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Service Agents Regulation and Related Laws Affecting Foreign Companies in Saudi Arabia

I. Introduction

After the promulgation in January, 1978 of the Saudi Arabian Service Agents Regulation (the Regulation),[1] which, in general, requires all non-Saudi companies with Saudi government contracts to have a Saudi service agent, a number of questions as to its proper interpretation immediately arose.[2] During the following four years, certain developments have provided answers to a number of these questions. These developments also indicate that the Saudi authorities have been making a concerted effort to enforce not only the Regulation but other regulations with particular application to foreign companies operating in the Kingdom.[3] The effects of this effort have been and are felt by foreign companies in the conduct of their day to day business.

During the same period, work was reportedly underway on what was thought to be a wholesale revision of the Saudi Arabian Commercial Agencies Regulation,[4] the regulation governing Saudi agents operating in the

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[1]Royal Decree M/2 of 1978.

[2]*See* Cartwright and Hamza, *The Saudi Arabian Service Agents Regulation*, 34 BUS. LAW. 475 (1979).

[3]Prior to 1977, foreign companies operating in the Kingdom did so typically under the "sponsorship" of their Saudi agents or the government ministries with which they had contracts, without any regard to local requirements to register, to pay taxes, etc. Undoubtedly, some companies continue to do so, but their numbers are diminishing quickly as a result of the authorities' withdrawal of their tacit consent to unregistered activity.

[4]Royal Decree M/11 of 1962, *amended by* Royal Decree M/5 of 1969 and Royal Decree M/8 of 1973. The Saudi Commercial Agencies Regulation reserves to Saudi individuals and companies wholly owned by Saudis the conduct of all trading activities in the Kingdom.

private sector. Finally, on June 23, 1980, Royal Decree No. M/32 was promulgated as a further amendment to the Commercial Agencies Regulation, and on March 30, 1981, the Ministry of Commerce of Saudi Arabia issued Implementing Regulations under Royal Decree M/32.[5] Except to note that these new regulations have been issued and are further evidence of the Saudi authorities' determination to enforce the Kingdom's regulations relating to foreign companies, and to point out that the Implementing Regulations make clear that they do not bear upon Saudi companies acting as service agents,[6] the amended Commercial Agencies Regulations are beyond the scope of this article.[7]

This article first summarizes the effect of the Regulation. It then deals with certain developments since its promulgation which illustrate how it has been interpreted and enforced in conjunction with other Saudi regulations, including the Companies Regulation[8] and the Foreign Capital Investment Code (the Investment Code).[9] It then describes the parameters of the so-called "disguised agency" problem.

II. Summary of the Service Agents Regulation

A. *Requirement for a Service Agent*

The Regulation, in general, requires that all "foreign contractors" including individuals and companies performing consulting as well as construction work for the government of Saudi Arabia, have a service agent.[10]

Article 3 excepts from this requirement foreign companies which have a Saudi partner. In practice, this means that if a foreign company has formed a joint venture with a Saudi national (usually taking the form of a Saudi limited liability company formed after the required approval under the Investment Code is obtained), then as to government contracts of that joint venture, no service agent is required.[11] In order to take advantage of incentives available under the Investment Code, the capital of such an entity

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[5]Minister of Commerce, Decision No. 1897 of 1981.

[6]Article 1 of the Implementing Regulations under Royal Decree M/32 provides that the Regulations do not apply to service agents governed by Royal Decree M/2. Prior to this clarification, it was reasonable to conclude that the two regulations applied concurrently to the Saudi agent acting for a foreign company even only in connection with government business, such representation being simply one form of commercial agency activity.

[7]*See* Cartwright, *The New Saudi Commercial Agencies Regulation*, 16 INT'L. LAW. 443 (1982). As a practical matter, notwithstanding the distinction in the application of the Commercial Agencies Regulation and the Service Agents Regulation between government and private sector business, many Saudi agents are at the same time both commercial and service agents since they represent foreign companies both vis à vis the government and in the private sector. The two regulations, therefore, do overlap in their application to many Saudi companies.

[8]Royal Decree M/2 of 1965.

[9]Royal Decree M/4 of 1979.

[10]A foreign company's agreement with its service agent must be in writing.

[11]On the other hand, the Regulation does not expressly prohibit such a joint venture from having an agent. If its agent is the Saudi partner in the venture, however, there may be a so-called "disguised agency" problem. *See* the discussion at § IV, *infra*. (Prior to the promulga-

must be at least 25 percent owned by Saudis. A joint venture may also take the form of an unincorporated contractual joint venture, a form which is most commonly used when the members want to limit their mutual endeavor to a single project. If the partners in an unincorporated joint venture include foreign companies, each must have a Saudi service agent (either the same or a different one), unless agency is prohibited by virtue of the nature of the government project. If the unincorporated joint venture includes a Saudi member, it is not necessary that the foreign members have a service agent, however.

The Regulation further provides, at article 4, that no agency is permitted, let alone required, in connection with armaments contracts and contracts for "services related thereto," or in connection with contracts between the Saudi government and foreign governments. Unfortunately, the precise scope of the armaments and related services exception has not been consistently defined by practice. Indeed, the position various ministries have taken on the question of what types of contracts constitute armaments or related services contracts sometimes seems inconsistent.[12] Even more unfortunately, the various ministries' position on the question of agency has occasionally come quite late in the tendering process. The "government to government" exception often overlaps with the armaments exception since many contracts involving the sale of arms are of this type. The Saudi-U.S. Joint Economic Commission and the U.S. Department of the Army are also the source of a number of government to government contracts not involving arms or related services, however.

B. *Saudi Service Agents*

The Regulation also imposes certain requirements that Saudis must meet in order to act as service agents. In summary, service agents must be individual Saudis actually resident in Saudi Arabia or Saudi companies which hold commercial registrations permitting them to engage in agency activities, and specifically, to represent foreign companies. If the work required by a given government contract includes principally "consulting services,"

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tion of the Service Agents Regulation, there was no legal requirement that a foreign company performing a government contract have an agent, although for practical reasons most did.).

[12]If a contracting ministry or department instructs bidders that there shall be no agents involved, even with respect to projects which clearly do not involve armaments or related services, the bidders are left in a legal and practical quandary. Articles 1 and 2 of the Regulation oblige such companies to have service agents, but the tendering ministry requires them to represent that they do not. The request for such a representation sometimes is accompanied by the admonition that a false representation will result in being excluded from any further work in the Kingdom. As a practical matter, a contractor has little choice in such a situation. If time permits, it may seek to form a joint venture with its "agent," in lieu of the agency relationship. It may seek to terminate its agent if it already has appointed one, or it can choose not to bid. The agent, of course, will wish to be compensated for any services rendered to date. In view of the "no agency" certification which may be required, such a termination payment probably may not be made contingent on the foreign company's being the successful bidder. Otherwise, it may be deemed a commission, one indicia of agency.

the foreign contractor's service agent must be a Saudi "consulting office."[13] (By contrast, a Saudi joint venture company need not refrain from bidding for consulting contracts with the government because its Saudi joint venture partner is not a Saudi "consulting office.")

C. *Conflicts of Interest*

The Regulation sets forth a series of requirements which generally seek to eliminate certain conflicts of interest in government procurement. For example, article 6 provides that a foreign contractor may have more than one service agent, each involved with separate (different) activities of the foreign contractor. This at least implies that in connection with the same government contract, a foreign company may have only one service agent. Service agents may represent no more than ten foreign companies at any one time.[14] Article 6 does not say that a service agent may only act for one competing bidder for a specific government contract, however. Most agency agreements, if not commonly accepted business practice, exclude such conflicts of interest, but they are not prohibited by the Regulation, and there is no specific requirement that they be disclosed.[15] (If a Saudi agent represents two companies wishing to bid for the same contract, he may "find" one of them another agent, but it is possible that the first agent will arrange to split the second's commission if the referred contractor is awarded the contract.)

The other anti-conflict of interest provision of the Regulation appears at article 9. This prohibits the same agent from acting for foreign companies seeking consulting and construction contracts with respect to the same project. (This provision suggests the correctness of the analysis of the term "consulting office" in other contexts of the Regulation; that is, it is the *role* to be played by a foreign company in connection with a particular government project that is controlling, not the inherent nature of the foreign company.)

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[13]This requirement has caused substantial confusion. Experience indicates, however, that what was intended was to require that a foreign company appoint a Saudi consulting office only if the government contract in question calls for the rendering of consulting services. Put another way, it is the nature of the services called for by a given government contract, not the nature of the potential contractor (*e.g.*, a firm of architects as opposed to a construction company) which controls. Further confusion results from the use of the term "consulting office." For certain purposes at least, by "consulting office" the Saudi Arabian Ministry of Commerce (which regulates such offices) means a firm which combines the talents of individuals (whether as principals or employees) qualified in different specialties within the same discipline; *e.g.*, mechanical and electrical engineers. But it appears that a single "consultant" may act as a service agent.

[14]This provision formerly caused substantial delays in registering foreign companies. This difficulty has been eliminated, however. *See* § III, *infra*.

[15]Fundamental principles of fair dealing under the Islamic Shari'a, the "common law" of Saudi Arabia, may be said to require disclosure.

D. *Limit on Compensation*

Article 8 of the Regulation provides that a service agent must be compensated for its services, and that the commission or fee may not exceed 5 percent of the price of the government contract in question. In practice, a service agent's commission is not frequently less than 5 percent, except in the case of very large contracts or where, by virtue of the foreign company's prior experience in the Kingdom, it requires little assistance from its service agent either in preparing its bid or, upon obtaining the contract, in performing it.

The terms of reference normally applied by many Western businessmen and lawyers (particularly lawyers in the service of certain U.S. government agencies) simply do not permit acceptance of the fact that the services to be performed by Saudi service agents can command the absolute amount of compensation which results from the application of the typical 5 percent measure, even in connection with contracts of modest size. The question, therefore, arises whether a part of the agent's commission is not being (what is politely called) "passed on"[16] to a government official instrumental in awarding the contract. Further, some U.S. companies have adopted corporate policies that test the permissibility of agency commissions by the application of a cost-benefit test. But in the Saudi Arabian frame of reference a cost-benefit analysis is often not the only or even the principal test of whether a commission is justifiable, and the failure of such a test certainly does not imply that a corrupt payment has been made. Rather, commissions are often justified on a simple "but for" basis; i.e., presumably but for the agent, the contractor would have no contract. The Saudi government's official policy, however, is to prohibit mere middlemen or business finders or brokers from acting as service agents.[17]

The government is well aware, of course, that agents' commissions are "built-in" to contractors' pricing. And recently, the "but-for" basis for commissions (even as limited by the 5 percent ceiling) appears to have undergone reexamination by some government officials, mainly senior tech-

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[16]This factor alone probably does not constitute "reason to know," especially if it can be demonstrated (as it probably can be in Saudi Arabia) that the amount reflects the application of a commonly accepted "going rate." Nevertheless, many fear that the "reason to know" standard imposed by the U.S. Foreign Corrupt Practices Act might be met by the failure of a cost-benefit analysis test and little else. A proposed amendment, which passed the Senate, would eliminate the reason to know standard, substituting a standard of liability based upon the direction or authorization by a U.S. concern of a corrupt payment. Authorization could be established expressly or by a "course of conduct."

[17]The Saudi government indicated that it intended Saudi businessmen, not mere "brokers" or "intermediaries" to be service agents and, therefore, the recipients of commissions. *See* communique of Council of Ministers appearing in the OFFICIAL GAZETTE No. 2664, February 25, 1977. Article 10 of the Regulation prohibits an agency relationship whose purpose is to exercise "undue influence or mediation." Presumably, the reason for this is mainly to seek to reduce influence peddling and bribery; but it may also support the notion that the Saudi government wished the benefit of commissions to fall upon those who would most likely use the proceeds to build an indigenous private sector economy; *i.e.*, established Saudi businessmen.

nocrats. Dissatisfaction with the 5 percent commission ceiling provided by the Regulation has been publicly voiced, and suggestions that it be changed have reportedly been discussed within the government. The most likely substitute would presumably be some absolute maximum commission (without reference to the size of the contract), or a sliding scale of maximum commissions depending on the size of the contract, such as was adopted in Abu Dhabi.[18] Reform in this area is probably being resisted by influential members of the Saudi private sector and, therefore, from certain quarters within the government as well.

Another response to the dissatisfaction with the 5 percent commission formulation of the Regulation has been to encourage, if not legally require, large government projects to be open only to foreign companies which bid in joint venture with a Saudi company, without a Saudi agent. The Royal Commission for Jubail and Yanbu, the government agency responsible for development of the two new industrial cities with those names, is in the forefront of this trend. Nevertheless, in substance the same abuse (i.e., overcharging by reason of the payment of what are essentially "commissions") still can, and does, remain in connection with joint venture bids. (*See* the discussion of Disguised Agency at § IV, *infra*).

III. The Regulation and Foreign Company Registration

To understand how the Resolution has been interpreted and enforced, one should be aware of one other Saudi regulation which directly affects foreign companies engaged in performing Saudi government contracts. The Companies Regulation, at article 228, requires foreign companies engaged in business in the Kingdom to register branches. The Ministry of Commerce permits foreign companies whose activities are confined to performing contracts with the government to satisfy this requirement in an expedited but temporary way, by registering a "temporary branch"; i.e., by obtaining, as it is now known, a "temporary license." (For years, this requirement was ignored by many foreign companies and by the Saudi authorities as well.)

About one year after the Regulation was issued, the Ministry of Commerce issued its Resolution 680.[19] Resolution 680 reminded foreign companies of the fundamental fact that if they are to do business in the Kingdom under government contracts or subcontracts, they are supposed to be properly registered to do so. It also provided a short registration grace period.

Temporary licenses are authorizations from the Ministry of Commerce to foreign companies which are Saudi government contractors or subcontrac-

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[18] *See* article 8 of Law No. 4 of 1977 of Abu Dhabi, which limits commissions to 2 percent on tenders up to Dhs 10 million, one and one-half percent on tenders exceeding Dhs 10 million but which are less than Dhs 50 million, and 1 percent on tenders exceeding Dhs 50 million. (As of June 10, 1982 Dh 1.00 = US $0.27.)

[19] Resolution 680 has been subsequently amended. *See infra* note 21.

tors to perform their obligations in the Kingdom. By definition, these licenses are limited to the duration of the government contract or subcontract for which they are obtained (indeed temporary licenses carry an expiration date tied to the date by which performance under the contract is to be completed) and to the types of activities which foreign contractors have agreed to perform thereunder. Activities which are not required by such contracts or subcontracts are not permitted.[20]

The promulgation and enforcement of Resolution 680 also provided a convenient vehicle for the enforcement of the Regulation. As noted, with certain exceptions the Regulation requires most foreign companies with government contracts to have a service agent. It was a simple matter to include in the Resolution 680 temporary license application form, a requirement that a foreign company's service agent furnish a letter to be appended to the form. Without this letter, signed by a Saudi manager of the service agent, the form would not be accepted and the foreign company could not obtain its license.[21] The requirement for a letter from the foreign company's service agent (which formerly had to contain a representation that the agent represented no more than ten foreign companies)[22] has now been eliminated, but a foreign company seeking a temporary license must still demonstrate it has a Saudi service agent by filing a copy of its service agency agreement.[23] (The Ministry of Commerce recently issued a suggested form of service agency contract.)

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[20]In practice, companies with temporary licenses, being prima facie in the Kingdom legally, sometimes engage in activities unrelated to those called for by the contracts on which their temporary licenses are based. But this unrelated activity is illegal.

[21]The Minister of Commerce subsequently issued Decision No. 940, effective October 27, 1981, requiring foreign companies to submit a number of documents in addition to those prescribed by Resolution 680 (including some issued by third parties) in order to obtain temporary licenses. Among other things, a letter from a bank approved by the Saudi Arabian Monetary Agency is required, as are certifications as to the satisfactory performance of prior contracts in the same field. These new requirements were inspired by a Decision of the Council of Ministers, at the insistence of the Saudi Ports Authority, which attempts to respond to complaints about the lack of capacity of certain foreign companies actually to perform the work that their contracts require them to perform. (These new documents are required to extend existing temporary licenses as well as to obtain new ones.)

[22]Some otherwise very straightforward Resolution 680 temporary licenses were undoubtedly withheld for some time while the foreign company's Saudi service agent tried to deal with the problem posed by this representation. The end result was predictable. Large Saudi agencies formed affiliates, among which the agencies' foreign company clients were divided so that no one entity represented more than ten companies.

[23]The Ministry of Commerce also has recently required that foreign companies seeking a temporary license furnish an undertaking to observe the government's requirements to purchase locally manufactured goods appearing on a list provided by the Ministry, to purchase foreign manufactured goods only on the local market from Saudi agents or distributors, if available, and to import their requirements for foreign goods not available in the Kingdom only through Saudi import agents. These new government requirements essentially prohibit foreign companies from importing in their own name goods purchased abroad, even if the goods are for their own use or for incorporation in a government project, a very substantial expansion of the long-standing requirement of the Commercial Agencies Regulation that trading in Saudi Arabia be reserved to Saudis. (*See* note 4, *supra*).

The temporary license application form itself does not permit any exemptions from the requirement that a foreign company have a service agent. Although it was immediately recognized that certain exemptions must have been intended (e.g., for armaments contractors),[24] for some time there was doubt whether government subcontractors had to have a service agent. The Companies Department of the Ministry of Commerce originally took the position that they did, and this was taken by some (including the authors) as substantial evidence that the Regulation was, in general, intended to apply to subcontractors.[25] If the Regulation applied to subcontractors, then presumably they were required to have service agents and to pay them commissions. Further, it was noted that if the main and all principal subcontractors had service agents and each paid its agent 5 percent of the value of its contract, total commissions paid with respect to one government contract would be staggeringly in excess of 5 percent of the main contract price, a result which may not have been intended.

After several months, the Companies Department backed away from its initial position. It issued a supplemental form of undertaking by foreign companies to be filed in conjunction with the basic Resolution 680 temporary license application form when no service agent is required. A foreign company may indicate on this form that it does not have a service agent either because (1) its government contract antedates the Regulation, (2) it is a subcontractor, or (3) its contract is for armaments or related services.[26] The result then is that the Ministry of Commerce has taken the view that, for company registration purposes, although the Regulation does not require a subcontractor to have a service agent, a subcontractor may have one. The Ministry has not reversed its initial position that subcontractors must have agents by providing that they may not. It rather has adopted a neutral position. Indeed, if a foreign subcontractor has an agent, in applying for its temporary license it may not claim the exemption provided by the supplemental undertaking, but rather must furnish the information which the application form requires as to the agent.[27] (To the authors'

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[24]When in doubt, presumably the contracting government ministry's determination that a contract is of this type should be controlling and, if necessary, the contracting ministry should be willing to formally so advise the Companies Department of the Ministry of Commerce.

[25]Notwithstanding that the Regulation itself speaks in terms only of government contractors (*i.e.*, foreign companies in privity of contract with the government and which have bound themselves to perform services in the Kingdom).

[26]The supplemental form does not include reference to the exemption for (non-armament) government to government contracts, but it is generally accepted that this kind of contractor can take the position, for registration purposes, that it is a "subcontractor." More significantly, the Ministry of Commerce also recently indicated that it may entertain applications for temporary licenses by Aramco contractors. Previously, foreign companies seeking to contract with Aramco had to have a Saudi commercial registration; *i.e.*, a permanent branch registration, which requires approval under the Investment Code.

[27]Notwithstanding the argument that the Regulation (including the 5 percent commission ceiling) does not apply at all, if a subcontractor on a government project has an agent, the Ministry of Commerce will not issue a temporary license if the commission to be paid is in excess of 5 percent.

knowledge, no one is suggesting that in addition to a revision of the 5 percent commission ceiling,[28] the Service Agents Regulation be amended to prohibit subcontractors on government projects from having agents. Such an amendment, however, could certainly have a dramatic effect on the cost of government projects.)

IV. Disguised Agency

Foreign companies which are in unincorporated joint ventures with Saudis need have no service agent in connection with government contracts. Similarly, foreign companies which have taken advantage of the incentives available under the Investment Code and the Tender Regulations[29] by forming Saudi joint venture companies, need have no Saudi agents. (The principal incentives are a five or ten year holiday from Saudi Arabian income tax and certain preferences in the award of government contracts.) Under the Investment Code, however, a joint venture company must have a Saudi shareholder who owns at least 25 percent of the capital of the company and, under the Tender Regulations, to achieve second preference, the Saudi company must have at least 50 percent Saudi capital. Nevertheless, venturers sometimes try to structure their joint venture as the economic equivalent of an agency. These arrangements typically are accompanied by the parties' agreement that the Saudi "venturer" need bring nothing to the joint venture except to furnish to it those kinds of services which are normally called for in agency agreements, and that the Saudi is entitled to a share in the company's gross revenue, not net profit, if any. It is not unusual for the Saudi party even to insist that the foreign company contribute to the joint venture company the Saudi shareholder's share of the capital. With accession to that demand, the last vestige of a true joint venture, as opposed to a disguised agency, disappears.[30]

The Saudi Companies Regulation makes it possible to structure a joint venture limited liability company's memorandum of association in a way that probably makes such an arrangement technically enforceable between the parties, and, of course, no such technical problem inhibits the members of an unincorporated joint venture. For various reasons, however, shareholders in Saudi companies may not wish their agreements in this regard to appear in the company's memorandum of association, a public document which must be published in the *Official Gazette*. But one effect of not setting out shareholders' agreements in this regard in a Saudi company's memorandum of association is that they may be thereby rendered unen-

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[28] *See* the discussion at § II.D. *supra*.

[29] Royal Decree M/14 of 1977.

[30] To protect themselves against the possibility that the joint venture company will not have profits sufficient to pay a "minimum" dividend, Saudi "joint venturers" also sometimes insist that their "commission" be guaranteed by the foreign venturer. (A Saudi limited liability company, the only Saudi entity available for most foreign investment, cannot issue preference shares.)

forceable,[31] although, for this reason alone, they probably are not illegal.

Obviously, if the disguised arrangement seeks to guarantee the Saudi shareholder a share of the joint venture company's gross revenue from government contracts greater than 5 percent, a persuasive argument can be made that the foreign company (as well as the Saudi) have, in substance, committed a violation of the Regulation by exceeding the 5 percent ceiling on commissions. One sanction for a violation of the Regulation by a foreign company is that it may be prohibited from engaging in any further business in Saudi Arabia.[32]

Even if a disguised agency arrangement calls for a "commission" to the Saudi shareholder of 5 percent or less of the joint venture's gross revenue, to the extent the joint venture has bid and obtained a government contract based in part on its "second preference" under the Tender Regulations, it may arguably have misrepresented itself to its governmental customer.[33] The Royal Commission for Jubail and Yanbu is quite careful about its being misled by bids of wholly Saudi owned companies, entitled to first preference under the Tender Regulations, where, for example, nearly all or a substantial part of the work called for will be subcontracted to foreign companies. There is no reason that it and other ministries will not become equally wary about second preference bidders.

Finally, under the Investment Code, the holiday from Saudi income tax for the foreign shareholder in a Saudi joint venture company requires that Saudis own at least 25 percent of the company's capital. It is nearly universally recognized that this does not mean that Saudi shareholders must also be entitled to at least 25 percent of the profits of the joint venture company, and, as noted, the Saudi Companies Regulation permits the shareholders to vary their respective shares in profits from their shares of capital by a provision in the memorandum of association.[34] It also apparently is the quite reasonable view of the Foreign Capital Investment Committee,[35] however, that implicit in the requirement that Saudis account for at least 25 percent of the capital, is the notion that they must have an interest in the company which is in fact that of a shareholder, i.e., the Saudi shareholders' capital

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[31] Article 171 of the Saudi Companies Regulation provides that unless the memorandum of association otherwise provides, each shareholder's share in the profits of the company will be the same as his share of the capital. It is possible, however, to provide in the memorandum of association that the shareholders may agree on their respective shares in the profits on a project by project, or annual, basis.

[32] From a U.S. standpoint, a joint venture that disguises an agency relationship probably raises more questions than it answers in terms of justifying the "commission" due.

[33] *See* article 1(d) of the Tender Regulations, *supra* note 31. Note, however, that Article 1(d) measures qualification for second preference only on the proportion of the company's capital that is Saudi owned. (It is doubtful that these preferences have, to date, in practice been important factors in the award of government contracts.)

[34] As noted, such provision usually takes the form of an agreement to agree on the division of profits. Even if a later agreement is binding on the shareholders, it may not be binding on the Saudi tax authorities. *See infra* note 37.

[35] An interministerial body which is attached to the Ministry of Industry and Electricity and which reviews foreign investment applications filed under the Investment Code.

must be at risk and must be more than de minimis.[36] If the disguised arrangements include a guarantee by the foreign shareholder that the Saudi shareholder will receive, at a minimum, a specified percentage of the joint venture company's gross income, that is arguably inconsistent with a basic characteristic of the ownership of capital in a company. This is especially true if the disguised arrangement also requires the foreign company to contribute the Saudi party's nominal share of the capital, or to make the Saudi party a non-recourse loan in the same amount. Upon discovery, the result could be the retroactive revocation of the foreign company's investment license or the withdrawal of benefits made available by the Investment Code, including the tax holiday.[37]

V. Conclusion

The Saudi authorities which deal most frequently with foreign companies, in the context particularly of foreign company registrations, foreign investment applications and government tenders, are becoming increasingly sophisticated in the enforcement of the requirements of the Service Agents Regulation. The Ministry of Commerce has been astute in employing the temporary license device as a tool for enforcing the requirement that foreign companies indeed employ service agents where required, and that they and their service agents observe other applicable legal requirements. Growing dissatisfaction with the Regulation's 5 percent commission ceiling may bring amendments to the Regulation which in turn will require more sophisticated enforcement devices. In the meantime, the phenomenon of disguised agencies poses difficulties with which the Saudi authorities have not yet systematically dealt.

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[36] Even if these two criteria are arguably technically met because the Saudi shareholder actually contributes his share of capital from his own funds and obtains no guarantee of his profit share from the non-Saudi shareholder, the nondisclosure of such an arrangement in the documents submitted to the Foreign Capital Investment Committee could constitute a violation of the Investment Code.

[37] *See* article 23 of the Implementing Regulations under the Investment Code. (It is generally understood that the Foreign Capital Investment Committee has the sole authority to grant and revoke tax holidays, and that the Saudi tax authorities have no independent authority in this regard. Should the tax authorities discover a disguised agency, however, they may bring it to the attention of the Foreign Capital Investment Committee, with the recommendation that the foreign investment license, and the tax holiday, be revoked. Indeed, the Saudi tax authorities have already taken the position that any share of a Saudi company's profit attributed to its foreign shareholders which exceeds their share in the company's capital, is taxable, notwithstanding a tax holiday.)