestone in Saudi arbitration history, bringing certainty and confidence to parties involved in a dispute. Today, parties involved in a dispute have a wide range of privileges unlike those granted under the 1963 and 1983 protocols.

#### **5.2.4 Proposed Modernisation of Arbitration Law in the KSA**

Saudi Arabia's legislative authority has proposed to restructure the current Saudi Arbitration Law. The proposed review and update of the arbitration law in KSA is mainly aimed at incorporating requirements of a modern legislation that embraces the principles of effective arbitration. In effect, it is expected that the Modern KSA Arbitration Law will incorporate the principles of the United Nations Commission on International Trade Law (UNCITRAL).<sup>411</sup> The new draft was approved in January 2012 by the *Shoura Council* that was presided over by Chairman Abdullah Al-Asheikh. This proposed modern Arbitration Law contains 58 articles to replace the current 25 articles. According to Al-Ghamdi, the Secretary-General to the Council, the new arbitral platform will be handled by competent arbitrators who are conversant with

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<sup>410</sup> Al-Faisal above n 40.

<sup>411</sup> Al Fadhel, M. A. (2010). Party Autonomy and the Role of the Courts in Saudi Arbitration Law  
<<https://qmro.qmul.ac.uk/jspui/bitstream/123456789/353/1/ALFADHELPartyAutonomy2010.pdf>>

international conventions.<sup>412</sup> However, the Islamic Law will still be upheld in the proposed modern arbitration law and verdicts issued by the new system will not be subject to appeal. The proposed modern law is also expected to sufficiently acknowledge the contractual and hybrid legal nature of the international arbitration law, contrary to the prevalent jurisdictional concept used in the KSA. The New York Convention provides an exception that requires countries to repudiate foreign awards that are viewed to be against the national values. However, the proposed modern Arbitration Law in the KSA is purported to comply with UNCITRAL.<sup>413</sup> In the proposed modern law, the KSA has cited that it will establish domestic legislations that deal with enforcement of arbitral awards that are issued by foreign jurisdictions.<sup>414</sup> This move will provide a reliable platform that allows the arbitration of domestic and international issues within the country. This proposed law will also curtail the current involvement of local courts in international arbitration proceedings.

### ***5.3 Conclusion***

Although they both address the issue of arbitration, the two Acts of 1983 and 1985 are quite different. To start with, the 1983 Act consists of articles which explain the protocols to be observed once a dispute arises. It explains the procedures to be followed such as receiving approval by the President of the Council of Ministers before the arbitration process begins, as

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<sup>412</sup> Ra Sooldeen, MD. (2012). Shoura OKs Draft Law on Arbitration  
<<http://arabnews.com/saudiArabia/article563799.ece>>

<sup>413</sup> Al Fadhel, above n 409.

<sup>414</sup> The Saudi Gazette, (2012). New Arbitration System Approved  
<[http://www.zawya.com/story/New\\_arbitration\\_system\\_approved-ZAWYA20120410045934/](http://www.zawya.com/story/New_arbitration_system_approved-ZAWYA20120410045934/)>

stated in Article 3. However, the articles are not arranged sequentially, unlike those in the 1985 Act.

In general, the arbitration legislation of 1983 is either vague or ambiguous in many areas, while that of 1985 is clear on the procedures and parties to be involved. For instance, the 1983 Act does not specify who the arbitrators are to be, but this is clarified in the 1985 Act. The 1983 Act specifies the cases for which arbitration should not be applied: *“Arbitration shall not be accepted in matters wherein conciliation is not permitted. Agreement to resort to arbitration shall not be deemed valid except by those who have the legal capacity to act.”* The new Act of 1985 clarifies the arbitration process and makes several additions to the Act of 1983.<sup>415</sup> The arbitration process does not necessarily contravene the Sharia law as arbitrators must take the Sharia law into consideration.<sup>416</sup>

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<sup>415</sup> Baamir and Bantekas above n 343, at 9.

<sup>416</sup> Ibid.

## **Chapter 6: Dispute Resolution Mechanisms**



## 6.1 Overview

The previous chapter covered the general historical and legal background of the arbitration process in Saudi Arabia. This chapter will therefore cover the disputes resolution mechanisms offered by the various commercial legislations and agreements mentioned in Chapter 4 that the Saudi Kingdom has since established and/or ratified. The chapter will only cover disputes between states (Saudi Arabia) and nationals of other states (foreign investors).

This chapter will attempt to answer the following overarching question: Is there a difference in dispute resolution mechanisms between different investment sectors and within sectors with different classes of investors as mentioned in Chapter 4? As explained in Chapter 4, there are two investor classes: Saudis and non-Saudis. The investment sectors include: oil, real estate, telecommunication, insurance, education, retail business, building and construction, agriculture, information technology, and aviation among others. Consequently, this chapter discusses a very complex area given that, pursuant to the *Royal Decree* 58 issued in 1963 as well as Article 3 of the Saudi Arbitration Law,<sup>417</sup> government agencies are not permitted to enter into arbitration with foreign investors unless with the express permission from the Saudi Council of Ministers, while on the other hand, the Kingdom has since ratified many local laws and entered into many multilateral and bilateral investment agreements that have made this Royal Decree mostly irrelevant.

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<sup>417</sup> See Royal Decree 58 of 1963; Law of Arbitration above n 322.

## 6.2 Introduction

Over the years, foreign direct investment activities have grown in scope and numbers particularly among the developing nations endowed with rich natural resources. Evidently, this increase has brought with it far-reaching legal ramifications. This is because the nature and scope of inter-state investments makes the occurrence of disputes inevitable as some investment agreements and/or contracts entered into between the host states, their agencies and foreign investors are very complex so that enforcing them becomes a daunting task.<sup>418</sup> In Saudi Arabia, a country endowed with natural resources and home to many multinational corporations, disputes arising between the state and its agencies on one hand and foreign investors on the other are arguably common perhaps due to the unique nature of the Sharia-based legal system that the Kingdom uses.<sup>419</sup>

In a bid to expedite and successfully resolve disputes, a number of frameworks have been developed. Basically, the existing commercial legislations arguably allow for disputes to be resolved through arbitration, relevant tribunals, and through the local court system depending on the investment sector and the investor class. Being a democratic country, Saudi Arabia has a functional judicial system capable of handling all manner of disputes.<sup>420</sup> Even so, given that the Kingdom hosts investors from countries practising completely different legal systems, the use of the local court system in resolving investment related-disputes, particularly those involving the Saudi government and/or its agencies and nationals of other countries, may to some extent not be

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<sup>418</sup> A. Newcombe and L. Paradell (2009). *Law and practice of investment treaties standards of treatment*, Kluwer, at 24-25.

<sup>419</sup> S.M Schwebel, (2010). The Kingdom of Saudi Arabia and ARAMCO arbitrate the Onassis agreement. *Journal of World Energy Law & Business*, xx(xx); at 1- 4.

<sup>420</sup> Bakhashab above n 309 at 153.

the preferred method of handling investment -related disputes.<sup>421</sup> Foreign investors may feel “insecure” under the local legal framework given it is derived from strict Sharia and Sunnah doctrines with which they might not be very conversant.<sup>422</sup>

Moreover, apart from the “normal” risks that foreign investments may face, there is always the possibility that a change of policy by the host nation may result in some not-so-favourable ramifications.<sup>423</sup> For instance, during the wave of nationalization that engulfed many developing nations between the early 1950s and late 1970s, many foreign-owned investment ventures were seized by oppressive governments.<sup>424</sup> Such risks may make foreign investors doubtful of the local protection mechanisms and therefore avoid some investment hubs if they deem that there are no guaranteed investor-protection mechanisms. Before undertaking investment ventures in Saudi Arabia, foreign investors would want to be assured of an impartial and reliable dispute resolution framework within which they can seek recourse in the event that the guaranteed rights and privileges are infringed by the Saudi government, its agencies or even its citizens.

Just like many other countries in the Middle East and Northern Africa (MENA) region, the Saudi government fully supports dispute resolution through arbitration and conciliation as long as the subject of arbitration is on the list of investment activities open to arbitration and that the investment is licensed under the Saudi Foreign Investment Law 2000.<sup>425</sup> In government-to-business relationships, and pursuant to Article 26 of the Foreign Investment Law Implementing

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<sup>421</sup> Al Ghazzawi and Buxton, above n 5 at 7.

<sup>422</sup> Ibid.

<sup>423</sup> Kutty, F. (2006). The Shari’a factor in international arbitration. *Loy. L.A. Int’l & Comp. L. Rev.*, 28, at 567.

<sup>424</sup> Vielleville, D.E. & Vasani, B.S. (2008). Sovereignty over natural resources versus rights under investment contracts: which one prevails? *Transnational Dispute Management*, Vol. 5, No. 2, at 2.

<sup>425</sup> Foreign Investment Law above n 91 art 26.

Rules, provision is made for settlement of disputes involving the Saudi government and foreign investors through arbitration subject to the provisions of the Royal Decree No. (46) Dated 12.7.1403 H.<sup>426</sup> It can be argued that the main reason that the Saudi government resolved to establish practical measures to expedite and amicably settle disputes is that it has become a common practice among pro-investment governments to assure potential foreign investors of the safety of their investments.<sup>427</sup> Being one of the most preferred investment hubs in the MENA region, the Kingdom can therefore arguably be described as investor-friendly in terms of offering investors legal protection from unfair treatment as well as easy access to amicable dispute resolution mechanisms.<sup>428</sup>

The Saudi government has achieved this aim in a number of ways. Perhaps the most important (in terms of universality) of these methods is the ratification of international arbitration treaties such as Trade Related Intellectual Property Rights (TRIPS).<sup>429</sup> As will be explained later in this chapter, these international arbitration treaties act as a guarantee to foreign investors that their investments will be governed not only by the Saudi laws but also by international statutes.<sup>430</sup> The second method is by ratification of bilateral and multilateral agreements intended to boost investment activities between the Kingdom and other nation-states and regions by providing amicable dispute resolution measures.<sup>431</sup>

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<sup>426</sup> Ibid.

<sup>427</sup> Bakhshab above n 309 at 153.

<sup>428</sup> Ibid, at 153-155.

<sup>429</sup> Ibid, at 156..

<sup>430</sup> ICSID Convention Preamble and Royal Decree M/8 (22/3/1394 H).

<sup>431</sup> M Al-Jarba, (2001). *Commercial arbitration in Islamic jurisprudence: A study of its role in Saudi Arabia context*. PhD Thesis at Aberystwyth University, at 23.

Perhaps the third and the most impacting (in terms of commitment to investor-protection on the part of the Saudi government) method employed by the Saudi government to enhance investment activities is the legislation of local commercial laws that were explained in great detail in the previous chapters. Ideally, these local legislations are meant to raise commercial activities in the Kingdom to international investment standards as well as making the Kingdom one of the most competitive investment hubs not only in the MENA region but also globally.<sup>432</sup>

As already explained above and from a business-to-business standpoint, Saudi Arabia is obligated by the ICSID to recognise arbitration as an alternative dispute resolution mechanism provided that it does not encroach upon the espoused national values, and that a number of prerequisite requirements are met.<sup>433</sup> In fact, misgivings about the feasibility of arbitration in Saudi Arabia have gradually disappeared over the years, particularly since the Kingdom has also ratified the ICSID Convention which demands that member states establish proper structures to facilitate investment dispute resolution using arbitration between its agencies or its citizens and foreign investors in instances when disputes arise.<sup>434</sup> However, Saudi Arabia entered a reservation to the effect that: "the Kingdom reserves the right of not submitting all questions pertaining to oil and to acts of sovereignty to the International Centre for Settlement of Investment Disputes, whether by way of conciliation or arbitration". Essentially, Article 13 of the Saudi Foreign Investment Law 2000 provides that all investment disputes involving the Saudi government/agencies and foreign investors should be amicably settled, Article (13) stipulates that:

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<sup>432</sup> Turck above n 8, at 416.

<sup>433</sup> Turck above n 8, at 415-418.

<sup>434</sup> Bakhashab above n 309, at 153-155.

*Disputes that may arise between the government and a foreign investor in relation to foreign investments that are licensed pursuant to this law shall, as far as possible, be settled amicably, failing which the disputes shall be resolved in accordance with the relevant laws.*

These relevant laws comprise the international investment agreements such as the ICSID, multilateral investment agreements such as those between GCC and Arab League countries, bilateral agreements such as those between the Kingdom and the US, Italy, Philippines, Malaysia, Germany, etc. Even so, the extent to which arbitration is utilised as an alternative investment dispute resolution mechanism in Saudi Arabia may actually be limited rather than actually expected.

In view of the above, it should be ascertained whether or not arbitration as a dispute resolution mechanism can be applied to every sort of dispute. In case of governmental agencies, it might be appropriate to note that in Saudi Arabia the legislator juxtaposes the possibility of arbitration with the right to conciliation. Unfortunately, the governmental authorities being deprived of the right to conciliation are required to refrain from the arbitration.

However, the right to arbitration should not be associated with conciliation because the two procedures are different. Arbitration is an alternative dispute resolution process which does not constitute an integral part of some other legal process. Conciliation, on the other hand, differs from arbitration in that it has no legal standing and no authority to collect evidence or examine witnesses. Also, the conciliator issues no award. The main goal of conciliation is to arrive at a compromise by meeting with the parties separately. Thus, if conciliation is regarded as the necessary prerequisite to arbitration, the significance of arbitration as an alternative dispute

resolution may be decreased, because the core purpose of arbitration lies in the unconditional resolution of disputes as an alternative to domestic legal procedures. Hence, although widely acknowledged as the most efficient way of settling both business-to-business and government-to-business investment disputes, arbitration in Saudi Arabia, as in many other Arab nations within the MENA region, is burdened by all manner of impediments which ultimately threaten its overall effectiveness.<sup>435</sup> This generalisation is drawn from the fact that many foreign investors always insist on including explicit arbitration clauses in the investment contracts signed between them and the Saudi government and/or its agencies.<sup>436</sup>

### ***6.3 Free Trade Agreements***

#### **6.3.1. The Role of FTAs in Minimizing Investment Risks in KSA**

Tradition shows that dispute resolution through arbitration and/or mutual conciliation is the most preferred method between government-to-business investment disputes.<sup>437</sup> Perhaps this is due to the inherent benefits of universality and efficiency as pertains to delivery of justice in the shortest and most amicable manner possible.<sup>438</sup> Moreover, based on the differences in the legal frameworks adopted by parties to many FTAs, it is only fair to assume that a dispute resolution mechanism that utilises international standards and procedures and not the host country's legal frameworks may be the most preferable.<sup>439</sup> No doubt this is an indicator that FTAs (Free Trade Agreements) play a core role in reducing investment risks as they promote faster and friendlier dispute resolution between the host government and the home government.

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<sup>435</sup> Al-Samaan, above n 1, at 301-302.

<sup>436</sup> D.E Stephenson and K. Al-Enezee, K. (2010). Enforcement of foreign arbitral awards in Saudi Arabia. *Financier Worldwide Magazine*.

<sup>437</sup> Schwebel above n 417.

<sup>438</sup> Bajaj above n 370.

<sup>439</sup> Ibid.

For instance, it can be interpreted that as a result of the FTAs as well as other international investment agreements, the Saudi government through the Arbitration Law and the Foreign Investment Law accords investors from FTA countries as well as other non-Saudi investors the opportunity to seek arbitration for investment disputes with the Saudi government and/or its agencies when the extent of the provisions of Article 3 of the Saudi Arbitration Law is limited.<sup>440</sup> Moreover, as explained above, investors from FTA countries that have existing mutual dispute resolution (arbitration) agreements with Saudi Arabia may not be subject to the provisions of Article 3 of the Saudi Arbitration Law because they are accorded “Saudi-citizens” status.<sup>441</sup> GCC investors and their counterparts from the Arab League nations qualify under this provision, with plans under way to extend such privileges to EU investors under the aegis of the EU-GCC FTA.<sup>442</sup>

It should be clarified that the role of FTAs in dispute resolution is immeasurable, substantiated by the fact that the states which negotiate FTAs usually incorporate dispute regulation clauses in their texts. Such clauses prescribe a number of rights and obligations which allow states to resolve different kinds of disputes. A detailed analysis of specific FTAs concluded between Saudi Arabia and other countries will be presented in later sections. However, the particularities as well as the regulative capability of the FTAs’ dispute resolution clauses are generalized below.

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<sup>440</sup> As previously explained, Article 3 of the Law of Arbitration Royal Decree No. M/46 12 (*Rajab* 1403 - 25 April 1983) bars Saudi government agencies from entering into arbitration with foreign investors unless with the express permission from the Council of Ministers.

<sup>441</sup> See the GCC Agreement.

<sup>442</sup> See the GCC, Arab League, and EU-GCC agreements.



When considering most of the FTAs, it is apparent that the dispute settlement sections frequently open with a fairly abstract regulation stipulating that the parties must at all times aspire to agree on the interpretation and application of the agreements. This formulation helps to clarify the core purpose of the dispute resolution clauses - to resolve disputes without creating new debates and controversies. In other words, the requirement to agree on the interpretation and application of the FTAs implies that the parties are obliged to explicate the meaning of the agreements by means of cooperation and consultation. Also, it can be argued that the reciprocal endeavours of the parties to ascertain the true content of the FTAs will assuredly facilitate the resolution of possible disputes between states.

The FTA is acceptable only if its dispute settlement provisions are imposed on all sorts of disputes between the parties including disputes concerning the interpretation or application of the agreement. The greatest advantage of such dispute settlement clauses is their general applicability. Moreover, it is possible to discern a wide range of dispute resolution tools which may be available to the parties of FTAs. Such instruments include consultations, commission meetings, conciliation and mediation, and arbitration by an arbitral panel. In the context of arbitration, it should be claimed that FTAs' dispute resolution clauses are also advantageous if they prescribe specific requirements to the arbitral panellists and designate the rules and procedures of arbitration.

However, it should be noted that the dispute resolution provisions of many FTAs demonstrate a set of gaps and shortcomings. Firstly, the articles that regulate various types of dispute settlement are not concentrated in a single chapter (the EU-GCC FTA, for instance).

Another limitation of the FTAs' dispute regulation clauses lies in the fact that most of them lack specific prescriptions regarding domestic proceedings and international commercial arbitration. The existence of such provisions would have established the comprehensive linkage between domestic legal process and arbitration as an alternative to it. In essence, they are connected with disputes arising from the FTAs and not between parties.

In the final analysis, the lack of relevant dispute resolution clauses in the FTAs creates significant problems for governments when settling their controversies and disagreements. Additionally, it should be asserted that only precise legal definitions and procedural steps can promote transnational investment relationships by establishing comprehensive guidelines and recommendations for settling such disputes.

### **6.3.2. Bilateral Agreements**

A number of bilateral agreements have since been ratified with a number of the Kingdom's major investment partners to enhance the smooth movement of goods, services, capital, and labour and to facilitate the processes of resolving investment disputes that may arise thereof.<sup>443</sup> For instance, when fielding questions from journalists, King Abdullah stated that the Kingdom has so far enjoyed numerous benefits from bilateral agreements with other nation states. He said:

*(...) the Kingdom and federal Russia are two giant oil countries and that petroleum is considered not only a key revenue for both of them but also an important factor and most influential in the world economy, a matter that necessitates cooperation and coordination*

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<sup>443</sup> Bakhshab above n 309, at 153-155.

*between us to guarantee secure oil supplies and achieve stability and balance in the world oil market for the benefit of producers and consumers as well.*<sup>444</sup>

By extension, foreign investors from nation states that have bilateral investment treaties with the Kingdom can resolve investment disputes that arise between them and the Saudi government and/or its agencies by utilizing arbitration contrary to the provisions of the Royal Decree No. 58<sup>445</sup> Royal Decree which barred government agencies from entering into arbitration with foreign investors. In response to questions from journalists, King Abdullah opined that:

*(...) the two countries [Saudi Arabia and Russia] have great economic capabilities, good natural resources, various investment opportunities and distinguished cultural and civilization heritage along with great political weight at the international arenas.*<sup>446</sup>

To enhance these economic capabilities, there must be appropriate measures in place to settle investment disputes that involve foreign investors and government agencies. Even so, it is prudent to note that the extent to which arbitration can be used by this category of investors is limited only to the investment sectors that are open to foreign investors.<sup>447</sup> It is also essential to highlight that foreign investors from nation states that have not entered into any bilateral or, by extension, multilateral investment treaties with Saudi Arabia, cannot utilise arbitration to resolve investment disputes with the Saudi government or even its agencies except in very special cases where the Saudi Council of Ministers has issued express permission to do so.<sup>448</sup>

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<sup>444</sup> King Abdullah above n 300.

<sup>445</sup> Bakhshab above n 308, at 153-155.

<sup>446</sup> King Abdullah above n 300.

<sup>447</sup> Foreign Investment Law above n 91 art 2.

<sup>448</sup> Law of Arbitration above n 322, art 3.

### 6.3.3. Greater Arab Free Trade Area (GAFTA)

One of the most important FTAs that Saudi Arabia subscribes to is the Greater Arab Free Trade Area (GAFTA). Together with the other sixteen Arab League countries within the MENA region, Saudi Arabia collaborates under the aegis of this agreement for purposes of facilitating faster trade development within the region.<sup>449</sup> A pro-investment measure taken by the Arab League trade bloc is the prohibition of nationalization of investment ventures owned (jointly or wholly) by Arab states nationals except in extreme situations when such a move is in the public interest.<sup>450</sup> In what seems to be a measure to comply with local legal frameworks adopted by the member states, the agreement accords them (member states) the opportunity to exclude certain investment areas and/or products if they contravene security, religion, health and/or environmental ideologies adopted by such member states. Hence, member states are required to provide a list of such sectors and/products as well as any amendments to these.

This free trade bloc includes an agreement for the settlement of investment disputes that was signed on December 6, 2000 by Jordan, Egypt, Syria, Iraq and Libya.<sup>451</sup> This agreement provides for the amicable resolution of investment disputes between host governments and nationals from the five nations (Jordan, Egypt, Syria, Iraq and Libya). Saudi Arabia is not party to this dispute resolution agreement although it is a member of the Arab League.<sup>452</sup> Therefore, based on the notion of reciprocity, signatories to this dispute settlement agreement are not given preferential treatment in Saudi Arabia beyond that already accorded to other Arab countries.

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<sup>449</sup> Greater Arab Free Trade Area (GAFTA), <<http://www.mit.gov.jo/Default.aspx?tabid=732/>>

<sup>450</sup> H. El-Kady (2006). The Proliferation of International Trade and Investment Arrangements in the Arab World: Key Issues and Challenges. *ATDF Journal*, 3(4), at 48.

<sup>451</sup> GAFTA above n 447.

<sup>452</sup> *Ibid.*

It appears that there is no “significant” difference between dispute resolution among Arab League and GCC member states that have subscribed to this dispute settlement mechanism and those that have not (at least in the case of Saudi Arabia). However, only a thorough analysis of other agreements can verify this supposition. This is because the Arab League agreement encourages complete unity among its member states in a wide range of investment areas.<sup>453</sup>

In addition, Saudi Arabia is party to the ICSID and therefore bound to accord nationals of other ICSID member states preferential treatment when it comes to settlement of investment disputes as long as doing so does not contravene the provisions of Royal Decree No., M/8 Dated: 22/3/1394 H. Therefore, investment disputes involving nationals from GAFTA member states and the Saudi government can still be resolved through arbitration.

An examination of the GAFTA necessitates a critical evaluation of the dispute resolution clauses which might be incorporated in the Agreement. In this connection, it should be clarified that the GAFTA Agreement is a combination of several reciprocal international documents, such as the Declaration Pan-Arab Free Trade Area Economic and Social Council’s Resolution of 1997, Executive Program of the Agreement, Agreement to Facilitate and Develop Trade among Arab States etc.<sup>454</sup>

The clauses of the Executive Program of the Agreement on Facilitating and Developing Inter-Arab Trade for Establishing Pan-Arab Free Trade Area that regulate the settlement of disputes are contained in the sixth section of the Program. According to the Program, all disputes

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<sup>453</sup> Economic Unity Agreement, above n 103.

<sup>454</sup> Arab Free Trade Agreement (1997), < <http://bilaterals.org/spip.php?article2309&lang=en>>

are required to be settled by a special committee.<sup>455</sup> Moreover, the Program's dispute regulation provisions stipulated in the sixth section are in line with Article XIII of the Agreement to Facilitate and Develop Inter-Arab Trade. However, one should take into consideration that the dispute settlement clause of the Sixth article is very abstract and contains no specifications with regard to dispute resolution procedures.

To continue, it might be appropriate to note that the Ninth article speaks of more detailed mechanisms of monitoring, enforcement and dispute resolution.<sup>456</sup> Hence, according to the aforesaid article, it can be concluded that the Economic and Social Council, the agency established to supervise the implementation of the Program, "settles disputes arising from the implementation of the Executive Program".<sup>457</sup> Also, the provisions of the Ninth article elaborate on the procedural particularities of the dispute resolution process which are: a) the Economic and Social Council performs a semi-annual review of the implementation of the Program; and b) the Program settles disputes that arise from the implementation of the Program, etc.<sup>458</sup> Thus, the dispute resolution process may be conducted by Arab experts who are hired either from World Trade arbitration panels or arbitrations ad hoc. Also, the Program prescribes that the recommendations, which are made by the arbitrators, must be submitted to the Committee for decision-making. It is apparent that this double-review requirement will increase the amount of time needed to settle the dispute.

As far as the Agreement to Facilitate and Develop Trade among Arab States is concerned, it should be ascertained that the dispute resolution clauses are prescribed in Article XIII of the

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<sup>455</sup> Ibid.

<sup>456</sup> Ibid.

<sup>457</sup> Ibid.

<sup>458</sup> Ibid.

Agreement. According to the aforesaid Agreement, the Council is responsible for the settlement of every dispute derived from the Agreement. Additionally, it is entitled to apply the dispute settlement provisions prescribed in Chapter Six of the United Agreement for the Investment of Arab Capital in Arab States and its annex. In view of the above, Article XIII requires that the Council determine the method of settling a dispute.<sup>459</sup>

In conclusion, after everything has been given due consideration, it appears that the GAFTA Agreement contains several dispute regulations clauses which are not prescribed in detail. In other words, the dispute settlement clauses are abstract and over-generalized. The Agreement does not contain the procedural steps of the dispute resolution process; nor does it specify what is required of the arbitrators.

#### **6.3.4. EU-GCC Free Trade Agreement**

Saudi Arabia is also a signatory to the EU-GCC Free Trade Agreement.<sup>460</sup> The EU-GCC FTA is a mutual trade agreement between all the six GCC member states and the member states of the European Union (EU). This agreement helps to cement trade ties between the GCC countries and the EU member states. Article 1 of the agreement outlines that the main objectives of the cooperation are:

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<sup>459</sup> Ibid.

<sup>460</sup> International Affairs: Free Trade Agreement: EU – Gulf Cooperation Council (GCC),  
<[http://ec.europa.eu/enterprise/policies/international/facilitating-trade/free-trade/index\\_en.htm/](http://ec.europa.eu/enterprise/policies/international/facilitating-trade/free-trade/index_en.htm/)>

- *to strengthen relations between the European Economic Community, on the one hand, and the GCC countries, on the other, by placing them in an institutional and contractual framework;*
- *to broaden and consolidate their economic and technical cooperation relations and also cooperation in energy, industry, trade and services, agriculture, fisheries, investment, science, technology and environment, on mutually advantageous terms, taking into account the differences in levels of development of the Parties; and*
- *to help strengthen the process of economic development and diversification of the GCC countries and so reinforce the role of the GCC in contributing to peace and stability in the region.*<sup>461</sup>

The 1989 EU-GCC Cooperation Agreement is the current framework for economic and political cooperation between the EU and the Gulf Cooperation Council. This Agreement contains the legal provisions that regulate the dispute resolution process. Thus, according to Article 21 of the Agreement, “any dispute which may arise between the Contracting Parties concerning the interpretation of this Agreement may be placed before the Joint Council”.<sup>462</sup>

In this connection, it should be noted that the first sentence of Article 21 concerns disputes around the explication and understanding of certain provisions of the Agreement. In other words, the contracting parties have not consented to submit to the Joint Council any dispute arising from

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<sup>461</sup> EU-GCC cooperation agreement art 1 (1989).

<sup>462</sup> Ibid art 21 (1989).



the application of the Agreement.<sup>463</sup> They have only agreed that the Joint Council will settle only the controversies and disagreements pertaining to interpretation.

Hence, it seems that Article 21 does not fully encompass the requirements of arbitration because it does not deal with the application of the Agreement. The matter of interpretation is quite different from the matter of application since the core purpose of the arbitration is to settle a dispute and not to create a new controversy.

Moreover, the second part of Article 21 stipulates that the failure of the Joint Council to settle the dispute results in the establishment of an arbitration panel. This provision in the Agreement implies that arbitration is not the primary method of dispute resolution because, according to Article 21 (1), the primary method is the meeting of the Joint Council.<sup>464</sup> Also, comparing the EU-GCC cooperation agreement with the GAFTA Agreement, it is possible to claim that the two documents approach the issue of arbitration differently. Hence, according to the GAFTA Agreement, the arbitrators' recommendations are reviewed and double-checked by the special committee, whereas the EU-GCC cooperation agreement regards the arbitration as the second link in the dispute resolution mechanism after the Joint Council.

The agreement is mostly centred on improving trade ties through the following undertakings, "common trade policy, fiscal aspects of a single currency and moving from customs union to a single market".<sup>465</sup> It is envisaged that from the region-based agreement, member states would achieve "progressive and reciprocal liberalization of trade in goods and

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<sup>463</sup> Ibid.

<sup>464</sup> Ibid.

<sup>465</sup> Ibid.

services.”<sup>466</sup> This, according to the deliberations, should be achieved through equitable and “a comparable level of market access opportunities” that take into consideration all the member states economic capabilities.<sup>467</sup>

At present, it can be said that this agreement is silent on how members should resolve disputes that arise from investment matters simply because there is no provision for this as yet.

### **6.3.5. Overseas Private Investment Cooperation (OPIC Convention)**

Perhaps the most notable of these bilateral investment agreements is the Overseas Private Investment Cooperation (OPIC Convention) entered into by the Saudi government and the US in April 26, 1975. Essentially, the ratification of the OPIC Convention saw Saudi Arabia agree to resort to arbitration in the event that a dispute should arise between the Saudi government or even a Saudi government agency and an American investor pursuant to Article 3(a) of the Convention. In fact, the central premise behind Article 3(a) is that disputes arising between American investors and host governments and/or their agencies, in this case the Saudi government, should first be settled in an amicable manner (by negotiation) before other resolution mechanisms are pursued.<sup>468</sup> However, in the event that this friendly resolution mechanism collapses without arriving at a conclusive answer, then either of the parties is mandated to take the dispute for arbitration pursuant to the provisions of Article 39 of the Convention.<sup>469</sup>

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<sup>466</sup> Ibid.

<sup>467</sup> Ibid.

<sup>468</sup> OPIC Convention art 3(a).

<sup>469</sup> Ibid, art 39.

So as to ensure impartiality and pursuant to Article 3(c)(i) of the Convention, parties involved in a dispute are required to choose their own preferred arbitrators; then a third arbitrator who is normally the chair, should be neither an American nor a Saudi.<sup>470</sup> However, Article 3(c)(i) of the Convention clarifies that both parties must give consent to the selected chair for him to be legally recognised.<sup>471</sup> The terms of the Convention are so binding that its Article 3(c)(ii) provides that in situations where one of the parties is reluctant to choose an arbitrator, the other party can petition the International Court of Justice President to appoint an arbitrator on behalf of the reluctant party, but not the whole of the arbitration process runs through this court.<sup>472</sup> The three arbitrators form a tribunal that is given the authority to draft its own schedule and procedures depending on the subject of the arbitration.<sup>473</sup> To ensure that neither party gains undue advantage over the other, the OPIC Convention provides that the arbitration process should be based on international law, with the award declared by a simple majority vote among the arbitrators.<sup>474</sup> This award is considered as binding and final – it cannot be challenged in any court of law.<sup>475</sup>

The US and Saudi Arabia continue to reap huge benefits from the OPIC. Speaking at a joint business forum held in Chicago and attended by Saudi Ministers of finance, commerce and industry, petroleum and mineral resources as well as the Saudi Ambassador to the US, Omar Bahalwa, a senior staff on the Committee for International Trade at the Council of Saudi Chambers, expressed his satisfaction regarding the rewards reaped as a result of the concerted

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<sup>470</sup> Ibid, art 3(c)(i).

<sup>471</sup> Ibid.

<sup>472</sup> Ibid, art 3(c)(ii).

<sup>473</sup> Ibid, art 3(c)(iv).

<sup>474</sup> Ibid art 3(c)(ii).

<sup>475</sup> Ibid.

efforts by Saudi and US governments to engender a mutually beneficial investment climate. The forum discussed a wide range of issues which included “*the stability of the Saudi economy, infrastructure opportunities, education, industry, and financial issues ...commercial investment opportunities [with specific preference given to] energy, petrochemicals, electricity, water, infrastructure, knowledge, financial markets, trade and investment, and agriculture.*”<sup>476</sup>

Bahalwa noted that “*The Kingdom will present to Americans at the forum investments in a wide range of fields, worth around a trillion Saudi Riyals.*”<sup>477</sup> During the same forum, the Saudi Ambassador to the US, Adel bin Ahmed Al-Jubeir, highlighted the importance of the forum to both countries. He stated:

*“The Saudi-U.S. relationship has grown and deepened over the past seven decades ... [and that the] conference will highlight the opportunities available to citizens of both countries as a result of the strong economic ties between them.”*<sup>478</sup>

On his part, the Minister of Petroleum and Mineral Resources, Ali Al-Naimi, stressed the importance of mutual relationships between the two countries, particularly in the energy sector. The Council’s Vice Chair, Abdulrahman Al-Juraisi strengthened this resolve by stating that over the years,

*“...the US has been one of the Kingdom’s most important trade partners, [and that] business sectors in both countries have a significant role in boosting economic relations... [with] trade between the two countries has soared to stand at SR193.3 [\$51.54 billion] in*

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<sup>476</sup> ‘U.S.-Saudi business opportunities forum opens in Chicago’, 2010.  
<[http://www.saudiembassy.net/latest\\_news/news04281001.aspx/](http://www.saudiembassy.net/latest_news/news04281001.aspx/)>

<sup>477</sup> Ibid.

<sup>478</sup> Ibid.

*2008 ... [with] direct U.S. exports to the Kingdom ... projected to rise to SR 63 billion [\$16.8 billion] in 2010.*<sup>479</sup>

### **6.3.6. Saudi Arabia and Philippines agreement**

Pursuant to Article 2 of the Agreement on Economic, Trade, Investment, and Technical Cooperation between the Republic of The Philippines and The Government of the Kingdom of Saudi Arabia, the two countries agreed to enhance economic development by cooperating in a number of investment sectors which include but are not limited to the following:<sup>480</sup>

- 1. Cooperation in the economic fields including industrial, petroleum, mineral, petrochemical, agricultural, livestock and health projects;*
- 2. Exchange of information, scientific research, technology; and*
- 3. Exchange of experts and training of personnel for specific cooperation programs.*

Moreover, based on the provisions of Article 3 of the same agreement, Saudi Arabia mutually accords “most favoured nation” (MFN) treatment to investors from The Philippines as a measure towards enhancing, expanding and diversifying business ties.<sup>481</sup> To underscore the magnitude of mutual treatment accorded to investors from either country, part of the article clarifies that:<sup>482</sup>

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<sup>479</sup> Ibid

<sup>480</sup> Agreement On Economic, Trade, Investment, And Technical Cooperation Between The Government Of The Republic Of The Philippines And The Government Of The Kingdom Of Saudi Arabia art 2.

<sup>481</sup> Ibid, art 3.

<sup>482</sup> Ibid.

*The MFN treatment shall not include privileges extended by the contracting parties to citizens or corporations of a third country as a result of a free trade zone, custom union, common market or any kind of regional economic cooperation system.*

As far as the issue of dispute resolution is concerned, it might be relevant to note that the Agreement does not define either the types of controversies that can be settled or mechanisms of dispute resolution. However, an analysis of the regulative provisions reveals indirect references to possible ways of dispute settlement. Thus, according to Article 7 of the Agreement, the contracting parties are required to establish a joint commission in order to augment the cooperation in all domains of the aforementioned agreement. Also, the parties are required to meet alternatively within the framework of the joint commission. Moreover, Article 4 of the Agreement implies that the consolidation and promotion of the cooperation between parties is possible by means of consultation.

In other words, it is recommended that the parties consult each other about the means and measures used to fulfil the terms of the Agreement. Indirectly, it seems prudent to presuppose that parties are entitled to consult each other about the means of dispute resolution, because they are entitled to consult each other about every issue which originates from the Agreement. Dispute resolution is an issue which is derived from the Agreement, and therefore, the parties are entitled to consult each other about the dispute resolution issue. This means that the Agreement is over-generalized regarding the dispute resolution issue.

Although this agreement does not mention how disputes arising between parties from these two countries will be resolved, it is essential to assert that MFN encourages the amicable settlement of disputes by employing the most efficient, quick and friendly method possible,

which in this case is arbitration. This generalisation is based on the provisions of Article 1(i) of the ICSID Convention which stipulates that:

*The purpose of the Centre shall be to provide facilities for conciliation and arbitration of investment disputes between Contracting States and nationals of other Contracting States in accordance with the provisions of this Convention.*<sup>483</sup>

Although the Saudi-Philippines bilateral agreement is silent on the dispute resolution method(s) that disputing parties should pursue, it is clear that the provisions of Article 1(i) are automatically applicable. Moreover, given that Article 7 of the Saudi-Philippines bilateral agreement specifies that representatives from the two countries will be meeting regularly to deliberate on the best ways of achieving the espoused goals of mutual cooperation in the investment fields outlined in Article 2 of the agreement, it is possible to argue that provisions for amicable settlement of disputes through arbitration may be under way.<sup>484</sup>

### **6.3.7. Agreement for Judicial Cooperation between States of Arab League**

In addition to the multilateral treaties described above, Saudi Arabia has been a party to the Agreement for Judicial Cooperation between States of Arab League since April 6 1983. Under this agreement, the member states are expected to recognise and by extension enforce subsequent awards without subjecting them to any judicial scrutiny as long as they are moral and do not in any way violate the existing public order as provided for by the underlying constitutional dispensation in the member state where they are being enforced. In addition, such awards should not be subjected to review if they do not contravene any of the underlying pillars

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<sup>483</sup> ICSID Convention, Regulations And Rules art 1(i), April 2006.

<sup>484</sup> Above n 478 art 2, art 7.

of Islam and/or Sharia law.<sup>485</sup> Nevertheless, it is clear here that public order and Sharia law are the two paramount factors governing the enforcement of such awards. For instance, Article 35 of the agreement partly reads:<sup>486</sup>

*Conciliation proved before the competent judicial authorities in accordance with the provisions of this Agreement in the territory of any of the contracting parties shall be recognised and effective in the territories of all other contracting parties after ascertaining that it has the force of an executive document with the contracting party in whose territory it was concluded, and that it does not contain any texts in contradiction of the provisions of Islamic Sharia or the constitution or public order or rules of conduct of the contracting party required to recognise such conciliation or put it into force ...*

Although the agreement delineates the boundaries between contravention of the set values of public order and the principles of Sharia law, it is very clear that awards can be rejected in Saudi Arabia or in any other member state, particularly if it is established that they necessitate the payment of interest, a thing forbidden under Sharia law.<sup>487</sup> Even so, it can be stated that, to date, no arbitral award has been rejected, perhaps because most of the arbitral proceedings are carried out by Muslim arbitrators well-versed in Sharia law requirements.<sup>488</sup>

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<sup>485</sup> Riyadh Arab Agreement for Judicial Cooperation art 25, 30 and 35 of the Arabic/Islamic - Miscellaneous, (Riyadh Arab Agreement for Judicial Cooperation, 6 April 1983)

<<http://www.unhcr.org/refworld/docid/3ae6b38d8.html/>>

<sup>486</sup> Ibid, art 35.

<sup>487</sup> Riyadh Arab Agreement above n 483.

<sup>488</sup> Stephenson and Enezee above n 434.



### 6.3.8. Other Bilateral Agreements

In addition to the bilateral agreements discussed above, Saudi Arabia has also entered into other bilateral investment treaties with other nation states including Russia, China, Egypt, Italy, Malaysia, Taiwan, Spain, Turkey, and Germany among others.<sup>489</sup> Drawing on the three examples explained above, it can be asserted that all the bilateral agreements that Saudi Arabia has so far ratified, provide for specific preferential mutual treatment for purposes of enhancing growth and cooperation in the specified investment sectors.<sup>490</sup> Moreover, from experience, part of this mutual economic cooperation entails amicable, faster, and efficient dispute resolution mechanisms.<sup>491</sup> For example, the Kingdom has entered into a series of bilateral agreements with Russia. These bilateral agreements span the oil, gas, scientific, technological and sports sectors. When fielding questions from reporters, King Abdullah opined that:

*(...) the two countries have great capabilities for wide range of cooperation, indicating that during his previous visit to Russia the two countries reached a group of agreements and memorandums of understanding in oil and gas sectors and scientific, technological, sports and commercial cooperation.*<sup>492</sup>

In recognizing the inherent benefits that these treaties bring to the Kingdom, it is only reasonable to expect that other bilateral investment treaties may have been signed as well, although they are yet to be implemented, or indeed, officially announced. Tellingly, these agreements are signed with the sole aim of protecting the investments of member states' nationals by providing easier

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<sup>489</sup> El-Kady above n 448.

<sup>490</sup> Above n 478, preamble.

<sup>491</sup> ICSID Convention, above n 481 at Preamble; Economic Unity Agreement, above n 103 Preamble.

<sup>492</sup> King Abdullah above n 300.

methods of legal recourse in the event a dispute between them (member states nationals) and the host nation arise. Therefore, it can be argued that even in the event that such agreements do not explicitly support a MFN treatment, they advocate ICSID-based resolution mechanisms (arbitration).

#### ***6.4. Local Commercial Legislations and Royal Decrees***

Drawing on the Foreign Investment Law and Arbitration Law as well as a host of Royal Decrees, it can be argued that there is great harmony in all the international investment agreements that Saudi Arabia is party to, at least when looking at the privileges granted to foreign investors as well adherence to the letter and spirit of the Sharia laws. Perhaps to support this generalisation, it is essential to invoke the Foreign Investment Law. Precisely, the law, the main aim of which is to outline in general terms the rights and privileges accorded to foreign investors as well the regulations they are expected to observe, explains that there should be no prejudice to other existing rules and regulations when it comes to matters of arbitration.<sup>493</sup> For instance, Article 13 of the Foreign Investment Law explains that investment disputes arising from licensed ventures between foreign investors and the Saudi government, its agencies, or even its citizens, are to be settled in the friendliest manner possible; in case of failure, the relevant laws can be invoked.<sup>494</sup> “Relevant law(s)” in this case is the Sharia-based Basic Law, while on the other hand “friendly” means the resolution of investment disputes through arbitration. Apparently, most of the international investment agreements support arbitration as

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<sup>493</sup> Foreign Investment Law above n 91 art 2.

<sup>494</sup> Ibid art 13.

the most suitable dispute resolution method as long as it is based on international standards and that it does not contravene the local legal frameworks.<sup>495</sup>

As explained in the previous chapters, in Saudi Arabia there exist a number of local legislations and Royal Decrees which stipulate how arbitration can be carried out, that is, who is eligible as well as the investment sectors that are open to arbitration.<sup>496</sup> To discuss this area thoroughly, it was important to begin with the Foreign Investment Law then proceed to the Arbitration Law of 1983, its amended 1985 version, and lastly the Basic Law/Sharia.

## **6.5. Arbitration under Sharia Law (Saudi Basic Law)**

The Saudi Sharia-based Basic Law allows for the resolution of commercial disputes through arbitration and/or mediation.<sup>497</sup> Basically, the law (Saudi Basic Law) accords foreign investors broad legal freedoms to resolve their disputes using arbitration. As explained in Chapter 4, these privileges vary with the different investor classes and/or investment sectors.<sup>498</sup> Even so, from a government-to-business perspective, it can be asserted that the law gives preference to foreign investors who profess the Islam faith, particularly those from GCC and Arab League member states when it comes to the choice of arbitrators. This is because Article 48 of the law stipulates that arbitrators must be Muslims with a thorough knowledge of the application of Sharia law.<sup>499</sup>

As clearly stated at the beginning of this chapter, Saudi Arabia is party to a number of free trade agreements as well as bilateral and multilateral investment treaties which allow

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<sup>495</sup> El-Kady above n 448.

<sup>496</sup> Foreign Investment Law above n 91; Law of Arbitration above n 323.

<sup>497</sup> A. Lerrick and Q.J. Mian (1982). Saudi business and labour laws: Its interpretation and application, at 176.

<sup>498</sup> Ibid.

<sup>499</sup> See Basic Law of Governance above n 39 art 48, which clarifies that the courts shall apply to cases before them the provisions of Islamic Shari'ah, as indicated by the Qur'an and the Sunnah, and whatever laws not in conflict with the Qur'an and the Sunnah which the authorities may promulgate; Al-Samaan, above n 1, at 250.

preferential arbitration treatment to various investor classes and investment sectors. Even so, drawing on the notions of national sovereignty as well as the unique Sharia principles, it is only fair to assert that these preferential investment agreements ought to be in tandem with the Basic Law.<sup>500</sup> For instance, the Arab League Judicial Agreement provides that the enforcement of arbitration awards should not be challenged unless it contravenes the supreme law followed in the member state where it is enforced.<sup>501</sup> In this regard, it is clear that these investment agreements are meant to only supplement the Basic Law by eliminating ambiguity when resolving investment disputes involving foreign nationals and Saudi government agencies. Moreover, given that Article 1, 5-8 of the Saudi Basic Law stipulates that every aspect of the Saudi society is to be guided by the principles of Islamic law, it follows that agreements ratified by the Kingdom cannot be in contravention of the Basic Law.<sup>502</sup>

On a different standpoint and based on the *Hanbali* teachings, from which the Saudi legal framework is fundamentally drawn, parties to an investment dispute are permitted to include in the contract other conditional clauses as long these do not contravene the fundamental principles of the Sharia law and the Sunnah.<sup>503</sup> As experience shows, these additional conditions include the incorporation of the clause allowing foreign investors the first resort to litigation while still maintaining their right to seek arbitration just in case one of the parties is not satisfied with the litigation results.<sup>504</sup> The Saudi Basic Law provides that parties who opt for litigation of a dispute arising from an investment do not lose their right to arbitration unless one of the parties raises

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<sup>500</sup> El-Kady above n 448.

<sup>501</sup> Riyadh Arab Agreement above n 483.

<sup>502</sup> Basic Law of Governance above n 39.

<sup>503</sup> Stephenson and Enezee above n 434.

<sup>504</sup> Diwan Alamzalim, decision. 72/T/4 of 1411 H (1991).

claims after the dispute has already been submitted to a competent authority for litigation.<sup>505</sup> In principle, parties engaged in an investment dispute do not lose their rights to arbitration even after taking such disputes to litigation because under Islamic law, courts do not adhere to the principle of *stare decisis*.<sup>506</sup> Islamic courts have been noted to put too much emphasis on hearing individual interpretations and understandings from the judges and arbitrators in every single case. This makes Islamic court decisions highly subjective and outcomes cannot be predicted with any certainty. Perhaps this situation is responsible for the apparent disregard of decisions arrived at by judges and/or arbitrators in an already-litigated/arbitrated dispute which re-emerges later perhaps for enforcement of a decision and/or award rendered thereof. No doubt this provision seems to favour foreign investors as it accords them the opportunity to legitimately seek alternative redress if they are not satisfied with the first decision.

By extension, foreign investors seem favoured by the teachings of Prophet Mohammed (Sunnah) that make up a significant portion of the Saudi Basic Law. In one of the most important teachings regarding judicial procedures, Prophet Mohammed questioned the authenticity of judgments that may be issued by any legal institution such as a court or an arbitration tribunal. In substantiation of his opinion, Prophet Mohammed believed that human beings are bound to make mistakes based on their immediate convictions regarding the situations presented to them. Therefore, Islamic courts cannot rely on case law principles when making decisions on litigations and/or arbitrations. Judges and arbiters alike should endeavour to take in the whole legal scenario

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<sup>505</sup> Ibid.

<sup>506</sup> *Stare decisis* is a case law principle under which judges are bound by decisions made in prior cases handling almost similar matters.

and make their own independent judgments based on their understanding of the existing statutes. More specifically, in one of his many *Hadiths*,<sup>507</sup> the Prophet Mohammed asserted that:

*I am only a man, and when you come pleading before me it may happen that one of you might be more eloquent in his pleadings and that as a result I adjudicate in his favour according to this speech. If it so happens and I give an advantage to one of you by granting him a thing which belongs to his opponent, he had better not take it because I would be giving him a portion of Hell.*<sup>508</sup>

In interpretation, this opinion seems to favour foreign investors from predominantly Muslim countries who may find it easy to settle investment disputes amicably without even proceeding to arbitration if they believe that the process will be biased. Moreover, it can be generally held that the Saudi Sharia-based Basic Law calls upon investors from predominantly Muslim nations (GCC and Arab League) to use their conscience rather than rely on judicial rulings which from experience have been faulty due to conscious bias.

#### **6.6. Arbitration among the Various Classes of Foreign Investors in KSA**

As explained earlier, foreign investors can be categorized under the following classes as determined by their countries/regions of origin: Non-Saudis, Arabs, GCC, Muslims, and non-Muslims. Based on the principle of reciprocity, foreign investors from nation states that do not have existing bilateral and/or multilateral investment treaties enjoy fewer privileges when it comes to arbitration of investment disputes compared to their counterparts from nation states that

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<sup>507</sup> *Hadiths* are thematic teachings by the Prophet Mohammed on various sensitive touching on Muslim daily lives. *Hadiths* can be equated to the biblical parables that Jesus Christ used in his teachings to emphasize on important spiritual messages.

<sup>508</sup> Sayen above n 313, at 933.

have mutual investment treaties with Saudi Arabia. In fact, Saudi Arabia accords special treatment to nationals of other states if it expects such states to reciprocate the same to its citizens.

The existence of these bilateral agreements is an indicator that the Kingdom fully recognises arbitration as the most suitable dispute resolution mechanism. During a seminar organized by the Kingdom on behalf of Islamic states, dubbed “Arbitration from Islamic and International Perspectives” the International Lawyers’ Federation president, Antowan Akel, opined that organizing

*(...) the seminar in the Kingdom reflects the desire of the Kingdom’s leadership to defend the causes of justice and peace. Hailing the significant and successful role played by Prince Dr Bandar bin Salman bin Mohammed Al-Saud, Advisor of the Crown Prince and Head of the Saudi Arbitration Team, Akel said that his efforts have yielded positive results and paved the way for the adoption of Arabic as one of the official languages of the Federation.*<sup>509</sup>

These sentiments were shared by the International Lawyers’ Federation vice-president Majid Karoub when he opined that:

*[The] organization of the seminar comes in line with the aspirations of the Kingdom’s leadership. He noted that the governing system in the Kingdom is based on justice, in accordance with the teachings of the Holy Qur’an. Karoub denounced last week’s Riyadh attacks, and said that the perpetrators of this vicious crime have nothing do with Islam. He expressed his appreciation to the Saudi Press Agency (SPA) for their coverage of the*

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<sup>509</sup> ‘Crown prince’s advisor opens seminar on arbitration’ (may20, 2003).  
<[http://www.saudinf.com/display\\_news.php?id=606/](http://www.saudinf.com/display_news.php?id=606/)>

*seminar. He announced that the new nominee for the post of Vice-President of the International Lawyers' Federation is Osama Al-Saleem.*<sup>510</sup>

Given the large numbers of nation states with which Saudi Arabia collaborates, either through bilateral and/or multilateral investment treaties, it is only fair to assert that different categories of foreign investors are given completely different treatment under the Saudi investment laws. GCC, Arab League, EU, American, Malaysian, Italian, Egyptian, German, Philippines, Turkish, Spaniard, Indian, Korean, Swiss, Austrian, Singaporean, Taiwanese, French, Belgian, Russia, Luxembourgian and Chinese investors are accorded preferential investment and dispute resolution treatment as Saudi Arabia has existing bilateral and/or multilateral investment agreements with them.<sup>511</sup>

By comparison, GCC investors are second after Saudi investors in terms of the investment privileges the Saudi government accords to them. As explained above, GCC investors are given the authority to invest and/or own real estate property within the localities of the two Holy Cities of Mecca and Medina.<sup>512</sup> Hence, it is only appropriate to argue that GCC investors have the legal capacity to institute arbitration proceedings in the event they are engaged in a dispute with a Saudi government agency regarding a property and/or investment activity in these two Holy Cities.<sup>513</sup> Moreover, pursuant to the Economic Agreement between the Gulf Cooperation Council States which include Bahrain, Kuwait, Oman, Kingdom of Saudi Arabia, United Arab Emirates,

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<sup>510</sup> Ibid.

<sup>511</sup> Economic Agreement above n 37, art 3; See also, the Agreement On Economic, Trade, Investment, And Technical Cooperation Between The Government Of The Republic Of The Philippines And The Government Of The Kingdom Of Saudi Arabia. See also, the International Affairs: Free Trade Agreement: EU – Gulf Cooperation Council (GCC), retrieved December 17, 2010, from: [http://ec.europa.eu/enterprise/policies/international/facilitating-trade/free-trade/index\\_en.htm/](http://ec.europa.eu/enterprise/policies/international/facilitating-trade/free-trade/index_en.htm/)

<sup>512</sup> Economic Agreement above n 37, art 3.

<sup>513</sup> Arbitration Law, above n 322 art 2 specifies that arbitration can only be carried out by persons with the legal capacity to do so; and Article x of the Foreign Investment Law which specifies that arbitration can only performed on disputes arising from investment activities licensed under the law (Foreign Investment Law).



and Qatar, host nations are required to treat investors from member states just the same way as they treat their own citizens.<sup>514</sup> For instance, the GCC Economic Agreement preamble calls for a strong and closely harmonised economic, financial, and monetary mutual relationship between the member states so as to promote faster and sustained economic growth.<sup>515</sup> Part of the preamble stipulates:

*... In the light of reviewing the economic achievements attained since the inception of the Council, including accomplishments attained by the Economic Agreement signed in 1981 ...and Seeking to achieve advanced stages of economic integration that would lead to a Common Market and an Economic and Monetary Union.... and Desiring to enhance the economy of the GCC Member States in the light of recent global economic developments which require further integration ... and Responding to the aspirations and expectations of GCC citizens towards achieving Gulf citizenship, including equal treatment in the exercise of their rights to movement, residence, work, investment, education, health and social services...*<sup>516</sup>

Analytically, the preferential treatment accorded to GCC investors is an express authority for them to utilise arbitration services even in situations where they are involved in investment disputes with the Saudi government and/or its agencies.

On the other hand, and pursuant to the spirit of Article 1 of the Economic Unity Agreement among States the Arab League to which Saudi Arabia is a signatory, it is expected that the member states should accord investors from other member states preferential treatment

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<sup>514</sup> Economic Agreement above n 37, art 3.

<sup>515</sup> Ibid, Preamble.

<sup>516</sup> Ibid.

so as to create “*A Complete economic unity*”,<sup>517</sup> particularly in the fields of “agriculture, industry, and internal trade”.<sup>518</sup> The preferential treatments should include but are not limited to the following:<sup>519</sup>

1. *Freedom of personal and capital mobility.*
2. *Freedom of exchange of national and foreign goods and products.*
3. *Freedom of residence, work, employment and exercise of economic activities.*
4. *Freedom of transport, transit and use of transport, ports and civil airports.*
5. *Rights of possession, bequeath and inheritance.*

To achieve this complete economic unity in the stated fields, member states are encouraged to put in place appropriate dispute resolutions mechanisms (arbitration) so as to expedite the process of moving goods, services, capital and labour within the Arab League region. Given that the provisions of the Arab League Agreement place special emphasis on agriculture, trade and industry, it must be noted that investors from non-Arab League countries do not enjoy similar treatment which in this case includes access to amicable investment disputes resolution mechanisms through arbitration in these three investment sectors.

On the other hand, non-Saudis from nation states with existing bilateral investment agreements are accorded preferential treatment as provided for by the respective agreements. In this regard, American, Malaysian, Italian, Egyptian, German, Philippine, Turkish, Spaniard, Indian, Korean, Swiss, Austrian, Singaporean, Taiwanese, French, Belgian, Luxembourgian and Chinese investors doing business in Saudi Arabia enjoy preferential treatment compared to their

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<sup>517</sup> Economic Unity Agreement, above n 103.

<sup>518</sup> Ibid art 2.

<sup>519</sup> Ibid.

counterparts from nations without existing bilateral and/or multilateral investment agreements with Saudi Arabia.<sup>520</sup> One of the preferential treatments given to these investors is the access to arbitration even when they are involved in investment disputes with the Saudi government and/or its agencies as well as access to investment ventures in sectors named in the infamous Saudi Negative List.

Pursuant to the provisions of the OPIC Convention and as previously explained in this chapter, American investors are given significant preferential treatment.<sup>521</sup> For instance, as opposed to the provisions of Royal Decree No. 58 which forbids the Saudi government and/or its agencies from entering into arbitration, American investors can enter into arbitration with the Saudi government and/or its agencies in the event of a dispute. Other categories of foreign investors who enjoy this privilege come from the GCC, Arab League and other countries with existing bilateral agreements with Saudi Arabia.<sup>522</sup> In addition, during the arbitration process, these preferentially-treated investors are also accorded an opportunity to choose their own representatives as well as the legal framework they consider the most impartial, as long as it does not contravene the Saudi Basic Law.<sup>523</sup>

As for foreign investors, their treatment all depends on whether their countries of origin have an existing mutual investment agreement with Saudi Arabia. Given that most foreign investors are from the GCC and Arab League member states, it can be asserted that they are accorded preferential treatment when it comes to matters of handling investment disputes using arbitration. As explained above, this special treatment includes entering into arbitration with the

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<sup>520</sup> Bkhashab above n 309.

<sup>521</sup> OPIC Convention art 3(a).

<sup>522</sup> Economic Agreement above n 37, art 3.

<sup>523</sup> Ibid.

Saudi government and/or its agencies in the event of a dispute or even investing in fields considered the preserve of Saudi nationals.<sup>524</sup>

Conclusively, it is arguable that arbitration in the KSA is widely accepted as an alternative means of dispute settlement. In response to questions from journalists, Dr. Abdul Rahman Al-Tuwaijri, who is the Secretary-General of the Supreme Economic Council (SEC) of Saudi Arabia, expressed the commitment of the Saudi government through the SEC to regularly conduct analysis of the Kingdom's investment climate with a view to making necessary adjustments. He said:

*The SEC has revised the list of economic sectors in which foreign investment will not be allowed, thus allowing foreigners to invest in new areas, ... the SEC opened new economic sectors for foreign investment in line with the Custodian of the Two Holy Mosques King Abdullah's reforms aimed at strengthening the economy, attracting more foreign investment and enhancing private sector participation.*<sup>525</sup>

Nevertheless, Dr. Al-Tuwaijri clarified that in a bid to keep the Two Holy Mosques pure as required by the Holy Book, bans on foreign investment within the precincts of the two Holy Cities of Mecca and Medina will continue to operate as they have been. This is because the Saudi Kingdom in its capacity as the Custodian of the Two Holy Mosques, King Abdullah has a duty to bar non-Saudis and by extension, non-Muslims, from carrying out any economic activities within the precincts of Mecca and Medina. Dr. Al-Tuwaijri said:

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<sup>524</sup> Ibid, art 3.

<sup>525</sup> 'Kingdom opens more economic sectors for foreign investments' (March 26, 2007).  
<<http://www.saudiembassy.net/archive/2007/news/page576.aspx/>>

*(...) restrictions on real estate investment in Makkah and Madinah would continue without change. The same is the case for tourist orientation and guidance services related to Haj and Umrah.*<sup>526</sup>

Moreover, in what can be interpreted as enforcing the spirit of sovereignty and the stringent Sharia values, the number of investment sectors on the Negative List will not decrease in the near future. In fact, bans on the following sectors will continue to be operational until such time that revisions are made in future:

*(...) distribution of cinema films and video cassettes (CPC 96113), transportation of passengers inside cities by train, air transportation services and satellite transmission services, ... recruitment and employment services; real estate brokerage; audiovisual and media services; land transport except transportation by train within cities; services rendered by midwives, nurses, physiotherapists and paramedics (CPC 93191); fisheries; and blood banks, poison centers and quarantines.*<sup>527</sup>

Clearly, arbitration among the various foreign investment classes is greatly hampered by the provisions of the Negative List.

## **6.7. Conclusion**

This chapter has presented a comprehensive account of some of the existing Saudi commercial legislations as well as bilateral and multilateral investment agreements that govern the various arbitration mechanisms for resolving investment disputes between foreign investors and the Saudi government. In this chapter, it is argued that various investor classes in Saudi

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<sup>526</sup> Ibid.

<sup>527</sup> Ibid.

Arabia are treated differently depending on whether mutual investment agreements (free trade area, bilateral, multilateral) exist between their countries of origin and Saudi Arabia. Basically, it is asserted that all categories of investors are accorded the right to resolve their investment disputes through arbitration. Even so, based on the provisions of Articles 1, 2 and 3 of the Saudi Arbitration Law of 1983 and its Implementing Rules of 1985, such rights are granted only to investment sectors available to investors of a certain country and/or a certain region as determined by the existence or absence of mutual investment agreements with Saudi Arabia.

## Chapter 7: ICSID and KSA Laws

### 7. 1. Overview

The steady growth of investment activities between investors and nation states has resulted in numerous disputes. The International Centre for Settlement of Investment Disputes (ICSID) is a body that seeks to mitigate the issues caused by such investment disputes. This chapter is intended to explain how investment disputes in the Kingdom of Saudi Arabia were handled both before and after the Kingdom ratified the ICSID. This will be tackled in the context of the competent authorities such as the Commercial and Committee for Settling Investment Disputes that were mandated to handle commercial disputes before the KSA acceded to the ICSID. The various investment regulations such as the Mining Law, Arbitration Law, and the Foreign Investment Law were all enacted after the ICSID accession. Lastly, the chapter will examine investment arbitration in general terms with special emphasis placed on the role played by the ICSD. An illustration of the variation in treatment by Saudi Arabia depending on bilateral agreements is the case of China permitting the ICSID to handle only those disputes relating to compensation, while other countries may have the ICSID handles many more disputes.<sup>528</sup>

Essentially, the KSA is party to a number of International Investment Agreements (IIAs). Specifically, it has entered into both bilateral and multilateral agreements with both Gulf States and western countries, notably the United States.<sup>529</sup> From a bilateral standpoint, the KSA is

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<sup>528</sup> 'Guide to Investment Regimes of APEC Member Economies', APEC #210-CT-03.7,  
<[http://publications.apec.org/file-download.php?filename=03\\_PRC\\_211\\_ieg\\_investment-guide.pdf&id=1120\\_toc](http://publications.apec.org/file-download.php?filename=03_PRC_211_ieg_investment-guide.pdf&id=1120_toc)>

<sup>529</sup> Shoult above n 190, at 110.

signatory to the OPIC, a regional arbitration treaty that allows for arbitration of investment disputes arising between the Saudi government or its agencies and the American investors.<sup>530</sup>

From the multilateral standpoint, the KSA ratified the ICSID back in 1980 meaning that it relinquished its authority to handle investment disputes, particularly those involving foreigners and Saudi nationals and/or state agencies.<sup>531</sup> The KSA is a member of the Gulf Cooperation Council as well as an observer to the Energy Charter Treaty.<sup>532</sup>

It is arguable that the Kingdom's entry into bilateral and multilateral agreements was meant to mitigate some of the drawbacks that come with uncontrolled international investment and globalisation. This issue was addressed by King Abdullah in his speech to members of the G-20 summit in 2008 when he emphasized that there is a great need for

*(...) international coordination and cooperation to find appropriate solutions to the crisis and its effects. This crisis revealed that undisciplined globalisation and inadequate control of the financial sectors contributed to its rapid spread around the globe.*

Part of the solutions that the King had in mind included forming mutual IIA such as the ones listed above. With such agreements, states can easily mitigate global economic crises. These sentiments are confirmed by Al-Dabbagh, the SAGIA chief when he was fielding questions from stakeholders. He said:

*(...) the era of the Custodian of the Two Holy Mosques King Abdullah bin Abdulaziz Al Saud has been characterized by development and modernisation in various areas,*

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<sup>530</sup> Ibid.

<sup>531</sup> Ahdab above n 331, at 605.

<sup>532</sup> Norton Rose above n 149.



*including the economic field which has witnessed a number of significant developments and reforms directly affecting the economic growth and prosperity in the Kingdom.*<sup>533</sup>

In addition to the IIAs, King Abdullah era has been characterized by what Al-Dabbagh termed as proper developmental and reform steps initiated by the custodian of the Two Holy Mosques. Al-Dabbagh opined that

*(...) a number of developmental steps and reforms took place in the Kingdom of Saudi Arabia in 2010 leading to the improvement of the Kingdom in a report of Doing Business, ranking the Kingdom as the first one at Arab level and the 11th at the global level.*<sup>534</sup>

According to Al-Dabbagh, these efforts have culminated in placing the Kingdom in a prime position. He said *“that the Kingdom comes on the list of the top five countries in the world that have carried out economic reforms over the past five years.”*<sup>535</sup>

## **7. 2. Introduction**

Litigations in Saudi Arabia, just as in many other jurisdictions, may be lengthy, expensive, and with difficult-to-predict outcomes.<sup>536</sup> Investments involving nationals and/or agencies from different countries are complex. They involve both major and minor transactional and legal dealings that touch on the areas of procurement, finance, marketing and branding, property leasehold, taxation and many more others that are directly or indirectly linked to the core investments<sup>537</sup> The scenario may be even more complicated if such disputes involve multi-jurisdictional investment disputes or high value investments involving private individuals and

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<sup>533</sup> SAGIA governor (feb. 09, 2011). ‘Kingdom among top five countries in the world in economic reforms’. [<http://www.sagia.gov.sa/en/sagia/media-centre/news/Kingdom-among-top-five-countries-/>](http://www.sagia.gov.sa/en/sagia/media-centre/news/Kingdom-among-top-five-countries-/)

<sup>534</sup> Ibid.

<sup>535</sup> Ibid.

<sup>536</sup> Shoult above n 190, at 104.

<sup>537</sup> Ibid, at 103-104.

state agencies.<sup>538</sup> It should be noted that the Kingdom is fully committed to partnering with the internal arbitration bodies in resolving investment disputes arising between foreign investors and government agencies.

In addition, under the Sharia laws, the Saudi courts are not obliged to approve monetary gains to parties claiming loss of future profits. Neither can the courts consent to the payment of interest on overdue amounts.<sup>539</sup> These are fairly strong impediments that threaten the smooth running of inter-jurisdictional business activities in Saudi Arabia. Foreign investors always seek alternative dispute resolution avenues to mitigate the inevitable contractual disputes.<sup>540</sup> As a matter of fact, it is very common among foreign investors to stress the importance of including explicit arbitration clauses when signing business contracts in Saudi Arabia.<sup>541</sup>

Investment arbitration in Saudi Arabia is governed by a range of commercial legislations drafted in accordance with the ICSID Convention regulations.<sup>542</sup> Basically, the ICSID is a unique legal framework that provides direct recourse to foreign investors short-changed by nationals and/or state agencies of the host nations.<sup>543</sup> To reinforce the ICSID provisions, the KSA legal framework through the Arbitration Law and Foreign Investment Law, provides explicit arbitration and mediation procedures that help to settle investment disputes between foreign nationals and/or state agencies.<sup>544</sup> No doubt, these ‘investment-confidence’ inducing legal

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<sup>538</sup> Ibid.

<sup>539</sup> Shoult above n 190, at 104.

<sup>540</sup> Ibid.

<sup>541</sup> Ibid, at 103-104.

<sup>542</sup> Baamir and Bantekas above n 343, at 245-246.

<sup>543</sup> Nelson above n 340, at 566.

<sup>544</sup> Baamir and Bantekas above n 343, at 239-269.

frameworks have been responsible for the steady growth of the Saudi export and import business over the years.<sup>545</sup>

In what seems to be overt support for the existing pro-investment legislations, prominent Saudi leaders have regularly gone public to reiterate the Kingdom's resolve to embrace arbitration as the most desired and fair investment dispute resolution instrument. These sentiments are shared by the Saudi Arbitration Team which is led by Prince Dr. Bandar Bin Salman bin Mohammed Al-Saud. When reiterating the Kingdom's support, Prince Dr. Bandar opined that the Kingdom espouses the tenets of peaceful resolution of investment disputes and therefore it is ready to partner with global bodies to enhance the smooth resolution of such disputes. He said:

*(...) my deep appreciation to the President of the International Court of Justice, Eminent Judge Gilbert Guillaume and Respected Judges who are members of the International Court of Justice, Secretary-General of the Permanent Court of Arbitration Mr Tjaco T. Van Den Hout, and all those who participated in organizing the Conference that took place at Peace Palace on 12 October 2001, under the title "Strengthening Relations with Arab and Islamic Countries through International Law."*<sup>546</sup>

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<sup>545</sup> Ibid, at 19.

<sup>546</sup> 'Saudi Arabia promotes peaceful resolution of international disputes' (feb. 14, 2003).

<[http://www.saudinf.com/display\\_news.php?id=252/](http://www.saudinf.com/display_news.php?id=252/)>

### ***7.3. Purpose and Scope of International Investment Treaties***

Developing nation states rely on direct foreign investments to boost their domestic economy.<sup>547</sup> However, the environments in which such foreign investments thrive are inherently uncertain and in many instances result in disputes. Such disputes may tilt the scale of confidence in a country's ability to safeguard investments if no checked and appropriate measures are taken to mitigate their effects.<sup>548</sup> Ideally, all domestic courts should be capable of handling all manner of disputes including investment-related ones. However, due to conflicting legal systems and issues of impartiality, foreign nationals may feel insecure when pursuing justice through domestic courts.<sup>549</sup> Host nation states may be tempted to invoke political overtones when handling foreign investment disputes to tilt the justice scale on their side.<sup>550</sup> From a different perspective, it is evident that foreign investments are normally complex and therefore pose significant challenges to the sometimes underfunded domestic courts.<sup>551</sup> In this regard, the handling of international investment disputes in the domestic courts which are already overburdened by domestic litigation may be overwhelming to them.<sup>552</sup> A combination of these impediments reduces the credibility of domestic legal systems in handling investments disputes between foreign nationals and state agencies.<sup>553</sup>

This inherent credibility crisis among domestic legal systems has spurred the move to establish international investment treaties that provide alternative universal dispute resolution

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<sup>547</sup> I.F.I Shihata, (1986). The settlement of disputes regarding foreign investment: the role of the World Bank, with particular reference to ICSID and MIGA. *AM. U.J. INT'L L. & POL'Y*, Vol. 1:97, 102.

<sup>548</sup> Rahman and Sheikh above n 362.

<sup>549</sup> Nelson above n 340, at 555-556.

<sup>550</sup> I. Adebisi (n.d.). Is the doctrine of sovereign immunity a threat to investment arbitration? University of Dundee Press, 1.

<sup>551</sup> Shoult above n 190, at 104.

<sup>552</sup> Ibid, at 103-105.

<sup>553</sup> Ibid, at 103-104.

mechanisms. Ideally, so as to enhance capital flows across the globe and hence economic development, there is the need to draft universally accepted laws that govern how nation states and foreign nationals treat each other when resolving investment disputes that are inevitably unavoidable.<sup>554</sup> In light of this information, autonomous dispute resolution- bodies with a global command can go a long way to addressing this shortcoming.<sup>555</sup>

According to Shihata, international investment treaties such as the ICSID Convention, Multilateral Investment Guarantee Agency (MIGA), Overseas Private Investment Corporation (OPIC), International Finance Corporation (IFC), and many others, provide the framework for the creation of arbitral tribunals that facilitate faster, fairer, and more efficient dispute resolution measures while balancing “the interests of investors and host countries.”<sup>556</sup> Shihata’s sentiments touch on the sensitive area of consultation among the stakeholders. These sentiments were expressed by the Saudi Foreign Affairs Minister, Prince Saud Al-Faisal, in his speech to the European Policy Centre in Brussels Belgium on February 19, 2004 during which he emphasized the importance of forming mutual organizations among nations so as to promote growth in investment activities. He said:

*From the outset, let me state our strong and clear conviction that change and reform are necessary in the Arab World if we are to truly advance. Such reform action must begin at home to ensure the welfare of the people by providing good governance and equality in the eyes of the law. Islam, as a religion, a culture, and a way of life, will certainly have to play a pivotal role in maintaining the social and political bonds during this turbulent*

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<sup>554</sup> ICSID convention above n 481, at 11.

<sup>555</sup> Ibid.

<sup>556</sup> Shihata above n 545.

*period. I hope to show the relevance of this point despite the prevailing Western view that Islam is an obstacle to modernisation.*<sup>557</sup>

It is arguable that reforms aimed at uniting the KSA with the rest of the world in matters of resolving investment disputes are most welcome. Even so, such reforms can have the greatest impact only if they are tailored around the stringent Islamic Sharia values. This is because, in the KSA as well as other Muslim nations, international arbitration treaties can endure the test of time only if they are in accord with the local legal frameworks.<sup>558</sup>

International arbitration treaties are what Nelson (2010) refers to as “enduring institution[s] that ... weather[s] worse backlashes” from anti-reformist and oppressive nation states.<sup>559</sup> In reference to the 1933 arbitration between Lena Goldfields and the Soviet Government, Justice V.V. Veeder famously opined that international arbitration treaties that internationalize trans-jurisdictional investment dispute resolutions were a major invention in the investment world which can be compared to “the caveman’s discovery of fire”.<sup>560</sup>

Some of the most notable arbitrations that underscore the importance and purpose of international arbitration treaties and that subsequently changed the world of investor-state disputes include the US – Iran Claims Tribunal in the 1980s and the Alabama Claims Tribunal that was formulated in 1874 to settle the US Civil War disputes between the US ship owners and Great Britain.<sup>561</sup> Others are the ARAMCO dispute that involved United States/British co-owned

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<sup>557</sup> Al-Faisal, above n 40.

<sup>558</sup> Baamir and Bantekas above n 343.

<sup>559</sup> Nelson above n 340, at 556.

<sup>560</sup> Ibid.

<sup>561</sup> Ibid.

oil Exploration Company (ARAMCO) and the Saudi Arabian Government,<sup>562</sup> as well as a gamut of cases arising from nationalization moves by the Libyan government in the 1970s. The circumstances surrounding these cases can be said to have been fuelled by high levels of uncertainty and bias on the part of the domestic legal systems of the host states. For instance, in the Libyan nationalization cases, the government under the dictatorship of Colonel Muammar Qaddafi literally commissioned the nationalization of several foreign-owned oil companies as a measure to establish a firm state control of the lucrative oil industry.<sup>563</sup>

Basically, international arbitration treaties are consensual. This is because it is universally agreed that no nation state should be forced into ratifying a treaty that undermines the spirit of national sovereignty which they espouse.<sup>564</sup> In fact, most of the international arbitration treaties are flexible so that nation states can categorically submit matters they wish to be handled within the jurisdiction of such treaties and matters they consider the preserve of their domestic court systems. Basically, the meaning and context of most international arbitration treaties place great emphasis on the spirit of mutual consensus whereby entities embroiled in an investment dispute are given leeway to settle the dispute in an amicable manner; failure to do so leads to such disputes being taken to arbitration.<sup>565</sup> This is meant to create friendly and mutually beneficial investment environments and, most importantly, to discourage exploitation and mistreatment of foreign investors.<sup>566</sup>

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<sup>562</sup> Saudi Arabia v. Arabian American Oil Co., 27 ILR 117, at 135 (1958)

<sup>563</sup> R.B Mehren and P.N. Kourides, (1981). International Arbitrations between States and Foreign Private Parties: The Libyan Nationalization Cases, 75 AM. J. INT'L L, at 476.

<sup>564</sup> M. Ball, M. (2005). International Arbitration: The Fundamentals.  
<[http://www.ili.org/images/books/intl\\_arb\\_fundamentals.pdf](http://www.ili.org/images/books/intl_arb_fundamentals.pdf)>

<sup>565</sup> Ibid.

<sup>566</sup> Ibid.

#### ***7.4. Ratification of The ICSID Convention***

Cases of investment disputes arbitration in Saudi Arabia can be traced back to the ARAMCO case that arose following the KSA government's introduction of new regulations not present in the original 1935 concession, and ARAMCO's failure to abide by the new regulations.<sup>567</sup> ARAMCO, Arabian American Oil Company, was given an exclusive oil exploration, extraction, development, transportation, and exportation concession in 1935.<sup>568</sup> The prices of oil shot up following post-war economic shifts, prompting the KSA to consider entering into new lucrative deals. A company owned by Aristotle Onassis, called Saudi Arabia Maritime Tankers Co., Ltd. (SATCO) was granted special rights to transport Saudi oil for a span of 30 years. Both the KSA government and ARAMCO agreed to settle the dispute through arbitration. Article 4 of the 1935 concession provided for an arbitration process that was based on KSA law "if the disputed questions were of the jurisdiction of Saudi Arabia [or]... in any other law the arbitral tribunal would deem applicable if the disputed questions were not of such jurisdiction."<sup>569</sup> The ensuing dispute was settled by a Switzerland-based arbitral tribunal. ARAMCO argued that the granting of exclusive transportation rights to Saudi Arabia Maritime Tankers was a violation of the 1935 contract.<sup>570</sup> The Saudi government was found guilty of extending rights granted to ARAMCO to a third party and agreed to comply by the arbitral tribunal ruling. The issues surrounding this historical dispute and the subsequent ruling marked the turning point in the KSA investment dispute resolution track record.<sup>571</sup>

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<sup>567</sup> Nelson above n 340, at 560.

<sup>568</sup> Saudi Arabia v. Arabian American Oil above n 560.

<sup>569</sup> Ahdab above n 331, at 600.

<sup>570</sup> Saudi Arabia v. Arabian American Oil above n 560.

<sup>571</sup> Nelson above n 340, at 560.



It was ruled that even though the arbitration was carried out within the Swiss jurisdictional framework, only international arbitration laws could be applied when granting awards to the aggrieved party and not the Swiss laws, but the KSA laws.<sup>572</sup> This was because the concession contract was made under the KSA laws.<sup>573</sup> However, the use of the Swiss legal framework was occasioned by the inadequacy of the Sharia-based KSA law, particularly in matters concerning “mining concessions in general and petroleum concessions in particular.”<sup>574</sup> . It was ruled, in fact, that the KSA law was inadequate for determining cases of such magnitude and therefore it needed to “be complemented by other sources of law.”<sup>575</sup> It was also ruled that the KSA was under all legal obligations to respect and uphold the 1935 concession terms, particularly the clauses that indicated that the KSA government would not undertake to alter or even impede rights granted to ARAMCO. Even so, it was made clear that the national sovereignty latitude extended by international arbitration treaties grant nation states legal capabilities to selectively agree to and grant rights during contract drafting that bars them from retracting their promises.<sup>576</sup>

Following the discovery and the beginning of exploration of oil in the KSA, it became apparent that private foreign-based investments in the oil industry were inevitable. The economy was growing at a faster rate than ever before.<sup>577</sup> Consequently, it slowly dawned on the KSA policy makers that investment disputes are inevitable, and hence, proper legal frameworks had to be established for future eventualities. Based on this realisation, on September 28, 1979 the

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<sup>572</sup> Ibid.

<sup>573</sup> Ahdab above n 331, at 601.

<sup>574</sup> Ibid.

<sup>575</sup> Ibid.

<sup>576</sup> Saudi Arabia v. Arabian American Oil above n 560.

<sup>577</sup> Saudi Arabia: Business Indicators Summary: International Dispute Resolution (2010).

<<http://www.estandardsforum.org/saudi-arabia/business-indicators?id=162/>>

Kingdom of Saudi Arabia signed the ICSID treaty, ratified it on May 8, 1980 and went ahead to give it formal enforcement on September 28, 1980.<sup>578</sup>

All along, the KSA has endeavoured to be among the world's most targeted investment destinations by the year 2010. However, this has not been an easy task given the inherent lack of investor confidence in the KSA Sharia-based court system.<sup>579</sup> This postulation is affirmed by the Saudi Minister for Foreign Affairs in his speech to the European Policy Centre Brussels, Belgium in February 19, 2004 when he sought to assure foreign investors that the KSA is a peaceful investment hub and that the Saudi government is committed to improving the investment climate. He said:

*It is true that we faced formidable challenges in the past, and that current developments confront us with serious issues.*<sup>580</sup>

For such an ambitious goal to be realised, there must be an appropriate legal framework that espouses international arbitration methods for resolving investment disputes. The ratification of the ISCID, enactment of the Arbitration Law, Foreign Investment Law, and Mining Law was driven by the aspiration to create such legal framework.<sup>581</sup> This was achieved by making provisions in the existing law which gave it a mandate and jurisdiction over some pertinent issues in KSA.

Moreover, it was acknowledged that litigations involving inter-jurisdictional investment contracts may pose significant challenges in terms of interpretation and delivery of impartial

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<sup>578</sup> Ibid.

<sup>579</sup> Shoult above n 190, at 104.

<sup>580</sup> Al-Faisal, above n 40.

<sup>581</sup> Al Malki above n 153, at 25.

rulings that extend justice to both contracting parties.<sup>582</sup> Special emphasis was also given to the notion that international dispute solving conventions such as the ICSID are more credible; hence, foreign nationals are more obliged to respect their rulings than national legal institutions whose credibility and impartiality may be wanting.<sup>583</sup> This is based on the fact that the people presiding over the conventions are well-informed about the local state of affairs. The ratification of the ICSID was meant to grant nationals of other states involved in contractual disputes with Saudi Arabia or state agencies an alternative legal recourse apart from the Saudi Sharia-based court systems.<sup>584</sup> In a nutshell and according to an official statement by King Abdullah in his speech to the Shoura annual meeting in 2008, it is arguable that the Saudi stance on foreign investment is based on the notion that the country's economic development is directly dependent on efforts made to diversify the revenue sources.<sup>585</sup>

Apparently, increased foreign investment traffic due to oil exploration, transportation, and exportation, meant more disputes which imposed a greater burden on Saudi courts. Hence, many disputes arose that required the application of KSA laws in settling them, a practice that most foreign investors are against. It was therefore a wise move by the KSA policy makers to reduce the case load handled by the Saudi courts.<sup>586</sup> Most importantly, the KSA policy makers were well aware that oil is the Kingdom's chief foreign exchange and in order to achieve the envisaged short- and long-term economic goals of being the friendliest country to invest in Middle East, the KSA needed to increase direct foreign capital inflow. In this regard, the KSA is

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<sup>582</sup> Shoult above n 190, at 104.

<sup>583</sup> Ibid, at 103-104.

<sup>584</sup> Shihita above n 545.

<sup>585</sup> Al Malki above n 153, at 23-25.

<sup>586</sup> Baamir and Bantekas above n 243.

still committed to enticing foreign investors for both capital and expertise gains.<sup>587</sup> Apparently, this can only be achieved by assuring investors of legal and economic protection against potential investment risks that are inevitable in the world of inter-jurisdictional economic activities.<sup>588</sup> Saudi leadership is well aware that for it to compete equally with other oil producers in the Middle East and world-wide, it needs to streamline its legal frameworks by entrenching foreign investment protectionist clauses in agreements.<sup>589</sup> Needless to say, the country needed to do away with all impediments that could potentially hamper the smooth flow of international capital. Given the Sharia-based legal system, it is obvious that foreign investors from non-Muslim countries might have felt uneasy about some sections of the Qur'an-based constitution, particularly the provision that the Saudi courts are not obliged to approve monetary gains to parties claiming loss of future profits or even the provision that the courts cannot give consent for payments to be made as interest on overdue amounts. Hence, there was a great need to integrate international standards with the country's legal framework in terms of investment.<sup>590</sup>

Nevertheless, the Saudi leadership has on several occasions through prominent government personalities come out in public to reiterate its commitments to supporting arbitration as an amicable way of resolving investment disputes. These government representatives are the same people who are called upon to settle disputes between foreign investors and the government or local investors, especially when the proceedings are outside the courts. Most of these assurances have been channelled through the Saudi Arbitration Team which is led by Prince Dr. Bandar Bin Salman bin Mohammed Al-Saud. When addressing

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<sup>587</sup> Al Malki above n 153, at 24.

<sup>588</sup> Rahman and Sheikh above n 362.

<sup>589</sup> Ibid.

<sup>590</sup> Shoult above n 190 at 103-105; Baamir and Bantekas above n 343, at 242-244.

delegates at an international arbitration meeting at The Hague Netherlands, Dr. Bandar assured the international community that:

*The Kingdom of Saudi Arabia appreciates the role carried out by the Permanent Court of Arbitration. It has, therefore, decided to ratify The Hague Treaty of 1907 and establish relations with the organisation. The Kingdom has appointed representatives at the Permanent Court of Arbitration, and I am honoured to be one of the four who have been appointed to represent the Kingdom. My colleagues are ... [and] we are eager to contribute by promoting the Kingdom's desire for consultation on a path of peace, security and justice, and to introduce our laws, which are in harmony with the Islamic Sharia.<sup>591</sup>*

These assurances are very important, particularly to non-Muslim investors who may feel that the Sharia-based Saudi laws are “unfriendly.” In addition, given the current civil uprisings in the Middle East and North Africa (MENA) region, this assurance serves to instil confidence in foreign investors that their investments can be safe even during times of social/political unrest or emergency.

Before the ratification of the ICSID treaty and the subsequent enactment of the Arbitration Law of 1983 and its Implementing Rules of 1985, arbitration in the KSA was governed by a range of legislations within the Commercial Court which later was superseded by the Committee for the Settlement of Commercial Disputes.<sup>592</sup> These two courts were responsible for handling all forms of “Company Code, Services Agency Code, Commercial Agency Code

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<sup>591</sup> Saudi Arabia promotes peaceful resolution of international disputes (Feb. 14, 2003).

[http://www.saudinf.com/display\\_news.php?id=252/](http://www.saudinf.com/display_news.php?id=252/)

<sup>592</sup> Baamir and Bantekas above n 343, at 242.

...commercial land and maritime issues”, as well as labour and workmen issues.<sup>593</sup> Each of these regulations was applied when adjudicating investment disputes within its mandate. However, the inherent bias and the lack of clarity posed a huge impediment to foreign direct investment.<sup>594</sup> Arguably, this scenario was partly responsible for the legislation of the 1983 Arbitration Law which was intended to address the existing shortcomings in the arbitration of investment disputes.<sup>595</sup> Interestingly, this law did not adequately address all the critical areas of international investment arbitration. Hence, there was the need to formulate a set of implementing rules that would give it meaning, purpose, and most importantly, enhance its capability to address the shortcomings in the scope of arbitration within the Kingdom.<sup>596</sup> This milestone was achieved in 1985 when the Implementing Rules were passed by the Council of Ministers.<sup>597</sup>

Apparently, this provision seems to grant the KSA substantial benefits particularly on matters concerning oil and a number of minerals. As a matter of fact, acting on the leeway allowed by this clause, the KSA law makes a clear distinction between the investment disputes that are to be admitted to the ICSID and those which are not. Consequently, this clause empowers the KSA especially in matters considered to be closely linked to the Kingdom sovereignty, and most importantly, on investment in particular sectors considered sensitive and therefore a preserve of the KSA entities.<sup>598</sup>

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<sup>593</sup> Ibid, at 245-246.

<sup>594</sup> Ibid, at 246.

<sup>595</sup> Ibid, at 245-246.

<sup>596</sup> Ibid, at 242.

<sup>597</sup> Council of Ministers Resolution 2/2021/M (27 May 1985).

<sup>598</sup> Shoult above n 190, at 112.

For instance, it is stipulated that the Kingdom “*reserves the right of not submitting all questions pertaining to acts of sovereignty*”.<sup>599</sup> Article (3) of the Mining Investment Law stipulates that “*Without prejudice to the provisions of Article (2) of this Law, the following shall be excluded from its provisions: (1) Petroleum, natural gas and derivatives thereof, and; (2) Pearls, corals and similar organic marine substances.*” Moreover, the Royal Decree Number M/8 Dated 22/3/1394H explicitly offers that, although the Kingdom willingly subscribes to the ICSID rules in regard to the arbitration of investment disputes between its nationals and/or agencies and foreign nationals running investments within the Kingdom: “*KSA reserves the right not to raise issues relating to oil in the International Centre for Settlement of Investment Disputes to be resolved either by conciliation or arbitration.*”<sup>600</sup>

Since some disputes categories are deemed to be beyond the jurisdiction according to notions of national sovereignty and the respect for sensitive national issues, it is obvious that the KSA courts handle all investment dispute matters that are not covered by the ICSID. Oil, the country’s most coveted revenue source, is considered as a symbol of national recognition and therefore disputes arising from oil investments are a preserve of the KSA courts and special tribunals.<sup>601</sup>

## ***7.5 Resolution of Oil Disputes***

Perhaps the most important step that the Saudi government ever took to improve dispute resolution mechanisms between its agencies and/or citizens and foreign investors was the ratification of the International Court for Settlement of Investment Disputes (ICSID) in

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<sup>599</sup> C.H Shreuer, (2001). The ICSID Convention: a commentary: A commentary on the Convention on the ... Cambridge University Press, at 113.

<sup>600</sup> Royal Decree No above n 428; Al Malki above n 153, at 25.

<sup>601</sup> Baamir and Bantekas above n 343, at 248.

September 28, 1979.<sup>602</sup> Although no single case has been processed using the ICSID statutes, it can be argued that the Convention which officially came into operation on May 8, 1980 has been phenomenal in enhancing foreign direct investment activities in the Kingdom. As outlined in the previous chapters, foreign direct investments in the Kingdom have increased enormously in all the investment sectors open to foreign investment.<sup>603</sup>

Even so, as discussed in the previous chapters, oil disputes cannot be settled under the ICSID Convention pursuant to Article 25(4) of the Convention as well as Royal Decree Royal Decree No., M/8 Dated: 22/3/1394 H.<sup>604</sup> Moreover, the submission of oil disputes to the ICSID would in the first place be a complete contravention of the very essence of the Convention. This is because the ICSID Convention was purposely formulated to enable the amicable resolution of disputes between foreign investors and parties from host nations.<sup>605</sup> Apparently, the oil industry in Saudi Arabia is considered out of bounds to foreign investors. Therefore, foreign investors (Muslims, non-Muslims, Arabs, non-Arabs, GCC, and non-GCC) cannot be involved in disputes in a commercial sector in which they cannot invest.<sup>606</sup>

Nevertheless, one can speculate whether the two provisions (Article 25(4) of the Convention and Royal Decree Royal Decree No., M/8 Dated: 22/3/1394 H) indicate that oil disputes cannot be resolved through arbitration. The answer to this question may draw divergent views; however, this study holds that oil disputes can indeed be arbitrated but within the frameworks of the Saudi (Sharia) legal system. This is because it is not on the list of matters

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<sup>602</sup> 'Arabia: Business Indicators Summary: International Dispute Resolution (2010)'.

<<http://www.estandardsforum.org/saudi-arabia/business-indicators?id=162>>

<sup>603</sup> Ibid.

<sup>604</sup> ICSID convention above n 481, 25[4]; Royal Decree No above n 428.

<sup>605</sup> Ibid.

<sup>606</sup> Saudi Mining Investment Law above n 279.



“wherein conciliation is not permitted” as provided for in Article 2 of the Arbitration Law.<sup>607</sup>

The Saudi legal framework bars arbitration only on matters of *hudoud* (adultery, murder, robbery, drunkenness, injury as well as other personal issues as provided for by the Holy Qur’an) and *iaan* (litigation processes that result in divorce of spouses due to irreconcilable crimes).<sup>608</sup>

Moreover, the Royal Decree No., M/8 Dated: 22/3/1394 H only cautions that the “KSA reserves the right not to raise issues relating to oil in the International Centre for Settlement of Investment Disputes to be resolved either by conciliation or arbitration.”<sup>609</sup> In this case, it does not bar arbitration which is carried out under the Saudi legal framework under the Saudi competent authorities as long as the parties involved in the disputes have fulfilled the basic requirements qualifying them for arbitration as specified by the Arbitration Law and its Implementing Rules. Such requirements include an agreement during the signing of a contract to resort to arbitration upon the occurrence of a dispute pursuant to Article 7 of the Arbitration Law, which reads in part, “[w]here parties agree to arbitration ... the subject matter of the dispute may only be heard in accordance with the provisions of this Law.”<sup>610</sup> When considered together with Article 2 of the same law (Arbitration Law) it is clear that this article gives the Saudi legal framework the mandate to handle oil-related disputes.<sup>611</sup>

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<sup>607</sup> Law of Arbitration above n 322, art 2.

<sup>608</sup> Implementation rules above n 307.

<sup>609</sup> Royal Decree No above n 428.

<sup>610</sup> Law of Arbitration above n 322, art 7.

<sup>611</sup> Royal Decree No above n 428.; Law of Arbitration above n 322, art 2.

## **7.6. Validity and Severability of the ICSID vis-à-vis the KSA Investment Regulations**

The ICSID regulations are reflected in the constant dispute arbitration process that characterizes the KSA Foreign Investment Law.<sup>612</sup> Such dispute resolution is subject to the will of the defaulting contracting parties to abide by the decision reached. In the event that neither party is willing to abide by the decisions reached by the Committee, then the law provides for recourse to arbitration. Article 26 of the Foreign Investment Law Implementing Rules stipulates:

*... The committee shall work to settle the dispute amicably. In case an amicable settlement could not be reached, the dispute shall be settled through arbitration according to the Arbitration law and its implementation rules issued by Royal Decree No. (46) Dated 12.7.1403 H..<sup>613</sup>*

This arbitral process is subject to the provisions of the Royal Decree No (46) Dated 12.7.1403H that offers explicit details on the implementation of the Arbitration Law of 1983. Ideally, the committee still retains its professional role of laying the foundation for the commencement of the arbitration process. Moreover, the activities of the committee and those of the subsequently formed arbitration tribunal during the dispute resolution process are to be undertaken in accordance with the provisions of Article 13(2) of the Law.<sup>614</sup>

Foreign investors operating in the KSA are subjected to strict vetting procedures to ensure that they operate within the provisions of the Act and the Rule.<sup>615</sup> Violations noted are compiled and their penalties listed by the Governor or his designate and the report passed on to

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<sup>612</sup> Royal Decree No above n 428.

<sup>613</sup> Foreign Investment Law above n 91 art 26.

<sup>614</sup> Law of Arbitration above n 322.

<sup>615</sup> Foreign Investment Law above n 91 art 12, 15.

the concerned foreign investor. If the foreign investor fails to correct the anomalies noted therein within the stipulated period of time, then the stipulated penalties are duly imposed.<sup>616</sup> However, acting on the spirit of amicable dispute resolution, the Law and the Rules provide for the formation of a committee comprised of a legal expert and at least two other members. The committee delivers its verdict after deliberating on all the accusations and defences presented to the committee by the foreign investor and the KSA government representatives and on the specific Act and Rule provisions touching on licensing, implementation, violations, and penalties.<sup>617</sup>

In the event that such verdict shows cause and reason that the foreign investor should incur penalties, further recourse is also available by way of an appeal put before the Board of Directors within thirty days from the date of the committee's verdict.<sup>618</sup> Article 24 of the Rules stipulates:

*The Foreign Investor to whom the penalty decision is issued according to Article 23 of The Rules may object to the rejection decision before the Board of Directors within thirty days effective from the date on which he is notified of the rejection decision.*<sup>619</sup>

Working within a thirty-day time frame, the Board of Directors makes a ruling. If it has found that the penalty was necessary, then the foreign investor still has an opportunity for further recourse to the Board of Grievances before 60 days elapse starting from the date the Board of Directors made their ruling. In essence, the KSA Foreign Investment Law and its Implementing

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<sup>616</sup> Foreign Investment Law above n 91 art 12.

<sup>617</sup> Ibid, art 23, 24, 25, 26.

<sup>618</sup> Ibid, art 15.

<sup>619</sup> Ibid, art 24.

Rules aim to provide a just investment environment.<sup>620</sup> Indeed, one may find that it is very unlikely that the rigorous processes involved in the enforcement of the investment regulations as well as dispute resolution measures can be circumvented or bypassed by the KSA government to punish foreign investors.<sup>621</sup>

In the event of a dispute arising from a contract whose parties have a prior clause detailing arbitration as a form of dispute resolution, the parties are obligated to consult an authority competent to handle such disputes. Such authorities may include the Sharia courts, Board of Grievances and the Committee of Settlement of Labour Disputes.<sup>622</sup> These three options are applicable only in the event that the dispute in question involves Saudi parties; however, if a foreign national and/or a representative of a state that is a member of the ICSID is a party, then it will be settled in accordance with the provisions of Arbitration and Foreign Investment Laws. This extension is also applicable in situations where the arbitrating authority has agreed to handle a given investment dispute.<sup>623</sup> For the arbitration process to be legally binding, all the parties in a dispute or their representatives (which in most cases are their attorneys) should sign the agreement. Other critical details include those pertaining to the dispute such as the official particulars of the arbitrators, their signatures confirming that they are not under any duress to arbitrate such cases, and their undertaking that they will deliver unbiased rulings based on the facts presented.<sup>624</sup>

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<sup>620</sup> Ibid, art 11.

<sup>621</sup> Al Malki above n 153, at 24.

<sup>622</sup> Baamir and Bantekas above n 343, at 242-244.

<sup>623</sup> Foreign Investment Law above n 91 art 26.

<sup>624</sup> Ibid..

### ***7.7 Structure of the KSA Investment Related Laws vis-à-vis the ICSID***

Foreign investors in KSA, as in any other sovereign state, enjoy a significant number of benefits and risks alike insofar as adherence to the set domestic and international investment regulations is concerned.<sup>625</sup> Basically, foreign investment in the KSA is governed by several conventions and regulations such as the ICSID, Arbitration Law and its implementing rules, Foreign Investment Law and its implementing rules, Mining Investment Law, and a number of Royal Decrees on Investment. While each of these legislations targets a particular facet of investment in the KSA, the underlying theme is more or less similar – to streamline the KSA investment environment with a view to making it more friendly for the operations of both foreigners and Saudis.<sup>626</sup> For instance, the arbitration law which was enacted in 1983 and given meaning by the subsequent implementation rules of 1985 is meant to provide a smooth and concise framework within which foreign nationals and/or entities and the Saudi nationals and/or state agencies can settle investment-related disputes using more open, impartial, and internationally acknowledged methods.<sup>627</sup>

Despite being a global dispute resolution vehicle comprised of many members, the ICSID seems reluctant to clarify the meanings of the key words “direct” and “investment.”<sup>628</sup> Apparently, even Article 25 that delineates which investment disputes falls within the ICSID jurisdiction is conspicuously silent. It stipulates only that:

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<sup>625</sup> Foreign Investment Law above n 91 art 6-8; See also, Protection and Promotion of National Industries Act issued by Royal Decree No.50 dated 23.12.1381 H.

<sup>626</sup> Al Malki above n 153.

<sup>627</sup> Council of Ministers Resolution No.7/2021/M dated 8/9/1405 H.

<sup>628</sup> Adebiyi above n 548, at 2.

*The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.*<sup>629</sup>

It is apparent that the drafters of the convention were reluctant to define investment in explicit terms.<sup>630</sup> Consequently, it has been always the duty of the contracting parties to broadly agree on what should and should not constitute such investments. To some extent, this leeway has favoured nation states rather than foreign investors.<sup>631</sup> As a potential foreign investment destination, the KSA enjoys great as a result of this Article, particularly when it comes to specifying those elements that define an investment. For instance, Article 1 of the KSA Foreign Investment Law defines foreign investment as, “*any foreign capital in an activity licensed by [the] the law.*”<sup>632</sup>

In accordance with this, the KSA is provided with equal leeway by Article 46 of the Convention that apparently limits the ICSID jurisdiction to issues that are “directly” related to the “investment” dispute in question.<sup>633</sup> In addition, ancillary and/or incidental issues that directly arise as a result of the dispute in question and that, according to the desecration of the tribunal are within the dictates of the dispute subject matter, should be perceived as “directly”

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<sup>629</sup> International Center for Settlement of Investment Disputes, Article 25(4).

<sup>630</sup> Adebisi above n 548, at 2.

<sup>631</sup> Ibid.

<sup>632</sup> Foreign Investment Law above n 91.

<sup>633</sup> Shreuer, above n 597.

related to the “investment” and hence tackled under the Convention laws.<sup>634</sup> On the other hand, it deprives the KSA of absolute powers particularly in determining which investment disputes issues are directly linked to an investment. This is because Article 46 of the ICSID provides that the element of directness is not subject to the consent of the parties involved in a dispute. In this regard, the subject matter of the dispute should not only be related to an investment issue but must be closely linked to it.<sup>635</sup>

Moreover, the Convention is not explicit regarding the interplay between the ICSID award rulings and matters considered by nation states as touching on their national sovereignty.<sup>636</sup> Although Articles 53 and 54(1) (2) of the Convention provide that an award given by ICSID tribunals should be considered as a final ruling made by a state’s domestic court system,<sup>637</sup> both Articles 54(3) and 55 subject the enforcement and execution of such awards to the domestic legal frameworks of the host state. More specifically, Article 55 stipulates that:

*Nothing in Article 54 shall be construed as derogating from the law in force in any Contracting State relating to immunity of that State or of any foreign State from execution.*<sup>638</sup>

Even so, the KSA provides a foolproof Foreign Investment Law that induces confidence on the part of the foreign investors.<sup>639</sup> Therefore, foreign investors should be very alert in ensuring the most basic legal frameworks are in place before committing themselves to a legally

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<sup>634</sup> International Center for Settlement of Investment Disputes, Article 46.

<sup>635</sup> Ibid, art 46.

<sup>636</sup> Adebisi above n 548, at 2.

<sup>637</sup> ICSID Convention above n 481, art 53 and art 54(1) (2).

<sup>638</sup> Ibid, art 54(3) and art 55.

<sup>639</sup> Ibid.

binding investment contract with nationals and agencies of foreign states.<sup>640</sup> For instance, Article 11 of the Foreign Investment Law seeks to assure foreign investors that no circumstances can lead to the loss of their capital and accumulated wealth by stipulating that:

*The investments of the Foreign Investor are not allowed to be confiscated either partially or entirely without a judicial verdict, and his property is also not allowed to be expropriated, either partially or entirely, except for public interest and in return for fair compensation in accordance with the law and regulations.*<sup>641</sup>

Based on the notion that government policy on foreign investment plays a huge role in attracting foreign investors, the inclusion of the above clause in the Law was meant to provide long-term relations that have clearly defined exit methods as well as ways of resolving disputes.<sup>642</sup> While ambiguous and biased legal provisions for foreign investment may cause doubts among potential foreign investors, explicit policies that provide clear procedures for amicably ironing out differences and resolving disputes between the contractual parties go a long way in promoting direct foreign investment.<sup>643</sup>

### ***7.8 Overlap between ICSID Rules and the KSA Investment Legislations***

Foreign investment in the KSA is governed by the Foreign Investment Law that was established in 2000 by the *Royal Decree No M/15 Muharram 1421/10 April 2000*.<sup>644</sup> Under this law, two powerful bodies, The Supreme Economic Council and The General Investment

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<sup>640</sup> Al Malki above n 153, at 25.

<sup>641</sup> Royal Decree on Foreign Investment Code: Royal Decree Number: M/1 Dated: Muharram 1, 1421 A.H. Corresponding to April 10, 2000 A.D, Art. 11.

<sup>642</sup> Al Malki above n 153, at 23-25.

<sup>643</sup> Al Malki above n 153, at 23-24.

<sup>644</sup> Royal Decree No M/1 5 Muharram 1421 / 10 April 2000.



Council, are mandated to coordinate all foreign investment matters. Run by a board of directors and a governor respectively, the two bodies are directly responsible for overall investment coordination, licensing, monitoring, and even disciplining of errant foreign investors pursuant to Articles 2, 3, 4, 12 and 17. Unlike the provisions of the ICSID that fail to offer a clear definition of an investment, the KSA Foreign Investment Law clearly defines what investment entails.<sup>645</sup> Articles 1(f) and 5 (1) (2) offer that foreign investment comprises of any form of capital investment jointly or wholly owned by foreign nationals as long as it is within the provisions of the law. Moreover, Article 1(e) of the Foreign Investment Law defines as foreign investor as “*a natural person who is not [of] Saudi nationality or corporate person whose partners are not all Saudi.*” Even so, not all investments qualify for ‘foreign investment’ status. For instance, Article 3 of the same law stipulates that some investment activities in the KSA cannot be left in the hands of foreign nationals.<sup>646</sup> These include “*Petroleum, natural gas and derivatives thereof, pearls, corals and similar organic marine substances.*”<sup>647</sup>

Upon licensure, foreign nationals and/or corporations intending to engage in business activities in the KSA should abide by all the laws governing fair investment activities within the KSA as well as the international jurisdictions. A breach of such laws may lead to severe actions being taken against them by the board of directors.<sup>648</sup> Such actions should be undertaken in accordance with the provisions of Article 12 (2) (a) (b) (c) which includes

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<sup>645</sup> Foreign Investment Law above n 91 art 1(f).

<sup>646</sup> Ibid art 1(e) (f), 3, 5 (1) (2).

<sup>647</sup> Saudi Mining Investment Law above n 277.

<sup>648</sup> Foreign Investment Law above n 91 art 13 (2) (a) (b) (c).

*...withholding of all or some of the incentives and benefits given the foreign investor ...  
[or the imposition of] a fine not exceeding 500,000 (five hundred thousand Saudi Riyals)  
... [or even in extreme cases] revoking of the foreign investment licence.*<sup>649</sup>

Even so, foreign investors are provided with recourse in the form of appeals that can be put before the Board of Grievances. In this regard, the laws provide that where the KSA is party to a contract that has resulted in a dispute, efforts will be made to exhaust all alternative avenues of justice within the KSA legal systems before subjecting such dispute to arbitral tribunals. Article 13(1) stipulates:

*Disputes arising between the government and the foreign investor in relation to its investments licensed in accordance with this Law shall, as far as possible, be settled amicably. Failing such settlement, the dispute shall be settled according to the relevant laws.*

This provision is galvanized by Article 13 (2) particularly in disputes involving foreign investors and Saudi entities.<sup>650</sup>

It is common practice across the globe for nation states to hide behind the confines of their sovereignty particularly on matters that touch on international dispute resolutions.<sup>651</sup> The fact that nation states are governed by unique national laws that seek to limit the extent which international dispute resolution treaties can be enforced domestically underscores this postulation.<sup>652</sup> After all, it is generally agreed that arbitration as an investment dispute resolution

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<sup>649</sup> Ibid.

<sup>650</sup> Ibid, art 13 (1) (2).

<sup>651</sup> Adebisi above n 548, at 4.

<sup>652</sup> Ibid.

measure can be acknowledged only if both contracting parties mutually consent to abide by the rules of a specific arbitral jurisdiction.<sup>653</sup> The KSA Royal Decree No: M/8 Date: 22/3/1394H explicitly outlines that although the Kingdom autonomously subscribes to the ICSID rules, it ought not to fully adjudicate all matters arising between foreign nationals and Saudi nationals, state agencies, and even the state, particularly if such matters are concerned with oil exploration and exportation.<sup>654</sup> In fact, all state agencies are obligated to seek state approval from the adjudicating authority before committing themselves to agreements that contain arbitration clauses. In essence, this means that the arbitration alternative provided for by the ICSID is not automatically applicable in contract negotiation and dispute resolution between state agencies and foreign nationals and/or entities.

As a matter of fact, Article 3 of the KSA Arbitration Law and Article 25(3) of the ICSID concur that arbitration clauses contained in investment contracts without due approval from relevant authorities can be disputed on the basis that the arbitration element in them is invalid. After all, it is imprudent to subject national sovereignty to arbitration mechanisms which are incompatible with the underlying domestic legal framework.<sup>655</sup>

### ***7.9 The Effectiveness of the ICSID in KSA Laws***

Apart from the investment-specific activities, foreign investors are entitled to take part in activities that lead to the enhancement of smooth business transactions and to dispose of the

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<sup>653</sup> Adebisi above n 548, at 7.

<sup>654</sup> Royal Decree No above n 428.

<sup>655</sup> Arbitration Regulations in 1983 (Royal Decree No: M/46 dated 1983) Article 3, and International Center for Settlement of Investment Disputes, at 25(3).

profits from activities as they may deem appropriate as long as they abide by the KSA laws.<sup>656</sup>

For instance, Article 8 of the Foreign Investment Law allows investors to

*...acquire necessary real estate as needed for operating the licensed activity, or for housing all or some of its staff, subject to the provisions governing real estate ownership by non-Saudis.*<sup>657</sup>

Furthermore, in a bid to create a level playing field for the foreign and Saudi investors, the Foreign Investment Law provides that country, industry, and business information, statistics, and critical data should be provided to foreign investors in real time to enable them to make informed investment decisions.<sup>658</sup> Analytically, this level of openness and flexibility should prevent investment disputes as contractual parties have got almost equal opportunities in terms of benefiting from the licensed investments.<sup>659</sup> For instance, the terms of Article 7 of the Foreign Investment Law that grants foreign investors the opportunity to repatriate the proceeds of their investments to their home countries, provides a huge incentive to foreign investors, particularly nationals from the developed world. Moreover, this provision allows proceeds to be used for either investment or other matters within the boundaries of the KSA as long as such activities in no way contravene the laws of the land.<sup>660</sup>

Although Article 11 of the Foreign Investment Law provides that foreign investment proceeds will not be in any way subject to state expropriation and/or confiscation, it is evident that foreign investors are still subject to the rules of the KSA government, especially when the

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<sup>656</sup> Foreign Investment Law above n 91 art 7.

<sup>657</sup> Ibid art 8.

<sup>658</sup> Ibid art 10.

<sup>659</sup> Al Malki above n 153, at 23-24.

<sup>660</sup> Foreign Investment Law, above n 91 art 7.

government through its agencies, the General Investment Authority and the Supreme Economic Council, invokes public interest sentiments as provided for by the law.<sup>661</sup> Again pursuant to the provisions of Article 12, foreign investment capital can be confiscated.<sup>662</sup>

### ***7.10 Risk of Foreign Investment in the KSA***

Foreign investors in the KSA face a number of risks. On analysis, it appears that such risks arise from failure to abide by the KSA investment laws. For example, if foreign investors are tardy in complying with the basic requirements of the signed contracts without reasonable explanations, they may lose their contractual rights. More specifically, foreign investors are obliged by the governing laws to take steps to establish their investment entities within the agreed time frame pursuant to Article 16 of the Foreign Investment Law Implementing Rules, which stipulates:

*The licensed investor shall start the practical steps required for setting up the entity in accordance with the time schedule submitted by him to The Authority. The Authority shall, if The Foreign Investor shows adequate reasons for delays in the implementation procedures, extend the period specified in the schedule, provided that the extensions shall not exceed one year in total. The extension shall not exceed one year unless a decision to that effect is made by the Board of Directors.*<sup>663</sup>

Apart from working within the set time frame to establish an investment entity, foreign investors are expected to respect the KSA laws and restrict themselves within the provisions of the licences provided thereof. The KSA ensures that foreign investors are engaged only in

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<sup>661</sup> Shoult, above n 190, at 112-113.

<sup>662</sup> Ibid.

<sup>663</sup> Law of Arbitration above n 322.

licensed activities by regularly conducting snap checks of the accounting documents as well as other equally telling records.<sup>664</sup> A breach of the contractual terms on the part of the foreign investor may lead to the revocation of licences pursuant to Article 17 of the Rules, Article 12 (2) (a) (b) (c) of the Foreign Investment Law, as well as all other provisions touching on licensing and the code of conduct expected of foreign investors.<sup>665</sup>

Unfortunately, the KSA government lacks sufficient transparency.<sup>666</sup> For instance, it still requires that foreign investors employ Saudis as part of the fulfilment of investment policies. Moreover, the government takes a long time to pay for goods and services manufactured by foreign companies. Also, it has been noted that the KSA record of respecting property rights contains all manner of inefficiencies.<sup>667</sup>

Overall, the KSA is considered as a relatively corrupt country. Indeed, according to the 2009 Corruption Perception Index, a study compiled by the Transparency International Corruption, the country is ranked at position sixty-three out of the 180 countries that were surveyed.<sup>668</sup> Relatively speaking then, these risks are immense. In fact, a combination of two or more of these risks may negatively dent the credibility of the KSA as a friendly destination for foreign direct investments. Foreign investors may feel insecure operating in an environment that is awash with corrupt and inefficient mechanisms for implementing public policy.

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<sup>664</sup> Foreign Investment Law, above n 91 art 19.

<sup>665</sup> Foreign Investment Law, above n 91 art 12 (2) (a) (b) (c).

<sup>666</sup> U.S. Department of Commerce (2010). Saudi Arabia Business Climate. Retrieved on July 14, 2010, from: [http://www.the-saudi.net/saudi-arabia/investment\\_climate.htm/](http://www.the-saudi.net/saudi-arabia/investment_climate.htm/)

<sup>667</sup> Ibid.

<sup>668</sup> Corruption Perceptions Index 2009. Retrieved July 14, 2010, from: [http://www.transparency.org/policy\\_research/surveys\\_indices/cpi/2009/cpi\\_2009\\_table/](http://www.transparency.org/policy_research/surveys_indices/cpi/2009/cpi_2009_table/)

## **7.2 Investment Arbitration**

Saudi Arabia recognises arbitration as an alternative recourse to settling investment disputes. The Secretary General of the Saudi Arbitration Union, Prince Dr. Bandar bin Salman bin Muhammad Al-Saud, in his speech to the international conference held in the Hague Netherlands on the reinforcement of arbitration as a globally-accepted alternative method for investment dispute resolution, affirmed this generalisation. While emphasizing the need for the Arab and Muslim world to unite with the rest of the world in upholding amicable dispute resolution mechanisms, he said that there is an urgent need to implement the measures so as to improve the KSA's investment ties in the world.

Apparently, this trend began well before the current investment arbitration treaties were ratified.<sup>669</sup> For instance, in the case of ARAMCO, the KSA government was fully aware of the terms of the concession signed in 1935 but went ahead to enter into an agreement with another party in complete violation of the existing contract with ARAMCO.<sup>670</sup> This underscores the fact that foreign investors are vulnerable to contractual breaches by the host states. Tellingly, the contemporary investment arbitration conventions were meant to act as impartial judges charged with the responsibilities of critically analyzing the facts presented by contractual parties with the view of delivering a fair award to the aggrieved party.<sup>671</sup> No doubt, this is a bad precedent that nation states are setting for the global investment arena as it undermines the credibility of international investment arbitration.

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<sup>669</sup> Ahdab above n 331, at 598-599.

<sup>670</sup> Saudi Arabia v. Arabian American Oil above n 560.

<sup>671</sup> Ibid.

Based on the fact that many nations are members of international investment arbitration conventions, the realm of arbitration has taken a bold step. The contemporary investment arbitration involves nation states and investors who specifically made explicit efforts to determine the arbitral tribunal in the event of a dispute. Popularly referred to as “concession arbitration” they involve not only investors from wealthy nations against developing countries, but also parties from developed nations. Nelson (2010) galvanizes this postulation by asserting that investment arbitration is not a preserve of the “developing countries but is a broadly applicable means of adjudicating all manner of investor-state disputes.”<sup>672</sup>

In this regard, arbitration as a form of alternative dispute resolution that cuts across developed and developing nation states is supposed to be friendly, simple, and voluntary.<sup>673</sup> A well-coordinated arbitration process between two estranged contractual parties can go a long way to promoting more productive investment activities for both foreign entities and the host state. Therefore, as an alternative to the tedious, rigorous, and unpredictable court litigations, arbitration should be an easy process for both contractual parties, since ideally it is less costly and, most importantly, fair and mutually enforceable. Most nations, especially those with significant deposits of natural resources, have enacted arbitration legislations that are intended to streamline investment dispute resolution modalities with a view to enticing foreign investments into their economies.<sup>674</sup> The Arbitration Law, Foreign Investment Law, Mining Investment Law, and a plethora of other minor legislations in the KSA underscore this fact. Moreover, the advantages of arbitration were emphasized by the Saudi Arbitration Team Chief, Prince Dr.

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<sup>672</sup> Nelson above n 340, at 567.

<sup>673</sup> Ball above n 562.

<sup>674</sup> Ibid.



Bandar Bin Salman bin Mohammed Al-Saud, during the interview with journalists in February 2003. He said:

*(...) with its effective leadership, [the Kingdom of Saudi Arabia] seeks to honour the great heritage embodied by the Islamic Sharia, and spread its principles, which aim to achieve happiness for mankind by protecting their rights. The Kingdom persistently calls for, and follows, the path of peace, and actively seeks to promote security and stability in the world. We believe that the best solution is one achieved by peaceful means.*<sup>675</sup>

This is no doubt a bold assurance to foreign investors doing business in the Kingdom given that it is coming from a prominent official. It seeks to dispel fears by sceptics that despite ratifying international arbitration such as the ICISD and enacting local arbitration laws, the Kingdom continues to demonstrate sovereignty overtones by suppressing would-be investment arbitration cases particularly if they involve a Saudi government agency.

### ***7.3 Oil Investment Disputes: the ICSID versus the KSA Commercial***

The KSA is fully committed to abiding by the rules and regulations of the international arbitration treaties, particularly those which it ratified back in 1980. This can be clearly seen in the wide range of “ICSID implementing laws” (commercial laws) that it has managed to legislate since its accession to the ICSID. These laws include the Arbitration Law, Foreign Investment Law, Foreign Capital Investment Law, as well as the Mining Law. A general overview of these laws indicates that the KSA is committed to actively partnering with the international community

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<sup>675</sup> Saudi Arabia promotes peaceful resolution of international disputes (Feb. 14, 2003). available at: [http://www.saudinf.com/display\\_news.php?id=252/](http://www.saudinf.com/display_news.php?id=252/)

in advancing its economic capability by mutually according protective rights to foreign investors.<sup>676</sup>

As highlighted in the previous chapters, this generalisation was confirmed when the King of the Kingdom of Saudi Arabia through the Royal Decree No., M/8 Dated: 22/3/1394 H approved the KSA's accession to the International Centre for the Settlement of Investment Disputes (ICSID) as a sign of goodwill in settling investment disputes through conciliation or arbitration, particularly those involving foreigners and Saudi nationals and/or state entities.<sup>677</sup> Even so, pursuant to the provisions of Article 25(4) of the ICSID,<sup>678</sup> the KSA did not relinquish all its authority over investment disputes resolution.<sup>679</sup> Article 25(4) of the ICSID specifies that:

*Any Contracting State may, at the time of ratification, acceptance or approval of this Convention or at any time thereafter, notify the Centre of the class or classes of disputes which it would or would not consider submitting to the jurisdiction of the Centre. The Secretary-General shall forthwith transmit such notification to all Contracting States. Such notification shall not constitute the consent required by paragraph (1).*

Consequently, in what seems to be a direct reaction to the provisions of this article, the KSA used the same executive order (Royal Decree No., M/8 Dated: 22/3/1394 H) to formally specify the “*the class or classes of disputes*” that “*it would not consider submitting to the jurisdiction of the Centre*”. This is succinctly and explicitly stated in the following words: “... *KSA reserves the right not to raise issues relating to oil in the International Centre for*

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<sup>676</sup> Law of Arbitration above n 322; Foreign Investment Law; Foreign Capital Investment Law above n 270; Saudi Mining Investment Law above n 277.

<sup>677</sup> Royal Decree No above n 428.

<sup>678</sup> The article grants contracting states a leeway to leave some classes of disputes under the jurisdictions of their respective national laws.

<sup>679</sup> Shreuer above n 597.

*Settlement of Investment Disputes to be resolved either by conciliation or arbitration.*”<sup>680</sup> For all intents and purposes, this provision has one clear meaning: All investment disputes in KSA are covered under the ICSID jurisdiction except those involving oil or as otherwise stipulated by any other valid law or decree as will be explained later in this chapter. For instance, Section 3 of the KSA Foreign Capital Investment Law that was enacted in 2000 specifies that matters that have significant impact on the national security and economic policies are to be kept away from foreigners.<sup>681</sup> As will be elaborated later in this chapter, sectors covered under this article include: oil industry, military industry, real estate in the areas around Medina and Mecca, information and publishing, and trade.<sup>682</sup>

Interpreted together (Article 25(4) of the ICSID and part of Royal Decree No., M/8 Dated: 22/3/1394 H), these two clauses give the contracting states (KSA) the leeway to make uncensored decisions on what to submit to the ICSID jurisdiction and what to leave under the domestic judicial system. The terms “*class or classes of disputes*” in Article 25(4) of the ICSID for instance, should be interpreted literally to mean virtually any investment dispute category depending on a contracting state’s preferences. Consequently, these categories significantly differ across contracting states depending on the nature of the national values embraced. Government agencies are also not supposed to submit disputes to the ICSID arbitration jurisdiction unless given the green light to do so by the Saudi Council of Ministers.<sup>683</sup>

On the other hand, the terms “*the right not to raise issues relating to oil in the International Centre for Settlement of Investment Disputes to be resolved either by conciliation*

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<sup>680</sup> Royal Decree No above n 428.

<sup>681</sup> Rahman and Sheikh above n 362.

<sup>682</sup> Ibid.

<sup>683</sup> Norton Rose above n 149.

*or arbitration*” as stated in the Royal Decree No., M/8 Dated: 22/3/1394 H are straightforward and should be interpreted in the same manner; that is, that all oil investment “issues” should not be subjected to arbitration under the Convention’s jurisdiction. Even so, as will be elaborated later in this chapter, this should not be taken to mean an outright ban on arbitration for matters arising from oil investments in the KSA.

Again, regarding Article 25(4) of the ICSID that requires contracting states to submit all their investment disputes to its jurisdiction except on those matters that are considered as of sensitive national value,<sup>684</sup> Royal Decree No., M/8 that categorically considers matters touching on oil as beyond the ICSID jurisdiction,<sup>685</sup> as well as Section of the Arbitration Law Implementing Rules that legalizes arbitrations in KSA except on *hudoud* and *haan*,<sup>686</sup> make it very clear that oil disputes are handled by the KSA’s domestic laws. It follows from the interpretation of Article 25(4) of the ICSID, according to which states are entitled to determine the classes of disputes that are not within the ICSID jurisdiction. Again, the fact that oil disputes are out of the ICSID jurisdiction is set forth in the provision that the process of resolving disputes where a state agency (sovereignty matters) is involved should not be taken to the ICSID but should be handled by the KSA legal framework except for situations where the Council of Ministers gives consent for ICSID arbitration.<sup>687</sup>

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<sup>684</sup> Article 25(4) of the ICSID.

<sup>685</sup> Royal Decree No above n 428.

<sup>686</sup> *Hudoud* are the crimes of murder, injury, adultery, drunkenness, theft and robbery, which are specifically provided for in the Qur’an, while *Laan* is a court procedure in which a confrontation between spouses takes place and through which they terminate their marital relationship after either spouse directs an accusation of adultery against the other. See Section 1 of the Implementation rules.27.05.1985G (08.09.1405H) 27 May 1985.

<sup>687</sup> Royal Decree No above n 428.; Implementation rules above n 308.

Even in the event that a foreigner is embroiled in oil disputes, the law is clear that such disputes should be settled either amicably or through arbitration within the provisions of the Saudi Arbitration Law.<sup>688</sup> This is pursuant to Article 13(2) of the Foreign Investment law which stipulates:

*Disputes arising between the foreign investor and its Saudi partners in relation to its investments licensed in accordance with this Law shall, as far as possible, be settled amicably. Failing such settlement, the dispute shall be settled according to relevant laws.*<sup>689</sup>

By extension, according to Article 26 of the Foreign Investment Implementing Rules that describes the modalities of arbitration under the KSA legal framework,<sup>690</sup> disputes arising between foreigners and Saudi nationals are to be settled amicably or through arbitration by a special committee: the Investment Disputes Settlement Committee as provided for by the Saudi Arbitration Law.<sup>691</sup> This committee is also the competent authority in charge of overseeing investment disputes in the KSA.<sup>692</sup>

In response to the question of whether oil investment disputes can be arbitrated, it is arguable that under the KSA legal framework pertaining to oil disputes, particularly the Arbitration Law, only *hudoud* and *iaan* matters cannot be subjected to arbitration.<sup>693</sup> In this regard, part of Article 2 of the Arbitration Law states that, “*Arbitration shall not be accepted in*

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<sup>688</sup> Foreign Investment Law above n 91 art 26 Law of Arbitration above n 322.

<sup>689</sup> Foreign Investment Law above n 91 art 13(2).

<sup>690</sup> Ibid art 26.

<sup>691</sup> Ibid, art 26; Law of Arbitration above n 322.

<sup>692</sup> Law of Arbitration above n 322, art 2.

<sup>693</sup> Implementation rules above n 308.

*matters wherein conciliation is not permitted....*”<sup>694</sup> Oil does not come under this category - the *hudoud* category includes crimes such as adultery, murder, robbery, drunkenness, injury and other personal issues as provided for by the Holy Qur’an,<sup>695</sup> while on the other hand, the *iaan* category includes litigation processes that result in the divorce of spouses due to irreconcilable wrongdoings.<sup>696</sup>

Based on these provisions, it is reasonable to assert that oil investments disputes can indeed be arbitrated under the KSA legal framework as long as the parties embroiled in such disputes have consented to arbitration pursuant to Article 7 of the Arbitration Law.<sup>697</sup> In interpretation of the provisions of this article (7) which states that, “[w]here parties agree to arbitration ... the subject matter of the dispute may only be heard in accordance with the provisions of this Law”,<sup>698</sup> it is clear that the KSA law does not bar arbitration in oil investment disputes. Moreover, when read together with the Royal Decree No., M/8 Dated: 22/3/1394 H as well as Article 2 of the Arbitration Law which states, “[a]rbitration shall not be accepted in matters wherein conciliation is not permitted. Agreement to resort to arbitration shall not be deemed valid except by those who have the legal capacity to act”,<sup>699</sup> it is clear that there are other impediments to arbitration applicable to all other types of arbitration, oil included.

Regarding the question about the applicability of arbitration in oil disputes by foreigners, the answer is simple: it is not legally possible within the KSA arbitration system, or better still, it is not applicable. Pursuant to the provisions of Article 2 of the Arbitration Law, it is arguable

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<sup>694</sup> Law of Arbitration above n 322, art 2.

<sup>695</sup> Implementation rules above n 308.

<sup>696</sup> Ibid.

<sup>697</sup> Law of Arbitration above n 322, art 7.

<sup>698</sup> Ibid.

<sup>699</sup> Royal Decree No above n 428; Law of Arbitration above n 322.

that foreigners do not have the rights to arbitrate in the event they are involved in oil investment related disputes (which is not possible based on the provisions of Article 3 of the Foreign Capital Investment Law).<sup>700</sup> The fact that the Saudi law bars foreigners from undertaking any oil-related investment activities makes them “legally unfit” to pursue arbitration as a form of dispute resolution. This is more precisely stipulated in Article (2) whereby:

*Arbitration shall not be accepted in matters wherein conciliation is not permitted.*

*Agreement to resort to arbitration shall not be deemed valid except by those who have the legal capacity to act.*<sup>701</sup>

Understandably, the rights to arbitration are not automatically granted to all investors in the KSA – it is the preserve of “selected” persons who meet the criteria set by competent authorities. For example, minors are not allowed to pursue arbitration recourse for settling investment disputes given they do not pass the “full legal capacity” requirement outlined in Article 2 of the Arbitration Law Implementing Rules.<sup>702</sup> Moreover, even their parents, guardians, or estate administrators are not allowed to opt for arbitration unless in situations where the relevant court gives consent.<sup>703</sup> It is therefore apparent that since the law bars foreigners from engaging in oil investments activities, they cannot seek arbitration in such matters – they can only arbitrate in matters that directly touch on their permitted activities in the KSA.

The Arbitration Act on which all arbitration processes in KSA are based is silent about whether oil disputes should be arbitrated, and by whom. Even so, there is no doubt that it should

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<sup>700</sup> Law of Arbitration above n 322, art 2.

<sup>701</sup> Ibid.

<sup>702</sup> Ibid.

<sup>703</sup> Ibid.

be settled under the KSA's domestic laws. Indeed, one may observe that oil does not fall under the categories of matters barred from arbitration, and since it is barred from the ICSID arbitration jurisdiction, it is obvious that it can be handled only by the KSA judicial system.<sup>704</sup> Even so, given the fact that the KSA lacks a domestic arbitration centre, all arbitrations are handled at the GCC arbitration centre located in Bahrain.<sup>705</sup> By virtue of membership of the GCC and based on the fact that the GCC arbitration is largely based on Sharia law provisions with minor parts borrowed from western jurisdictions, awards rendered thereof are wholly enforceable under the KSA legal system.<sup>706</sup>

From a different perspective, given that the Convention was specifically meant to encourage mutual settlement of “investment disputes between a contracting state and a national of another contracting state”,<sup>707</sup> it is useless to argue that the exclusion of oil-related investment disputes from the Convention's jurisdiction is unjustified; after all, oil investment disputes (if any) should involve only Saudi nationals as foreigners are prohibited from engaging in oil investments.

#### ***7.4 ICSID Weaknesses***

To demonstrate that the Convention is not an explicit authority for arbitration but an implied one, there are a number of articles that cast fears as to the applicability of arbitration as a source of recourse for the settlement of investment disputes arising between contracting states and nationals and/or agencies of other contracting states.<sup>708</sup> For example, owing to the provisions

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<sup>704</sup> Ibid.

<sup>705</sup> Norton Rose above n 149, at 4.

<sup>706</sup> Ibid, at 5.

<sup>707</sup> Shoult above n 190, at 111.

<sup>708</sup> ICSID Convention above n 481.



of the Preamble as well as Article 25(1) of the Convention, it is arguable that contracting states are not bound by the mere ratification of the treaty to submit investments disputes for arbitration.<sup>709</sup> The preamble states that:

*...Recognizing that mutual consent by the parties to submit such disputes to conciliation or to arbitration through such facilities constitutes a binding agreement which requires in particular that due consideration be given to any recommendation of conciliators, and that any arbitral award be complied with; and **Declaring** that no Contracting State shall by the mere fact of its ratification, acceptance or approval of this Convention and without its consent be deemed to be under any obligation to submit any particular dispute to conciliation or arbitration....,*<sup>710</sup>

While for its part, Article 25(1) stipulates:

*The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.*<sup>711</sup>

Interpreted together, these two critical clauses of the Convention lead to the postulation that the Convention is not fully binding as contracting states can refuse to honour arbitration

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<sup>709</sup>Shoult above n 190, at 111.

<sup>710</sup> ICSID Convention above n 481.

<sup>711</sup> Ibid.

clauses or arbitration agreements on the grounds that they are in contravention of the national values and sovereignty irrespective of whether such agreements fall within the provisions of Article 24(5) of the Convention.<sup>712</sup> After all, “*the mere fact of its ratification*” is not enough to warrant arbitration unless “*the parties to the dispute consent in writing to submit to the Centre*”.<sup>713</sup> For instance, though the KSA fully subscribes to the Convention’s jurisdiction in matters other than those covered by Article 25(4) and as elaborated by various KSA commercial laws, government agencies are not permitted to seek arbitration unless they obtain express permission to do so from the Saudi Council of Ministers courtesy of the provisions of Article 1 of the Arbitration Law which succinctly stipulates that:

*Government bodies may not resort to arbitration for the settlement of their disputes with third parties except after approval of the President of the Council of Ministers. This provision may be amended by a Resolution of the Council of Ministers.*<sup>714</sup>

Another phenomenal shortcoming that attests to the above postulation that the Convention “is not an explicit authority to arbitration but an implied one” is the conspicuous silence in delineating the modalities of submitting consent for arbitration whether during contract signing or even after a dispute arises.<sup>715</sup> Perhaps the drafters of the Convention wanted to test the goodwill of the contracting states in enforcing arbitration obligations within their jurisdictions. In this regard, and bearing in mind the provisions of the Preamble to the Convention, there has been significant uncertainty about whether the mere ratification of the Convention automatically binds host states to arbitration procedures except in situations where the disputes involved are covered

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<sup>712</sup> Ibid.

<sup>713</sup> Ibid.

<sup>714</sup> Law of Arbitration above n 322, art 1.

<sup>715</sup> Shoult above n 190, at 111.

by the provisions of Article 25(4) of the Convention.<sup>716</sup> This uncertainty has resulted in a number of “mitigation” measures. For instance, it has been a “normal” practice among actors to justify consent if the parties to an investment contract exchanged letters justifying such, included arbitration clauses during the signing of a contract, or even agreement to pursue arbitration when a dispute arises.<sup>717</sup> Again, it is also expected that as part of the ratification process and the subsequent inclusion of the Convention in the domestic legal frameworks, contracting states are expected to legislate laws that explicitly specify the process of expressing consent.<sup>718</sup>

### ***7.5 KSA Arbitration Laws from a Global Perspective***

It is noteworthy that the KSA is currently a signatory to several global institutions for trade regulation, especially the IIAs. The fact that the KSA has entered into both bilateral and multilaterals between Gulf States and western countries including the US is indicative of the country’s commitment to joining the international community and to abide by the international trade protocols imposed on firms trading in the global market.<sup>719</sup> The fact that the KSA has increasingly embraced trade relations with other nations and is currently trading with numerous international markets is aptly indicative that this progressive Arab nation is striving to attain the highest possible level of globalisation. In the words of Held and colleagues, “globalisation is the widening, deepening and speeding up of worldwide interconnectedness’.<sup>720</sup> As noted previously, the KSA ratified the ICSID back in 1980 meaning that it relinquished its authority to handle

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<sup>716</sup> ICSID Convention. above n 481.

<sup>717</sup> Shoult above n 190, at 111.

<sup>718</sup> Ibid.

<sup>719</sup> Ibid, at 110.

<sup>720</sup> David Held and Anthony McLew and David Goldblatt and Jonathan Perraton, *Global Transformations: Politics, economics and culture*. (Stanford: Stanford University Press, 1999), at 2.

investment disputes particularly those involving foreigners and state agencies.<sup>721</sup> The KSA is a member of the Gulf Cooperation Council as well as an observer of the Energy Charter Treaty.<sup>722</sup>

Further, as pointed out by Siwek and Sumberova, the proper understanding of globalisation should not only be predominantly “as an objective process with a different implication for the objective reality where globalisation is taken only as a “change in the spatial organization of social, economic, political and cultural life”.<sup>723</sup> Rather, it should also be conceptualized from the subjective dimension, a dimension “that concentrates either on what people think about globalisation or on how people become conscious of the world as a whole and with what implications or how is the world-as-a-whole represented in people’s minds?”<sup>724</sup> From this subjective perspective of globalisation, then, it is clear that the government and the people of Saudi Arabia are accommodating and willing to adopt globalised trade. Such willingness is demonstrated by their concession to and ratification of international trade institutions as well as internationally standardized trade protocols.

For instance, besides being party to several IIAs, the Kingdom of Saudi Arabia is signatory to several bilateral agreements. One of these organizations is the OPIC. OPIC is a regional arbitration treaty that allows for arbitration of investment disputes arising between Saudi government or its agencies and the American investors.<sup>725</sup> It is remarkable that while much of the Arab world harbours anti-American sentiments and refuses to enter into any form of agreement with America, the KSA has forged a bilateral agreement with the US to facilitate mutual trade

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<sup>721</sup> Ahdab above n 331, at 605.

<sup>722</sup> Norton Rose above n 149.

<sup>723</sup> Tadeusz Siwek and Monika Sumberova. “Why Beyond Globalisation?” In *Beyond Globalisation: Exploring the Limits of Globalisation in the Regional Context* (Conference Proceedings), 5-8. Ostrava: University of Ostrava Czech Republic, 2010, at 2.

<sup>724</sup> Ibid.

<sup>725</sup> Shoult above n 190, at 110.

between the two. Evidence of this is a change in the socio-political consciousness of the Saudi administration, one necessitated by the need to participate in international trade. Dang Anh and Simon Marginson contend that “globalisation means that people’s imaginations are not confined by their local cultural or national territorial boundaries”.<sup>726</sup> It is thus clear that the policies and political trends of the KSA are no longer limited by their own regional and national sentiments, but have embraced the need to co-exist with the most powerful trading nations in the globe, and with whose patronage the goal of being an investment hub can be achieved.

Further, it is evident that the KSA seeks to strengthen its local institutions and investment environment by embracing international standards in, for example, arbitration. By accepting that foreign investors can seek international restitution in dispute resolution, the KSA has enabled that what might be perceived as a local weakness (Sharia-based legal systems) is adequately strengthened for a global investment community. Dang Anh and Simon Marginson argue that “the principal implications of globalisation for social theory are the relativisation of the national and local by the global, the growing importance of the global dimension of activity in its own right, and the flourishing of convergent cross-border subjectivities”. Globalisation detonates all generic theorizations that are premised on a bounded nation state or exclude external relations from the domain of subjectivity”.<sup>727</sup> The KSA’s ratification of international protocols to complement its local institutions and mechanisms is indeed a sign of the “flourishing of convergent cross-border subjectivities”.<sup>728</sup> It is thus arguable that the Kingdom’s entry into

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<sup>726</sup> Dang Anh and Simon Marginson, Vygotskian socio-cultural theory and globalisation: Implications for educational research. *Working Paper*, Paper code: 1737. University of Melbourne, at 3.

<sup>727</sup> Anh and Marginson above n 726.

<sup>728</sup> Ibid.

bilateral and multilateral agreements was meant to mitigate some of the drawbacks that come with uncontrolled international investment and globalisation.

As quoted previously, King Abdullah addressed and emphasized in the 2008 G-20 summit the KSA's great need for "international coordination and cooperation to find appropriate solutions to the crisis and its effects. This crisis (2008 credit crisis) revealed that undisciplined globalisation and inadequate control of the financial sectors contributed to its rapid spread around the globe".

The realization that KSA cannot survive as an island nation, and the fact that the more it interconnects itself with the globe, the more it will be affected by other states, is a step towards a globalised Saudi economy. King Abdullah's speech makes it clear that Saudi has a role to play in the international community and that it is now a part of an increasingly connected world. This is in agreement with Appadurai who argues that "globalisation is manifest in 'a complex, overlapping, and disjunctive order', not a linear process (since) it is characterized by fundamental disjuncture between global flows in the realms of economy, culture, technologies and politics".<sup>729</sup> While the KSA's increased globalisation has several negative implications including the loss of a significant part of its sovereign independence, it is viewed as largely advantageous to the Saudi society. For instance, Agne argues that "globalisation enables a nation to build on its democracy by having its governance a subject of peer review by other trading

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<sup>729</sup> Arjun Appadurai, *Modernity at Large: Cultural dimensions of globalisation*. (Minneapolis: University of Minnesota Press, 1999), at 32.

partners”, where democracy is deemed as the masses’ “political practice the concepts of being affected and being able to participate” in decision making processes of the state.<sup>730</sup>

It can therefore be argued that a government that commits to globalisation is progressively democratic, legitimate and anchored in a transparent proper governance practice. Indeed, in addition to the IIAs, the King Abdullah era has been characterized by what Al-Dabbagh termed as appropriate developmental and reform steps initiated by the custodian of the Two Holy Mosques. Al-Dabbagh opined that “... a number of developmental steps and reforms took place in the Kingdom of Saudi Arabia in 2010 leading to the improvement of the Kingdom in a report of Doing Business, ranking the Kingdom as the first one at Arab level and the 11th at the global level”.<sup>731</sup> According to Al-Dabbagh, these efforts have culminated in positioning the Kingdom in a prime position. He stated that “the Kingdom comes on the list of the top five countries in the world that have carried out economic reforms over the past five years.”<sup>732</sup>

Whenever investors can see such national commitment, commitment to proper governance, to transparent political agenda, to progressive economic policy implementation and to the willingness of adopting international standards and practices, foreign investment inflows increase. Such has been the success story of the KSA. As outlined in the previous chapters, foreign direct investments in the Kingdom have grown in leaps and bounds in all the investment sectors open to foreign investment.<sup>733</sup> Therefore, it comes as no surprise that in 2010, the Kingdom of Saudi Arabia realised its main economic goal. According to the *United Nations*

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<sup>730</sup> Hans Agne, A Dogma of Democratic Theory and Globalisation: Why Politics Need not Include Everyone it Affects, *European Consortium for Political Research* 12, no. 3, at 433.

<sup>731</sup> SAGIA governor above n 531.

<sup>732</sup> Ibid.

<sup>733</sup> Arabia: Business Indicators above n 575.

*Conference for Trade and Investment (UNCTAD) 2010* report, the Kingdom of Saudi Arabia (KSA) still received the most FDI inflows in 2010, which amounted to \$28 billion US Dollars. Egypt came second with \$6 billion, and Qatar third with \$5.5 billion US Dollars. Lebanon, for its part, maintained fourth place, albeit with a slight increase from \$4.8 billion in 2009 to \$5 billion in 2010, while the United Arab Emirates (UAE) was ranked fifth with \$4 billion approximately. Acting on the need to increase the number of foreign direct investments in the Kingdom as part of the envisaged 10x10 goal, the Saudi government increased the number of investment activities in which foreigners could be involved.<sup>734</sup> For instance, it has allowed internationally-owned companies to explore downstream gas sites in addition to engaging in a wide range of activities in the petrochemicals sector.<sup>735</sup> Other sectors opened to foreign investment include: insurance, mobile telecommunication, education, and pipeline services.<sup>736</sup>

In addition, the KSA government has also tried to encourage foreign companies already doing business in the Kingdom to expand their activities to encompass these newly-opened investment opportunities as well as the existing ones.<sup>737</sup> This expansion of investment opportunities for foreigners can be interpreted as an indirect measure of blurring the lines between the different classes of investors in the KSA (Saudis and non-Saudis). The creation of the International Centre for Settlement of Investment Disputes (ICSID) in 1996 set up a forum that would ensure that disputes involving foreign investors are handled effectively, which has been successful to date.<sup>738</sup> Essentially, these legislations, Royal Decrees and agreements, as well as their accompanying implementing rules, have directly impacted on making the KSA a

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<sup>734</sup> SAGIA above n 146.

<sup>735</sup> Saudi Arabia Investment Guide above n 85.

<sup>736</sup> Ibid.

<sup>737</sup> Ibid.

<sup>738</sup> Investment, ICSID above n 169.



relatively friendly destination for foreign direct investments (FDI). In fact, they demonstrate the Saudi government's commitment to opening up new investment opportunities that initially were considered unfeasible due to inherent risks or even the lack of technical know-how. Most importantly, the laws underscore the Saudi government's commitment to reducing the list of investment activities not allowed to foreign investors as well as wholly or partly relinquishing some of the state-run corporations to private investors.<sup>739</sup> Consequently, it can be affirmed that it is these regulations that have contributed to placing the KSA among the top rated places to do business, at position 13 overall, out of the 181 countries studied by World Bank in 2009.<sup>740</sup>

All these improvements represent the multifaceted approaches that the KSA is taking towards globalisation - multifaceted because globalisation itself incorporates very many and expansive factors. As argued by Bohman, "the social fact of globalisation proves exemplary because ... globalisation is by definition a fact that can be experienced from many different perspectives and as such can best be understood in a multiperspectival practical inquiry into the framework of decision-making and problem-solving". Similar convictions were also published by Bunch (1990), Ackerly (2000) and Bohman (2002).<sup>741</sup> The KSA's progress in internationalizing its policies, practices and legal frameworks is perhaps the single most successful attainment of an Arab state.<sup>742</sup>

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<sup>739</sup> Legal considerations above n 170.

<sup>740</sup> Ibid.

<sup>741</sup> Brooke Ackerly, *"Political Theory and Feminist Social Criticism"* (Cambridge: Cambridge University Press, 2000); Charlotte Bunch, "Women's Rights as Human Rights: Towards a Revision of Human Rights." *Human Rights Quarterly* 12, no. 4 (1990), at 486 – 498; James Bohman, "Critical Theory as Practical Knowledge". In Paul Roth and Stephen Turner (eds), *Blackwell Companion to the Philosophy of the Social Sciences*, at 91–109 (London: Blackwell, 2002).

<sup>742</sup> Ibid.

However, the problem is that the steady growth of investment activities between investors and nation states has resulted in numerous disputes. The International Centre for Settlement of Investment Disputes (ICSID) is a body that seeks to mitigate the issues caused by such investment disputes. Litigations in Saudi Arabia, just as in many other jurisdictions, may take a long time, consume a lot of money, and usually it is very difficult to predict their outcomes.<sup>743</sup> Investments involving nationals and/or agencies from different countries are complex. The scenario may be even more complicated if such disputes involve multi-jurisdictional investment disputes or high value investments involving private individuals and state agencies.<sup>744</sup> It should be noted that the Kingdom is fully committed to partnering with the internal arbitration bodies in resolving investment disputes arising between foreign investors and government agencies.

This problem is compounded by the fact that, under the Sharia laws, the Saudi courts are not obliged to approve monetary gains to parties claiming loss of future profits. Neither can the courts give consent for the payment of interest on overdue amounts.<sup>745</sup> These are fairly strong impediments that threaten the smooth running of inter-jurisdictional business activities in Saudi Arabia. Investment arbitration in Saudi Arabia is governed by a range of commercial legislations drafted in accordance with the ICSID Convention regulations.<sup>746</sup> These impediments mark the areas in which the KSA has not yet been globalised.<sup>747</sup>

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<sup>743</sup> Shoult above n 190, at 104.

<sup>744</sup> Ibid, at 103-104.

<sup>745</sup> Ibid.

<sup>746</sup> Baamir and Bantekas above n 343, at 245-246.

<sup>747</sup> Cynthia Stohl, "Globalisation theory." In S. May and D. Mumby, Eds., *Engaging organizational communication theory and research: Multiple Perspectives*, at 223 - 262. (Thousand Oaks, CA: Sage, 2005).

## 7.6 Conclusion

Arbitration in the KSA has come a long way. However, meaningful arbitration can be said to have gained ground after the country ratified the ICSID convention and the subsequent domestic investment and arbitration legislations. However, since its ratification of the ICSID Convention, the KSA has submitted only one case under the Convention, which was concluded following an application for the claimant to withdraw the case. This should not be seen as a sign of lack of utilisation of the ICSID arbitration provisions; rather, it should be seen as a sign of goodwill on the part of the KSA to settle investment disputes amicably at an early stage as provided for by Article 26 of the Foreign Investment Law Implementing Rules.<sup>748</sup> Prince Saud Al-Faisal supported such an approach in his speech to the European Policy Centre Brussels, Belgium on February 19, 2004 when commenting on efforts made by the Saudi government to streamline its investment climate. He said:

*Our reform efforts, though implemented gradually, are cumulative in effect. Gradual change may seem slow or less impressive to some, but if reforms are to endure and be effective, they have to respond to the will of the people and maintain the unity of the nation.*<sup>749</sup>

Conclusively, both the ICSID and the KSA domestic investment legislations provide room for mutual agreement between disputing parties before matters are brought to the attention of the arbitral tribunals. In any case, the low number of cases brought to the attention of the ICSID is an indication that the KSA government, agencies, and nationals, as well as foreign

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<sup>748</sup> Foreign Investment Law above n 91 art 26.

<sup>749</sup> Ibid, at 3.

investors in the KSA have embraced the principles of mutual dispute resolution measures. The withdrawal of the only case ever presented to the ICSID only proves this fact.

## **Chapter 8: Sovereignty and Protection of Foreign Investments in Saudi Arabia**

### ***8.1 Overview***

As noted in the previous chapters, according to the provisions of Article 25(4) of the International Centre for Settlement of Investment Disputes (ICSID) and the Royal Decree No. M/8 Dated: 22/3/1394H, all investment disputes in the KSA are handled within the ICSID framework, with the exception of oil disputes.<sup>750</sup> This chapter attempts to explain how oil investments are protected and how oil disputes are settled within the KSA's legal framework. The chapter seeks to answer the following three questions: How can non-Saudis protect their oil investments? Can they seek arbitration? Do the KSA's domestic laws allow arbitration for disputes arising from oil investments? In doing so, the chapter will consider the essentially sensitive issue of sovereignty and protection of foreign investments in the KSA. This will be addressed within the context of the interplay between international public law and the KSA legal frameworks governing oil investment disputes, that is, Arbitration Law, Foreign Investment Law, Foreign Capital Investment Law, and the Mining Law. Areas to be tackled include: protection given to foreign investors, the notion of sovereignty, arbitration subject-matters, composition of arbitral tribunals, arbitration procedures, and the enforceability of arbitral awards.

### ***8.2. Introduction***

The rights and interests of foreign investors in the KSA and in all other host states are protected by various legal frameworks under the umbrella of the International Investment Agreements (IIAs).<sup>751</sup> These IIAs ensure that host nations will accord substantial protection

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<sup>750</sup> ICSID above n 481; Royal Decree No above n 428.

<sup>751</sup> Newcombe and Paradell above n 416, at 1.

against legal and financial exploitation by domestic legal frameworks by providing mutual rewarding “investor/state” arbitration infrastructures that empower the foreign investor to demand the inclusion of arbitration clauses prior to the signing of investment contracts with host nation entities.<sup>752</sup> Arguably, these disputes have produced a great deal of legal jurisprudence as authorities attempt to mitigate the effects of such disputes. Today, the arbitration jurisprudence has developed considerably in order to accommodate a wide range of investment disputes that initially were considered the preserve of domestic legal frameworks. Some of the most notable of these IIAs are ICSID, Multilateral Investment Guarantee Agency (MIGA), Overseas Private Investment Corporation (OPIC), United Nations Commission on International Trade Law (UNCITRAL), New York Arbitration Convention, as well as a combination of bilateral agreements between trade partners.<sup>753</sup> Even so, the jurisdiction of these IIAs is limited to the extent that they do not encroach on national sovereignty and stability.<sup>754</sup> It is therefore not a surprise that the majority of them contain provisions which still grant the contracting states the power to choose which investment disputes should be handled by the IIAs and which should be left to the preserve of the domestic courts.<sup>755</sup>

### ***8.3 Sharia and Sovereignty***

Sovereignty in a political context means exerting authority and/or leadership on a group of people living within a clearly defined geographical region, in this case, a nation state, kingdom or a territory.<sup>756</sup> To this end, it should be noted that nation states, kingdoms, or

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<sup>752</sup> Ibid, at 30.

<sup>753</sup> Ibid, at 23-30.

<sup>754</sup> Ibid, at 26.

<sup>755</sup> Ibid, at 25-30.

<sup>756</sup> B. Conforti, (2005). *The Law and Practice of the United Nations*, (3<sup>rd</sup> ed.). (Leiden: Martinus Nijhoff Publishers), at 25.

territories can exert their authority and/or leadership only if they are independent, that is, they are free from any external rule. Therefore, every independent state, kingdom or territory strives to uphold and protect its sovereignty to the greatest extent possible perhaps due to the accompanying, inherent benefits. The main reasons for defending the national sovereignty are many and obvious. They may include, but are not limited to, the following: protection of the national resources, the cultural and religious values, as well as to protect the people, and the national political ideologies. In most instances, nation states achieve these ends by establishing laws and/or declarations and enshrining them in the constitutions.<sup>757</sup>

### **8.3.1 Meaning and Nature of Sovereignty in Sharia Law**

The sense of national sovereignty in Saudi Arabia, a state that strictly follows the Islamic Sharia doctrines, is guarded by the Book of God, the national constitution and a range of secular legislations and Royal Decrees. This is in line with Surah 67 (Al-Mulk) of the Book of God which stresses the importance of upholding God's will (sovereignty) by protecting the sanctity of His creation, upholding His teachings and promises, protecting mankind and all the holy sites, as well as protecting the sanctity of natural wealth. For instance, Verses 1-7 Surah 67(Al-Mulk) stipulate that:<sup>758</sup>

- 1. Blessed is He in Whose Hand is the dominion, and He is Able to do all things.*
- 2. Who has created death and life, that He may test you which of you is best in deed. And He is the All-Mighty, the Oft-Forgiving;*

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<sup>757</sup> *United Nations Charter art 4*, Benedetto Conforti, *The Law and Practice of the United Nations*, 3rd ed. (Leiden: Martinus Nijhoff Publishers, 2005), at 25.

<sup>758</sup> Holy Qur'an, Verse 1-7 Surah 67 (Al-Mulk).

*3. Who has created the seven heavens one above another, you can see no fault in the creations of the Most Beneficent. Then look again: "Can you see any rifts?"*

*4. Then look again and yet again, your sight will return to you in a state of humiliation and worn out.*

*5. And indeed We have adorned the nearest heaven with lamps and We have made such lamps (as) missiles to drive away the Shayâtin (devils), and have prepared for them the torment of the blazing Fire.*

*6. And for those who disbelieve in their Lord (Allah) is the torment of Hell, and worst indeed is that destination.*

*7. When they are cast therein, they will hear the (terrible) drawing in of its breath as it blazes forth.*

In interpretation, these verses emphasize the importance of acknowledging and giving respect to God in His capacity as the creator of heaven and earth. Most importantly, these verses clearly stipulate the nature of punishments that mankind stand to face in the event that they do not uphold and protect the sacred sovereignty of individuals as manifested in God's creation. For instance, Verse 1 emphasizes the importance and the level of control and/or authority that God wields over his creation.<sup>759</sup> On the other hand, Verses 2 and 3 emphasize the sanctity of God's creation and His capacity to leverage this creation through forgiveness of sins and putting to task the creation in order to test its ability to protect and uphold the sanctity of His entire creation.<sup>760</sup>

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<sup>759</sup> Holy Qur'an, Verse 1 Surah 67 (Al-Mulk).

<sup>760</sup> Holy Qur'an, Verse 2 and 3 Surah 67 (Al-Mulk).



In addition, Verses 4 and 5 caution against those who may be tempted to disregard or fail to uphold the sanctity that accompanies God's creation. Verse 4 categorically provides that any attempt to perceive God's creation as incomplete will be met with dire consequences.<sup>761</sup> On the other hand, Verses 5, 6 and 7 exhort God's creation to take severe measures to condemn those who are not committed to upholding the sanctity of God's creation to eternal fire.<sup>762</sup> On analysis, these seven verses in addition to others in Surah 67 (Al-Mulk) indicate that any act of disobedience toward Allah is akin to compromising the sense of sovereignty espoused by the Holy Qur'an as well as the national constitutions.

The whole of Surah 67 (Al-Mulk) stipulates the importance of sovereignty among God's creation. No doubt this is sovereignty with a deeper and more important meaning compared to the mere exertion of authority over a people living within a clearly-defined geographical region. This is sovereignty that is vested in the values of family life and manifested in the great yearning for eternal life.

As explained earlier in this chapter, long before Saudi Arabia promulgated the current constitutional dispensation, it relied entirely on the Book of God for guidance in matters of governance and administration of justice. However, acting on the need to create a universal code whose provisions can easily be understood and respected by both Muslims and non-Muslims, the Basic Law was promulgated. Even so, the Basic Law is a complete reflection of the Holy Qur'an and the Sunnah. Hence, it is arguable that the Saudi national constitution upholds both the national and the religious principles of sovereignty (Islamic Sharia), especially since the Kingdom is home to the Two Most Holy Mosques of Mecca and Medina.

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<sup>761</sup> Holy Qur'an, Verse 4 Surah 67 (Al-Mulk).

<sup>762</sup> Holy Qur'an, Verse 5, 6, and 7 Surah 67 (Al-Mulk).

### 8.3.2 Protection of Foreign Investors

The protection of foreign investors in the KSA is guaranteed by the Book of God, Sunnah, Basic Law, as well as a number of secular codes that have been enacted over the years. Pursuant to Article 48 of the Basic Law, the protection accorded to foreign investors stems from the Sharia law. This is because Sharia law is the supreme law of the land and cases brought to the Saudi courts are handled within the provisions of this law. More specifically, this article (48) stipulates that:

*The courts shall apply to cases before them the provisions of Islamic Sharia, as indicated by the Qur'an and the Sunnah, and whatever laws not in conflict with the Qur'an and the Sunnah which the authorities may promulgate.*<sup>763</sup>

This article can be interpreted as allowing for the application of secular investment codes such as the Foreign Investment Law, Real Estate Regulation, Capital Markets Regulation, and Arbitration Law as well as bilateral and multilateral agreements that the Kingdom has since ratified when determining the nature of protection privileges to accord foreign investors. In addition, it is imperative to note that the Islamic Sharia law is created on a non-discriminatory platform. It does not discriminate against Muslims and non-Muslims or even between foreigners and Saudis. This protection is accorded to foreign-owned investments as well as to personal property. For instance, apart from acquiring land to develop the licensed projects, foreign investors are also given the opportunity to acquire land for housing their staff.<sup>764</sup> Therefore,

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<sup>763</sup> Saudi Basic Law, n 39 art 48.

<sup>764</sup> Foreign Investment Law, above n 91 art 8.

foreign investors in the Kingdom are guaranteed protection, at least to the extent permitted by the existing (if any) mutual agreements between their countries and the KSA. This is in line with King Abdullah's assertions during the 2008 G-20 meeting. In reference to international investment cooperation, the King stated:

*We must work together to continue efforts aimed at the liberalization of trade and investment, which in recent decades has helped to improve living standards and raise millions out of poverty.*

This official statement indicates that the Kingdom is committed to working closely with countries that value the spirit of mutual cooperation. In fact, these protection privileges are necessary as they help increase the number of direct foreign investments in the Kingdom. To this end, the Saudi government provides the following privileges as part of its strategic measures aimed at encouraging more foreign direct investments into the Kingdom. Pursuant to Article 1 of the Saudi Arbitration Law, foreign investors are free to seek an alternative dispute resolution mechanism in the event that a dispute occurs. This article gives a wide leeway to parties establishing an investment contract as it accords them an opportunity to include an arbitration clause prior to the signing of the contract, and to resolve a dispute by arbitration even when there is no arbitration clause in the contract.<sup>765</sup> In addition, foreign investors are assured of their protection by Article 13 of the Foreign Investment Law as well as Article 26 of the corresponding Implementing Rules.<sup>766</sup>

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<sup>765</sup> Law of Arbitration above n 322.

<sup>766</sup> Foreign Investment Law above n 91 art 13, at 26.

<sup>765</sup> Foreign Minister Remarks (March 9, 2011). Available at; [http://www.saudiembassy.net/latest\\_news/news03091101.aspx/](http://www.saudiembassy.net/latest_news/news03091101.aspx/)

On the other hand, it is arguable that the notion of sovereignty may negatively affect investment activities in the Kingdom in the coming days and months. What are considered by the KSA to be purely sovereign matters can be observed from the Saudi government's reaction to the ongoing civil unrest in the MENA region. The Kingdom's leadership has strongly drawn the line between what are purely internal matters and matters that allow foreign input. Some of these reactions can be perceived as threats to foreign investments as they explicitly underscore the notion of sovereignty. For instance, recently the Saudi Foreign Minister, Prince Saud Al-Faisal, held a press conference where he cautioned against foreign involvement in internal matters other than those touching on investments. He said that

*(...) the Kingdom's laws and regulations are based on Sharia (Islamic law) and are meant to ensure the country's security, stability and integrity.*<sup>767</sup>

Clearly, and in the face of the growing civil strife in the MENA region, this announcement may deter potential investors who may feel that both their welfare and their investments are not guaranteed under the Islamic law, particularly if they are not Muslims or if they come from nations that do not have existing mutual trade agreements with Saudi Arabia.

#### ***8.4. Sovereignty over Natural Resources***

The issue of state sovereignty vis-à-vis the exploration and exploitation of oil, gas and other valuable minerals has over the years produced considerable debate among the industry players. Specifically, among the developing nations where many such minerals are located, there have been many activities and debates concerning the legal and administrative protection

accorded to foreign multinational companies representing developed nations.<sup>768</sup> Vielleville and Vasani argue that three core factors have influenced this lucrative yet sensitive realm of international trade.<sup>769</sup> They assert that the creation of a strong union of nations has fostered a nascent environment that gives developing nations space to assert themselves in the global economic arena.<sup>770</sup> They also opine that the demise of colonialism has played a critical role insofar as the expansion of the international community is concerned.<sup>771</sup> Lastly, they believe that the skyrocketing of the prices of primary resources such as “oil, gas, and other minerals led to an uneasy interdependence between foreign investors and host States,”<sup>772</sup> has played a very important role in revitalizing the economic capabilities of many developing countries and, most importantly, the tilting of the global balance of power.

Initially, the multinationals caught the developing countries totally unprepared in terms of the capital required to exploit these immense deposits of valuable minerals. Hence, they succeeded in forcing the developing nations into signing lengthy and “hard-to-reverse” concessions some of which extended to sixty years. As expected, the prime share of such concessions went to multinationals with the developing nations getting very little of their own wealth. This situation led to the build-up of tension which reached its peak in the mid-20<sup>th</sup> century. The developing nations complained that such concessions were not only exploitative but were also an abuse of their national pride and sovereignty and hence there was an urgent need for them to be renegotiated or even terminated depending on the “mood” of the government of the

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<sup>768</sup> D.E. Vielleville and B.S Vasani, (2008). Sovereignty over natural resources versus rights under investment contracts: which one prevails? *Transnational Dispute Management*, Vol. 5, No. 2, at 1.

<sup>769</sup> Ibid.

<sup>770</sup> Ibid.

<sup>771</sup> Ibid.

<sup>772</sup> Ibid.

day. For instance, in the Middle East where the large oil companies can be found, host nations invoked their domestic law in trying to legalize such nationalization practices, with some states arguing that their domestic law considered concessions as “administrative contracts” and therefore subject to regular administrative changes.<sup>773</sup> The ARAMCO case explained in the previous chapters illustrates this fact. In this particular case, the Saudi government argued that it could alter the terms and conditions pertaining to oil concessions at will, given that the Saudi law recognised them as administrative contracts.<sup>774</sup> However, such claims were dismissed by the arbitral tribunal on grounds that like any other private contract, oil concessions could not be altered by the host states without the consent of the other parties.<sup>775</sup> Consequently, there were numerous cases of nationalization of large oil industries controlled by overseas entities.

Recently, there has been a growing wave of “statization”<sup>776</sup> whereby host countries opt to use “unethical” means to force multinational companies running the oil industry to cede some ownership of such industries.<sup>777</sup> A notable case is that of Venezuela where the government announced its desire to take over more than thirty privately-owned oil fields.<sup>778</sup> Such radical measures have resulted in a series of litigations/arbitrations where the estranged private companies perceive such radical measures as uncalled-for, while the host countries reason that the oil industry constitutes a great chunk of their national identity and sovereignty. The majority of these litigations have been taken to the ICSID for arbitration. They include: Exxon Mobil

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<sup>773</sup> Ibid, at 9.

<sup>774</sup> Ibid., at 9-10.

<sup>775</sup> Ibid.

<sup>776</sup> Statization differs from nationalization in that, it entails the gaining of full and direct control of some specific enterprises by the host nation while on the other hand nationalization entails the process of gaining the control over an entire industry by the host nation. Vielleville and Vasani above n 766.

<sup>777</sup> Vielleville and Vasani above n 766.

<sup>778</sup> Ibid.

Corporation filed a case in 2007 following the country's takeover of Cerro Negro, an up-grader company it was running at the time; Tidewater Inc. also filed a case worth \$45 million in 2009, Universal; Compression International Holdings filed a case in 2009 seeking over \$400 million in compensations; and OPIC Karimum filed a case in June 2010, among others.<sup>779</sup>

The United Nations has played a key role in ensuring that these trends are closely monitored within the provisions of the law. It has achieved this through a series of resolutions that seek to recognise the sovereignty as well as the principles of good faith as the two key legal hurdles that must be mutually dealt with in international investment engagements.<sup>780</sup> The first in this series was *Resolution No. 626 (VII) of December 21, 1952* that acknowledged the right of a people to sovereignty and exploitation of their own natural resources. *Resolution No. 1803 (XVII) of December 14, 1962* affirmed nationalization as a necessary measure but could only be carried out “for public purposes, security or national interest” and most importantly, the private investors would be entitled to “appropriate compensation” according to both the domestic and international law provisions.<sup>781</sup> *Resolution No. 3201 (S-VI) of May 1, 1974* Article 4(e) gave states the authority to nationalize their resources without any undue pressure to achieve this as long all the parties concerned were fully consulted.<sup>782</sup>

*Resolution No. 3201* was supplemented by *Resolution No. 3281 (XXIX) of July 26, 1974* that ensured the host nations acted within the provisions of good faith when carrying out

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<sup>779</sup> FACTBOX-Arbitration cases against Venezuela nationalizations, July 2010, <<http://www.reuters.com/article/idUSN0222521320100702/>>

<sup>780</sup> Vielleville and Vasani above n 766.

<sup>781</sup> Ibid, at 4.

<sup>782</sup> G.A. Res. 3201, 6th Special Session, GAOR, Supp. (No. 1), U.N. Doc. A/9559 (1974).

nationalization activities.<sup>783</sup> This resolution, together with others that preceded and followed it, sought to legalize nationalization processes on the basis of national sovereignty;<sup>784</sup> however, they enforced the requirement that private entities should be fully compensated.<sup>785</sup> By extension, the provisions of this regulation are also enforceable today given that host states are expected to accord foreign investors together with their investments “minimum standards of protection” as espoused in the principle of good faith to which most domestic laws are expected to conform.<sup>786</sup> In the KSA, the Foreign Investment Law grants foreigners immunity from mistreatment in the event that they want to dispose of their assets, wind up the investment, repatriate profits from such investments, or even settle contractual obligations.<sup>787</sup>

As per these resolutions, that is, 626 (VII), 1803 (XVII), 3201(S-VI), and 3281(XXIX), it is apparent that nations with mineral wealth should not be coerced into ceding some of their sovereign rights regarding the exploration and mining of such wealth. In this regard, nationalization is a positive step towards such sovereignty and economic independence; however, host states should not take advantage of this to mistreat foreign investors who have already sunk huge amounts of their money into the mineral industries. Here, the principle of good faith should apply.

### ***8.5 Sovereign Rights and Obligations over Natural Resources***

The end of the 20<sup>th</sup> century saw a shift in ideology where the already nationalized oil industries started being privatized courtesy of the sprouting bilateral and multilateral treaties

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<sup>783</sup> G.A. Res. 3281, 29 GAOR, Supp. (No. 31), UN Doc. A/9361 (1974).

<sup>784</sup> Vielleville and Vasani above n 766, at 4.

<sup>785</sup> Ibid, at 5.

<sup>786</sup> Ibid.

<sup>787</sup> Foreign Investment Law above n 91 art 7.



occasioned by the urge to create a friendly investment environment. Perhaps as a result of frustrations on the part of the developing nations due to dwindling profits from the bilateral and multilateral treaties created at the end of the 20<sup>th</sup> century, there has been a reversal of the trend witnessed in the mid 20<sup>th</sup> century.<sup>788</sup> Again, the plummeting oil prices occasioned by global market shocks and crises particularly in the Middle East led to significant reduction of oil revenue.<sup>789</sup> Needless to say, this scenario greatly dented states' overall spending amidst rapidly growing populations and demands for more consumer goods and services. Consequently, this trend occasioned the clamour for the revaluation of states' capability in running the lucrative industry. In mitigation, industry players and economists alike hypothesized that private entities would be the best positioned in managing the industry.<sup>790</sup>

In the KSA, the response to these ever-changing economic and industry-specific trends has been no different.<sup>791</sup> Following the call for privatization of key economic sectors, the KSA government instituted a number of administrative reforms aimed at liberalising the domestic economy, particularly in the oil industry. The Foreign Investment Law of 2000 is indeed a direct response to these changing economic ideologies regarding the oil industry.<sup>792</sup>

Essentially, this law sought to make the KSA a friendly investment destination for foreigners by granting a wide range of privileges which were initially unavailable to foreigners,<sup>793</sup> while still emphasizing the notion of sovereignty in the sense that the KSA

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<sup>788</sup> The developing nations started gaining some confidence with the bilateral and multilateral treaties, particularly on the premise that they were formed on the basis of the spirit of good faith and mutual obligations.

<sup>789</sup> There was a growing conviction that states were unable to competitively run some of the sensitive economy sectors due to lack of capital, political goodwill, and technical know-how.

<sup>790</sup> Vielleville and Vasani above n 766, at 2.

<sup>791</sup> Ibid, at 98.

<sup>792</sup> Ibid.

<sup>793</sup> Foreign Investment Law above n 91 art 6-11.

government reserves the right to vet, allow, monitor, or even expel foreigners who engage in unlawful practices.<sup>794</sup> For instance, the law allows foreigners to run fully-owned subsidiaries and branch offices in the KSA and to own real estate in areas away from the two cities of Medina and Makah;<sup>795</sup> on the other hand, foreigners are expected to institute an “accredited accounting system” and take practical steps to establish the licensed entity within the time frame indicated in the licence.<sup>796</sup> Again, as highlighted in Chapter 2, for the first time foreign investors were permitted to send the proceeds of their investments back to their home countries.

Things took an even better turn when the so-called “Negative List” was revised by the Supreme Economic Council in 2003. This revision opened up to foreign investment critical sectors of the economy such as education, telecommunication, insurance, and trade.<sup>797</sup> Notable projects launched following this liberalization include the ambitious gas project considered the greatest of its kind in the Kingdom as well as in the region once it is completed. The Kingdom has also embarked on a number of desalination projects aimed at increasing its overall energy production capacity to cater for the increasing domestic market. Moreover, there are a number of petrochemical projects that have been kick-started to tap into the immense oil resources in the Kingdom. No doubt, these are phenomenal changes given that initially they were reserved only for Saudis. All this has been made possible through the partnership between the Saudi government and its nationals on the one hand and foreign entities on the other.<sup>798</sup> Arguably, this

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<sup>794</sup> Ibid, art 2-5, 12.

<sup>795</sup> Ibid art 5.

<sup>796</sup> Ibid art 16-19.

<sup>797</sup> Shoult above n 190, at 98.

<sup>797</sup> G.A. Res. 3281, 29 GAOR, above n 781.

<sup>798</sup> Shoult above n 190, at 98.

is a sign of goodwill and commitment to the tenets of the UN *Resolution No. 3281 (XXIX)* on the part of the KSA government in providing “fair” investment terms to foreign investors.

### ***8.6 Arbitration from the KSA Legal Framework Perspective***

As outlined in the previous chapters, the ICSID Convention was specifically created to “*encourage private foreign investment in developing countries.*”<sup>799</sup> It would achieve this by facilitating “*conciliation and arbitration ... [infrastructures for solving] investment disputes between a contracting state and a national of another contracting state.*”<sup>800</sup> Even so, with this level of uncertainty, even the very humble objectives it espouses might not be realised all the time. Tellingly, the KSA’s legal framework does not provide a clear methodology for pursuing arbitration as recourse for investment dispute resolution in the event of an investment dispute involving a foreign investor. Both the Arbitration Law and its Implementing Rules conspicuously miss this critical aspect by failing to offer an explicit delineation on consenting to arbitration through the Convention.<sup>801</sup> As a matter of fact, the enforceability of an arbitration clause is cast into doubt by the requirement that the parties should deposit a duly signed arbitration instrument with the authority handling the arbitration detailing their names and most importantly, their consent to arbitration in the event that a dispute arises. It is this instrument that validates the arbitration.<sup>802</sup> In fact, as of 2009, the KSA has not submitted any case to the Convention for arbitration - a trend with both negative and positive connotations in regard to the KSA’s willingness to honour its obligations to the Convention.<sup>803</sup>

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<sup>799</sup> Ibid, at 111.

<sup>800</sup> Ibid.

<sup>801</sup> Ibid.

<sup>802</sup> Law of Arbitration above n 322.

<sup>803</sup> Shoult above n 190, at 111.

### ***8.7 Arbitration: KSA Domestic Laws versus International Arbitration Treaty Standards***

As noted previously, litigations in Saudi Arabia, as in many jurisdictions, can be time-consuming, expensive and uncertain in predicted outcomes.<sup>804</sup> The situation becomes more complex when such litigations involve nationals and/or agencies from other countries that do not practise Sharia law. As a matter of fact, the application of what Sayen (1987) refers to as “ancient legal rules” to some of the common commercial litigations involving complex procedures, poses real risks to the Kingdom’s quest to become the leading business hub in the Middle East given that potential investors usually weigh the future benefits against the expected risks of an investment environment before committing their monies to investment.<sup>805</sup>

Moreover, Sayen (1987) argues that although the judges who serve in the KSA Sharia courts and on governmental boards are qualified and impartial, their efficiency is greatly curtailed by the huge backlog of cases as the Saudi judicial system is still understaffed, under-equipped, and poorly managed.<sup>806</sup> In fact, there have been many complaints from foreign investors who feel that the system is still too young to handle complicated investment disputes.<sup>807</sup> Cases involving complex financing networks may pose real challenges to the domestic legal system particularly in matters relating to the security of goods, transactions, funds, and information in the age of information technology.<sup>808</sup>

These opinions are shared by senior government officials such as the former deputy minister for commerce and industry, Fawaz Al Alamy who said that there is a need to put in

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<sup>804</sup> Ibid, at 104.

<sup>805</sup> Sayen above n 313, at 211.

<sup>806</sup> Ibid.

<sup>807</sup> Ibid.

<sup>808</sup> Ibid.

place workable dispute resolution mechanisms so as to speed up investment activities. When giving his opinions on the existing dispute resolution mechanisms in the Kingdom, he said:

*(...) dispute resolution was cumbersome, local hiring requirements are burdensome, and the licensing process is time-consuming.*<sup>809</sup>”

To this end, the former deputy minister opined that the government should be more objective in its actions. He added:

*We also have to apply transparency, predictability and due process. All of these will attract FDI, and therefore we will have more jobs for newcomers.*<sup>810</sup>

In light of this information, there is no doubt that the credibility of the process of settling oil investment disputes in the KSA, and the Kingdom’s commitment to embracing the standards of good faith set by international law, particularly the international arbitration treaties, is brought into question.<sup>811</sup> Notwithstanding that most international arbitration treaties grant contracting states the freedom to choose which categories of investment disputes to submit to IIAs jurisdiction, the manner in which the KSA legal system functions raises many doubts in the minds of foreign investors, particularly those outside the GCC jurisdiction. Even so, based on Vielleville and Vasani (2008)’s argument that, “[t]he rights granted to foreign investors under domestic law are standalone protections guaranteed by the State to all foreign investors and do not require a special agreement in order for them to be valid,”<sup>812</sup> it can be opined that perhaps the

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<sup>809</sup>SAGIA (jan 31, 2011). Foreign investor bans in saudi to end ‘very soon’, says government advisor.

<<http://www.sagia.gov.sa/en/sagia/media-centre/news/foreign-investor-bans-in-saudi-to-end-very-soon-says-govt-advisor/>>

<sup>810</sup> Ibid.

<sup>811</sup> Vielleville and Vasani above n 764, at 8.

<sup>812</sup> Ibid, at 14.

implied minimum protection provided for by the raft of KSA commercial legislations is enforceable and therefore a valid alternative to international public law.

### ***8.8 Minimum Standards of Treatment***

In regards to the minimum protection accorded to investors within the KSA, the implementation rules of arbitration have done a commendable job, at least when compared to the 1983 Act<sup>813</sup> which “reduced the scope” of the KSA arbitration system by:

*Ignoring arbitration clauses ... or by regulating the field thereof in certain specific areas, such as the Commercial Agency Act, the Act on the relations between foreign companies and contractors and their Saudi sponsors and Commercial Companies Act.*<sup>814</sup>

Moreover, the arbitration system clearly differentiates between institutional and ad hoc arbitration procedures, national and international arbitration procedures, as well as the difference between arbitration procedures that are based on arbitration agreements and clauses.<sup>815</sup> For instance, under the national arbitration procedures covering oil investment disputes, a number of arbitration authorities exist.<sup>816</sup> They include: the labour courts, the Sharia Courts, the Commission for Financial Titles, the Board for Settlement of Commercial Disputes, as well as the Diwan Al-Mazelem.<sup>817</sup>

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<sup>813</sup> Ahdab above n 331.

<sup>814</sup> Ibid.

<sup>815</sup> Ibid.

<sup>816</sup> National arbitration entails disputes that are settled through by arbitral tribunals/committees within the KSA, - it is the opposite of international arbitration, which deals with matters that exceeds the legal mandate of the host state.

<sup>817</sup> Sayen above n 313, 594.

Irrespective of the authority handling a dispute, the central premise is that such authority must supervise and control all the stages and occurrences arising from the arbitration process.<sup>818</sup> In this regard, the authority must take into account all the details pertaining to such disputes as well as both parties' consent to taking their dispute to arbitration.<sup>819</sup> Even so, such authorities are not permitted to delve into the content of the dispute but only to oversee the implementation of the arbitration tools so as to ensure a smooth process.<sup>820</sup> The executive officer (secretary) of the authority handling arbitration acts as the chief administrative officer and interpreter of the rules and regulations of the Arbitration Act and its Implementing Rules.<sup>821</sup> For instance, in the event that parties fail to appoint the arbitrators, it is the duty of the authority secretary to appoint arbitrators if requested to do so by either party.<sup>822</sup>

This is pursuant to the provisions of Article 10 of the Arbitration Law which succinctly stipulates that:

*Where parties fail to appoint the arbitrators or one party abstains from appointing the arbitrator(s) who are to be chosen solely by him, or where one arbitrator or more refuses to work, or withdraws, or a contingency arises which prevents him from undertaking the arbitration or if he is dismissed and there is no special stipulation by the parties, the authority originally competent to hear the dispute shall appoint the arbitrator(s) as necessary, upon request of the party interested in expediting the arbitration, in the presence of the other party or in his absence, after being summoned to a session to be*

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<sup>818</sup> Implementation rules above n 308.

<sup>819</sup> Law of Arbitration above n 322, art 6.

<sup>820</sup> Implementation rules above n 308.

<sup>821</sup> Law of Arbitration above n 322, art 8.

<sup>822</sup> Ibid, art 10.

*held for this purpose. The number of arbitrators appointed shall be equal or complementary to the number agreed upon among the parties. The decision in this respect shall be final.*<sup>823</sup>

Again, the secretary to the authority ensures that the arbitration process takes place within the set time frame and considers deadline extension requests if there is reasonable evidence that such extension is warranted.<sup>824</sup> Upon the termination of the arbitration process, the authority is also expected to register awards granted thereof as well as prepare the ground for any appeal regarding such awards.<sup>825</sup> Moreover, the law is more strict on the misuse of the rights granted to the disputing parties by safeguarding against the malicious dismissal of an arbitrator appointed by either of the disputing parties or even appointed by the authority that has the immediate jurisdiction over the arbitration unless in situations where both the disputing parties agrees to this.<sup>826</sup>

As a sign of good will on the part of the KSA government to subscribe to the provisions of the international arbitration treaties, the law removed from the legislative authority the powers to grant state agencies permission to pursue arbitration, and granted them to the Council of Ministers.<sup>827</sup> Initially, these powers were vested only in the Saudi legislative authority. This law produced more flexibility and efficiency in the KSA arbitration system. This postulation is based

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<sup>823</sup> Ibid.

<sup>824</sup> Law of Arbitration above n 321, art 9.

<sup>825</sup> Law of Arbitration above n 322, art 18.

<sup>826</sup> Ibid, art 11.

<sup>827</sup> Ibid, art 3.



on the fact that getting the legislative authority to issue such permission may take a long time as opposed to a Council of Ministers which, through its President, can do so easily and quickly.<sup>828</sup>

## **8.9 Enforceability of Arbitral Awards**

In regard to the enforcement of the award rendered by the arbitral tribunal, it is stipulated in Article 19 of the Arbitration Law that the authority with jurisdiction to handle the dispute should allow enough room for any objection from either party.<sup>829</sup> In the event that no objection is forthcoming, the authority is obligated to ensure that the award does not violate any public policy.<sup>830</sup> To achieve this, the authority is mandated to review the award to ensure that its enforceability is not hindered by any hidden legal hurdle, although the regulations are silent on the extent of such review.<sup>831</sup> Even so, the regulations are unclear in regard to an appeal to a higher authority in the event that the authority overseeing the arbitration of a certain dispute dismisses objections from either of the parties regarding the enforceability of the rendered award.<sup>832</sup> Under normal circumstances, an arbitral award cannot be enforced if the overseeing authority is of the opinion that the arbitrators were not impartial, or if key arbitration procedures were not followed as provided for by the law. Perhaps this is one of the major unique features of the Saudi arbitration system vis-à-vis the state of things in other countries.<sup>833</sup>

Moreover, so as to ensure efficiency and impartiality during arbitration, the Arbitration Law stipulates that arbitrators chosen by the parties must be well versed in both Sharia law and

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<sup>828</sup> Ibid.

<sup>829</sup> Ibid.

<sup>830</sup> Ibid, art 20.

<sup>831</sup> Sayen above n 313, 221.

<sup>832</sup> Ibid.

<sup>833</sup> Ibid, at 222.

Saudi commercial laws.<sup>834</sup> To avoid bias, such arbitrators should also be male of Saudi nationality or to some extent experts professing Muslim faith.<sup>835</sup> Again, the numbers of such arbitrators must be odd; in this case they are usually three to ensure easy ruling and grant of arbitral award since it is determined by a majority vote.<sup>836</sup> Persons selected as arbitrators should be of high moral integrity and should not have committed or been found guilty of *hudoud* crimes at any time in their lives.<sup>837</sup> Most importantly, and as mentioned earlier, the process of arbitration is closely monitored by the competent authority with the original mandate to hear the dispute.<sup>838</sup> This ensures that no party digresses from the provisions, thereby improving the chances of the subsequent arbitral award being accepted upon the conclusion of the arbitration process.<sup>839</sup>

### **8.10 Conclusion**

The KSA commercial laws, particularly those dealing with arbitration of investment disputes, are silent on the settlement of oil disputes. Its exclusion from ICSID jurisdiction casts doubts as to whether disputes arising from it can be arbitrated, and if so, how. It is hoped that this chapter has provided a clear answer to this issue. In essence, oil disputes can of course be arbitrated not by international arbitration treaties, but by the KSA judicial system. The principle of sovereignty as provided by Article 25(4) of the ICSID and Royal Decree No., M/8 Dated: 22/3/1394 H disqualifies oil from being considered by ICSID. Again, based on the notion that the ICSID is meant to settle disputes between foreigners and entities from host states, oil disputes can be dealt with only by the KSA domestic law given that oil investments are a preserve of

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<sup>834</sup> Ibid, at 221.

<sup>835</sup> Norton Rose above n 149, at 5.

<sup>836</sup> Ibid.

<sup>837</sup> Ibid.

<sup>838</sup> Ibid.

<sup>839</sup> Sayen above n 313, at 220-221.

Saudi nationals and/or Saudi state agencies. This is because oil is considered as a critical facet of the KSA economy, national identity and sovereignty. Conclusively, the new arbitration system is far more in harmony with the internal laws particularly on matters of enforcement of arbitral awards as well as consenting to arbitration through either arbitration clauses and/or arbitration agreements. The fact that the overseeing authority is charged with the responsibility of ensuring that all procedures are strictly followed increases the probability of awards rendered thereof being successfully enforced.

## **Chapter 9: Conclusion and Recommendations**

### ***9.1 Overview***

In **Chapter 1**, the investment climate in Saudi Arabia was discussed. It was highlighted that the Holy Qur'an is the constitution of the land and that all laws governing investments are subordinate to the constitution.<sup>840</sup> Consequently, an investor's property is protected by Sharia law and local laws. Sharia law does not discriminate against foreigners or locals. The chapter introduced the theoretical background upon which the present study was based, namely the theory of globalisation. This helped to provide a context from which the study's aims and objective were subsequently derived, as well as to qualify what the study hoped to achieve. It emerged that, although Saudi Arabia is a sought-after investment destination in the Middle East, there are restrictions that regulate the types of investments in which foreigners can engage. Investment opportunities are important in banking, economic goods, housing and telecommunication. In the KSA, foreign investors are motivated by resolution of disputes. In the event of a dispute, the foreign investor chooses an arbitrator to try and resolve the dispute.<sup>841</sup> If it fails, a courtroom solution is then sought. Disputes with government are resolved through the ICSID.

Investors in the Kingdom of Saudi Arabia encounter problems such as the influence of Sharia law on foreign investments, preferential treatment given to foreign investors from the Gulf States, lack of trust, and inadequacies of laws protecting foreign investments. It is in this spirit that this research sought to "understand the interrelationship between Sharia law,

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<sup>840</sup> F. Farsy (1986). Saudi Arabia: A case study in development. London: Routledge.

<sup>841</sup> A.H. Cordesman (2003) Saudi Arabia Enters the 21<sup>st</sup> century. London: Greenwood.

investment climate, Royal Decrees, ICSD rules and dispute resolution mechanism”.

Consequently, it will be able to provide investors and academics with literature that will enable them to understand the investment climate in the KSA and how to address legal issues pertaining to their investments. The principal assumptions were that all foreigners are subjected to Sharia law, and that arbitration was the best means of resolving conflicts. The study was undertaken using both primary and secondary sources that related to the objective of the study. A brief structure of the study was then outlined.

**Chapter 2** examined the influence of Sharia law on investments in KSA. It was highlighted that although there is a secular law – the Basic Law that accommodates foreign investors – the foundation of all laws in KSA is the Holy Qur’an. Sharia law is a reflection of God’s Will and cannot be challenged by any secular legislation. The Basic law promulgated in 1992 is subordinate to Sharia law and its letter and spirit conforms to the Book of God and the Sunnah. There has been increased adherence to the Qur’an even after the promulgation of the Basic Law.<sup>842</sup>

Sharia law has a deeply rooted history; hence its influence on the Saudi system of governance. Most notable, the Qur’an prohibits persons from engaging in activities that flout Allah’s teachings. The KSA has the responsibility of safeguarding the two holy mosques of Mecca and Medina as provided for by Article 24 of the constitution. However, these two cities being holy to Muslims, foreigners (non-Muslims) are not allowed to own real estate or even carry out investment activities in the two cities. Sharia law is also applied in areas where there is no existing secular legislation. It is explained that the King has issued a number of Royal

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<sup>842</sup> Should above n 190.

Decrees due to pressure from Western investors to facilitate investment by Westerners in a Sharia-compliant environment.<sup>843</sup>

Sharia law is extremely accommodating towards investment activities as long as the activities do not contravene the conventional Islamic financing structures. It is highlighted that investment activities that result in the award and/or receipt of *Riba* (interest) are prohibited under Islamic Sharia law as they constitute *haram*. The need for foreign investors to become fully acquainted with the Islamic finance structure is outlined. This will enable them to differentiate between what constitutes *haram* and what constitutes ethical business practice.

The influence of Sharia law is further evident in the Foreign Investment Law. This law empowers the Supreme Economic Council of Saudi Arabia to have authority over those activities in which foreign investments are prohibited. Sharia law has a positive impact on reducing the risks faced by foreign investors because it prohibits risky businesses which do not guarantee returns. Again, Sharia law also obliges the Saudi government to provide to both foreign and domestic investors a friendly investment climate free from corruption and unfair competition. Foreign investors are obliged to comply with all laws and regulations in force in the KSA.<sup>844</sup>

**Chapter 3** analysed the various classes of foreign investors in the KSA and the influence of Sharia law on these different classes. The Foreign Investment Law perceives foreign investors as citizens of other nations pursuing investment activities in the KSA. Investors are broadly categorized as either Saudi investors or non-Saudi investors. The effect of this classification is that each class of investor has its own restrictions and privileges. Saudi nationals are protected from unnecessary competition although the Saudi economy is significantly influenced by foreign

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<sup>843</sup> M.A Ramady (2010). The Saudi Arabian economy: Policies, achievements & challenges. New York: Springer.

<sup>844</sup> Ibid.

investors. Non-Saudi investors are treated according to the provisions of the Foreign Investment Law. These investments are classified as either jointly owned by a national and a foreigner or fully owned by a foreign investor. Non-Saudi joint investments enjoy certain incentives from the government under the Foreign Investment Law.<sup>845</sup>

Arab investors are considered as nationals of the Arab League, whether they profess the Christian or Muslim faith. They are given a wide range of economic, social and cultural privileges. These privileges are crucial in that they enable the Arab League states to achieve unity and a strong economic growth. Gulf Cooperation Council investors are accorded privileges as Saudi nationals. Consequently, they are not subject to the Capital Investment Law. Investors from other countries are given equal treatment regardless of whether they are Christian or Muslim. Nationals of GCC are treated as Saudi nationals. The exclusion of foreigners from certain privileges and protections prevents home investments from stagnating due to competition from foreign firms. Businesses are also classified based on the capital outlay.

All classes of investors are Sharia-compliant. Sharia law classifies foreign investors according to various categories based on the anticipated mutual benefits. Consequently, although foreigners can own 100% of a company, the company will still be bound to operate as prescribed by law. Again, although Saudi nationals can invest in almost all sectors of the country's economy, foreign nationals are prohibited from certain sectors.<sup>846</sup>

**Chapter 4** considered the various aspects of dispute resolution. Increase in foreign investments leads to an increase in the number of disputes needing attention; hence the need for a

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<sup>845</sup> Shoult above n 190.

<sup>846</sup> A. Jaitten (2006). Investing in Saudi Arabia; International business perspective. New York: LAP Lambert Academic

faster and friendlier means of dispute resolution. Foreign investors can seek resolution of disputes from the courts. Alternatively, they can seek resolutions through Alternative Dispute Resolution Mechanisms (ADR) of which arbitration is the most popular. Application of litigation in dispute resolution has been overshadowed by ADR due to the limitations that face litigation such as the language barrier, inconsistencies in litigation law, high costs, bureaucracies, lack of credibility in domestic courts, risk of partiality, variation of litigation procedures and religious differences.

ADR takes place through arbitration, conciliation or mediation. ADR is more popular than litigation since foreigners are allowed to choose the means of resolving their disputes. ADR has several advantages: liberty in choosing arbitrators, expediency of arbitral proceedings, cost effectiveness, fairness and efficiency, uniformity and versatility, and promotion of investment cooperation.

Arbitrators are usually persons of high moral integrity and experts in the Muslim faith, thereby giving credibility to their arbitral award. Disputes with the government are referred to ICSID or arbitrated depending on the area of investment. They can also be resolved based on the existing bilateral or multilateral investment agreements between the KSA and the investor's country. Disputes with private Saudi businessmen are resolved via arbitration and not ICSID. The arbitration procedures must uphold the Sharia-based Basic Law as it is the best dispute resolution mechanism for such disputes.<sup>847</sup>

By making available these favourable means of dispute resolutions, the KSA has strategically positioned itself as the investment destination of choice in MENA.

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<sup>847</sup> Farsy above n 838.



**Chapter 5** presented the history of arbitration and its compliance with Sharia law. It is mentioned that arbitration, which is linked to business opportunities in oil and other basic commodities, arose from a need to resolve disputes with parties who do not follow the Sharia. It is also highlighted that arbitration is advocated by the Qur'an. A leading oil producer, Saudi Arabia found itself in many commercial disputes that could not be handled by Sharia, especially those cases that involved Western partners who did not follow Sharia. There are plans to put in place an international conciliation centre within the Kingdom. This institution would play a role in streamlining the process of resolving investment disputes through arbitration. The implications of the 1963 protocols, the 1983 Act and the 1985 Act are discussed at length. The 1963 protocols are considered complicated and do not give people the right to representation in the resolution of disputes. The 1983 Act had flaws in that the arbitration process was time-consuming and arbitrators were not critically scrutinized during selection. Moreover, an event such as the withdrawal of arbitrators from the process was a further complication not provided for by the Act. The procedures needed readjustments. The 1985 Act complied with international arbitration standards and thus facilitated arbitration worldwide. It was flexible, less costly and defined the expected code of conduct. It was much clearer than the 1983 Act. For example, the needs of business people were given more consideration as they could select specialized committees for given processes. Consequently, it was instrumental in instilling confidence in foreign investors, thereby assisting the Kingdom to advance in trade both locally and internationally.<sup>848</sup>

**Chapter 6** discussed dispute resolution mechanisms and classes of foreign investors in the KSA. The need for an impartial and reliable dispute resolution mechanism to engender an

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<sup>848</sup> Shoult above n 190, at 101.

attractive investment climate is highlighted. The international treaties, bilateral and multilateral agreements, and legislation of local commercial courts, have all demonstrated the Saudi government's commitment to protecting investors.

Dispute resolution processes for the different classes of investors are discussed. GAFTA states signed an agreement that provides for amicable resolution of investment disputes. Saudi Arabia is not bound by this agreement. Still, there exists no significant difference between the methods of resolving disputes of Arab League nations and those of GCC member states.

Investment disputes can be resolved via arbitration. Saudi Arabia is a signatory to the GCC-FTA. However, the agreement is silent on how members should resolve disputes. Members of the EU who have bilateral agreements with Saudi Arabia subscribe to the dispute mechanism outlined in those agreements. An outline is provided of the role of Free Trade Agreements in minimizing investment risks in Saudi Arabia in order to promote a faster dispute resolution mechanism between host governments and foreign investors.<sup>849</sup>

Major investment partners have the privilege of accessing easier processes for the resolution of investment disputes. However, this privilege is limited to the investment sectors that are open to foreign investors. The OPIC agreement has seen Saudi Arabia agree to resort to arbitration in the event of a dispute arising between a Saudi entity and an American investor. The agreement provides that arbitration be under international law to ensure fairness. The award as declared is final and cannot be challenged in any court of law. The agreement between Saudi Arabia and the Philippines does not mention how disputes arising between partners from these two countries should be addressed. MFN entails the amicable settlement of disputes by employing the fastest, friendliest and most efficient method possible: arbitration.

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<sup>849</sup> Jaitten above n 844.

It has been mentioned that oil disputes cannot be settled under the ICSID convention because the oil industry is not open to investment by foreigners. Non-Saudis can opt for arbitration only in disputes that touch on licensed ventures. Only Saudis are allowed to arbitrate regarding investment activities on the Negative List. The Basic Law allows for the resolution of commercial disputes through arbitration and/or mediation. These laws appear to favour foreigner investors from predominantly Muslim countries.

Also discussed in this chapter is the fact that investors from countries that have existing bilateral and/or multilateral investment treaties enjoy more privileges than their counterparts whose states have no agreements with Saudi Arabia. The various classes of investors are given preferential treatment depending on the nature of the agreement between Saudi Arabia and the foreigner's country. Foreign investors are accorded privileges based not on their religion, but on the agreements between the KSA and the investor's home country.<sup>850</sup>

**Chapter 7** examined ICSID and KSA laws. ICSID seeks to resolve issues arising from investment disputes. The need for an alternative means of dispute resolution is outlined. The purpose and scope of international treaties is also discussed. In developing countries, domestic legal systems tend to be overburdened to the extent that this reduces their credibility in handling investment disputes between foreign nationals and state agencies. International investment treaties fulfil this need by providing an alternative means of dispute resolution. International treaties are consensual, and therefore flexible. International arbitration treaties also serve to guarantee foreign investors that their investments are governed not only by Saudi laws but also by the international laws. The chapter also provided a brief overview of the globalisation theory and how it applies to Saudi's status in dispute resolution policies. This section reviewed the

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<sup>850</sup> Farsy above n 838.

globalisation theory and highlighted several relevant perspectives of the theory in regards to KSA bilateral trade agreements and how such agreements govern dispute resolution and foreign investment protection. By so doing, the chapter helped identify the extent to which Saudi Arabia has globalised its market in a bid to attract and retain investment inflows.

The ARAMCO case is touted as being a turning point in dispute resolution in the KSA, highlighting the inadequacy of the KSA's Sharia-based laws in handling particular matters; hence, the need for appropriate legal frameworks for dispute resolution. Ratification of ICSID would build investor confidence and aid in resolution of litigation where not all parties subscribe to Sharia law. Before the ICSID, arbitration was governed by legislation enclosed in the commercial court. The KSA law clearly distinguishes between those investment disputes that can be admitted to the ICSID, and those which cannot.

Saudi Arbitration Law recognises the validity of arbitration clauses mutually agreed upon by the contracting parties during the time of drafting a contract. However, the law does not encompass all types of investment disputes so as to cushion the government against unfavourable arbitral tribunal awards. It is noteworthy that the KSA's legal framework is most unlikely to be circumvented by the government to punish foreign investors. The spirit of the rules and regulations governing foreign investments in KSA is intended to streamline the investment environment and make it friendlier to investors. However, the convention is not clear regarding the interplay between ICSID award rulings and matters considered by hosting states as touching on their national sovereignty.<sup>851</sup>

In a bid to create a level playing field for foreign investors and Saudi investors, the Foreign Investment Law provides that foreign investors be empowered with adequate

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<sup>851</sup> Ramady above n 841.

information concerning investments in the KSA. This places them in a position to make informed investment decisions. The risk posed to foreign investments in the KSA is also discussed. It is pointed out that the risk mostly arises due to failure to abide by the KSA's investment laws. Other risks include inefficiencies of the government in tackling corruption, and stringent investment policies. Also mentioned is the fact that Saudi Arabia recognises arbitration as an alternative recourse to settling investment disputes. It is in this light that investment arbitration conventions were meant to act as impartial judges in resolving disputes between host states and foreign investors.<sup>852</sup>

**Chapter 8** discussed the sovereignty and protection of foreign investments in Saudi Arabia. It emphasizes that the rights and interests of foreign investors in the KSA are protected by various legal frameworks falling under the International Investment Agreements (IIAs). IIAs ensure that host nations provide substantial protection against legal and financial exploitation by domestic frameworks. It is explained how Sharia law stresses the importance of sovereignty by protecting the sanctity of Allah's creation, His teachings and promises, and protection of mankind and all holy sites, as well as sanctity of natural wealth. Protection of foreign investments is guaranteed by the Book of God, Sunnah, Basic Law and a number of secular codes. Sharia law provides a non-discriminatory platform for business ventures. King Abdullah has also expressed commitment to ensure protection of foreign investments within Saudi Arabia. These factors have resulted in the increase of direct foreign investments in the Kingdom.

It is mentioned that after a period of exploitation by Western multinationals, developing nations have started taking control of their oil and other natural resources in a bid to exercise sovereign control over these resources. The UN has also passed resolutions that recognise

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<sup>852</sup> Cordesman above n 839.

people's sovereignty and the principles of good faith in order to facilitate nationalization of resources. However, at the end of the 20<sup>th</sup> century, previously nationalized industries were privatized. This was a bid to create a friendly investment environment and run industries efficiently. Again, the Foreign Investment Law of 2000 made the KSA a friendly investment destination while still affirming the government's control in ensuring that the sovereignty of the State is not contravened.

Concerning investment disputes, it was clarified that all investments in the KSA were covered under the ICSID jurisdiction except for disputes involving oil. Arbitration is not legally possible within the KSA arbitration process and is not applicable. Arbitration is possible only when a court gives consent to the two parties to arbitrate. In this regard, the KSA judicial system handles the oil disputes.<sup>853</sup> It was noted that ICSID had some weaknesses, demonstrated by the fact that contracting states were not bound by the treaty to submit investment disputes for arbitration. Again, contracting states can fail to honour arbitration clauses on the basis that they contravene their national values and sovereignty. The KSA's legal framework inadequately addresses dispute resolution through arbitration. Commercial litigation in the KSA is time-consuming and the judicial system is not capable of delivering credible rulings. The fact that the KSA rarely submits disputes to IIA jurisdictions brings into question the KSA's conduct in resolving investor disputes.

It is noteworthy that previously "negatively listed" investment opportunities have been opened up to foreigners. Profits made in the KSA can be transferred to home countries. Arbitration authorities are charged with supervision and control of all activities involved in the arbitration process. In enforcing an arbitral award, the authority with jurisdiction to handle the

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<sup>853</sup> Cordesman above n 839.

dispute should allow enough room for objection from either party. The arbitral award may not be enforced in the event of any irregularities in the arbitration process. The importance of arbitrators being persons of strong character and upright morals was also stated.

**Chapter 9** summarized the thesis, presented and discussed the findings and concluded with several recommendations.

## ***9.2 Findings***

In this study of the investment climate in Saudi Arabia, the following findings were made.

### **9.2.1 Influence of Sharia Law on investment opportunities**

The influence of Sharia law on the foreign investment is substantial. Secular Law and hence laws influencing foreign business such as Foreign Investment Law are based on the Qur'an. Businesses ventures must only comprise activities that are allowed by Sharia. For example, although a foreigner can own 100% of a company, the company is still bound to operate in compliance with Islamic Sharia. Again, the Qur'an dictates areas where foreigners can set up businesses and where they cannot. For instance, as it has been mentioned earlier, foreigners are legally barred from setting up business in Mecca and Medina. It also dictates what investments foreigners can make within the Kingdom by establishing a "Negative List" of investments that cannot be undertaken by foreigners. For example, foreigners cannot invest in the oil industry. Foreign investments are protected by Sharia law. This has also helped to mitigate the risks involved in making investments in the KSA. Dispute resolution procedures

follow the guidelines of Sharia law. It is noteworthy that Sharia law is remarkably fair and does not leave the chance for the discrimination of one party whether a Muslim or a Christian.

### **9.2.2 Influence of business classification on protection**

It was discovered that privileges related to doing business and the means of dispute resolution in the KSA are dependent on the classification of a business. Citizens of Saudi Arabia receive the most privileges and protection, notably immunity from unnecessary competition. GCC citizens are second in line. GCC member states have agreed that their citizens should receive the best treatment accorded foreigners in a GCC state. Arab League citizens receive treatment almost similar to that accorded to GCC citizens. It was also found that the treatment of investors was according to geographical lines and not religious ones. For example, both a Muslim and a Christian from an Arab League country would receive the same protection and privileges.

It is noteworthy that nationals of states with existing bilateral agreements with the KSA receive privileges as provided by the agreements. These privileges are usually within the limits of the investment sectors that are open to foreign investors. These bilateral agreements serve to boost trade and cooperation between the two countries.

### **9.2.3 Dispute resolution mechanism**

The need for a reliable and fast means of dispute resolution is evident in the KSA. This is true given the rising numbers of disputes as more investors come to Saudi Arabia for investment opportunities. The Kingdom of Saudi Arabia has developed various favourable means of handling disputes between various classes of investors operating in the country. While there are legislations and courts to handle litigation, arbitration is the most popular means of dispute



resolution. This can be attributed to the fact that arbitration is friendly, gives a more inclusive award to the parties involved and is cost effective. Noteworthy is that the KSA has ratified several IIAs to facilitate a “foreigner friendly” dispute resolution process and build investor confidence. Among these IIAs is the ICSID convention. The ICSID convention aids in the resolution of disputes between foreigners and the KSA. Although the KSA has ratified the ICSID, it is not tied down to implementing arbitrary awards granted by the ICSID if it feels that the award violates its sovereignty. Again, the KSA law makes a clear distinction between those investment disputes that are to be admitted to the ICSID and those that should not. For instance, oil disputes are not settled under the ICSID due to the fact that the oil industry is not open to foreign investors. Again, Free Trade Agreements also influence the type of dispute resolution mechanism to be used. While some FTAs have clauses on how disputes should be resolved, other FTAs are silent.

The 1985 Act has also positively impacted on dispute resolution by complying with international arbitration standards. This has helped to create a suitable investment climate in the KSA. It is also noted that while disputes between foreign investors and the government can be referred to the ICSID or arbitrated depending on the area of investment, disputes between foreign investors and Saudi private businessmen are resolved via arbitration.

### ***9.3 Discussion of Findings***

The findings of the present study irrefutably establish that the Kingdom of Saudi Arabia has undergone numerous political, social and economic changes in the last three decades, embracing various aspects of globalisation in a bid to attract more and more foreign investment

into the country. According to Held et al., “*the concept of globalisation implies, first and foremost, a stretching of social, political and economic activities across frontiers such that events, decisions and activities in one region of the world can come to have significance for individuals and communities in distant regions of the globe.*”<sup>854</sup> It is evident that many of the concepts that were previously thought of as rigid and uncompromising in the Islamic world have a measure of convergence with the conventional world. If globalisation moves societies towards commonality as discussed previously in this dissertation, then it comes not as a surprise that there are many ways in which Saudi Arabia’s investment environment is equivalent to that of the conventional Western markets.

The definition of globalisation proposed by the Geneva Centre for Security Policy conceives globalisation is “a process that encompasses the causes, course, and consequences of transnational and trans-cultural integration of human and non-human activities”, such activities being “economic integration; the transfer of policies across borders; the transmission of knowledge; cultural stability; the reproduction, relations, and discourses of power; it is a global process, a concept, a revolution, and “an establishment of the global market free from socio-political control””.<sup>855</sup> The study found that in the last three decades, the KSA has undergone most of these transformations and initiated a series of activities that might be classified as embracing the concept of globalisation as fronted by Al-Rodhan and Stoudmann. It is expected that progressive globalisation of the KSA investment environment will enable greater levels of FDI, since FDI is a principle tenet of globalised trade.<sup>856</sup>

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<sup>854</sup> Held and McLew above n 718.

<sup>855</sup> Nayef Al-Rodhan and Gerard Stoudmann, “Definitions of Globalisation: A Comprehensive Overview and a Proposed Definition”. (Geneva: Geneva Centre for Security Policy, 2006), at 2 – 3.

<sup>856</sup> Clark, Ian, *Globalisation and International Relations Theory* (Oxford: Oxford University Press, 1999), at 8.

For instance, it has been variously held that because the KSA is largely a Muslim nation with a dominant Islamic culture, conventional businesses cannot survive in it. This study established that this is a misconception with no basis in facts. Regarding Sharia law as it pertains to foreign investment, the study found that Shariah law has a substantial influence on the investment opportunities and risks in the KSA, mainly because the law determines the type of businesses in which foreigners can invest, where such businesses are located, and the type of trade in which the businesses can engage. The study found that foreign businessmen in the KSA can undertake only those activities that are allowed by Sharia. Further, although a foreigner can own 100% of a company, the company is still bound to operate in compliance with Islamic Sharia. Additionally, it emerged that foreigners cannot invest in the oil industry.

Given that most of the KSA's laws including those influencing foreign business such as Foreign Investment Law are based on the Qur'an, foreign investors might presume that the KSA investment environment is hostile towards Western investors. The reality is actually the opposite. The present study found that foreign investments are protected by Sharia law. This has also helped to mitigate the risks involved in making investments in the KSA. Dispute resolution procedures follow the guidelines of Sharia law. It is noteworthy that Sharia law is remarkably fair and does not allow the chance of discrimination against any one party whether Muslim or Christian.

The assimilation of globalist laws and policies, a cultural permissiveness and mutual inclusivity of the modern KSA while being favourable to globalisation, raises controversy amongst some scholars. There are those who view this progress as the indoctrination of an Arab state with Western philosophies and culture. Immanuel Wallerstein, for instance, regards globalisation as indicative of "the triumph of a capitalist world economy tied together by a global

division of labour”.<sup>857</sup> Others have argued that the continued admission of Arab states into the global trade environment is the objective of the Western powers, predominantly the USA, to extend their control of the states over which they can no longer militate.<sup>858</sup> Others claim that by embracing globalisation of trade, developing nations are simply offering Western corporations and economies an opportunity to diversify their risks and to share their risks with societies that represent minimal risks. Giddens, for instance, argues that globalisation is “the intensification of worldwide social relations which link distant localities in such a way that local happenings are shaped by events occurring many miles away and vice versa”.<sup>859</sup>

The foregoing debate, while being valid and worthy of research interest, is not of any significance to the present discussion, however. The present study was strictly intended to evaluate the investment opportunities and risks within the KSA. The study has sufficiently found that the KSA has in recent times taken very bold steps to globalize its trade and to open doors for foreign investors. The same progressive attainments have resulted in the development of legal frameworks or the adoption of global systems to address disputes involving foreign investors in KSA. It is thus accurate to conclude that in so far as the investment environment is concerned, the KSA’s commitment to globalisation has been beneficial and largely productive for both the Saudi society and for the foreign investors currently in, or intending to enter, the KSA market.

From another perspective, the study found that while becoming increasingly global (meaning open, liberal and standardized), the KSA investment environment is still facing some hurdles. Of specific note is that the country still enforces some protectionist measures against a

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<sup>857</sup> Immanuel Wallerstein, “The Modern World System: Capitalist Agriculture and the Origins of the European World-Economy in the Sixteenth Century (New York: Academic Press, 1974).

<sup>858</sup> Robert Holton, *Globalisation and the Nation-State* (London: Macmillan Press, 1998), at 11.

<sup>859</sup> Anthony Giddens, *The Consequences of Modernity* (Cambridge: Polity Press, 1990), at 64.

truly global market. While investigating the influence of business classification on protection, the study found that privileges associated with business dealings and means of dispute resolution in the KSA are dependent on the classification of a business. Specifically, Saudi nationals receive the most privileges and protection, notably the immunity from unnecessary competition. It then emerged that GCC citizens are second in line. GCC member States have agreed that their citizens should receive the best treatment accorded foreigners in a GCC state. Arab League citizens receive treatment almost similar to that accorded to GCC citizens.

Such differentiations are to be expected even in the most globalised nations. Appadurai argues that “the critical point is that both sides of the coin of global cultural process today are products of the infinitely varied mutual contest of sameness and difference on a stage characterized by radical disjuncture between different sorts of global flows and the uncertain landscapes created in and through these disjuncture”.<sup>860</sup> It is therefore understandable that even when globalisation calls for the abolition of protectionist trading policies, there are some protectionist measures that will still remain since countries are different and are faced by different circumstances. Only if such differences are eliminated can the world become really global. There will always, for instance, be a preference for the US to trade with Britain more than with Germany, and a willingness to enter into a protectionist alliance with Canada rather than Russia.<sup>861</sup>

Progress in globalisation will see the elimination of these biases and preferences as states become closer and closer until there are no favourites, amongst all nations. It can be claimed that the KSA is en route towards that end, having clearly started to embrace global partnerships.

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<sup>860</sup> Arjun above n 727..

<sup>861</sup> Chi-yu Chang, “How American Culture Correlates the Process of Globalisation”, *Asian EFL Journal* 6, no. 3 (2004) at 23.

After all, “globalisation means the onset of the borderless world”.<sup>862</sup> There is thus the sense of progress in the way that the KSA is becoming mutually interrelated with other nations, and becoming aware of the need to forge international alliances since, as Roland Robertson posits, globalisation is “both the compression of the world and the intensification of consciousness of the world as a whole”.<sup>863</sup>

A significant outcome in this regard is that the study found evidence indicating that treatment of investors was divided along geographical lines and not religious lines. For example, both a Muslim and a Christian from an Arab League country are entitled to the same protection and privileges. Further, despite the region-based trade protectionism discussed above, the KSA is starting to seek and honour other non-region-based alliances. The study found that states with existing bilateral agreements with the KSA receive privileges as provided by the agreements. These privileges are usually within the limits of the investment sectors that are open to foreign investors. According to the study’s findings, these bilateral agreements serve to boost trade and cooperation between the two countries. With disregard for the political implications of such progress, it is clear that the KSA is making foreign investment increasingly possible and less risky.<sup>864</sup> The scholars argue that the benefits of globalisation are in “the intensification of economic, political, social and cultural relations across borders”.<sup>865</sup>

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<sup>862</sup> Kenichi Ohmae, *The Borderless World: Power and Strategy in the Global Marketplace* (London: HarperCollins, 1992), at 16.

<sup>863</sup> Roland Robertson, *Globalisation: Social Theory and Global Culture* (London: Sage, 1992), at 8.

<sup>864</sup> Hans-Henrik Holm and Georg Sorensen, eds., *Whose World Order? Uneven Globalisation and the End of the Cold War* (Boulder: Westview Press, 1995), at 1.

<sup>865</sup> Ibid.

#### ***9.4 Recommendations***

The justice system in Saudi Arabia needs reforms in order to be able to cope with the rising number of investment disputes. This will facilitate timely and credible rulings from the justice system. The justice system should continue to uphold Sharia law as its applications this far have yielded benefits and shielded investment partners from scams and unfair business practices. An empowered justice system will be in a position to stem corruption in the country and other legal issues that pertain to investment. It will also enable the justice system to adequately address dispute resolution through arbitration.

There is a need for FTAs to be reviewed and those that lack dispute resolution guidelines upgraded to contain these guidelines. This will facilitate smoother and friendlier resolution of disputes between signatories to FTAs. Countries seeking investment in the KSA need to establish cordial relations with the King and seek FTAs so that their nationals are accorded preferential treatment.

The Supreme Economic Council needs to reduce the number of economic activities that are “negatively listed”. This will help to boost foreign investments in the state, resulting in income for the state and better quality goods for nationals of Saudi Arabia. This will also open up areas that were considered as “Saudi domains” for competition, thus reaping the benefits of competition. There is a need for the KSA to give the ICSID full rein in matters of arbitration and be obliged to implement all arbitrary awards granted by the ICSID. This will boost investor confidence in the KSA’s system of dispute resolution.

With the rising civil unrest in the MENA region, it is appropriate for the government to establish mechanisms that will ensure investors’ security and continuity of their businesses should the unrest spread to the KSA. It is more prudent to ensure that adequate

measures are put in place to ensure that unrest does not occur in the Kingdom. This is because it would have a negative effect on the already favourable perception of the Kingdom as an investment destination.

It can be concluded that arbitration has found favour with many investors as their first choice means of conflict resolution. This can be evidenced by investor's reluctance to seek redress from courts as they are slow. Consequently, the Kingdom's justice structures should seek to encourage arbitration and initiate structures that will mainly oversee the success of arbitration as a means of dispute resolution. The criteria for choosing arbitrators need to remain stringent in order to sustain investor confidence in this means of dispute resolution.

More research needs to be done in this area focusing on issues such as the satisfaction level of investors with outcomes of arbitration committees, the extent of the influence of ICSID in resolving disputes, and the effect of Arab practices such as *Wasta*<sup>866</sup> on the arbitration committees.

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<sup>866</sup> R. Mead and T.G Andrews (2009). International Management. New Jersey: John Wiley & Sons.



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