

Saudi Arabia:

Tax Rules for Regional Headquarters

February 2024



In brief

Another big step has been taken in the way towards developing the tax practices and landscape in Saudi in line with Saudi 2030 Vision to make Saudi Arabia a pioneering investment hub. The long-awaited Tax Rules for the Regional Head Quarters "RHQs" have now been published by ZATCA with an immediate effect from the date of publishing (i.e., 16/08/1445 AH corresponding to February 16, 2024).

The rules clarify several key matters to the tax and investment society, this includes the following, among others:

- Key Definitions regarding the RHQ.
- Tax Incentives.
- Exemption duration and criteria.
- Economic substance rules for the RHQs.
- Tax Compliance Requirements.
- Fines and penalties in case of violating the rules.
- Rights of both ZATCA and the RHQ in case of tax audits and disputes.

In detail

The Tax Rules for the RHQs may be summarised as follows:

Key Definitions regarding the RHQ:

The Rules state some key definitions with respect to the RHQs, these include the following among others:

- **Regional Headquarters:** The regional headquarters or a unit of a Multinational Group duly established under the laws of Saudi Arabia and the concept of regional headquarters activities of international companies applies according to the National Classification of Economic Activities.
- **Eligible Activities:** The main activities of the Regional Headquarters towards strengthening the group's profile in the region and providing strategic supervision and administrative guidance and support for the internal business of the company, subsidiaries and other related companies according to the National Classification of Economic Activities.
- **Related Companies or Related Persons:** Shall have the same meaning prescribed in the Transfer Pricing Bylaws.
- **Tax Incentives:** Mean the tax benefits and exemptions available for Regional Headquarters, as prescribed in the Royal Decree.
- **Economic Substance Requirements:** The requirements that must be satisfied by the Regional Headquarters to ascertain the substance of the economic activities in the Kingdom.

Takeaways of the key definitions:

- The RHQ is allowed to perform certain activities to remain qualified as an RHQ, these activities as regarded as the eligible activities.
- Transfer Pricing By-law is strongly correlated with the Tax Rules for the RHQs and is the reference to define the related parties.
- Tax incentives as per these rules are solely granted to the RHQs as long as they remain qualified as an RHQ.
- RHQs must satisfy the economic substance requirements stated as per the Rules to remain qualified as an RHQ,



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Tax Incentives:

Regional Headquarters meeting the qualification criteria shall be eligible to enjoy the following tax incentives:

- Zero percent (0%) income tax on the qualifying income.
- Zero percent (0%) Withholding Tax “WHT” on the payment made by the RHQ to non-residents, meeting any of the following criteria:
 1. Payments of dividends.
 2. Payments to related parties.
 3. Payments to third parties for services necessary for the RHQ’s activities.

With that said, it’s critical to note that the WHT exemption shall not apply in any of the following cases:

- If the payment made by the RHQ is related to non-qualifying activities.
- In any of the tax evasion cases prescribed as per the RHQs Tax Rules.

Furthermore, it’s worth mentioning that income derived by the RHQ from non-qualifying activities shall be treated according to the provisions of the relevant tax regulations in the Kingdom.

It is also worthy to highlight that the provisions of the in-force treaties in Saudi and international obligations shall apply to the RHQs.

Furthermore, for the sake of all international treaties, conventions or other agreements to which the Kingdom is party, RHQs are considered tax residents to the extent they meet the tax residency criteria according to Saudi Income Tax Law.

Duration of the tax Incentives:

- The tax incentives are applicable to the qualifying activities for renewable Thirty (30) years, starting from the date of obtaining the RHQ license to carry out the qualifying activities.
- The tax incentives shall expire on the earlier of:
 - The elapse of the 30 years period.
 - The entity cease to be qualified as an RHQ for whatsoever reason.

Takeaways of the Tax Incentives:

- Enjoying the RHQ tax incentives is dependent on the fulfilment on the exemption criteria.
- The RHQ tax rules state the tax avoidance cases which are eligible to tax incentives.
- Although the tax incentives shall be valid for renewable 30 years, they may cease at any point of time in case on not meeting the RHQ requirements or in case of tax avoidance.

Economic substance rules for the RHQs:

In addition to the set requirements by the competent authority, RHQs shall fulfill ALL of the following Economic Substance requirements:

1. The RHQ should have a license from the competent authority and shall ONLY carry out the licensed activities as per such license.
2. The RHQ shall have adequate assets including suitable building to carry out the RHQ activities.
3. The activities of the RHQ, including holding the board meeting through which the strategic decisions are taken, shall be directed and managed in the Kingdom.



Economic substance rules for the RHQs (Cont'd):

4. The RHQ should commensurately incur operating expenditures in the Kingdom with the performance of the RHQ's activities.
5. The RHQ MUST generate revenues from the qualifying activities in the Kingdom.
6. The RHQ MUST have at least one resident director in the Kingdom.
7. The RHQ MUST employ an adequate number of full-time employees in the tax year that commensurate with the level of the RHQ's activities.
8. The RHQ;s employees MUST have the necessary knowledge and expertise to deliver their duties and fulfill their responsibilities.

Takeaways of the Economic Substance for the RHQs:

- The RHQs Tax Rules set strict criteria for the RHQ's economic substance, these criteria should be completely fulfilled and maintained during the entire lifecycle of the RHQ.
- Failing to meet the economic substance criteria may expose the RHQ to considerable penalties and consequences which reach the level of revoking the tax incentives granted to the RHQ in certain cases.

Tax Compliance Requirements:

RHQ is required to comply with the tax and zakat regulations with respect to filing the tax and Zakat returns.

In addition to the above, the following is a unique compliance requirement to the RHQ:

- Annual report, according to the form provided and the specified procedures by ZATCA , to ensure and validate the compliance with the Economic Substance Requirements.

Takeaways of the Tax Compliance Requirements:

- The RHQs shall be prepared to prepare and submit the Economic Substance Compliance form that will be provided by ZATCA, more details to follow in this regard following ZATCA's introduction of that form.

Fines and penalties:

RHQ shall be exposed to certain fines and penalties in case of non-compliance with the RHQs Tax Rules, these fines and penalties shall apply without prejudice the other penalties stipulated as per the Tax Regulations:

- In case of not fulfilling any of the RHQ Economic Substance Requirements during the validity period of the license, ZATCA shall notify the RHQ with the violation committed by the RHQ and grant it (90) days from the notification date to rectify the violation, in case of failure to remedy the violation during the granted period, the following penalties shall apply:
 - SAR 100,000 provided that the violation is remedied within (90) days from the date of imposing the fine.
 - In case of failure to remedy the violation within the above prescribed period, or the violation is repeated within (3) years from the date of imposing the above mentioned fine, a fine of SAR 400,000 is imposed provided that the violation is remedied within (90) from the date of imposing the fine.
 - In case the violation persist following imposing the second fine mentioned above, ZATCA in coordination with the competent authority may consider suspension of the Tax Incentives.

Fines and penalties (Cont'd):

RHQ MUST comply with the Transfer Pricing By-Laws and any amendments to it, also RHQ MUST ensure that all transactions with related parties are conducted at Arm's Length.

In addition to the above-mentioned Fines and Penalties, ZATCA in Coordination with the Competent Authority may revoke the tax incentives for the RHQ in any of the tax avoidance cases mentioned per the RHQ Tax Rules.

Takeaways of the Fines and penalties:

- In case of non-compliance with the Economic Substance Requirements, the RHQ may be granted a penalty-free period to remedy the violations. Failure to remedy the violation within the penalty-free period may expose the RHQ to considerable penalty.
- Tax incentives granted to the RHQ require compliance to the Tax Rules of the RHQ including the Economic Substance Requirements, non-compliance may have severe consequences that may reach the level of revoking the tax incentives.

Rights of both ZATCA and the RHQ in case of tax audits and disputes.:

ZATCA is entitled to practice all its organising and executive duties according to the Law, including the following:

- Obtaining the information.
- Conducting examination, audit and assessment of the RHQ activities according to the provisions of the Tax and Zakat regulations.
- ZATCA shall monitor and verify the fulfilment of the Economic Substance Requirements by the RHQ on annual basis.

On the other hand, the RHQ is entitled to the following benefits and rights:

- Submit a request for a ruling from ZATCA to provide an interpretation or clarification on tax matters related to these Tax Rules and the Tax Regulations in the Kingdom.
- The RHQ is entitled to appeal against assessment, reassessment and the penalties imposed by ZATCA.
- The RHQ also has the right to submit an appellate and grievance according to the procedures stipulated as per the Tax and Zakat regulations.

Takeaways of Rights of both ZATCA and the RHQ:

Given that the RHQ Tax Rules are newly introduced in the Kingdom including unprecedented criteria such as the Economic Substance Requirements, it is understood that there could be difference in the views between the RHQs and ZATCA regarding the interpretation of the Tax Rules, accordingly, Tax and Zakat dispute may arise. Therefore, it's essential to the RHQs to adhere to the following:

- Maintain proper supporting documents for all transactions and activities.
- Be fully compliant with Transfer Pricing By-laws and ensure that all transactions with related parties are conducted at Arm's Length.
- Be fully compliant with the Economic Substance Requirements all the times and maintain supporting documents proving this compliance.

The takeaway

The RHQ Tax rules cover several aspects and the takeaway of each aspect has been explained in detail above, however, the foremost takeaway is to maintain and document the compliance with the RHQ requirements, including but not limited to the Economic Substance Requirements.

Our team are ready and will be glad to support you to be in compliance with the Tax Rules of the RHQs.

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Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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