



**COUNTRY  
COMPARATIVE  
GUIDES 2023**

# **The Legal 500 Country Comparative Guides**

## **Saudi Arabia**

# **ALTERNATIVE INVESTMENT FUNDS**

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This country-specific Q&A provides an overview of alternative investment funds laws and regulations applicable in Saudi Arabia.

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# SAUDI ARABIA

## ALTERNATIVE INVESTMENT FUNDS



### 1. What are the principal legal structures used for Alternative Investment Funds?

Depending on the types of the assets in the fund, Alternative investment funds can be either private or public funds (though private funds are more popular noting that the types of assets allowed in public funds are limited).

Public funds investments may only be securities, money market transactions concluded with a party subject to Saudi Central Bank supervision or equivalent regulator outside the Kingdom, bank deposits with local bank or institution regulated by SCB or an equivalent regulator outside KSA, real estate, and commodities.

Private funds investments can be of any assets regardless the types or descriptions, provided that the fund manager has stated those areas/assets of investment and any applicable policies and/or restrictions clearly in the fund's terms and conditions and in the offering documents.

Typically, the fund takes a contractual form, it is established by signing the terms and conditions of the fund between the first unitholders and the fund manager.

Public Real estate investments funds can in principle take any structure that CMA approves, however real estate investment funds can also be close-ended.

### 2. Does a structure provide limited liability to the investors? If so, how is this achieved?

Yes. It is stated in the applicable Regulations that, except for the loss of investment in the Fund, the Fund's unit holder may not be liable for the debts of the public funds.

### 3. Is there a market preference and/or most preferred structure? Does it depend on asset class or investment strategy?

Funds may be private or public though private are more common, as such no means to ascertain the market preference specially that alternative investment funds are mostly private funds. Assets and investment strategy may be an impacting factor to choose between private and public fund structure.

### 4. Does the regulatory regime distinguish between open-ended and closed-ended Alternative Investment Funds (or otherwise differentiate between different types of funds or strategies (e.g. private equity vs. hedge)) and, if so, how?

No.

### 5. Are there any limits on the manager's ability to restrict redemptions? What factors determine the degree of liquidity that a manager offers investor of an Alternative Investment Fund?

As for public funds, the fund manager may defer fulfilling a request for redemption to the next dealing day if the total redemptions in the day amounts at a total of 10% or more of the net assets value of the fund. As part of the information memorandum, the manager should lay down a fair and equitable procedures to elect which redemption requests are to be deferred.

CMA may order to suspend redemptions. From his side the fund manager may not restrict redemptions unless the manager reasonably believe that suspension is in the best interest of the unitholders, or in case of a suspension of dealing in the principle market in which securities or other assets are dealt, either in general or

in relation of assets which the fund manager reasonably believes to be material to the net asset value of the fund.

In this case the fund manager shall (i) ensure that the suspension remains only for as long as it is necessary and justified having regards to the best interests of the unitholders; (ii) review the suspension in regular intervals and consult with the fund board, the custodian and the fund operator; (iii) immediately inform the CMA and the unitholders of the suspension along with the justifications, and inform the CMA and the unitholders as soon as the suspension ends and publish a notice in this regard in the website thereof and on the exchange website.

The Investment Fund Regulations ("IFRs") provide that the manager of a private fund shall develop, maintain and disclose in the terms and conditions of the fund a clear policy covering the valuation, pricing and dealing in the units. The manager should also adopt a consistent approach to the valuation of the units for the purpose of unit issuance, subscription, transfer and redemption.

## **6. What are potential tools that a manager may use to manage illiquidity risks regarding the portfolio of its Alternative Investment Fund?**

This highly depends on the terms and conditions of the fund and the applied investment strategy. Investment decisions of the manager should conform to well and prudent investment practice and adhere to such terms and conditions. The manager should apply best efforts to ensure: (i) sufficient liquidity to meet anticipated redemption requests; (ii) no concentration in particular assets class, country, geographic area, industry, sector, except to the extent this concentration is disclosed in the terms and conditions; (iii) ensuring a prudent distribution of risks while having due regard to the investment objectives, policies and the terms and conditions.

Also the manager is under a duty to exert effort to ensure that sufficient liquidity is available to meet any foreseen redemption application in case the investment fund is open-ended.

As regards public funds, the IFRs provide certain restrictions on the manager's freedom, for example (i) the manager may not invest the assets or monies of the fund in assets that impose any liability to the obligation of a third party or any other liability towards any person whatsoever (ii) Assists and monies of the fund may not be used to buy an asset that results in unlimited liability

on the fund (iii) investment of the fund in other funds is subject to a set of restrictions.

Non-specialised public investment funds (i.e. funds other than specialised investment funds are financial market funds, feeding funds, holding funds and capital protection funds) are subject to intensive investment restrictions unless they enjoy an exemption from CMA, while most of those restrictions relate to investment in securities, debentures and the like, following examples may be relevant: (i) No more than 15% of the net value of the fund may be invested in derivative contracts, (ii) No more than 10% of the net value of the fund may be invested in non liquidable assets, (iii) No more than 25% of the net value of the fund may be invested in another fund, (vi) investment in assets belonging to the same group may not exceed 25% of the net total assets of the fund.

As for real estate funds, the manager is under an obligation to manage available liquidity for the benefit of unitholders in low risk investment channels and without charging additional management fees to the invested amounts. Borrowing is also restricted to 50% of the fund's monies and assets as per latest audited financial statements unless the fund is listed in the parallel market, were borrowing may not exceed 100% of such assets.

## **7. Are there any restrictions on transfers of investors' interests?**

Yes. Transfer of funds unit after the first issuance may only be made (i) to existing unit holders or (ii) to sophisticated investors; or (iii) where the minimum amount payable for such units is not less than 1 Million SAR or its equivalent (approximately US\$265,000).

As for real estate funds, as a general rule, related parties may not sell any units in the fund during the fund's period, however, a unit holder who subscribed to the fund in return to a cash right and whose ownership exceeds 5% of the net assets of the real estate investment fund may sell the units thereof unless the same is considered a 'related party' other than by virtue of such ownership.

## **8. Are there any other limitations on a manager's ability to manage its funds (e.g., diversification requirements)?**

This highly depends on the terms and conditions of the fund and the applied investment strategy. Investment decisions of the manager should conform to well and prudent investment practice and adhere to such terms

and conditions. The manager should apply best efforts to ensure (i) sufficient liquidity to meet anticipated redemption requests; (ii) no concentration in particular assets class, country, geographic area, industry, sector, except to the extent this concentration is disclosed in the terms and conditions; (iii) ensuring a prudent distribution of risks while having due regard to the investment objectives, policies and the terms and conditions.

Certain restrictions apply to real estate funds. Non-specialised public investment funds are also subject to a number of diversification requirements. See answer to 6 above.

**9. What is the local tax treatment of (a) resident, (b) non-resident, and (c) pension fund investors (or any other common investor type) in Alternative Investment Funds? Does the tax treatment of the target investment dictate the structure of the Alternative Investment Fund?**

Generally the income of non KSA nationals residing in the Kingdom, and non residents is subject to a 20% income tax. Tax treatment does not have an impact on the fund's structure.

**10. What rights do investors typically have with respect to the management or operations of the Alternative Investment Fund?**

Below are the major rights that investors have.

1. The manager is under an obligation to develop a policy for meetings of unitholders
2. Certain decisions require the prior consent of unitholders (in the form of an ordinary decision); namely: (i) a change which significantly alter the purposes, nature or objectives of the fund; (ii) a change that alters the risk profile; (iii) a change that results in a material increase of the aggregate payments made out of the assets of the close-ended fund; (iv) a change that results in negative or material effect on the rights of unitholders in the close-ended fund and/or (v) a change of the due date or maturity date of the private fund.
3. In case the fund is open-ended, unitholders have the right to redeem their unites before the changes enter into effect and without

obligation to pay redemption fees.

4. Fund managers are required to prepare annual and short form reports to be provided for unitholders upon request without a charge no later than 70 days from the end of the relevant period.

Major restrictions on investors are:

1. The requirement of disclosure to Exchange when a unitholder becomes the owners of more than 5% of the fund units.
2. The restrictions applicable on the transfer of interests (please see 7 above).

**11. Where customization of Alternative Investment Funds is required by investors, what types of legal structures are most commonly used?**

We are unaware of a particular/ prevailing practices in this regard.

**12. Are managers or advisers to Alternative Investment Funds required to be licensed, authorised or regulated by a regulatory body?**

Yes. Managers need to be Authorised Person from CMA to exercise management business, and advisors need to be Capital Market Institutions (i.e. authorised persons) to provide advisory services (unless the advisory service to be provided relates to investments outside KSA, in which case the advisor need to be regulated by a regulatory authority that applies standards equivalent to those applied by CMA).

**13. Are Alternative Investment Funds themselves required to be licensed, authorised or regulated by a regulatory body?**

Yes.

Establishment of, and placement of units in public fund and real estate fund need an approval from CMA, and an application for approval shall be submitted to CMA. CMA may approve the application in whole or in part, approve the application subject to such conditions and limitations as CMA considers appropriate, or refuse the application, giving reasons.

As to a private fund, a notification of the establishment

of the fund needs to be submitted to CMA. Placement should be private and should follow a series of notifications and submissions that shall be made to CMA. Although this is not a licencing/ authorisation process, CMA has the power to carry on enquiries and/or require additional information and may ultimately decide that the placement may not be made if it believes it is not commensurate with the abilities of the manager.

Subject to meeting certain requirements, foreign investment funds are not required to establish themselves in the jurisdiction however they shall utilise the services of a local distributor (who should be Authorised Persons to do the business of arranging or management for the placement of fund units and the distributor shall undertake to the process of private placement and make the necessary submissions to CMA the type of license required will change as of 1 January 2022, where such distributor will need to hold a an authorisation for dealing )or investment management and fund operation)).

#### **14. Does the Alternative Investment Fund require a manager or advisor to be domiciled in the same jurisdiction as the Alternative Investment Fund itself?**

Yes. Local investment funds should be managed by a Capital Market Institution that is authorised by CMA and such Institution will necessarily be a KSA company.

As for foreign investment funds, those will typically have a foreign manager however unites thereon may not be offered for placement in the Kingdom except by a local Distributor (Please see answer 13), and the local distributor shall have attended to the registration requirements before placement.

#### **15. Are there local residence or other local qualification or substance requirements for the Alternative Investment Fund and/or the manager and/or the advisor to the fund?**

Yes. The manager should be a KSA company authorised by CMA (some authorised local companies in the sector are subsidiaries to foreign companies). Please refer to answer 2.2

Certain jobs within the authorised company may only be undertaken by full time, resident officers.

#### **16. What service providers are required by**

#### **applicable law and regulation?**

One or more custodian authorised by CMA shall be appointed to take custody of the investments of the fund. The custodian should not be a fund manager or sub-manager to the fund or an affiliated to the aforementioned.

The manager is at the option to appoint a sub-manager, advisor, or distributor who must be authorised by CMA. Also, the manager may appoint a sub-manager operating outside KSA to manage foreign investments of the fund and the sub-manager may not be authorised by CMA, provided that sub-manager is regulated by a regulatory authority that applies equivalent standards to those applied by CMA.

The fund manager need to hold a license for management and fund operation, where the manager only holds a license for management, the same shall engage another Capital Market Institution that holds funds operation license to undertake to the operation of the fund.

#### **17. Are local resident directors / trustees required?**

Yes. It is assumed that the director/ trustee of the manager be registered with CMA and resident in KSA.

#### **18. What rules apply to foreign managers or advisers wishing to manage, advise, or otherwise operate funds domiciled in your jurisdiction?**

As a general rule, advisors and managers may not provide their services in KSA unless they are local companies authorised by CMA.

The manager may avail from the services of a foreign advisor in regard to the investments/ assets of the funds that are outside KSA provided that such advisor is regulated by a regulatory authority that applies equivalent standards to those applied by CMA.

#### **19. What are common enforcement risks that managers face with respect to the management of their Alternative Investment Funds?**

A breach of the provisions of the law or the regulations may result in the application of the following sanctions:

1. Warning the person concerned.
2. Obliging the person concerned to cease or refrain from carrying out the act which is the subject of the suit.
3. Obliging the person concerned to take the necessary steps to avert the violation, or to take such necessary corrective steps to address the results of the violation.
4. Obliging the violator to pay up to three times the gains realized or the losses avoided as a result of the violation to the account of CMA, or compensating the persons who sustained damages as a result of the violations committed.
5. Suspending the trading in the Security.
6. Barring the violating person from acting as a broker, portfolio manager or investment adviser for such period of time as is necessary for the safety of the market and the protection of investors.
7. Seizing and executing on property.
8. Travel ban.
9. Barring from working with companies falling under the authority of CMA.

CMA may as an alternative impose one or more of the following measures:

1. Warning the person concerned.
2. Obliging the person concerned to cease or refrain from carrying out the act which is the subject of the suit.
3. Imposing a fine on any violator up to Five Million SAR for each violation committed.

## **20. What is the typical level of management fee paid? Does it vary by asset type?**

The percentage ranges usually between 0.25 percent to 1.50 percent of the total assets of the fund. It is not usual that the fee vary by asset type (we have seen funds with multiple types of assets but the percentage applies across the board).

The fee may in less common instances be a percentage of the subscription (e.g. 2%) to be collected in advance from the subscribers.

## **21. Is a performance fee typical? If so, does it commonly include a "high water mark", "hurdle", "water-fall" or other condition? If so, please explain.**

The regulations allow incentives and other performance related bonuses provided that such terms are disclosed in the fund's T&Cs. Our observation is that this is not so common for public funds. As for private funds, we lack the means to ascertain this. In general, any interest-based scenario is not common.

## **22. Are fee discounts / fee rebates or other economic benefits for initial investors typical in raising assets for new fund launches?**

The regulations do not prevent this provided that such terms are disclosed in the fund's T&Cs. Our observation is that this is not so common for public funds. As for private funds, we lack the means to ascertain this.

## **23. Are management fee "break-points" offered based on investment size?**

The regulations do not prevent this provided that such terms are disclosed in the fund's T&Cs. Our observation is that this is not so common for public funds. As for private funds, we lack the means to ascertain this.

## **24. Are first loss programs used as a source of capital (i.e., a managed account into which the manager contributes approximately 10-20% of the account balance and the remainder is furnished by the investor)?**

The regulations do not prevent this provided that such terms are disclosed in the fund's T&Cs. Our observation is that this is not so common for public funds. As for private funds, we lack the means to ascertain this.

## **25. What is the typical terms of a seeding / acceleration program?**

We are unaware of such terms.

## **26. What industry trends have recently developed regarding management fees and incentive/performance fees or carried interest? In particular, are there industry norms between primary funds and secondary funds?**

The method of calculation may vary, examples are a



percentage of the average value throughout the year, percentage of the sum invested, and percentage of the annual value of the assets as is in the valuation days. In general, any interest-based scenario is not common.

## **27. What restrictions are there on marketing Alternative Investment Funds?**

Marketing materials for public funds should disclose the method of acquiring the Fund's T&Cs, information memorandum, and reports, and a referral to the statement of risks as provided in the T&Cs.

Information regarding the performance of the fund or its manager are allowed subject to meeting extensive conditions that ensure transparency towards potential investors. Marketing materials should be provided to CMA within 5 days from their date.

It is forbidden that the advertisement contain a speculation of the return or the investment performance (except where there is a minimum guaranteed were applicable), nor a testimony or statement by the actual or presumed owners of units in the fund or other funds managed by the same manager.

As for private funds, marketing may only be directed to the category of investors to which a private placement may be offered.

Advertisements (which means any kind of communication whatsoever with the view of promoting/convincing an investor to participate in the fund may only be made by an authorised person or at least the content of the advertisement should be approved by an authorised person.

Advertisements are subject to detailed stipulations that revolve around transparency, clarity, fairness, and completeness.

Direct contact for marketing purposes requires that the recipient consent to receiving the call or that the same reasonably predict receiving such calls having regards the relation with the caller.

As for real estate funds, all marketing materials should be submitted to CMA before use, the regulation provides for particular data to be provided in the marketing materials, namely method of acquiring a copy of the funds terms and conditions and financial reports, purpose, capital and term of the fund, CMA approval number and date and other official approvals, a statement that the value of investment is variable, and a referral to the statement of investment risks as provided in the T&Cs. The marketing material should not provide

any speculation for the future performance of the fund.

## **28. Is the concept of “pre-marketing” (or equivalent) recognised in your jurisdiction? If so, how has it been defined (by law and/or practice)?**

No.

## **29. Can Alternative Investment Funds be marketed to retail investors?**

Yes. As per a new amendment to the regulations effective as of 1 January 2022, private placement of private investment funds and foreign investment funds may be marketed to retail investors; maximum to be subscribed by retail investors is SAR 200,000 or the equivalent (approx. USD53000).

## **30. Does your jurisdiction have a particular form of Alternative Investment Fund be that can be marketed to retail investors (e.g. a Long-Term Investment Fund or Non-UCITS Retail Scheme)?**

There are two categories of investment funds that can be marketed to retail investors, those are private funds and foreign funds, however there is no specific category of funds that is dedicated to retail investors.

## **31. What are the minimum investor qualification requirements for an Alternative Investment Fund? Does this vary by asset class (e.g. hedge vs. private equity)?**

As for the time being, the qualification requirements are as follows:

- To qualify as a potential investor, the client should be a Sophisticated Investor or otherwise the minimum subscription value shall be no less than one (1) million Saudi Riyals (“SAR”) or equivalent (approximately US\$265,000). Please see the answer for Question 4.4 for details.
- Sophisticated Investors are
- “Authorized Persons acting for their own account;
- Clients of a person authorized by CMA to conduct managing activities provided that: a. The offer and all relevant communications are

made through an Authorized Person; b. The Capital Market Institution has been appointed as an investment manager and is enabled to decide to accept the offers on the client's behalf without reference to the Client;

- The government of Saudi Arabia, any supranational authority recognized by CMA, the Exchange and any other stock exchange recognized by CMA or the Depositary Centre;
- Investment Institutions acting for their own account;
- Professional Investors;
- Registered persons with a Capital Market Institution if the offer is made through the respective Capital Market Institution itself; and
- Any other persons prescribed by CMA.

"Investment Institutions" are defined as:

- "any company which owns, or which is a member of a group which owns, net assets of not less than 10 million SAR (approximately US\$2.65m);
- any unincorporated body, partnership or other organization which has net assets of not less than 10 million SAR; and
- any person ("A") whilst acting in the capacity of director, officer or employee of a person ("B") falling within sub-paragraphs (1) or (2) where A is responsible for B undertaking any securities activity")."

As of 1 January, 2022, offering may only be made to Qualified Investors, Institutional Investors, and retail investors provided that the minimum subscription be no less than 200,000 Saudi Riyals (approx. 53,000 USD).

### **32. Are there additional restrictions on marketing to government entities or similar investors (e.g. sovereign wealth funds) or pension funds or insurance company investors?**

No.

### **33. Are there any restrictions on the use of intermediaries to assist in the fundraising process?**

1. The use of sub-contractors and distributors shall be made by virtue of a written agreement,
2. The sub-contractor or the distributor should

be an Authorised Person to provide management services.

3. The sub-contractor or the distributor should be a Capital Market Institution Authorised by CMA to provide management services. (As of 1 January 2022, the same shall be licensed by CMA to provide investment management or investment management and fund operation.
4. The use of a foreign sub-manager established in a jurisdiction and be subject to the standards of a regulatory body equivalent to those applied by CMA is possible in relation to assets not located in KSA.
5. The fees due for the sub-contractor or the distributor shall be paid from the own resources of the manager.

### **34. Is the use of "side letters" restricted?**

The CMA regulations does not allow nor disallow the use of side letters with explicit provisions, however the manager is under an obligation to treat investors with transparency and fairness and without discrimination, therefore side letters may be perceived as a breach of the required equal treatment.

The CMA dispute settlement committees (which enjoy a quasi judicial capacity) have not been seized with the opportunity to examine side letters according to our best knowledge.

Although regular courts are not competent to look into securities disputes (which competence is seized to CMA committees), their precedents may give a speculation on how side letters may be perceived by the committees. The courts usually give effect to side letters regarding the relation between its parties in so far as no public order issues are involved. If the dispute involves a third party the third party may invoke the side letter if s/he can prove its existence and content in a legitimate manner or otherwise invoke the stimulated contract. It is presumed that side letters in relation to investment fund management be perceived the same way (so long as they do not alter imperative provisions).

### **35. Are there any disclosure requirements with respect to side letters?**

No. However please see our answer to Q 34.

### **36. What are the most common side letter terms? What industry trends have recently developed regarding side letter terms?**



Please see our answer to Q 34.

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