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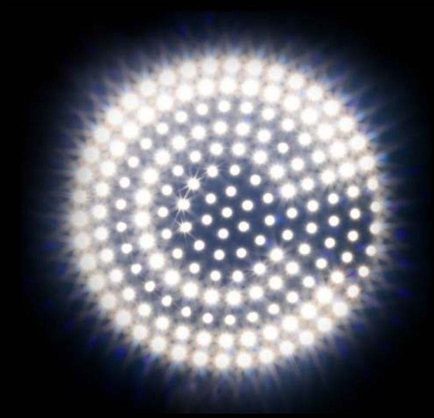
International Tax
Saudi Arabia Highlights 2018



Investment basics:

Currency – Saudi Riyal (SAR)

Foreign exchange control – No

Accounting principles / financial statements – Saudi Organization of Certified Public Accountants (SOCPA) standards generally are used. If an issue is not covered by SOCPA standards, IFRS is the standard. Saudi Arabia is in the process of transitioning to IFRS. Banks and insurance companies use IFRS. Listed companies were required to adopt IFRS from the financial period beginning from 1 January 2017, with 1 January 2016 being the transition date for IFRS convergence (the beginning of the earliest comparative year). Other entities are required to adopt IFRS from the financial period beginning from 1 January 2018, with 1 January 2017 being the transition date for IFRS convergence.

Principal business entities – These are the limited liability company (LLC), joint stock company and branch of a foreign entity.

Corporate taxation:

Residence – A corporation (defined in Saudi law as a public company, limited liability company or partnership limited by shares) is resident in Saudi Arabia if it is registered in accordance with the regulations for companies in Saudi Arabia or if it is headquartered in the Kingdom.

Basis – A resident corporation is taxed on income arising in the Kingdom. A nonresident carrying out activities in the Kingdom through a permanent establishment (PE) is taxed on income arising from or related to the PE.

Since September 2017, the definition of a resident corporation that is subject to tax includes a company with shares owned directly or indirectly by persons engaged in the production of oil and hydrocarbon materials; with the effect that the state-owned oil company and its Saudi subsidiaries operating in production of oil and hydrocarbon materials are subject to tax. Prior to this date, Saudi and GCC shareholders involved in this business were subject to zakat.

Taxable income – Income tax is levied on a non-Saudi's share in a resident corporation; zakat is levied on a Saudi's share. Citizens of Gulf Cooperation Council countries (GCC) are treated as Saudis.

The tax base for a resident corporation is the non-Saudi's share of income subject to tax from any activity in Saudi Arabia, less allowable expenses. The tax base for a nonresident carrying out activities in Saudi Arabia through a PE is the income arising from the activities of the PE, less allowable expenses.

The tax base of a corporation is determined independently from its shareholders, partners or subsidiaries, irrespective of whether the corporation is consolidated for accounting purposes.

The tax base of persons engaged in the production of oil and hydrocarbon materials will be their taxable income, less expenses allowed in accordance with the tax legislation.

Taxation of dividends – Dividends received are taxed as income.

An exemption is available for cash or in-kind dividends received by a Saudi resident corporation which owns at least 10% of the payer company for at least one year.

Capital gains – A 20% capital gains tax is imposed on the disposal of shares in a resident company by a nonresident shareholder. Capital gains arising on the disposal of securities traded on a stock exchange outside the Kingdom are exempt from capital gains tax provided the securities also are traded on the Saudi stock exchange, irrespective of whether the disposal was made via a stock exchange or through other means.

No gain or loss arises on the transfer of assets between group companies provided that the companies are wholly owned directly or indirectly within the group and the assets are not disposed of outside the group for two years from the date of transfer.

Losses – Tax losses may be carried forward indefinitely, provided the maximum amount deducted in each tax year does not exceed 25% of the annual taxable profits, as reported on the tax return. Corporations are able to carry forward losses, irrespective of whether there has been a change in ownership or control, provided they continue to perform the same activity. A transfer of assets within a group of companies is not considered as a change in ownership or control. The carryback of losses is not permitted.

Rate – The corporate income tax rate is 20% on a non-Saudi's share in a resident corporation and on income derived by a nonresident from a PE in Saudi Arabia. The rate on taxpayers working in the exploitation of natural gas sector is 30%. The tax rate on taxpayers engaged in the production of oil and hydrocarbons is determined on the basis of the company's capital investment, as follows: 85% where the capital investment is USD 60 billion or less; 75% where the capital investment is between USD 60 billion and USD 80 billion; 65% where the capital investment is between USD 80 billion and USD 100 billion; and 50% where the capital investment exceeds USD 100 billion.

Capital investment is defined as the total cumulative value of fixed assets, whether tangible (e.g. equipment, machinery, etc.) or intangible, including exploration, drilling and development expenses.

Zakat is assessed at 2.5% on the higher of the zakat base and the net adjusted profit of a Saudi shareholder.

Surtax – No

Alternative minimum tax – No

Foreign tax credit – No

Participation exemption – No

Holding company regime – The profits of a Saudi resident subsidiary remitted to its Saudi resident holding company will not be taxed, provided: (i) there is a minimum holding of 10%; (ii) the investment is held for at least one year; and (iii) the income of the subsidiary is subject to tax in Saudi Arabia. Limited rules also exist for groups wholly subject to zakat.

Incentives – The government grants 10-year tax incentives on investments in the following six underdeveloped provinces: Hail, Jizan, Abha, Northern Border, Najran and Al-jouf. Investors will be granted a tax credit against the annual tax payable in respect of certain costs incurred on Saudi employees.

Withholding tax:

Dividends – A 5% withholding tax is levied on dividends paid to a nonresident, unless the rate is reduced under a tax treaty.

Interest – A 5% withholding tax is levied on interest paid to a nonresident, unless the rate is reduced under a tax treaty.

Royalties – A 15% withholding tax is levied on royalties paid to a nonresident, unless the rate is reduced under a tax treaty.

Technical service fees – A 5% withholding tax is levied on technical service fees paid to a nonresident third party, unless the rate is reduced under a tax treaty; a 15% withholding tax rate applies to technical service fees paid to related parties.

Branch remittance tax – A 5% withholding tax is imposed on the remittance of profits abroad.

Other taxes on corporations:

Capital duty – No

Payroll tax – No

Real property tax – No, but a 2.5% land tax applies on all undeveloped land within urban boundaries.

Social security – For Saudi employees, the employer must contribute 12% of the employee's salary to the General Organization for Social Insurance (GOSI), and the employee contributes 10%. The employer also pays accident insurance equal to 2% of the salaries paid for non-Saudi employees.

Stamp duty – No

Transfer tax – No

Excise duty - Excise tax was introduced as from 11 June 2017 and is chargeable on the importation or production of excisable goods released for consumption in Saudi Arabia. The excise duty rate is 50% on soft drinks and 100% on energy drinks and tobacco products. Any person intending to import, produce or hold (under a suspension arrangement) any excisable goods in Saudi Arabia must register for excise tax. Any person holding excisable goods valued in excess of SAR 60,000 (whether or not otherwise registered or required to register) must submit a one-off transitional return and pay the excise tax due within 45 days. Thereafter, those registered for excise tax must submit returns reporting their total excise liabilities on a bimonthly basis (i.e. one return every two calendar months) together with payment within 15 days of the end of the tax period.

Anti-avoidance rules:

Transfer pricing – Saudi tax law does not contain any detailed transfer pricing regulations or guidelines. However, related party transactions and the arm's length principle are covered under certain general anti-avoidance provisions. The general anti-avoidance measures provide for the following:

- Transactions between related parties must be conducted on arm's length terms;
- The excess of the cost of materials supplied or services provided by related parties over the prices used by independent parties will be disallowed; and
- Taxpayers should maintain documentation to support the precise determination of tax payable.

The Saudi tax authorities may challenge any transaction and:

- Disregard a transaction that has no economic effect;
- Reclassify a transaction whose form does not reflect its substance;
- Reallocate income and expenses between related parties or parties under common control to reflect the income that would have resulted from a transaction between independent and unrelated parties; and
- Estimate the appropriate tax base and impose penalties.

Taken together, the above provisions empower the Saudi tax authorities to examine related party transactions, request relevant documentation and adjust income or expenses based on the arm's length standard which, at times, may differ from the OECD standards, depending on the local practices. Although the OECD transfer pricing guidelines generally are taken into account in examining the arm's length nature of related party transactions, they are not binding on the Saudi tax authorities.

Thin capitalization – Saudi Arabia does not have specific thin capitalization rules, but there is a rule limiting the deductibility of interest expense to the lesser of: (i) the actual interest expense, or (ii) interest income, plus 50% of taxable income (excluding interest income and interest expense).

Controlled foreign companies – No

Disclosure requirements – No

Other – There are general anti-avoidance provisions in the tax law; see above under "Transfer pricing."

Compliance for corporations:

Tax year – The tax year is the state's fiscal year. The taxable year of a taxpayer starts from the date it obtains a commercial registration or license, unless other documents support a different date.

A taxpayer may use a different tax year in the following circumstances: (i) the different year was approved by the Directorate before the effective date of the income tax regulations; (ii) the taxpayer uses a Gregorian financial year; or (iii) the taxpayer is a member of a group of companies or a branch of a foreign company that uses a different financial year.

Consolidated returns – Consolidated returns must be filed for zakat and in the case of wholly owned subsidiaries. However, zakat returns of the subsidiaries are filed for information purposes. Consolidated returns are not permitted for income tax purposes.

Filing requirements – Tax returns for a corporation must be filed online with the tax authorities within 120 days from the fiscal year-end. A taxpayer whose taxable income exceeds SAR 1 million before the deduction of expenses must have the accuracy of the return certified by a licensed certified accountant. Additionally, audited financial statements must be filed with the Ministry of Commerce within 120 days of the year-end.

Penalties – The penalties for failure to file a tax return are the higher of 1% of revenue (up to a maximum of SAR 20,000), or between 5% and 25% of the unsettled tax, depending on the length of the delay. In addition, there is a fine of 1% of the unsettled tax for every 30 days' delay in settlement.

Rulings – No

Personal taxation:

Basis – There is no personal income tax (employment tax) in Saudi Arabia; however, nonresidents conducting business in the Kingdom or deriving income from a PE in Saudi Arabia are taxed as described above under "Corporate taxation."

Residence – An individual is resident in Saudi Arabia for a tax year if he/she has a permanent residence in the Kingdom and is present in the Kingdom for a period of at least 30 days in total in the tax year, or is present in the Kingdom for a period of at least 183 days in the tax year.

Filing status – Only individuals that carry on a business or profession are required to file a tax return.

Taxable income – The concept of taxable income is only applicable for individuals that carry on a business or profession, who are subject to the same rules as companies.

Capital gains – A 20% capital gains tax is imposed on the disposal of shares in a resident company. Capital gains on the disposal of shares traded on the Saudi stock exchange are tax exempt if the shares were acquired after 2004.

Deductions and allowances – No, except for individuals that carry on a business or profession.

Rates – Individuals carrying on a business or profession are taxed at the same rate as companies, i.e. 20%.

Other taxes on individuals:

Capital duty – No

Stamp duty – No

Capital acquisitions tax – No

Real property tax – No

Inheritance/estate tax – No

Net wealth/net worth tax – Zakat is levied on the registered businesses of Saudis.

Social security – Saudi employees must contribute 10% of salary to the GOSI; the employer contributes 12%.

Expatriate levy – An annual dependent levy of SAR 1,200 applies as from July 2017 per expat dependent residing in Saudi Arabia. This amount increases to SAR 2,400 from July 2018, SAR 3,600 from July 2019 and SAR 4,800 from July 2020.

Compliance for individuals:

Tax year – No

Filing and payment – No

Penalties – No

Value added tax:

Taxable transactions – VAT was introduced as from 1 January 2018 and the VAT system is closely aligned to the international VAT models used in many OECD countries. VAT applies to almost all supplies of goods or services, subject to limited exceptions. Exempt supplies include, margin-based financial services, life insurance and residential property rental. Food, education and healthcare are fully taxable.

Rates – The standard rate of VAT is 5%. Certain goods and services are zero-rated in accordance with the GCC's Framework Agreement which specifies some mandatory areas for zero-rating in all six GCC Member States (including exports of goods and services outside the GCC, and the supply of qualifying medicines, medical goods and investment metals).

Registration – The standard VAT registration threshold is an annual turnover of SAR 375,000. However, businesses with an annual turnover of less than SAR 1 million are exempt from the mandatory registration requirement until 1 January 2019. Businesses who do not apply for registration within the specified period are subject to a fine of SAR 10,000.

Filing and payment – VAT tax periods may be monthly or quarterly. Taxpayers must calculate the net VAT for the period and submit the VAT return electronically by the end of the following month, together with the payment required. VAT reporting can be carried out on a "cash accounting" basis for small businesses with turnover of less than SAR 5 million. Businesses with annual turnover of less than SAR 40 million may use a quarterly filing period.

Source of tax law: Income Tax Regulations (Muharram 1425H March 2004)

Tax treaties: Saudi Arabia has concluded 47 tax treaties.

Tax authorities: General Authority of Zakat and Tax (GAZT)

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