



**KSA Transfer Pricing Draft
Regulations**
Summary of initial views

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Introduction

On 10 December 2018, the Kingdom of Saudi Arabia (KSA) General Authority of Zakat and Tax (GAZT) released a draft of the long anticipated [Transfer Pricing regulations](#). This alert contains a **summary of our initial views based on the regulations**, but there is also a significant amount of consistency with the OECD guidance. Additional clarifications are set out as per the below:

- When are the regulations effective?
- To whom will the regulations apply?
- Disclosure form
- Article 13
- Choice of methods
- Comparability
- Interaction with Permanent Establishment (PE) Regulations
- De-minimis Limit
- General comments

When are the regulations effective?

There will be a period of consultation to the 9th of January; however, the regulations will be effective for accounting periods ended 31 December 2018 and there are important compliance obligations set out below (including a new transfer pricing disclosure form that needs to be filed within 120 days of the end of the accounting period).

To whom will the regulations apply?

The regulations apply to all taxpayers and cover any transaction between Related Persons or Persons Under Common Control.

Related Persons (structural and transactional definitions)

The regulations provide a detailed definition for Related Persons, which is broadly consistent with OECD standards. It is however worth mentioning that rules establish (among other things) that two persons would be considered Related Persons if they are Persons Under Common Control or if one has Effective Control over the other (see below). It should be noted that the definition of control does not link to other areas of KSA tax law in which control relationships exist (however, the 50% trigger is one that many will be familiar with).

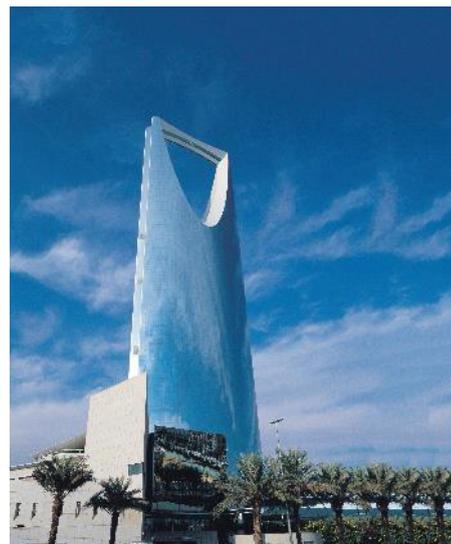
In addition, the definition of "MNE" within the context of Country by Country Reporting states that there must be entities in two or more tax jurisdictions (or one entity and a PE). It may be envisioned that domestic transactions are carved out but we will know more in due course during the consultation period. The trigger for 25% of borrowings under guarantee (see below) will have direct relevance in KSA due to prevalence of guarantees (mainly outbound) on borrowings to support operating companies - in addition there are other control triggers referred to below that are transaction based rather than structural based which will be important to understand when assessing whether transfer pricing regulations apply.

Person under the definitions in this regard requires legal personality and is stated to include Permanent Establishments.

Persons under Common control

Two or more juridical persons are deemed to be under common control if:

- The Person or Related Persons, either individually or jointly, control directly or indirectly 50% or more of such Persons. We note that the regulations provide specific definition for control in the context of partnerships, capital companies and agencies.
- The Person or Related Persons, either separately or jointly, directly or indirectly is or are able to control the business decisions of such juridical person or otherwise have Effective Control over such juridical person.
- Person under the definitions in this regard requires legal personality and is stated to include Permanent Establishments.



“ The regulations apply to all taxpayers and cover any transaction between Related Persons or Persons Under Common Control.”

Effective control

This term refers to the ability of a Person to control the business decisions of another Person as indicated below:

- A Person or Persons have the ability to conclude an agreement to provide management services to the company or otherwise effectively perform the functions of management for the other Person;
- A Person or Persons have the ability to act as trustee (manager) of the other Person or Persons under a trust arrangement;
- A Person or Persons have the ability to directly or indirectly control the composition of 50% or more of the board of directors or have the right to appoint or dismiss the representatives of management of the other Person or Persons;
- A Person or Persons have a legal or de facto right to receive, directly or indirectly, 50% or more of the profits of the other Person or Persons;
- A Person or Persons have provided loans to the Person or Persons directly or indirectly, and the total outstanding balance of such loans is 50% or more of the funds necessary for the borrowers' business;
- A Person or Persons have issued guarantees to cover 25% or less of the total borrowings of a Person;
- 50% or more of a Person's business activities depend on transactions with such other Person or Persons;
- A Person or Persons are Related Person to a Person who directly or indirectly holds 50% or more of a juridical person or they participate, directly or indirectly, in the management of the juridical person;
- A Person is or Related Persons, jointly or severally, are the principal or supplier of a Person under an exclusive agency, distributorship arrangement or any such similar contract for the sale of goods, services or rights and such Person is a dependent agent of the principal and who is prohibited from entering into other similar agency, distributorship arrangement or any such similar arrangement for the duration of the Person's relationship with the principal;
- In the case of Non-resident Person or Related Persons, where a substantial portion of the business activities of a Resident Person depends on Transactions with the Non-resident Person or Related Persons, and the Resident Person's business activities depend on rights in intangible property granted to such Person on an exclusive basis directly or indirectly by the Non-resident Person or Related Persons; or
- The Person is or Related Persons, jointly or severally, are able to control the business decisions of the other Person in any other way as evidenced by the facts and circumstances.



“Effective control refers to the ability of a Person to control the business decisions of another Person.”

Disclosure form

The regulations suggest that taxpayers will be required to file a 'Disclosure Form' together with the annual income tax return due 120 days after the financial year-end. The required contents of this Disclosure Form are set out below:

- General information on the parties to the Controlled Transaction, e.g. legal names, locations, among others;

- Information about business restructurings, if any;
- Information about legal and beneficial owners;
- Total revenue, total expenses and amount of net profit (loss);
- Type and nature of the relationship amongst parties to the Controlled Transaction.
- Nature of the business activity or activities of the parties to the Controlled Transaction;
- Aggregate amounts of consideration, nature of receipt or income or nature of payment or expenditure.
- Transfer Pricing method applied;
- A statement certifying whether or not the taxpayer has entered into Controlled Transactions without monetary or non-monetary consideration
- Existence of Transfer Pricing documentation, including the Master File and Local File.

Article 13

There is a requirement to file CbCR and notifications for groups with turnover exceeding SAR 3.2bn (approximately USD\$850m). There is also a requirement to prepare Masterfile and Local files – the regulations are all in line with OECD guidance with no surprises.

Choice of methods

The choice of transfer pricing method is in line with OECD guidance and prescribed methods (comparable uncontrolled price, resale price, cost plus, transactional net margin and transactional profit split). In addition, there is commentary that one method will be sufficient as opposed to multiple methods being adopted. This is a helpful concession and meets with the “purist Transfer Pricing” view rather than looking at 1-2 methods to manage overall risk.

Comparability

When assessing comparability of transactions in support of arm’s length pricing, the regulations provide the following clarifications:

- The OECD’s “Five Factors” of Comparability should be applied (characteristics of property/services, functions/assets/risks, contractual terms, economic circumstances, business strategies), are set out along with an additional sixth factor “any other Economically Relevant Terms” –this is a helpful addition and in general, there is a good amount of deference to facts and circumstances throughout the draft regulations;
- There is flexibility for GAZT and businesses to pick the point in the range that suits the facts and circumstances of the case;
- There is confirmation that no “secret comparables” should be relied upon by tax authorities or taxpayers – this is a good lesson from other jurisdictions to encourage greater transparency between GAZT and business.

Interaction with Permanent Establishment (PE) Regulations

There was an initial concern that the current PE regulations in KSA with deemed profit margins as high as 80% for certain activities would be at odds with the OECD principles. This first draft of the regulations confirms that the arm’s length principle should apply to PEs and this is a helpful clarification.

De-minimis Limit

There is a helpful exemption for intra-group transactions less than SAR6m (approximately USD\$2m) which will help start-ups, mainly domestic groups and smaller enterprises.

General comments

Whilst the disclosure submission is an additional administrative burden on businesses and will need some attention, the confirmation of permanent establishment attributions and deference to facts and circumstances throughout make this a positive set of draft regulations.

Contacts

Deloitte has a growing team of Transfer Pricing specialists, covering the entire GCC region; details of our senior contacts are set out below.



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