

# Investment and Taxation in Saudi Arabia

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# Investment and Taxation in Saudi Arabia

## Topics

- Some Issues/Difficulties
- Mode of Operations
- General Overview of Saudi Income Tax and Zakat
- Tax Incentives in Saudi Arabia
- Saudi Arabia Double Tax Treaties

# ISSUES - DIFFICULTIES – DOING BUSINESS IN THE KINGDOM OF SAUDI ARABIA

Issues/Difficulties	How We Can Help?
■ <b>Finding an appropriate sponsor for conducting business activities in KSA.</b>	■ Particularly where Joint Ventures are concerned, this can be problematic . We can assist in the due diligence process in identifying potential suitable sponsors.
■ <b>Establishing and Administering Bank accounts.</b>	■ In practice, care should be taken to ensure that the General Manager appointed to conduct your day to day operations has sufficient authority and powers as well as administering your bank accounts in Saudi Arabia. We can assist in providing such powers in the entity's Articles of Association.
■ <b>Time taken to establish legal entities in KSA.</b>	■ You should factor in lead time and flexibility in setting up any entity in Saudi Arabia. Establishing an entity can take time as well as obtaining licences from appropriate Ministries. due diligence procedure in identifying suitable potential sponsors.
■ <b>Saudization rules.</b>	■ Ensuring that you comply with the Saudization rules for employing a certain quota of Saudis. We can assist in advising on the quotas required.
■ <b>Taxation issues.</b>	■ Any services that may be provided by you may trigger off “Permanent Establishment” under Saudi Arabia’s Tax Laws giving rise to potential tax implications. KPMG Tax and Zakat advice should therefore be sought on the optimal tax position.
■ <b>Employees and Visas.</b>	■ Determining the number of employees you wish to employ and securing sufficient visas in time. Visas can take time so you need to work in advance of determining how many employees to deploy and skill sets required. We can provide advise on seeking visas but we cannot obtain these for you.
■ <b>Compliance with Saudi Labour Laws,</b>	■ Ensuring that all employees enter into Contracts of Employment that are compliant with Saudi Labour Laws and Regulations. We can assist in that process. In drafting the employment contracts.
■ <b>Repatriation of Profits.</b>	■ This is an issue faced by many foreign companies proposing to conduct business in KSA. We can assist in KPMG Tax providing Tax advice on the repatriation of profits.
■ <b>Property and Conveyancing.</b>	■ Purchase of property and the registration of such property in your name. KPMG can assist in representing you before the Notary Public.
■ <b>Lease Agreements.</b>	■ Due to the lack of proper Landlord Tenant laws, we advise to seek KPMG services in drafting the proper lease agreements and pitfalls to avoid.
■ <b>Insurance.</b>	■ KPMG can advise on what are the necessary insurance policies that need to be obtained in Saudi Arabia.
■ <b>Distribution and licensing Agreements.</b>	■ Special arrangements have to be taken into consideration during the drafting of such agreements to protect your interests, and we can assist in that process.

# Mode of Operations

## Types of Legal Entities

A Foreign Investor may conduct business in one of the following forms :

- A Closed Joint Stock Company;
- A Limited Liability Company;
- A Permanent Branch;
- A Temporary Commercial License;
- A Representative Office; and
- A Technical and Scientific Services Office.

# Mode of Operations ( Continued)

## Limited Liability Company (LLC):

- A Saudi LLC can be 100% foreign-owned.
- LLC may bid on and perform private or public sector projects.
- Shareholder liability in LLC is generally limited to capital contributions. (as long as they adhere to the regulations eg. Accumulated losses less than 50% of share capital)
- LLC most often used when the investor intends to operate in the market for an extended period of time.
- There is no minimum share capital required for a LLC in terms of the Saudi Companies Regulations, however in practice and in terms of SAGIA requirements a Saudi LLC is subject to minimum capitalization that range from SR 100,000 to SR26,000,000 depending on the nature of the activity.

# Mode of Operations ( Continued)

## Branch:

- A branch office is a flexible alternative available to a foreign investor.
- May serve as a vehicle for permanent presence to provide support to affiliated and non-affiliated companies in Saudi Arabia.
- The license of a branch is not tied to a particular project.
- A branch may sponsor its own employees.
- A branch is subject to a minimum capitalization requirement for services activities of SR500,000.

# Mode of Operations ( Continued)

## Technical and Scientific Services Office:

A foreign company performing a government or public sector project can operate under a temporary license which authorizes activity related to a specific project only.

- Foreign companies with commercial agents may establish a technical and scientific services office (TSSO).
- TSSO is to provide technical, scientific advisory and consulting services to local agents and customers.
- TSSO is not permitted to carry out commercial activity. TSSO expenses must be funded by the principal.

# Mode of Operations ( Continued)

## Trading Activities

- For the purpose of conducting trading activities (buying and selling of goods) in Saudi Arabia without a physical presence in the Kingdom then it would be necessary for the appointment of a Saudi Agent to facilitate the distribution/sales of the goods.
- However, if the foreign investor would like to have a physical presence and be directly involved with the buying and selling of the goods, then based on the Saudi Investment Law, the foreign investor must enter into a joint venture with a Saudi partner, with the following conditions:
  - Foreign equity restricted to 75%;
  - Minimum foreign investment is Saudi Riyals 20 million by each foreign investor;
  - Minimum 15% Saudi employees should be trained each year;

# Mode of Operations ( Continued)

## Some prohibited/restricted activities

There are certain activities on the “negative list” which are restricted. These activities include:

- Oil exploration, drilling and production except certain mining services.
- Manufacturing of military equipment, devices and uniforms
- Manufacturing of civilian explosives.
- Catering to military sectors
- Security and detective services
- Real estate investment in Makkah and Madina.
- Tourist orientation and guidance services related to Hajj and Umrah.
- Recruitment and employment services including local recruitment offices
- Real estate brokerage
- Certain types of Printing and publishing
- Certain radio and Television Broadcasting Studios
- Certain Foreign Media Offices and Correspondents

# Mode of Operations ( Continued)

## Some prohibited/restricted activities (Continued)

- Certain Promotion and Advertising
- Public Relations
- Publications
- Press Services
- Production, selling and renting of computer software
- Media consultancies
- Typing and copying
- Motion picture and video tape distribution
- Commission agents
- Audiovisual and media services
- Land transportation services, excluding the inter-city passenger transport by trains
- Services provided by midwives, nurses, physical therapy services and quasi-doctoral
- Fisheries

The background of the slide features several overlapping, semi-transparent globes in shades of blue and white. The globes are arranged in a way that they appear to be floating or overlapping each other, creating a sense of global connectivity. The text is centered over a dark blue rectangular area that is semi-transparent, allowing the globes behind it to be visible.

# GENERAL OVERVIEW OF SAUDI INCOME TAX & ZAKAT

# Overview of Saudi Income Tax & Zakat

## TAX LAW

# General Overview of Saudi Income Tax

- Saudi has system of Income Tax, Capital Gains Tax (CGT), Withholding Tax (WHT) and Zakat;
- Tax Laws (including CGT and WHT) codified under New Income Tax Law;
- Zakat not codified and based on provisions of Royal Decrees, Ministerial Resolutions, Religious Fatwas and DZIT circulars;
- Process underway to codify Zakat into law – latest development - draft law submitted to Shura Council for comment;
- Inter-play between Income Tax and Zakat important in the case of “mixed-companies”;
- Special tax rules which apply to Natural Gas Investment activities;
- No payroll taxes, indirect taxes, stamp duty, transfer duty, etc. VAT on the horizon

# Tax Law

## Types of Taxes

TYPE	EFFECTIVE
. Corporate Income Tax	Tax years beginning after July 30, 2004
. Withholding Tax	July 30, 2004
. Natural Gas Tax	January 1, 2004
. Capital gain on sale of shares	Tax years beginning after July 30, 2004

# Tax Law

Tax Rates	
Corporate Tax	20%
Natural Gas Activities <ul style="list-style-type: none"><li>- Income tax</li><li>- NGIT tax</li></ul>	30% 30% up to 85%
Oil and hydrocarbon activities	85%
Capital gains tax	20%
Withholding tax	Range from 5% to 20%

# Tax Law

Withholding Tax Rates	
Management fee	20%
Royalties / License	15%
Services by head office or related party*	15%
Rent, Technical and Consulting Services, Air ticket, Freight, International Communication, Interest, Insurance, Reinsurance, Dividends paid to non-resident shareholders	5%
Any other payments from a Saudi source	15%

# Tax Law

## Filing Deadlines

Type of Returns	Deadline
▪ Registration	before the end of first fiscal year
▪ Annual Corporate Tax	on or before <u>120 days</u> following the end of taxable year
▪ Annual WHT	on or before <u>120 days</u> following the end of taxable year
▪ Monthly WHT	on or before <u>10th of the month</u> following the month of payment to recipient.
▪ Capital Gain Tax	on or before <u>60 days</u> following the transfer of shares

# Tax Law

## Penalties for Non-Compliance

Type	Fine
<ul style="list-style-type: none"><li>Non-registration with tax authority</li></ul>	SR 1,000 to SR 10,000
<ul style="list-style-type: none"><li>Non-submission of tax return</li></ul>	1% of gross receipt not to exceed SR 20,000 or 5% to 25% depending on delay period
<ul style="list-style-type: none"><li>Delay fine (in addition to non-submission)</li></ul>	1% for each 30 days delay
<ul style="list-style-type: none"><li>Evasion fee</li></ul>	25% of difference in tax

# Other Taxes

▪ Customs Duty	GCC unified customs tariff is 5% (at first point of entry into the GCC) on CIF invoice price (subject to certain exceptions)
▪ VAT / Sales Tax / Other taxes	Saudi Arabia does not impose any Sales Tax or VAT
▪ Personal Income Tax	No salary or payroll taxes applicable in Saudi Arabia
▪ Social Security	2% of basic salary and housing for ALL employees and, 9% for Saudi employees payable by employer

# Overview of Saudi Income Tax & Zakat

## ZAKAT

# General Overview of Zakat Regulations

- Applicable to Saudi registered companies with Saudi/GCC shareholding
- Levied at the rate of 2.5% on the higher of Zakat Base or Adjusted Profits
- Zakat Base calculated by taking into Owners Equity (Share Capital, Long-term liabilities, accumulated reserves, etc) and deducting allowable assets (investments in land, fixed assets, investments in Saudi companies).

# Zakat

- Certain Provisions of the new Tax Law are applicable to zakat payers
  - Depreciation Rules;
  - Filing Deadline ( within 120 days);
  - Fiscal year Provisions ( short/long period);
  - Method of Accounting ( accrual/audited accounts, etc);
  - Withholding Tax Requirements;
  - Contract Reporting Requirements

# Overview of Saudi Income Tax & Zakat

## TAX INCENTIVES IN SAUDI ARABIA

# Tax Incentives

- Taxation incentives, available only for remote locations of (Hail, Northern borders, Jazan, Najran, Al Baha, Al Jouf) but may apply to the Saudi JV as well:
  - Tax deduction of 15% of paid up capital (cash or other assets), for Investments (or project expansions) in rural areas.
  - Tax deduction equivalent to 50% of Annual training costs (for Saudi employees).
  - Tax deduction equivalent to 50% of Annual salaries of Saudi employees.

# Tax Incentives

- The above incentives are subject to the following conditions;
  - Projects value should not be less than SR 1 million.
  - Not less than 5 Saudi employees hired or trained (all in technical and managerial positions)
  - Minimum one year contracts signed with Saudi's to be trained or employed.
  - The work location of (employees or trainees) should be in the same area of the project. The training program (or training institution), (in or out of KSA) should be approved by relevant government agencies.
  - This exemption (decree) will be initially active for the next 10 years.

# Other Incentives

- Freedom of transfer of funds to and from the Kingdom including repatriation of the foreign investor's shares of profits, sale of Equity shares or liquidation surplus
- Protection of private property, trademarks, trade names, etc.
- Access to low cost financing/loans for qualifying industrial projects
- Exemption from customs duty for qualifying manufacturing projects
- Right to own land and building(real estate)required and necessary to carry out the licensed activities in accordance with the provisions of the Non-Saudi Real Estate Acquisition Act
- Foreign investors and non-Saudi staff can be sponsored by the licensed facility

# SAUDI ARABIA TAX

## SAUDI ARABIA DOUBLE TAX TREATIES

# Double Tax Agreements (DTA)

- Currently Saudi Arabia has signed more than twenty DTAs.
- DTA help eliminate double taxation on cross-border transactions by granting taxing rights to only one country or providing for an exemption or credit system.
- In some cases, DTAs concluded with Saudi help eliminate certain taxes (for instance UK DTA exempts Saudi WHT on interest payments) or reduce WHT in some cases (eg royalty WHT rate in terms of UK and Saudi treaty reduced to 8%), etc).
- As per Article 35 - International Agreements:
  - “ To the extent that the terms of a treaty or other international agreement to which the Kingdom of Saudi Arabia is a party are inconsistent with the provisions of this Law (apart from the anti-avoidance provisions of this Law) the terms of the treaty or international agreement prevail over the provisions of this Law”

# Double Tax Agreements (continued)

## Saudi Tax Treaties

Effective Tax Treaties			
Treaty country	Effective date	Treaty country	Effective date
Austria	1 January 2008	Pakistan	1 January 2007
China (PRC)	1 January 2007	South Africa	1 January 2009
France	1 January 1981	South Korea	1 January 2009
India	1 January 2007	Spain	1 January 2009
Italy	1 January 2010	Turkey	1 January 2010
Malaysia	1 January 2008	United Kingdom	1 January 2010
Russia	1 January 2009	Syria	1 January 2011
Netherlands	1 January 2011	Belarus	1 January 2011
Greece	1 January 2011		

**Note:** *The effective dates are for Saudi Arabia only.*

# Double Tax Agreements(continued)

## Treaties signed but not yet in force

Treaty country

Treaty country

Bangladesh

Netherlands

Belarus

Tunisia

Cuba

Greece

Vietnam

Uzbekistan

Singapore

## Treaties being negotiated

Treaty country

Treaty country

Luxembourg

Japan

Egypt

Switzerland

Ethiopia

Brazil

Germany

Morocco

Ireland

# Saudi Arabia and UK Double tax treaty: Salient Features

## Main features of The Saudi Arabia and UK double tax treaty (Effective from 1 January 2010)

- The term “Permanent Establishment” (PE) is clearly defined.
- Presence for a period of more than six months is essential at a building or construction site, assembly or installation project or supervisory activities to be considered as a PE.
- Presence for a period more than 183 days (within any 12 month period) is essential to create a PE for the rendering of services, including consultancy services through employees.

# Saudi Arabia and UK Double tax treaty

## Salient Features ( Continued)

- Withholding tax on dividend payment shall not exceed 5% in case of payment to beneficial owner and 15% where qualifying dividends are from a property investment vehicle (5% rate as per Saudi tax law)
- Withholding tax on interest payment shall be exempt (5% as per Saudi tax law).
- Withholding tax on royalty payment shall not exceed
  - 5% for use or right to use industrial, commercial or scientific equipment;
  - 8% in all other cases (15% as per Saudi tax law).

# Saudi Arabia and UK Double tax Treaty

## Salient Features ( Continued)

- “Fees for Technical Services” appears to be covered under income from business profits.
- Based on Article 7 (Business Profit) of the treaty, no tax should be assessed on a UK entity if it does not have a PE in Saudi Arabia (less than six months stay in Saudi Arabia).
- Treaty does not appear to provide any withholding tax relief on payment of directors’ fees and other similar payments to non-resident directors.
- Any income ,which falls under the category of “other income” should not be subject to tax ,in case of no PE., as it does not fall under any Articles of the tax treaty dealing with specific incomes (e.g. business profit, etc.).
- Capital gains on sale of shares, may be taxed in Saudi, if the seller had a participation of at least 25 percent in the capital of that company.

# Double Tax Agreements (Continued)

## Claiming Benefits

The DZIT has recently issued a circular (23 May 2010) which specifies new rules that will be applicable with regard to claims in respect of beneficial withholding tax provisions under various Double Tax Avoidance Agreements (DTAAs) entered into by Saudi Arabia.

The new rules stipulate that while making payments to a non-resident (belonging to a country with which Saudi Arabia has a DTAA), tax should be withheld in accordance with the domestic withholding tax rates (without giving regard the concessional provisions of the DTAA at the first instance).

Additionally, the circular sets out the procedure that needs to be followed to obtain a refund of overpaid tax in cases where the rate under an applicable DTAA is lower than the rate under Saudi tax law.

# Double Tax Agreements (Continued)

## Claiming Benefits (continued)

The circular rules that the withholder (payer) should submit a letter to the DZIT requesting a refund of the overpaid amount, along with the following documents:

- A letter from the recipient of the payment (non-resident) requesting a refund of the overpaid taxes;
- A certificate issued by the tax authorities of the beneficiary's jurisdiction, certifying that the beneficiary is a resident of that country in accordance with Article 4 of the relevant DTAA and that the amount paid is subject to tax in that country; and
- A copy of the withholding tax form used to pay the tax, together with the bank receipt confirming settlement of the WHT with the DZIT.

## ***Presenter's Contact Details***

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