The General Authority of Zakat and Tax (GAZT) releases an update on the deductibility of input tax

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Dear clients and contacts,

The GAZT has released an important guideline detailing the conditions to exercise the right to deduct input VAT.

General Conditions for Input Tax Deduction

Taxable customers in KSA must ensure that all the below conditions are met before exercising the deduction right.

- The customer must ensure that the supplier is registered for VAT purposes with the GAZT. This can always be verified through GAZT's website.

- The input VAT must of course be KSA VAT (a separate refund procedure, the modalities of which still need to be published, exists for recovering VAT from other GCC countries.).

- The supplier must have properly charged VAT on the supply (this implies that the supply was indeed subject to KSA VAT and for example not zero-rated or exempt).

- The taxpayer must be in the possession of a valid Tax Invoice or similar accepted documentation

- The taxpayer claiming the deduction must also be the customer for VAT purposes. Indeed, in certain cases, the customer may not necessarily be the person benefitting from the supply nor the person making payment of the consideration due.

- In case a nominal supply arises but the supplier is not asking the customer to pay the corresponding VAT charge from the customer, the customer may not deduct such VAT.

- In case the Taxable customer either makes exempt suppliers or engages in non-economic activity (i.e. provides public services), the purchased goods or services must be directly and exclusively attributable to making taxable supplies.

- The purchased goods or services must not be used or intended for use for the owner's/employees' private purposes. In such cases, the nominal supply rules may need to be considered.

- The purchased goods or services must not relate to expenditure for which input tax recovery is prohibited (see article 50 of the KSA VAT Regulations).

Tax Invoice or Alternative Documentation Requirement

The GAZT may accept the following alternative documentation instead of a valid Tax Invoice:

- Valid Simplified Tax Invoice, or

- Alternative commercial documentation that provides sufficient evidence as to the particulars of the supply (acceptable at GAZT's discretion).

In case a Tax Invoice is not in Arabic and/or has missing content requirements, the GAZT may at its discretion accept such a Tax Invoice subject to its containing certain crucial elements pertaining to the supply. Furthermore, the customer must have documentary evidence that he has paid the applicable VAT (e.g. possession of bank transfer/payment receipt).

The GAZT's willingness to accept the customer's deductibility of input tax based on a Tax Invoice that does not strictly meet the Tax Invoice content requirements does not imply that the supplier will not be held liable by GAZT for failing to issue a compliant Tax Invoice.

Deduction of VAT on Imported Goods

VAT levied on imports of goods into the KSA from outside the GCC is deductible subject to the following conditions:

- The Taxable customer is the importer of record as per the customs documentation, and the Taxable customer holds and retains such customs documentation, and

- The Taxable customer must be the owner of the goods and must intend to use the goods for the purposes of his taxable economic activity.

Import tax may be reported and deducted in the VAT return relating to the tax period in which the import tax is paid to customs.

Deductibility of VAT on Lost, Destroyed, and Stolen Goods

A Taxable customer who initially deducts input tax in relation to purchased goods which are subsequently lost, destroyed or stolen is not required to make an adjustment to such input tax. However, the customer must have written off the value of such goods in its accounting records. Furthermore, the customer must

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retain any available evidence in relation to the occurrence of one of the above events, such as police records and/or insurance documents.

Deductibility of VAT on Capital Assets

For KSA VAT purposes, a Capital Asset is an asset purchased by a Taxable customer intended for long term business use. Both tangible as well as intangible assets are included under the scope of Capital Assets. When a Taxable customer purchases a Capital Asset, the customer can initially fully deduct input tax charged on the purchase if the asset's intended use is for a taxable economic activity (and subject to the other conditions). However, the Capital Asset's usage during the "Adjustment Period" must be monitored and could result in an adjustment to input tax previously deducted in case the asset's usage changes.

Deductibility of VAT on Incidental Activities

In case a Taxable customer incurs VAT that is not related to the customer's ongoing economic activity but is used for any of the following:

- raising capital for an ongoing economic activity that relates to making taxable supplies,

- for a business activity considered to be outside the scope of VAT, such as the transfer of an economic activity or part of an economic activity as a going concern, or

- another one-off event that is incidental to an economic activity related to making taxable supplies,

then the customer may deduct any VAT charged in accordance with the proportional deduction method. However, in case the customer only makes taxable supplies, then the customer would be eligible to fully deduct any such VAT charges.

For more information, please **contact us**.