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ASG Analysis: Saudi Arabia Extends Local Content Requirements to State-Owned Entities

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Key takeaways

- On June 21, Saudi Arabia's Council of Ministers approved new regulations that require companies that are majority-owned by the Saudi government to comply with the regulations of the Local Content and Government Procurement Authority (LCGPA). This may have significant implications for companies that do business with the likes of Aramco, SABIC, Ma'aden, STC, and other large Saudi state-owned enterprises (SOEs).

- These enterprises must now give favorable treatment to local content and small and medium enterprises (SMEs), as well as track and report local content usage to the LCGPA.

- The updated regulations, which we expect will be enforced gradually, are in line with Vision 2030 Saudization efforts to increase localization across all sectors, industries, and processes. They represent an expansion of local content rules that were announced in 2019.

- To prepare for these new regulations, companies should review their exposure, begin preparing for compliance, and build relationships with local producers in relevant industries.

Background and context

The Saudi Council of Ministers issued a decision (Cabinet Resolution 658) that extends Saudi Arabia's local content laws beyond government procurement to include procurement by companies in which the state holds a 50 percent stake or more. This could include companies owned by a Saudi government agency or ministry, the Saudi Public Investment Fund (PIF), or another state-owned organization or investment body. Extending local content policies to SOEs will in turn have implications for organizations that are suppliers to these companies, requiring that they meet a variety of local content requirements (see below) to be enforced by the LCGPA.

Original laws covering government procurement

The LCGPA was established in 2019 (see our previous analysis) with the mandate of formulating and enforcing policies and regulations to develop local employment opportunities and boost the national economy through local content and local manufacturing regulations.

Upon the establishment of the LCGPA, all government agencies should have been subject to local procurement laws in the below areas:

- **Measurement:** Any agency applying for a government contract or soliciting a request for proposal from a given vendor would require that all vendors interested in bidding provide their local content score. Some projects are required to meet a minimum threshold.

- **Commitments:** If a given vendor has not used enough local content, they would be disqualified from a bid and, in some cases, asked to commit to a certain score by the end of their contract.

- **Mandatory local content products:** If a given product is available locally from a sufficient number of suppliers in the Kingdom (enough to have a competitive sector and avoid a monopoly), agencies are required to use locally produced products and forbidden from importing said product.

Original local content and procurement laws were not enforced until recently; it took time for the LCGPA to establish itself and understand how to implement the above regulations in practice. The Saudi government just recently began enforcing these laws on the highest value contracts (over SAR 50 million).

New regulations to cover state-owned enterprises

The June 21 decision extends local content regulations to companies that are majority-owned by the state. These new regulations may have a major impact on companies that do business with SOEs. As of last month, any company majority-owned by the Saudi state must track its own local content score and comply with the below rulings when soliciting vendor proposals:

- **Mandatory list of national products:** Companies must comply with an LCGPA-provided list of national products based on requests from manufacturers. Any national products on this list must be purchased locally.

- **Mandatory reporting:** Companies must report annually their local content score.

- **Price preference for SMEs:** All contracts with an estimated cost of less than SAR 50 million ($13.3 million) can buy local products at a 10 percent premium.

- **Price preference for local content:** National products may be given a price preference.

- **Weighting of local content score:** As part of a financial bid, the weighting of a vendor's local content score must not be less than 30 percent.

Timeline for compliance

The LCGPA has given companies a clear timeline for compliance. These new regulations enter effect on December 18, 2022.

Within a year of the regulations' entrance into force – i.e. by December 18, 2023 – all companies that are 100 percent owned by the Kingdom must be in compliance. For companies in which the government holds more than a 50 percent stake but less than 100 percent, the regulation encourages compliance within the first year and makes it mandatory after that.

If past is precedent, though, it may take some time for the LCGPA to figure out how the new regulations will take effect for SOEs. We expect that they will be enforced over time.

Implications for companies doing business in the Kingdom

While many companies working in the Kingdom, state-owned or otherwise, already had internally developed local content programs in de-facto support of Vision 2030, these programs will no longer be sufficient. CEOs now face compliance and reporting requirements from LCGPA.

To prepare, companies that do business with the government and SOEs should:

- **Start thinking about compliance.** Understand your exposure and what amount of your business is currently conducted with Saudi SOEs.
- **Prepare for compliance.** Begin understanding the rules, details, and key stakeholders of the LCGPA.
- **Build relationships with local producers in given industries.** Creating relationships with local content producers in relevant industries is key to ensure competitive pricing, efficient procurement agreements, and effective partnerships.

Companies should also consider recent efforts to attract multinational companies to the Kingdom with the new Regional Headquarters (RHQ) program (see our previous analysis). It is possible that the RHQ program will fold into LCGPA requirements – meaning that all companies that sell to SOEs would need to have regional headquarters in Saudi Arabia.

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