

KSA: Amendments to the implementing regulations of the Tax Law

April 2018

In brief

A number of amendments were made to certain articles of the Saudi Arabian (KSA) Income Tax law (“Tax Law”) pursuant to Royal Decree No (M/131) on 29/12/1438 AH (September 20, 2017).

Following the publication of this Royal Decree, the Minister of Finance has now issued Ministerial Resolution (“MR”) No. 1727 dated 25/5/1439 AH (February 11, 2018) which provides alignment of the KSA Tax Law with the Tax By-laws or Implementing Regulations.

The latest MR is one of a number of important legislative changes made to key fiscal laws in KSA, all of which need to be considered carefully given the recent pro-active approach of the tax authorities with regard to tax compliance in KSA.

In detail

Ministerial Resolution 1727 amends certain articles of the Tax By-law

The Ministerial Resolution No. 1727 provides amendments to Articles 1, 5, 7, 8, 9 and 58 of the Tax By-law. It is important to note that further analysis of these changes including practical application by the KSA tax authority (“GAZT”) is advised.

We have summarized below the key changes to the Tax By-law.

Article 1 and 5: General provisions

Persons subject to taxation include resident capital companies with respect to shares owned directly or indirectly by non-Saudi persons. The term indirect ownership means ownership up to the second level.

It also includes a resident ‘capital company’ (includes a joint stock company and limited liability companies) with respect to shares owned either directly or indirectly by persons operating in oil and hydrocarbon production.

The amendment states that shares owned by non-Saudis for speculation purpose in capital companies listed on the KSA stock market are not considered as non-Saudi shares.

A capital company’s share of profits or losses arising from investments accounted for under the equity method shall not be included as part of the tax base.

Finally, the amendment emphasizes that consolidated tax filing is not allowed even if a company is consolidated with other companies or a group of companies for accounting purposes.

Article 7: Exempt income

Capital gains on the sale of shares listed and traded on the Saudi Stock Exchange [“Tadawul”] are tax-exempt subject to the disposal being made in compliance with the KSA Capital Market Laws and the shares were purchased after issuance of the KSA Tax By-laws in July 2004.

The change in law now extends the tax exemption to shares traded on stock exchanges outside KSA provided such securities are also traded on the Tadawul, and the shares were acquired after issuance of the KSA Tax Law in July 2004.

Tax-exempt income also includes dividend income in cash or kind (bonus shares) from investments in a KSA resident company or a nonresident company provided that:

- a. The ownership in the investee company is 10% or more;
- b. The period of ownership is one year or more.

Dividend income from local KSA companies was exempt under Ministerial Resolution 3294, but this amendment now exempts foreign dividend income as well.

Article 8: Gains and losses on disposal of assets

Intra-group transfers of cash, shares, financial securities and other tangible and intangible assets can now be done tax neutrally provided the following conditions are met:

- Such companies should be part of a group of capital companies that are wholly owned directly or indirectly by one capital company.
- Such assets should not be disposed to a company outside the group before two years passes from the date of the transfer.

The 'cost base' of the relevant intragroup transactions will be net book value to achieve the no gain no loss result. Previously, there was no specific exemption for intra-group transfers of assets.

This amendment aligns the Law with re-organisation regimes that exist in many countries and concurs with previous rulings from Appeal Committees that share transfers within a KSA group should not be subject to tax.

It is not yet clear whether non-resident companies or cross border transactions would also benefit from the above reorganization relief.

Article 9: Contribution to authorized retirement funds

For tax purposes a KSA capital company may deduct contributions to retirement funds, social insurance funds and any other fund established to provide for End-of-Service Benefits or compensate for medical expenditure of beneficiaries, subject to the following:

- The fund shall have an independent legal status (whether established in or outside KSA), and separate accounts, audited by an independent certified auditor.
- The deduction does not exceed the unfunded liabilities relating to these funds, which were not paid from the beginning of the fiscal year in which deduction is made.
- Employment contracts recognize such contributions by employers as employees' right.
- The taxpayer should provide the GAZT with information relating to those funds including:

- Articles of Association of the fund, (objectives, subscription conditions, rights and sources of funds),
- Audited financial statements,
- Names of the beneficiaries of the fund and amounts paid to them each year.
- Employees' contribution to such a fund are not tax deductible

Article 58: GAZT right to information

The GAZT has the right to carry out a field inspection to examine the taxpayer's books and records and to seek additional information. A fine of SR3,000 (US\$800) will be imposed on any taxpayer who does not cooperate with the concerned GAZT's employee to perform his assigned task.

In the case of non-cooperation by the taxpayer, GAZT has the right to request other competent authorities to oblige the natural or corporate persons to provide the required information.

If GAZT is not able to obtain the required information, GAZT has right to raise a tax assessment on the taxpayer at its discretion and as it deems appropriate based on the information available.

All persons, natural or corporate, taxpayers or non-taxpayers, including charity and endowment organizations, public corporations and associations and government agencies, shall provide GAZT with the following:

- The requested information concerning the implementation of the provisions of the Tax law and effective international tax agreements.
- Information on the contracts entered with the private sector (excluding contracts with a value of less than SR100,000) and any amendments thereto within three months of the date of signing.
- Notify GAZT within 30 days of the date of ceasing execution of a contract.
- A copy of the contract if GAZT requests it.

Each party breaching its obligations with respect to the above requirements shall be jointly liable with the taxpayer for any tax claim or fines arising therefrom.

Effective date

The amendment to the By-laws is effective immediately subject to the date of applicability of the amended provisions of Tax Laws by Royal Decree No (M/131) dated 29/12/1438 AH (September 20, 2017).

The takeaway

There is some clarity required from GAZT on the above key changes especially on the application of the indirect ownership up to the 'second level' and whether the tax neutral intra-group transfer of assets would include cross border transactions.

Furthermore, given the GAZT's focus on broadening its tax and zakat base and ensure full compliance, we recommend that clients ensure that contract reporting obligations are met to avoid any adverse implications in the event of non-compliance.

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