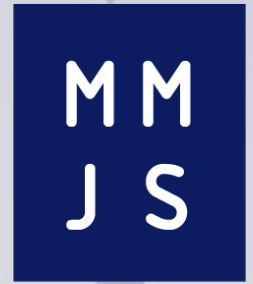




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TRANSFER PRICING - KINGDOM OF SAUDI ARABIA ("KSA") PERSPECTIVE

TRANSFER PRICING (“TP”) IN MIDDLE EAST (“ME”)

Historically, tax authorities in the ME did not explicitly focus on TP – although anti-avoidance rules prevalent in most countries

Post-BEPS, countries in the region have signed up to the Implementation Framework (4 minimum standards) – these include Bahrain, Egypt, KSA, Oman, Qatar and UAE

Egypt and KSA introduced detailed TP documentation and Country-by-Country Reporting (“CbCR”) requirements in 2018 and 2019 respectively. Qatar has also introduced CbCR.

UAE has introduced economic substance regulations and cabinet resolution for CbCR approved

Other countries (e.g. Bahrain, Oman) could be expected to follow



- KSA's final TP bylaws released in Feb 2019, detailed TP guidelines in Mar 2019. **OECD consistent with certain exceptions**



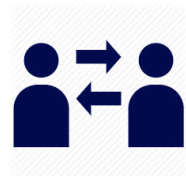
- TP bylaws **apply from FY 2018** although GAZT may open previous years for audit as well



- KSA **income tax payers and mixed companies** (zakat + income tax payers) subject to TP bylaws



- For 100% zakat payers – only arm's length principle applies. CbCR could be applicable, depending on group revenue threshold



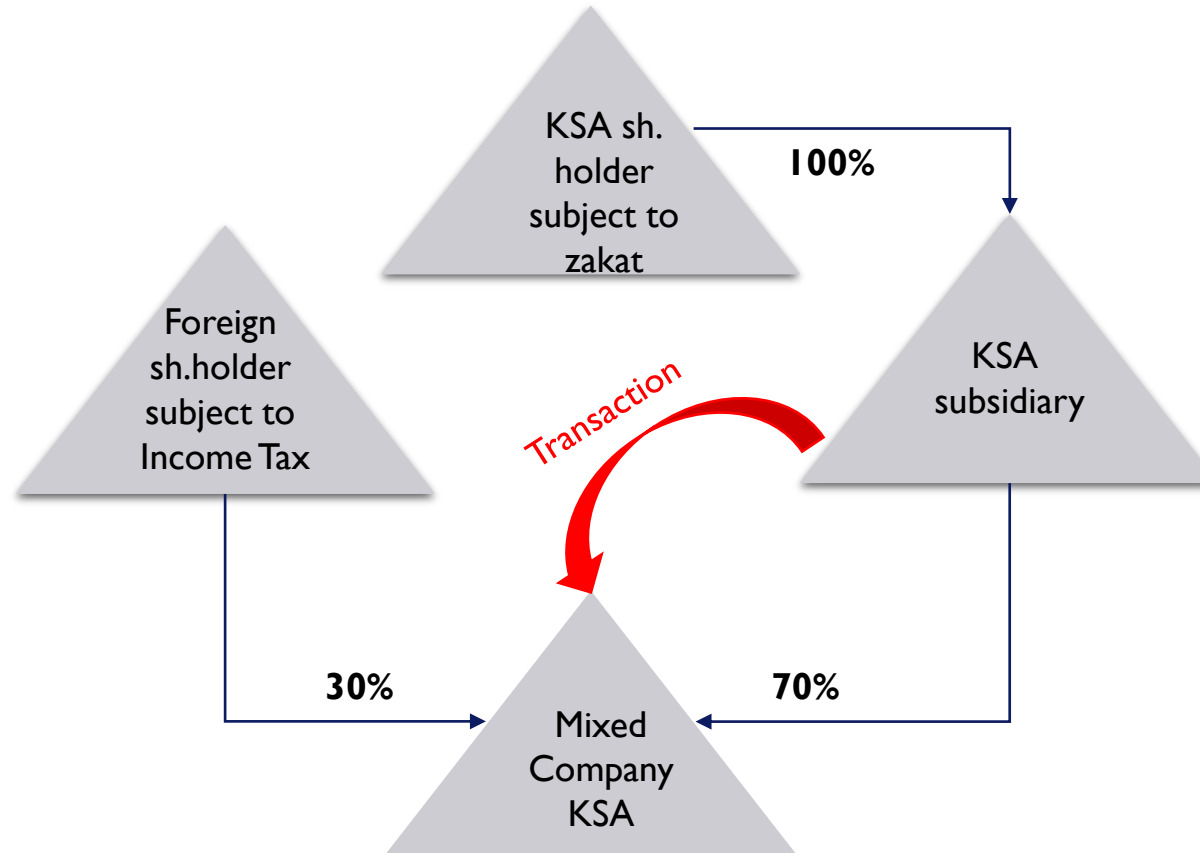
- Related party transactions with both **overseas/domestic related entities** covered

KSA TP BYLAWS APPLICABILITY

	100% taxpayer	Mixed taxpayer	100% zakat payer	Natural person	100% or mixed taxpayer (related transactions < SAR 6m)
TP Bylaws	✓	✓	✓*	X	✓
CT Disclosure Form	✓	✓	X	X	✓
Local File	✓	✓	X	X	X
Master File	✓	✓	X	X	X
CbCR	✓	✓	✓	X	✓

* Arm's length principle applies

KSA TP BYLAWS APPLICABILITY - ILLUSTRATION



- TP bylaws applies to KSA mixed company's transactions, to the extent it's subject to income tax
- Due to 30% foreign holding, income tax base of KSA mixed company = 30% of taxable income
- W.r.t balance 70% of taxable income, arm's length principle applies

KSA-SPECIFIC RELATED PARTY DEFINITION

I. Control - Direct & indirect ownership

II. Effective Control - ability of a person to control business decisions of another person

a) via governance

e.g. through management agreement, trust arrangement or control of board of directors

b) via business

concentration of transaction (e.g. single customer, supplier relationship under an exclusive agency or distributorship arrangement)

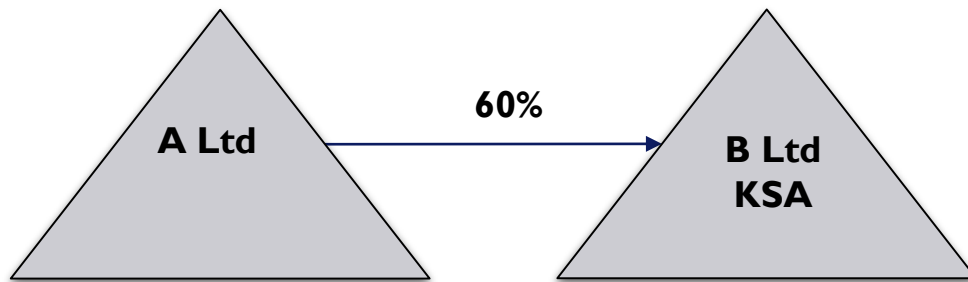
c) via funding

debt financing (e.g. > 50% of outstanding debt provided by one entity; guarantees covering > 25% of borrowings of an entity) except where lender/guarantor is a financial institution

I. CONTROL VIA OWNERSHIP

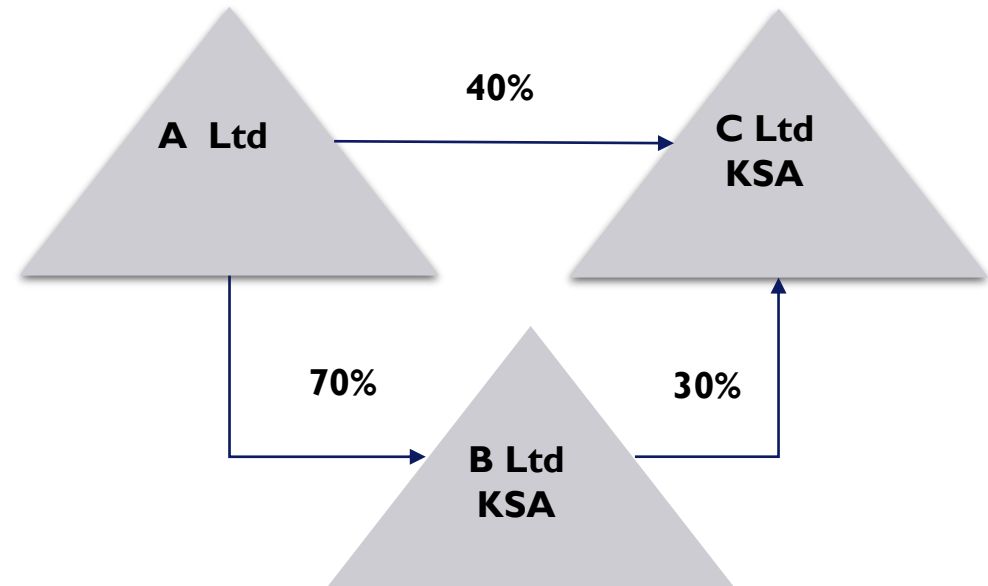
Direct/indirect ownership of $\geq 50\%$ in another entity is control.

(a) Direct Control



- A Ltd controls 60% of B Ltd. Therefore, A Ltd has direct control over B Ltd.

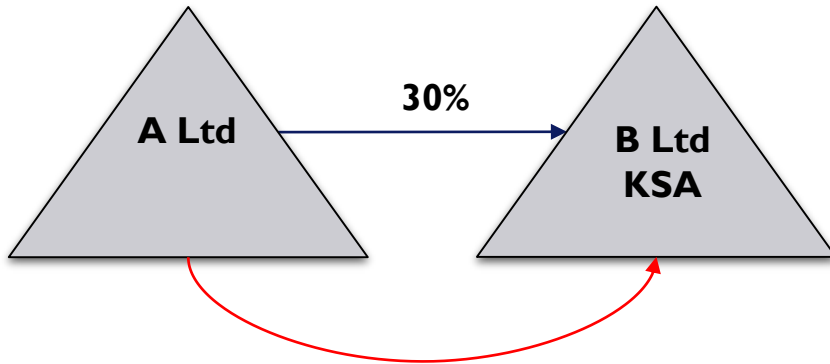
(b) Indirect Control



- No direct control by A Ltd over C Ltd since direct holding $< 50\%$
- Via ownership in B Ltd, A Ltd owns total 61% in C Ltd. (directly 40% and indirectly 21% ($70\% \times 30\%$)). Hence, 50% criteria met

II CONTROL VIA (a) GOVERNANCE & (b) BUSINESS

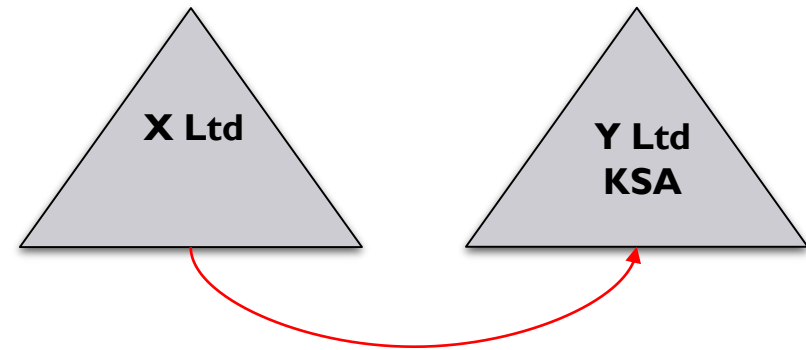
Control via Governance - illustration



- Management/trusteeship services
- Power to appoint >50% BoD

- A Ltd owns <50% of B Ltd but is able to appoint >50% of board of directors of B Ltd
- Hence, A Ltd and B Ltd are related parties by “effective control”.

Control via Business - illustration



Exclusive
distribution
arrangement

- Y Ltd is exclusive distributor of X Ltd in KSA. Y Ltd prohibited from entering into other similar arrangements. X Ltd has potential to “effectively control” Y Ltd’s business decisions.
- **Broad definition of “control via business” need to examine on case to case basis.**

II (c) CONTROL VIA FUNDING

Illustration

A Ltd

Liability	SAR	Assets	SAR
Capital Stock	25	Property, Plant & Equipment	75
Retained Earnings	15	Other current assets	50
Current Liabilities (*)	25		
Loan from B Ltd	60		
Total Liabilities	125	Total Assets	125

Illustration 1

- Debt from B Ltd = 55% $(60/(60+25+25))*100$ of A Ltd's total book value less retained earnings
- Hence debt from B Ltd > 50% of A Ltd's total book value less retained earnings
- **Lender B Ltd has effective control over A Ltd***

* except where lender/guarantor is a financial institution

Illustration 2

- Current Liabilities of A Ltd guaranteed by C Ltd = 29% $(25/85*100)$ of A Ltd's total borrowings
- Hence C Ltd's guarantee amount > 25% of A Ltd's total borrowings
- **Guarantor C Ltd has effective control over A Ltd***

ILLUSTRATION - HOW DOES KSA TP IMPACT YOU?

Scenario 1: Pre KSA TP laws

Group entity A	
Manufacturing (KSA)	
Revenues	105.0
Labour	60.0
Materials	25.0
Other opex	15.0
Total costs	100.0
Profit mark-up	5.0
Tax @ 20%	1.0

Group entity B	
Procurement/distribution (UAE)	
Revenues	307.5
COGS	105.0
Mktg & branding	50.0
Labour/other opex	50.0
Total costs	205.0
Profit mark-up	102.5
Tax @ 0%	0.0

3P retailer

3P retailer

Total taxes paid @ group level = 1

Potential profit mark-up adjusted by GAZT, unless TP analysis performed to demonstrate mark-up was ALP

Scenario 2: Post KSA TP laws

Group entity A	
Manufacturing (KSA)	
Revenues	105.0
Labour	60.0
Materials	25.0
Other opex	15.0
Total costs	100.0
Profit mark-up	5.0
GAZT-adj profit	20.0
Profit adjustment	15.0
Tax @ 20% on adj profit	4.0

Group entity B	
Procurement/distribution (UAE)	
Revenues	307.5
COGS	105.0
Mktg & branding	50.0
Labour/other opex	50.0
Total costs	205.0
Profit mark-up	102.5
Tax @ 0%	0.0

3P retailer

3P retailer

Total taxes paid @ group level = 4 plus fines on underpaid tax and/or penalties for payment delays

KSA TP FILING REQUIREMENTS

1. Controlled Transaction Disclosure Form (“CTDF”)

- Accountant’s certificate certifying group TP policy to be submitted with CTDF
- Applies to **all taxable entities**

2. TP Documentation (Master file & Local file)

- TP documentation encouraged in Arabic (English may be acceptable)
- Applies to all taxable entities whose **controlled transaction value > SAR 6m annually**

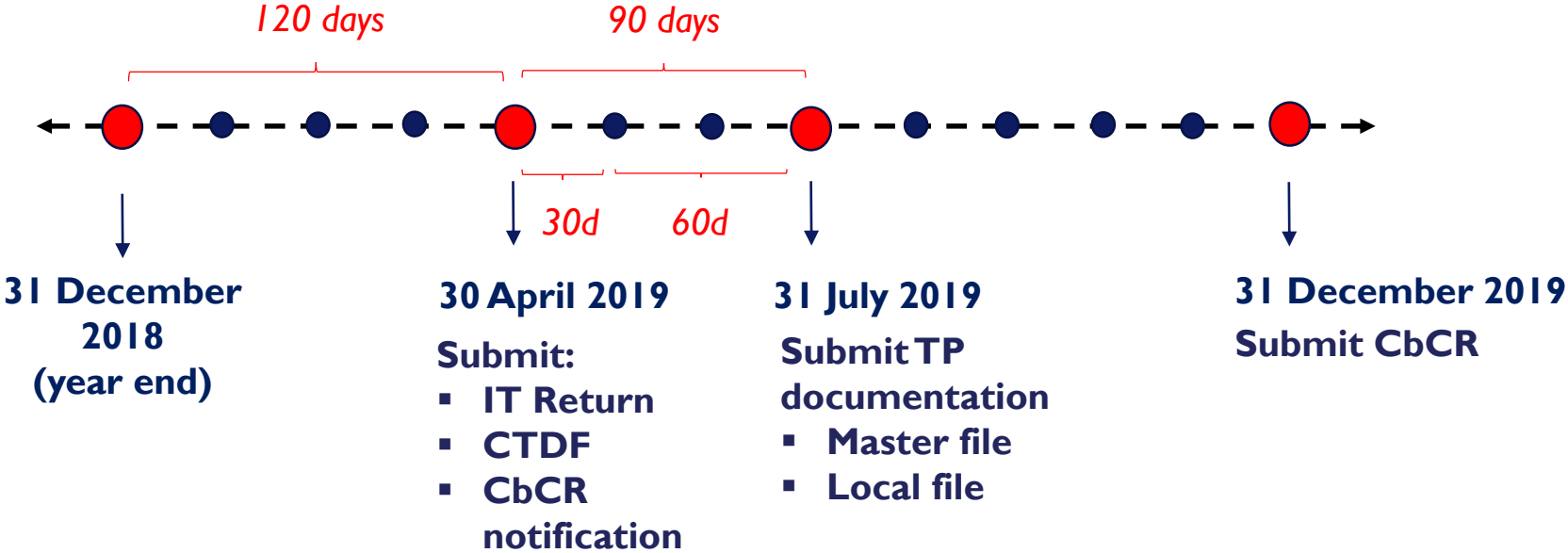
3. Country-by-Country Report (“CbCR”)

- High level group data - revenues by related/unrelated party, earnings, tax paid, employees etc.
- Applies to groups whose previous FY **consolidated group revenue > SAR 3.2 bn annually**

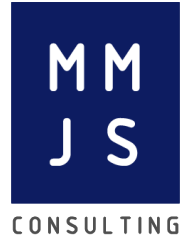
KSA TP FILING REQUIREMENTS



DEADLINES CHRONOLOGY



I. CONTROLLED TRANSACTION DISCLOSURE FORM



CTDF to be filed by all taxpayers having related party transactions. Information in CTDF includes:

- Name and **details of related parties** along with their jurisdictions
- Nature of **transactions** with related parties (i.e. tangible, intangible, services, financial)
- **Value/amount** of each category of transaction(s)
- **TP method** applied to determine arm's length value of each category of related party transaction(s)
- Details of any non-monetary or **free of charge related party transactions**
- Confirmation whether **TP documentation** consistent with KSA requirements has been maintained

A **Chartered Accountant's certificate** confirming that the group's TP policy is consistent with the arm's length principle needs to be filed with CTDF.



2. KSA TP DOCUMENTATION

MASTER FILE

- Organizational structure, illustrating group's legal ownership structure, geographical location of operating activities
- Description of group business including products/services offered, supply chain, key profit drivers, intra-group arrangements etc.
- Information on group's intangibles identifying location of development, ownership & exploitation
- Information on group's intercompany financial activities including material financing arrangements with related/independent parties
- Information on group's financial & tax positions



LOCAL FILE

- Local entity's management structure, organizational chart etc.
- Detailed description of local entity's business activities and strategy, its key competitors
- Description of and agreements relating to all material related party transactions of local entity
- A functional analysis
- A detailed comparability analysis involving selection of most appropriate method & tested party; description of search methodology, listing/description of comparable data; and any adjustments performed
- An industry analysis
- Financial information

3. COUNTRY-BY-COUNTRY REPORT (“CbCR”)

CbCR to be submitted by group’s ultimate parent entity or another nominated group entity in place of the parent entity

Table 1 Information by tax jurisdiction

- Revenues – total and by related/unrelated party(ies)
- P&L before tax
- Tax paid (cash basis)
- Accrued taxes
- Stated capital
- Accumulated earnings
- Number of employees
- Tangible assets (non-cash)

Table 2 Listing of all group entities by jurisdiction

- Classification of each group entity’s business into 13 pre-specified categories (e.g. R&D, manufacturing, group finance, holding company, other)

Table 3 Other information

- Information explaining contents of tables 1 and 2

KSA TP IMPLICATIONS



- **Penalties/fines** for non-compliance, possible **TP adjustments** in case of non-arm's length pricing



- For entities headquartered in UAE with a KSA presence, your centralized head-office, procurement, intellectual property or financing structures could be **scrutiny targets**



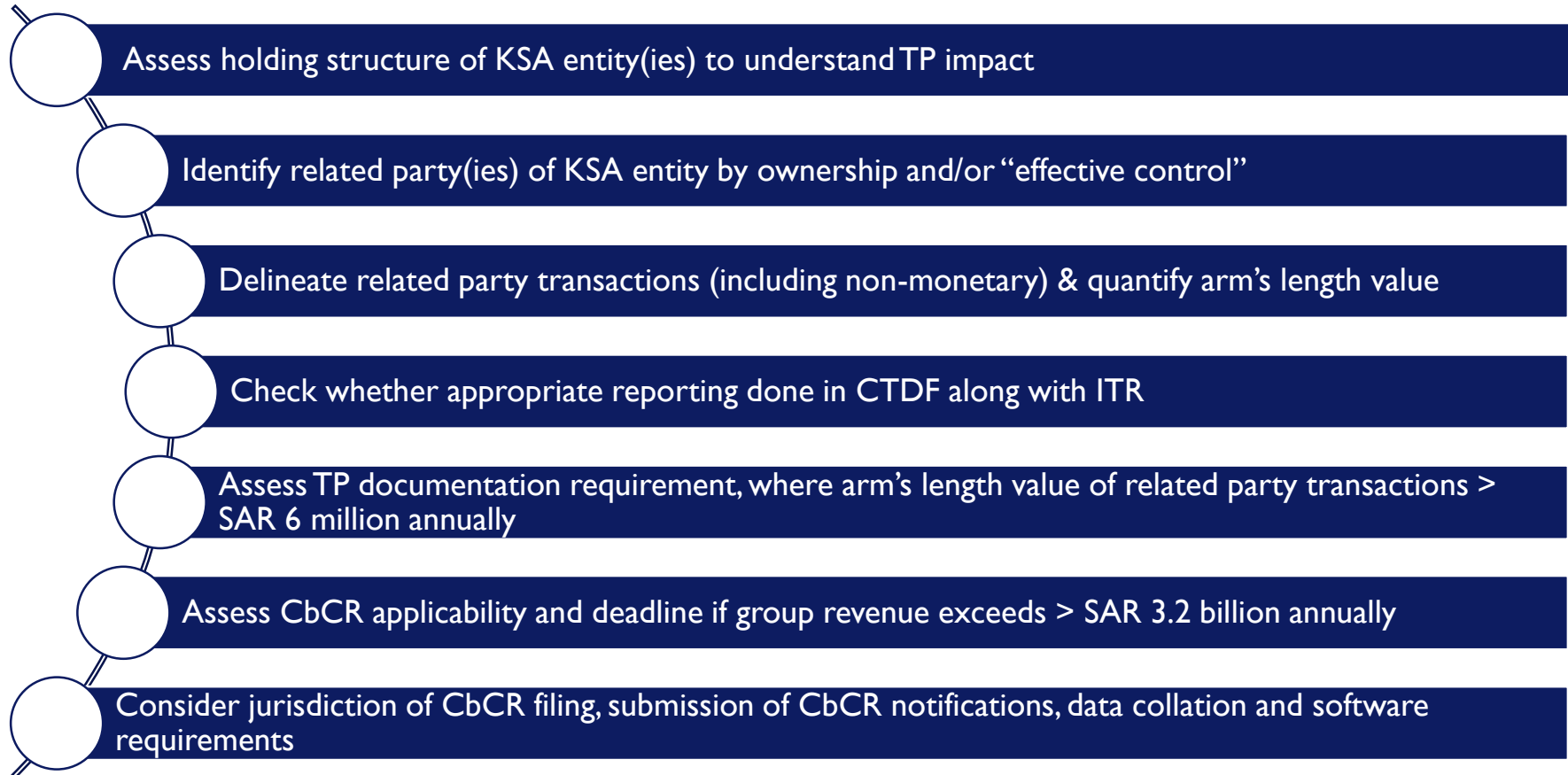
- **Recurring losses, free-of-charge services** and/or intra-group dealings of KSA entities with **group entities in low/no tax jurisdictions** (e.g. UAE, Bahrain) could also be subject to scrutiny



- GAZT may slice/dice CbCR data to **identify “high-risk” areas**. CbCR to be **shared with other tax authorities**

WHAT NEXT FOR KSA BUSINESSES IMPACTED?

PERFORM KSA TP IMPACT ASSESSMENT



Finally, assess impact of applicable fines/penalties if any of above not implemented!



CONTACT US

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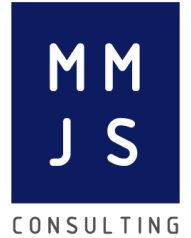
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