The Arab States' Gulf Cooperation Council: Unified Rules for Trade and Industry

I. Introduction

As a well-launched attempt by a concerned group of sovereign nations\(^1\) to overcome the insularities of historical boundaries and to promote coherent initiatives for commerce and national security, the Cooperation Council for the Arab States of the Gulf (GCC) will have significant impact in the area on cross-border trade, industrialization and other business activity.\(^2\) This article reviews the relevant legal framework under which the six member states have to some degree transferred their sovereign prerogatives to the organization. This is followed by an exposition of the further agreements and implementing decisions that the GCC itself has promulgated, and finally, some internal laws of the member states are examined to illustrate the extent to which they are in harmony with, or continue to be contrary, either in text or policy, to the positions taken by the GCC. In this latter respect, the focus will be on the local laws of Saudi Arabia, but the matters addressed suggest areas in which similar inquiries may be made in each of the member states to

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\(^1\) The United Arab Emirates, State of Bahrain, Kingdom of Saudi Arabia, Sultanate of Oman, State of Qatar, and State of Kuwait.

\(^2\) Aside from press releases and informal conversations with members of the staff of the Office of the GCC Secretariat General, the principal source of information about the GCC is the GCC Information Center in the Office of the Secretariat General in Riyadh where an expanding library is maintained together with an archive of Gulf newspaper and magazine releases containing statements by responsible officers of the GCC organization. Inquiries may be addressed to the GCC Secretariat General's Office, Legal Affairs Sector, Man and Environment Affairs Sector, Economic Affairs Sector, or other sectors or directly to the Information Center, Riyadh, P.O. Box 7153, telex 203635 SJ.
evaluate the compatibility of internal policies and regulations with those promulgated by the GCC.

II. GCC Organizational Documents

The founding document is, of course, the GCC Charter itself, signed by the six member states on May 25, 1981. The Charter sets forth basic objectives\(^3\) to be achieved through coordination and integration and then establishes the principal entities through which the GCC functions.

A. Principal Bodies

1. Supreme Council

The highest authority is the Supreme Council\(^4\) comprised of the heads of the member states. It has convened annually in November to review and approve recommendations of the Ministerial Council and to take up matters upon its own initiative.\(^5\) Attached to the Supreme Council is the Commission for Settlement of Disputes.\(^6\)

2. Ministerial Council

The Charter establishes a ministerial council consisting of the foreign ministers of the member states or other delegated ministers. The council meets quarter-annually and its functions include proposing to the Supreme Council policies, studies and projects. It may also appoint technical or specialized committees for study and presentation of proposals.\(^7\)

3. Secretariat—General

The executive branch of the GCC is the Secretariat General who is appointed by the Supreme Council for a three-year term. The Secretariat General is charged with preparation of studies, reports, the preparation of drafts of administrative and financial regulations, budgetary matters, and the execution of resolutions and recommendations of the Supreme and Ministerial Councils.\(^8\)

B. Rules of Procedure

Concurrently with the signing of the Charter, the member states signed separate rules of procedure of the Supreme Council, the Ministerial Council

\(^3\) Charter, art. 4.
\(^4\) Charter, art. 7.
\(^5\) Charter, art. 10.
\(^6\) Charter, art. 11.
\(^7\) Charter, art. 12.
\(^8\) Charter, arts. 14 and 15.
and the Commission for Settlement of Disputes. The Commission has jurisdiction over disputes between member states and controversies as to interpretation or execution of the Charter. It is a precondition to jurisdiction that a matter be referred to the Commission by the Supreme Council.9

III. Unified Economic Agreement

The foregoing is to give a sense of the executive and legislative context in which implementing resolutions and decisions are made with respect to the Unified Economic Agreement completed a few weeks after the Charter, on June 8, 1981. The Agreement became effective in 1982 after its approval by the Supreme Council, and expressly supersedes member states’ local laws and pre-existing bi-lateral agreements to the extent the same conflict with the Agreement.10

The Unified Economic Agreement and implementing decisions are of immediate significance to GCC residents and others involved in the private business sector. Its scope and importance to the business community are suggested by its chapter titles: trade exchange (chapter 1); movement of capital, citizens, and exercise of economic activities (chapter 2); coordination of development (chapter 3); technical cooperation (chapter 4); transport and communication (chapter 5); financial and monetary cooperation (chapter 6).

A. Examples of Agreement Implementation

The Agreement is the focus of regular on going implementation as indicated by several examples:

1. Chapter 1, article 2, requires member states to exempt from customs duties agricultural, animal, industrial and natural resource products of national (GCC) origin.

2. By resolution of the Supreme Council in November of 1982, two requirements for exemption from customs duties are imposed:
   a. The seller must be a GCC member state citizen, or a company which is at least 51 percent owned by GCC citizens. In the case of an industrial company, it will qualify for exemption even if not 51 percent owned by GCC citizens during a period of one year from the effective date of the resolution, namely March 1, 1983 through March 1, 1984.
   b. The product must be either of GCC member state origin or at least 40 percent value must have been added by the seller to the product’s final value. (It may be that if less than 40 percent value is added, the customs

duties will be imposed pro rata—that is, if 20 percent value is added, duties may be reduced by 50 percent. This point awaits further confirmation, however.)

3. Article 20 of the Agreement requires member states to allow vessels “belonging to any member state” to use port facilities and otherwise be placed on a parity of treatment with nationals of the member state. Controversy subsequently arose as to whether this article was confined solely to government-owned vessels. A clarifying interpretation states that a vessel will qualify for favorable treatment under this article if it is owned wholly or partly by a GCC national, and it is flying under the flag of a GCC member state. (An earlier interpretation indicating that satisfaction of either of these conditions would qualify the vessel for favored treatment was rescinded.)

4. Article 6 recognizes that each member state may bar the entry of goods according to its local regulations. There are published lists of goods prohibited by each of the member states. These, incidentally, are goods deemed illegal, not merely goods intended to be excluded to prevent competition with local products.

5. Article 4 requires member states to establish uniform minimum tariffs applicable to products of non-member states. By resolution adopted in November of 1983, the minimum tariff on such foreign merchandise, effective September 1, 1983, is 4 percent; the maximum is 20 percent. All member states have raised their minimum tariffs to 4 percent. There is a further resolution, however, imposing customs duties of 30 percent on merchandise of a special nature, described as tobacco and the like. Member states are given an option to impose duties higher than 30 percent on products in this category.

B. Standards Organization and Gulf Investment Corporation

After the close of each annual session of the Supreme Council of the GCC, there is issued a final declaration describing the principal matters addressed by the session. Although these declarations are typically preoccupied with security matters and the status of efforts to resolve regional conflicts, they also provide a concise statement of significant developments in the implementation of the Unified Economic Agreement.

Two such developments were highlighted in the declaration following the 1982 meeting of the Supreme Council. In that year, the Supreme Council affirmed the conversion of the Saudi Organization for Specifications and Measurements into a Gulf organization specializing in this field for the member states. The Ministerial Council is authorized to approve the regulations of the Organization and to determine its powers and relationship to the
member states. The standards and specifications of the Organization are to be binding on all member states. At the present time, the Saudi Commercial Agency Regulations require that all agreements between foreign manufacturer-suppliers and in-Kingdom dealers or distributors shall stipulate that the foreign seller's goods conform to all relevant specifications and standards of the Saudi Organization. It should be anticipated that similar requirements will be adopted by each of the member states if they have not already done so.

In 1982, the Gulf Investment Corporation was established and is to have an initial capital of U.S. $2,100,000,000. The mandate of the Corporation is to seek opportunities for financing, preferably as a joint venture partner within and outside Arab states, in the private as well as public sectors. The Corporation will seek self-sustaining projects and should not be regarded as an aid institution. At the moment, it is still in the process of organization and receiving its capital contributions from member states. The Corporation's principal staff is in Kuwait where its portfolio of invested capital is managed. The Corporation has not yet commenced project financing.

C. CONFORMITY OF LOCAL LAW—
SOME EXAMPLES FROM SAUDI ARABIA

1. Taxation

As indicated above,11 the Unified Economic Agreement provides that the applicable provisions of the Agreement prevail in cases of conflict with local laws of member states. While it remains to be seen to what extent this will occur in practice, a significant instance of an amendment of local law to conform to the spirit and text of GCC pronouncements occurred in 1985 when the Saudi Ministry of Finance and National Economy issued a decision12 to the Saudi Department of Zakat and Income Tax which directed that GCC citizens and companies be given the same tax treatment as Saudi citizens. The decision, which implements a Royal Decree, provided as follows: GCC citizens are exempt from Saudi income tax but are obligated, as are Saudis, to pay Zakat.13 Similarly, GCC partners and shareholders of companies will not be liable for income tax, but if the company is partly owned by non-GCC citizens, income tax will be assessed on the share of the income of the non-GCC owners and Zakat will be assessed on the GCC citizens' share.

There are two significant requirements stated in the decision which are

11. See supra note 8.
13. Generally speaking, the Zakat is a religious tax.
preconditions to GCC companies receiving such favorable tax treatment:
1. the GCC company must submit to the Saudi Department of Zakat and
   Income Tax official confirmation of its place of incorporation and the
   nationality of its shareholders, together with a certified copy of its articles of
   association, and 2. the company must furnish a copy of its license to operate
   in the Kingdom of Saudi Arabia. This second requirement has created
   considerable uncertainty, particularly in banking circles, about the applica-
   bility of the tax exemption to GCC companies which are not licensed or
   operating in Saudi Arabia.

   It had been expected, or at least hoped, during the months that preceded
   the issue of the decision that payments made from within Saudi Arabia, such
   as bank fees and interest, management fees and other Saudi source income,
   would, if paid to an institution formed under the laws of a member state and
   owned by member state citizens, be exempt from Saudi withholding tax
   requirements. Those requirements, simply stated, are that payments from
   within Saudi Arabia to a non-Saudi enterprise are subject to Saudi income
   tax. Unless the foreign recipient has a Saudi tax file number and files Saudi
   declarations of tax, an obligation is imposed on the party in the Kingdom
   making the payments to withhold Saudi income tax.\textsuperscript{14} The tax withholding is
calculated on the basis of a so-called deemed profit method.

   It is the practice of foreign lending banks to require Saudi borrowers to
gross-up their interest payments by whatever additional amount may be
necessary to cover Saudi income tax. Since no withholding, and therefore no
gross-up payment, is required with respect to interest and other fees paid to
Saudi banks, to date the tax structure has given Saudi banks a competitive
advantage in the Kingdom over foreign banks, an advantage which banks
formed in other GCC member states had expected to be terminated by the
decision last January. The Saudi Department of Zakat and Income Tax has
been requested to clarify this point but, to date, no ruling has been made.
Thus, it remains uncertain whether Saudi source income paid to GCC
enterprises not licensed and operating in Saudi Arabia will be exempt from
Saudi income tax.

2. Restriction on Foreign Banks

   On January 15, 1983, the Saudi Arabian Monetary Agency (SAMA)
issued a circular prohibiting Saudi banks from inviting non-Saudi banks to
participate in in-Kingdom loans denominated in Saudi riyals, subject to
certain exceptions.\textsuperscript{15} No relaxation of that rule has been issued by SAMA

\textsuperscript{14} Income Tax Regulations issued by Royal Decree No. 3321, 21/1/1370H, as amended.
\textsuperscript{15} Saudi Arabian Monetary Agency Circular No. 5013/M/M/68, dated Jan. 15, 1983.
and it is unlikely that any change in favor of GCC banks will be made in the near future.

3. Ownership of Saudi Real Estate

GCC citizens may acquire real estate in Saudi Arabia subject to limitations as to which there seem to be no final decisions as yet. The topic was considered by the Supreme Council in November, 1984, and draft proposals for uniform laws are currently being studied by the member states. The twelve-article proposal, in essence, would allow a GCC national to own up to three thousand square meters solely for residential use unless another use is permitted by local law. If vacant land is acquired, construction of the residence must begin within three years and be completed within five years of purchase. The property may not be resold for a period of eight years.

4. GCC Citizens Doing Business in Saudi Arabia

a. Licensing GCC Companies

A GCC firm operating in the areas of agriculture, animal husbandry, industrial, and contracting projects will be treated as a Saudi national firm for licensing purposes provided the company is 100 percent owned by GCC nationals and at least 25 percent owned by Saudi nationals. The 25 percent requirement will not be applied to firms engaged in industry in Saudi Arabia. The 25 percent requirement with respect to GCC firms in the other categories of business applies only to the first five years of their presence in Saudi Arabia after which 25 percent Saudi ownership will not be required. GCC firms meeting these requirements will be treated as if they were 100 percent Saudi companies.

b. Industrial and Contracting Projects

Subject to the foregoing, a GCC citizen or company may obtain a license to establish an industrial project directly from the Saudi Ministry of Industry and Electricity. It will not be necessary to meet minimum capital requirements or to obtain a foreign capital investment license unless the GCC enterprise is partly owned by a non-GCC entity. A GCC entity may obtain a license directly from the Saudi Ministry of Commerce to engage in a contracting project, without any requirement for a Saudi sponsor or agent.

c. Trading

Further clarification is needed about the right or privilege of GCC citizens to engage in retail trade in other member states. From the Saudi perspective, it would appear that a citizen of another GCC member state would not

16. Royal Decree No. 4584, 7/6/1403H.
be permitted under Saudi law to make direct retail sales in Saudi Arabia of products either of member state or third country origin. Sales would be limited to duty free exports to Saudis who would resell at retail. A GCC entity licensed to manufacture in Saudi Arabia may sell its manufactured products directly, but would not be allowed to sell directly any other products, even if related to the manufactured product line. This topic, however, is on the agenda for a conference to be held soon among GCC representatives and those of the Saudi Ministries of Commerce and Finance.

5. The Thirty Percent Rule
Since 1983 Saudi Arabia has required non-Saudi prime contractors to governmental employers to subcontract 30 percent of the contract to 100 percent Saudi owned enterprises. In late 1983, it was informally indicated that a prime contractor at least 51 percent owned by Saudis would qualify as a Saudi owned entity exempt from the 30 percent requirement. This position was reversed in August of 1984 and then recently reinstated by the Ministry of Finance. No formal ruling has been issued as to whether a non-Saudi GCC national would be exempt from the 30 percent requirement or, in the case where a non-Saudi owned prime contractor was required to subcontract to 100 percent Saudi owned subcontractors, whether a GCC national would qualify for such a subcontract.

The Saudi Tenders Regulations and various directives for protection of national industry require purchase of Saudi products if the quality and price, although less favorable than that of other products available, fall within a stipulated range. To date, these regulations and ministerial directives have not been amended to relax the application of these requirements in favor of GCC nationals. There have been informal indications, however, that if the product is manufactured in Saudi Arabia by a GCC entity licensed in Saudi Arabia, the product will be treated as a Saudi product for all purposes.

7. Proposed Unified Legal System
Various departments of the GCC organization have under study matters related to a unified legal and judicial system for the GCC. In addition, a draft agreement, together with implementing rules, for establishing a GCC commercial arbitration center has been prepared for a forthcoming meeting of Ministers of Justice of member states. There are also under consideration an agreement for uniform service of process in initiating court action, and, of particular interest, an agreement for cross-border enforcement of judgments.
IV. Conclusion

A. Some Proposals

Since there is now considerable impetus and motivation to address at the GCC level various gaps in commercial law in the member states, areas which do not to any great degree impinge on the province of Shariatic law, it would seem appropriate to expand the current study of a unified legal system to include some of the following:

1. Now that the GCC has a standards and specifications organization, it would be a logical step to adopt a much needed uniform products liability law. In place of traditional measures of damages and methods of determining liability before a non-specialized tribunal, laws and procedures more appropriate to the complexities of litigation in this area should be adopted.

2. Citizens of various GCC member states participate in the ownership of joint stock companies. This suggests, although realization may be quite some time away, that preparation should be made for a unified capital market structure with uniform procedures for transfer and registration of shares and a regulatory agency to ensure an orderly and fair capital market. The technology for a unified GCC capital market is at hand, awaiting only the formulation of a legal and regulatory framework.

3. Bank financing for business ventures would be facilitated if more types of collateral or security devices were available other than the traditional personal guarantee, real estate mortgage, assignment of specific contract proceeds or pledge of shares of a publicly owned joint stock company. Other types of security, such as security interests in a partner-shareholder's interest in a limited liability company, and in accounts receivable, inventory and equipment, are presently unavailable to the businessman who needs to borrow on a secured basis.

4. Finally, it would seem that the day is here when increasing numbers of GCC businesses will undertake industrial and commercial activities without necessarily sharing ownership with foreign partners to obtain expertise and technical know-how. The time is at hand for such know-how and related patent and trademark rights to be licensed directly to the local enterprise for exploitation in GCC markets. This beneficial development for the local businessman will be greatly facilitated, and foreign owners of technology will feel more secure in disclosing and licensing that technology, if the GCC will address the problem of protection of patent and trademark rights through uniform laws granting effective procedures for enforcement.

B. Outlook for Further Economic Unification

As the foregoing indicates, the elimination of local protectionist trade
rules is far from completed, and one can expect continued emphasis by Saudi ministries and government departments on requirements that their contractors "buy Saudi." Last month, for example, it was officially directed that all Saudi government contracts shall include a clause requiring contractors to use Saudi Airlines exclusively for transport of the contractors' personnel and freight. On the other hand, it was recently announced by the Saudi Minister of Finance and National Economy that in 1984 trade between Saudi Arabia and the other GCC member states had reached the level of Saudi Riyals 10 billion (or approximately 2.8 billion U.S. dollars). Moreover, over the past several years, as GCC activity has increased there have been many positive signs of relaxation of national barriers, as for example, in the adoption of GCC passports and residence permits, the preliminary approval for those in the medical, accounting, engineering and legal professions to become licensed to practice in GCC countries other than their home country, the adoption of an official policy to give priority in government projects to national products of GCC member states even if their cost may be higher, up to 10 percent than the cost of such products available in non-GCC states (subject, of course, to the first priority in favor of available domestic products), the unification of GCC port services rates and the undertaking of a study earlier last year to connect the GCC member states with a unified electric power network to permit, among other things, for directing electric power surpluses from one member state to another or to make available the resources of one member state to another where damage, intentional or accidental, may have occurred to power plants. Despite the many positive steps towards cooperation and unification, however, the next years will be a time of testing of the resolve for unification in view of the developing stringent economic situation throughout the member states.