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GLOBAL TRANSFER PRICING SERVICES

Global Transfer Pricing Review

Saudi Arabia

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TAX



Saudi Arabia

KPMG observation

While Saudi Arabia does not have complex transfer pricing rules, transactions between related parties must be concluded on terms as if the parties were independent. As a result we are seeing the Department of Zakat and Income Tax (DZIT) scrutinizing cross-border transactions between related parties and challenging such transactions where arm's length principles are not satisfied.

Even though there is a need to maintain arm's length pricing under Saudi tax law, there are no detailed transfer pricing rules in Saudi Arabia to reach an acceptable arm's length price for a particular transaction. In the absence of such detailed rules, the Saudi tax authority generally accept a price if they are satisfied that it represents a fair market value (FMV) of the subject services or supplies.

The lack of specific transfer pricing rules does provide wide powers to the Saudi tax authority to accept or reject any particular pricing mechanism. Hence, it is always better to provide as much objective support as possible for arm's length pricing between related parties to be able to defend any potential challenge from the Saudi tax authority.

Basic information

Tax authority name

Department of Zakat and Income Tax (DZIT).

Citation for transfer pricing rules

No specific transfer pricing rules have been issued by the Saudi tax authority; however, the principle of arm's length transactions has been embedded within Saudi tax law.

Effective date of transfer pricing rules

Not applicable.

What is the relationship threshold for transfer pricing rules to apply between parties?

Not applicable.

What is the statute of limitations on assessment of transfer pricing adjustments?

There is no specific statute of limitations set out in Saudi tax law; however, there is a general statute of limitations which

shall apply in case the Saudi tax authority is making adjustments to taxable income from the perspective of arm's length price. The specific limitation is 5 years, and 10 years in cases where the tax return was not filed, or if filed, was found to be incomplete or incorrect with intent to evade tax.

Transfer pricing disclosure overview

Are disclosures related to transfer pricing required to be prepared or submitted to the revenue authority on an annual basis (e.g. with the tax return)?

No.

What types of transfer pricing information must be disclosed?

Not applicable.

What are the consequences of failure to prepare or submit disclosures?

Not applicable.

Transfer pricing study overview

Is preparation of a transfer pricing study required – i.e. can the taxpayer be penalized for mere failure to prepare a study?

No.

Other than complying with a requirement per the previous question, describe the benefits, if any, of preparing and maintaining a transfer pricing study?

While not required by law, the preparation and maintenance of a transfer pricing study would greatly assist in supporting an expense or deduction in the event of a tax query or audit in Saudi Arabia.

Furthermore, entities which have substantial losses or periods of sustained losses, usually come under greater scrutiny by the DZIT. Accordingly, the risk of the DZIT challenging or disputing the

expenses and costs charged to Saudi Arabia would be much higher than usual in such instances.

Therefore, a transfer pricing study supported by contemporaneous documentation such as intercompany agreements, invoices etc. would be useful in defending prices and expenses charged in such circumstances.

To satisfy the requirement and/or obtain the benefits, are there any requirements on when the transfer pricing study must be prepared and submitted?

Not applicable.

When a transfer pricing study is prepared, should its content follow Chapter V of the Organisation for Economic Co-operation and Development (OECD) Guidelines?

Not applicable.

Does the tax authority require an advisor/tax practitioner to have specific designation in order to prepare or submit a transfer pricing study?

While there is no requirement for submission of transfer pricing study, in cases when the Saudi tax authority is not completely satisfied, especially in case of imports, it may request the taxpayer to secure an International Market Value (IMV) Certificate from the auditors of supplying offshore entity.

Transfer pricing methods

Are transfer pricing methods outlined in Chapter II of the OECD Guidelines acceptable?

Yes.

Is there a priority among the acceptable methods?

Not applicable.

If there is no priority of methods, is there a "best method" rule?

Not applicable.

Transfer pricing audit and penalties

When the tax authority requests a taxpayer's transfer pricing documentation, how long does

the taxpayer have to submit its documentation?

Not applicable.

If an adjustment is proposed by the tax authority, are dispute resolution options available to the taxpayer outside of competent authority?

If an adjustment is proposed by the Saudi tax authority because of a dispute in the arm's length price and an addition is made to taxable income because of this, such adjustment will become part of a larger tax assessment by the Saudi tax authority. However, such assessment orders can be challenged by the taxpayer like an assessment order addressing any other issues. A taxpayer can appeal against such an order in the Preliminary Appeal Committee (First Appellate Authority), and if he is not satisfied, in the Higher Appeal Committee (Second Appellate Authority); the Board of Grievance will be the last Appellate Authority.

If an adjustment is sustained, can penalties be assessed? If so, what rates are applied and under what conditions?

Penalties are applicable under general provisions of Saudi tax law. Penalties resulting from misrepresentation is 25 percent of the tax sought to be evaded; additionally, there is also a delay fine on unpaid or underpaid tax amounting to 1 percent for each 30 days.

To what extent are transfer pricing penalties enforced?

Not applicable.

What defences are available with respect to penalties?

Not applicable.

What trends are being observed currently?

Not applicable.

Special considerations

Are secret comparables used by tax authorities?

Not applicable.

Is there a preference, or requirement, by the tax authorities for local comparables in a benchmarking set?

While there are no local comparables in any benchmarking set used by the DZIT in Saudi Arabia, the DZIT has a right to raise an arbitrary assessment in the case of any transaction between related parties or parties under common control, to allocate income or deductions between these parties as is necessary to reflect the income that would have resulted from a transaction between independent persons.

Furthermore, the tax law provides for the DZIT to adjust the tax base of an individual taxpayer and other person to prevent any reduction in tax payable as a result of income splitting (assumed to apply to corporate taxpayers as well). For purposes of the above, income splitting means:

- the transfer of income, directly or indirectly, from one person to an associate
- the transfer of property (including money), directly or indirectly, from one person to an associate with the result that the associate realizes income from that property, where the reason or one of the reasons for the transfer is to lower the total tax payable upon the income of the transferor or the transferee.

In determining whether the taxpayer is seeking to split income, the DZIT may consider the value given by the transferee.

Do tax authorities have requirements or preferences regarding databases for comparables?

Not applicable.

What level of interaction do tax authorities have with customs authorities?

The Saudi tax authority (DZIT) interacts quite extensively with customs authorities, and many taxpayers have received notices in the past for the gap in their purchases/imports or sales/ exports etc as reported to/recorded by the two respective authorities.

In practice, the DZIT often compares the value of the goods as per the invoice/ contracts, the auditors' certificate, the amount declared for customs duty, the value as reflected in the financial statements, etc.

In the case where the cost of 'Imported Goods' reflected in the income statement would not match with the value of goods declared for customs duty purposes, the DZIT may disallow deduction of the difference and accordingly raise the assessment of the corporate tax liability and penalty for the period of default.

It is therefore important to ensure consistency between the value of the goods as disclosed in the contract/ invoice, auditor's certificate, customs clearances, financial statements, etc.

Are management fees deductible?

Yes.

Are management fees subject to withholding?

Yes, at 20 percent.

Are year-end transfer pricing adjustments permitted?

Not applicable.

Other unique attributes?

Not applicable.

Other recent developments

While there is a trend that Saudi tax authority has started challenging pricing of some of the cross-border transactions, KPMG in Saudi Arabia have not seen a significant build-up in efforts to formulate formal transfer pricing rules.

The DZIT issued a circular (in May 2010) regarding withholding tax (WHT) on payments made to countries with whom a Double Tax Treaty (DTT) exists. As a result of this new DZIT clarification, WHT on payments made to non-residents residing in countries with whom Saudi Arabia has a treaty that allows for exemption or reduced WHT rates, Saudi residents payees are required to apply full rate of WHT as provided under the tax law, and later claim refund of the overpaid WHT. The circular has also provided some mechanics of the process and required documents.

Tax treaty/double tax resolution

What is the extent of the double tax treaty network?

Saudi Arabia has expanded its double tax treaty network in recent past and around 30 tax treaties are now in effect.

All of the Saudi Arabian treaties (except France) follow the Organisation for Economic Co-operation and Development (OECD)/ United Nations (UN) model and include the 'Associated Enterprises' article. However, the practical application of this provision is yet to be challenged by the DZIT in Saudi Arabia.

If extensive, is the competent authority effective in obtaining double tax relief?

This is yet to be ascertained in terms of the existing tax treaty network in Saudi Arabia.

When may a taxpayer submit an adjustment to competent authority?

Not applicable.

May a taxpayer go to competent authority before paying tax?

Not applicable.

Advance pricing agreements

What Advance Pricing Agreement (APA) options are available, if any?

None. However, non-binding rulings or interpretations may be requested to obtain an understanding of the possible approach to be adopted or treatment acceptable from a Saudi tax perspective from the DZIT.

Is there a filing fee for APAs?

Not applicable.

Does the tax authority publish APA data either in the form of an annual report or through the disclosure of data in public forums?

Not applicable.

Please provide some information on how successful the APA program is and whether there are any known difficulties?

Not applicable.

Language

In which language or languages can documentation be filed?

Arabic.

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