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INSIGHT: Transfer Pricing Regulations in Saudi Arabia and Egypt—A Comparison

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The Kingdom of Saudi Arabia (''KSA'') has introduced comprehensive transfer pricing bylaws (and guidance on how these should be interpreted). The other territory in the Middle East that has detailed transfer pricing regulations is Egypt.

This Insight compares these two transfer pricing regimes in terms of the similarities and departures. This Insight will be helpful for multinational entities operating in the region and also for ministries of finance and tax authorities in the region who are soon to introduce transfer pricing regulations of their own.

Common Ground

Despite not being members of the Organization for Economic Co-operation and Development (''OECD''), both regimes apply the OECD ''three tiered'' approach to transfer pricing with a requirement for groups to prepare the masterfile, local file and Country-by-Country Reporting (''CbCR'').

Both regimes also reference the OECD transfer pricing guidelines (in respective domestic transfer pricing guidance) and there is a good amount of consistency with those OECD guidelines in particular with respect to the selection of transfer pricing methods.

Both regimes have also built the OECD ''six-step'' risk control framework (see Appendix A) into the guidelines. However, the regimes depart in a number of areas as noted below.

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Definition of Control/Association

The Egyptian Transfer Pricing Guidelines confirm that persons are associated if they are related and affect the determination of the tax base by virtue of the following:

- husband, wife, descendants/ascendants;
- a corporation and the person who directly/indirectly holds at least 50 percent of the number or value of shares or voting rights;
- partnerships, active partners and silent partners;
- any two or more enterprises in each of which another person holds at least 50 percent of the number of value of shares or voting rights.

The KSA Transfer Pricing Bylaws and guidelines confirm that persons are associated if they are:

- relatives, partners in a partnership;
- a partner in a partnership directly, indirectly (or both) controls 50 percent of the voting rights, income, capital of the partnership; a shareholder in a capital company directly, indirectly (or both) controls 50 percent of the voting rights, income or capital of the capital company; as for agencies administering property held in a trust, fund or any such similar arrangement;
- under common control, effective control (see below) or participates directly or indirectly in the management, control or capital of the other, or otherwise has effective control of the other.

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The effective control definition is widely drawn, as set out in my previous BNA Insight, and includes a number of transactional-based tests grouped into the following:

- control via governance (e.g. board of directors/ trustee influence);
- control via funding (e.g. overreliance on loans/ guarantees);
- control via business (e.g. overreliance on one customer/supplier).

Filings with the Tax Authority

The KSA transfer pricing regulations require the submission of transfer pricing information embedded into the corporate income tax return. A similar process is applied in a number of other jurisdictions (e.g. India and Australia) and is the starting point for transfer pricing audits. The KSA disclosure form also requires an affidavit from a licensed auditor that the group has adhered to its transfer pricing policy.

Egypt, in the past, followed a more traditional approach to transfer pricing audits in which queries will be initiated by research/reviews into accounts, tax returns and other documents. However, the October 2018 update to the guidelines confirmed that the local file must be submitted to the Egyptian Tax Authority (''ETA'') two months after the tax return filing.

Country-by-Country Reporting

The ETA have a lower revenue threshold for domestic headquartered groups having to file a CbCR with the ETA (145 million euros/$163 million) compared with 750 million euros for foreign parented groups (aligned with the OECD standard and most other jurisdictions).

Six Factors of Comparability

Both Egypt and KSA apply six factors of comparability (in comparison to the five factors set out by the OECD). The six factors are quite different as the comparison table identifies.

Certainty—Advance Pricing Agreements

Egypt offers unilateral, bilateral and multilateral advance pricing agreements which can help to provide certainty for multinational businesses.

At present, the KSA regulations are silent on this matter; however, the KSA tax authorities will provide rulings (named and unnamed) on tax matters and this may be extended to transfer pricing arrangements.

Bench Marking

There are some clarifications with respect to bench marking that depart from the OECD guidelines. The KSA guidelines state that loss-making groups should be removed from comparable analysis (this is often a preference of tax inspectors in practice around the world despite the fact that the OECD guidance require loss makers to be included).

The KSA guidelines also recommend that the median of an arm's length range is applied unless it can be demonstrated that a particular position is more relevant. The Egyptian guidelines follow the OECD more closely in this regard.

Both regimes also confirm that searches for comparables should in the first instance be limited to the local market and then if local comparables cannot be identified the scope may be expanded to regional and then global comparables.

Both regimes have also (helpfully) stated that certain elements of the transfer pricing compliance process should only be updated every three years (comparability analysis for KSA and bench marking for Egypt).

Final Comments

The main differences between the two regimes relate to the KSA wide definition of effective control.

The Egyptian guidelines follow the OECD more closely in this regard. The regimes have a good amount of consistency with the OECD guidelines in general and this is helpful for taxpayers in complying with the regulations—however, both regimes have chosen to require taxpayers to submit transfer pricing documentation in some form to the tax authority.

The Egyptian transfer pricing regime has been in existence for a number of years (the guidance was updated in October 2018 but this was based on initial guidance from 2010) and the KSA regime is (relatively) new in comparison.

A number of other territories in the Middle East are soon to introduce transfer regulations of their own and it will be interesting to see the type of regime that is adopted in other locations and whether any of the departures from the OECD guidance are recreated.

Multinational groups will appreciate that it is not so much the letter of the law but the approach adopted by tax authorities in implementing the law that can create disputes.

Appendix A: Six-step Process (Common to Both Regimes)

1. Identification of economically significant risks with specificity.
2. Determination of contractual assumption of the specific, economically significant risks assumed by the associated enterprises.
3. Functional analysis to determine the capacity in which the associated enterprises that are parties to the transaction operate with respect to the assumption and management of the specific, economically significant risks.

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4. Interpreting steps 1–3 and whether contractual assumption of risk is consistent with actual conduct.
5. Reallocation of risks where a person does not have the financial capacity to assume the risk.
6. Price the transaction taking into account risk allocation.

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