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ASG Analysis: What Does the Saudi Regional Headquarters Program Mean for Companies Doing Business in the Region?

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Key takeaways

- Over the past year, Saudi Arabia has intensified its efforts to attract multinational companies to the Kingdom. This is in line with broader efforts under Vision 2030 to diversify the economy, create employment opportunities, and attract foreign direct investment.
- The Saudi government has chosen a carrot-and-stick approach to encourage companies to relocate their regional headquarters to the Kingdom. The stick took the form of a February 2021 official announcement that multinational companies with regional headquarters outside Saudi Arabia will no longer be eligible for government contracts starting in 2024 (see previous ASG Analysis).
- The carrot is the broader Regional Headquarters (RHQ) program launched last year by the Saudi Ministry of Investment (MISA), which plans to offer multinational companies a variety of incentives in exchange for establishing their regional headquarters in the Kingdom.
- At this point, there is still a great deal of uncertainty about the Saudi RHQ push. For example, it is still unclear exactly how Riyadh will implement the RHQ policy, what changes companies will need to make to their regional corporate structures to comply with the policy, or what incentives will be available to companies that relocate their regional headquarters to the Kingdom.
- Another important question is how the UAE will respond to companies that relocate their RHQs to Saudi Arabia. Publicly, the UAE has signaled that it welcomes healthy competition with the Kingdom. Privately, however, Emirati leadership is concerned.
- Multinational companies doing business in the Gulf (especially those that have significant business with the Saudi government) cannot afford to ignore the RHQ program. Companies should proactively engage with relevant Saudi and Emirati stakeholders to avoid being caught in the middle of the growing economic competition between the two longstanding allies.
- Companies should also take the time now to develop clear strategies to respond to the Saudi RHQ push. These strategies should be well-rounded and holistic, encompassing organizational, tax, operational, legal, and political dimensions. (See here for more on the considerations for companies.)

What is an RHQ?

MISA has developed a specific and relatively narrow definition of an RHQ and a set of requirements for companies to qualify for an RHQ license. These requirements have been laid out in RHQ program documents but not yet enacted into law, which leaves them open to change as MISA begins to implement the policy.

An RHQ is **currently defined** as a unit of a multinational company established under the laws of Saudi Arabia for the purpose of supporting, managing, and providing strategic direction to its branches, subsidiaries, and affiliates operating in the MENA region.

To be eligible for an RHQ license, the RHQ must:

- Operate as a registered foreign company or branch in Saudi Arabia with its own separate legal entity;
- Have a physical office and act as the "center of administrative power" in the region;
- Cover subsidiaries or branches of the company located in at least **two different countries** other than Saudi Arabia and the country of incorporation; and
- Not conduct any commercial operations (defined as activities that generate revenue).

The RHQ must provide all the **mandatory licensing activities** including (among others) formulating, monitoring, and coordinating regional strategy; reviewing financial performance; business planning and budgeting; and operational and financial reporting.

The RHQ must also provide at least three of the **optional licensing activities** such as sales and marketing support; human resources and personnel management; accounting, logistics and supply chain management; research and development; and operations control.

What else do we know?

- **The original RHQ statement is sweeping in scope.** The February 2021 government statement announcing that companies with RHQs located outside the Kingdom will be barred from government contracts starting in 2024 is both vague and sweeping. The statement indicates that the ban will apply to contracts with all government agencies, institutions, funds, and possibly government-owned enterprises. On the other hand, the language of the statement telegraphs a degree of uncertainty and leaves the door open to future adjustments. For example, it says only that the government "intends" to stop contracting with companies that have RHQs outside the Kingdom, not that it definitively will.
- **The RHQ program is a priority for Saudi leadership**. Several signs point to the RHQ issue being a top priority for the Saudi government. First, the publication of the RHQ policy announcement last February was accompanied by an organized promotional push on social media involving senior Saudi officials. The ministers of investment, finance, and labor, as well as the head of the Council of Saudi Chambers, all issued strong public statements in favor of the policy. Since then, the Saudi government has made a big show

of announcing the names of companies that have agreed to establish regional headquarters in the Kingdom (see more below).

- **The broader direction of Saudi policy is clear.** The RHQ program is consistent with broader efforts under Vision 2030 to diversify the economy, create employment opportunities for Saudis, and attract foreign direct investment (FDI). The Saudi government may believe that the only way to meaningfully increase local investment by foreign companies is to bring their leadership to the Kingdom. Increased competition between Saudi Arabia and the UAE (particularly Dubai) for FDI is a logical consequence of the RHQ push but not the primary driver.

- **Companies are already taking this seriously.** At the annual Future Investment Initiative (FII) conference in October 2021, MISA announced a list of nearly two dozen multinational companies that had signed MOUs agreeing to establish a regional headquarters in the Kingdom. Most of these companies are in sectors that depend heavily on the Saudi government for business, such as engineering and construction, pharmaceuticals and medical devices, technology products and services, and consulting. The language of the MOUs was very high-level and did not require companies to make any binding commitments. Companies only had to state their intent to establish an RHQ in Saudi Arabia that would cover the MENA region.

- **The contours of an incentive package are taking shape.** The RHQ program will offer a package of incentives for companies to establish regional headquarters in the Kingdom. MISA is still ironing out the details of the incentives and obtaining the necessary legal authority to offer these incentives from different Saudi government ministries. The current draft incentives package includes various labor and visa policy exemptions, including a 10-year exemption from Saudization requirements; spousal work permits and extension of the dependent age limit to 25 years old; exemption from visa limits and accelerated visa issuance; and waiver of professional accreditation requirements. These incentives would only apply to the RHQ function itself, not to a company's normal commercial operations in the Kingdom. MISA has reportedly reached an agreement with the Ministry of Human Resources and Social Development, which is responsible for labor policy issues, to offer these incentives, though no official announcement has yet been made. It is still unclear whether the RHQ program will include any tax incentives (see below).

Outstanding questions

There are numerous areas of technical and strategic uncertainty related to the Saudi RHQ push.

- **How strictly will the Saudi government enforce the RHQ policy?** This is probably the most pressing question for most multinational companies doing business in the Kingdom. It is not clear that the Saudi government will be able to strictly enforce the policy banning companies with RHQs outside the Kingdom from qualifying for government procurement, especially in the case of companies that bring unique skills, brands, or services. If past is precedent, the Saudi government will allow flexibility to make exceptions and may opt to enforce the policy gradually or selectively. For example, in 2016 the Saudi government began allowing foreign companies to obtain trading licenses without a local partner in exchange for making significant commitments to local investment within the first five years.

The government ended up taking a selective approach to approving license applications, based on the perceived credibility of the company and its investment plans, and has done comparatively little follow-up to ensure that companies are meeting their commitments.

- **What will constitute an RHQ in practice?** Although MISA has developed an RHQ definition that is quite specific on paper, it is still unclear how the ministry will apply this definition to the numerous different possible regional structures that could arise, especially those that abide by the letter but not the spirit of the policy. For example, could a company add two smaller Gulf markets (e.g., Bahrain and Kuwait) to its existing Saudi branch while continuing to manage the other MENA markets from Dubai? Could a company move the regional headquarters for only one of its business units or divisions? Alternatively, could a company simply declare that it no longer has a regional headquarters at all and thereby evade the RHQ policy altogether? In principle, all these configurations could comply with the letter of the RHQ policy, but ultimately RHQ licenses will be issued on a case-by-case basis, and companies should take care to consider the potential downsides of appearing to circumvent the policy.

- **What about tax incentives?** When the RHQ program was first announced, program documents listed various tax incentives, but these were notably removed from more recent versions. The tax incentives question is much broader than the RHQ program and involves stakeholders beyond MISA. In parallel to the RHQ program, the Saudi government is creating a number of special economic zones (SEZs) to help attract investment in high-priority sectors, especially manufacturing and exports. The push is being led by the Economic Cities and Special Zones Authority (ECZA), which is chaired by the Minister of Investment, Khalid Al-Falih. We understand that the SEZ regulatory framework is being finalized and will likely include significant tax incentives, such as long-term tax holidays and the waiving of restrictions on foreign ownership and capital repatriation. RHQs may receive special tax incentives within the SEZs, or possibly even outside of them, but this is not clear yet. Discussions involving MISA, ECZA, the Ministry of Finance, the General Authority for Zakat, Tax, and Customs Authority (ZATCA), and other relevant stakeholders are still ongoing and have proven challenging thus far. Companies that rush into establishing RHQs in the Kingdom may soon find themselves considering another move to an SEZ.

- **How will the UAE respond?** Publicly, the UAE has maintained that it welcomes healthy competition with the Kingdom. Privately, however, the RHQ program is one of the top three concerns of Emirati leadership (alongside national security and economic diversification). Growing competition from Saudi Arabia including and beyond the RHQ program is spurring further reforms in the UAE aimed at enhancing the country’s economic competitiveness. Whereas Saudi Arabia is upping pressure on companies to invest and hire locally, the UAE is further relaxing rules around foreign labor while encouraging companies to invest in the local economy. For example, Dubai recently announced that it will issue five-year visas for foreign workers and allow people to live in the emirate for up to six months after leaving a job. The UAE seems to be betting that by reinforcing the advantages that made it a regional business hub in the first place it can preserve its status as the preferred location for companies’ regional headquarters.

Considerations for business

While much is still unclear about the RHQ program, companies should not take a passive approach. Below are several steps that companies (especially those that depend heavily on Saudi government procurement) should consider taking in the coming months to mitigate potential risks to their business.

- **Make good-faith gestures.** While we wait for the details of the RHQ program to become clearer, companies should focus on the policy's spirit and consider ways they can proactively demonstrate their commitment to the Kingdom. It is important for companies to communicate that they understand the importance of the RHQ program and to make sure that their Saudi government interlocutors are aware of the steps they are already taking in terms of localization and local investment. Good-faith gestures at this early stage will win goodwill and help companies position themselves favorably in future discussions.

- **Engage with RHQ program stakeholders**. Companies should start engaging early with officials at MISA who are leading the Saudi RHQ program, as well as with other important investment and localization stakeholders such as the Royal Commission for Riyadh City (RCRC), which is leading a massive project under Vision 2030 to transform Riyadh into a leading business hub. By investing in these relationships now, companies will be better able to keep apprised of new developments related to the RHQ program and the incentives available for relocation. Companies should take care to verify that any government stakeholder who makes promises regarding incentives has the legal authority from other relevant government entities to offer those incentives, good intentions and wishful thinking aside. RHQ licenses will eventually be issued on a case-by-case basis, so strong relationships with RHQ program leadership and other relevant stakeholders will be crucial if and when companies decide to establish an RHQ in the Kingdom.

- **Preserve key relationships in the UAE**. Companies that are considering changes to their regional corporate structure in response to the RHQ program should proactively take steps to preserve their relationships with key stakeholders in the UAE. Companies should engage in honest and respectful conversations with their Emirati counterparts about the RHQ program, reassure them of their continued commitment to the UAE, and sensitize them to any possible changes in corporate footprint in the UAE. We have heard anecdotally of companies facing blowback in the UAE from officials who felt blindsided when Saudi Arabia announced companies' plans to establish an RHQ in the Kingdom.

- **Develop a broader strategy.** Given the sensitivities from a legal, geopolitical, and stakeholder management perspective, companies should take the time now to develop a clear overarching strategy to respond to the RHQ program in a way that minimizes the potential business risks related to the policy and ideally maximizes the benefits of RHQ relocation, while preserving key relationships in the UAE. This strategy will need to be well-rounded and holistic, encompassing organizational, tax, operational, legal, policy, and political dimensions. It should consider the broader policy context in Saudi Arabia; beyond the RHQ push, the government's focus on localization (in terms of both content and employment) and cost-efficiency is here to stay. The strategy should also take into account the reality of growing economic competition between Saudi Arabia and the UAE, which will play out in different ways in years to come.

Advice from our experts

Imad Al-Abdulqader

Head of ASG's Office in Riyadh

Saudi expert on investment and regulatory issues; Former Director of Investor Attraction at the Saudi Arabian General Investment Authority (SAGIA)

> "No company that does business in Saudi Arabia can afford to ignore this. Despite some short-term uncertainty, the long-term direction is clear."

> "UAE leadership is closely watching Saudi Arabia's next moves and will look for innovative ways to stay ahead. Smart companies will seek to build stronger relationships in both countries."

Jan Kamphuisen

Head of ASG's Office in the UAE

Expert in UAE government relations; Ran political risk consulting in the MENA region for a leading global risk consultancy

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ASG's Middle East & North Africa practice has extensive experience helping clients navigate markets across the region, especially Saudi Arabia and the UAE. For questions or to arrange a follow-up conversation with our experts please contact Michael Bessey.