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VAT

VAT Grouping Guideline

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1. INTRODUCTION

1.1. IMPLEMENTING THE VALUE ADDED TAX (VAT) LAW IN THE KINGDOM OF SAUDI ARABIA (KSA)

The Unified VAT Agreement which was set for the Cooperation Council for the Gulf Arab States (the “GCC”) was approved by the Kingdom of Saudi Arabia by a Royal Decree No. M/51 dated 3/5/1438 H. Pursuant to the provisions of the Agreement, the Kingdom of Saudi Arabia issued the VAT Law under a Royal Decree No. M113 dated 2/11/1438 H (“the VAT Law”) and its corresponding Implementing Regulations (the “Implementing Regulations”) which was issued by the Board of Directors of the General Authority of Zakat and Tax (“GAZT”) by Resolution No.3839 dated on 14/12/1438 H.

1.1.1. General Authority of Zakat & Tax

The General Authority of Zakat & Tax (GAZT), also referred to as “the Authority” herein, is the Authority in charge for the implementation and the administration of VAT in KSA (which may be referred to hereinafter as the “Tax” (if the context did not refer to a deferent meaning). In addition to the registration and deregistration of VAT taxable persons; the administration of VAT return filing and VAT refunds; and undertaking audits and field visits. GAZT also has the power to levy penalties for non-compliance with legal provisions relating to the VAT.

1.1.2. What is VAT?

The Value Added Tax (“VAT”) is an indirect tax which is imposed on the importation and supply of goods and services at the production and distribution stages, with certain exceptions. VAT is implemented in more than 160 countries around the world.

VAT is a tax on consumption that is paid and collected at every stage of the supply chain, starting from when a manufacturer purchases raw materials to when a retailer sells the end-product to a consumer. Unlike with other taxes, persons subject to the VAT will do the following:

- Collect VAT from their customers equal to a specified percentage of each tax eligible sale; and
- Pay VAT to their suppliers, if any, from whom they have received goods and services, equal to a specified percentage of each tax eligible purchase

When taxable persons sell a good or service, a 5% VAT charge – assuming a standard case – is assessed and added to the final sales price. The taxable persons will account for that 5% that they have collected from all tax eligible sales separately from their revenue in order to later remit a portion of it to the Authority. The VAT of taxable persons’ collection on their sales is called the Output VAT.

The same will apply to purchases done by taxable persons, in that VAT will be added at the rate of 5% to purchases of goods or services from other taxable persons (on the assumption that the basic rate applies to those supplies). The VAT a business pays to its suppliers is called the Input VAT.

Further general information about VAT can be found in the KSA VAT Manual at vat.gov.sa.

1.2. THIS GUIDELINE

The purpose of this guideline is to provide additional clarification with associated detail in what is related to Tax Grouping. Hence, this guideline is directed to persons eligible to apply for Tax Grouping.

And whereas This guideline represents GAZT's views on the application and fair treatment of the Unified VAT Agreement, the VAT Law and the Implementing Regulations in what is related to Tax Grouping as of the date of this guideline, but does not include, or purport to include, all the relevant provisions in relation to the Tax Grouping from the Agreement, the VAT Law or the Implementing Regulations. As well as It is not binding on GAZT or on any taxpayer in respect of any transaction carried out and it cannot be relied upon in any way.

However, for advice on specific transactions you may apply for an explanatory ruling or visit the official VAT website at (vat.gov.sa), which contains a wide range of tools and information that is a reference to support the taxable persons, as well as visual guidance materials, all relevant information, and FAQs.

2. DEFINITIONS OF KEY TERMS

A Tax Group for VAT purposes (also referred to in this guideline as **VAT Group**, or **Tax Group**): is a group of two or more legal persons resident in the Kingdom of Saudi Arabia who are treated as being a single taxable person for VAT purposes⁽¹⁾ and registered for VAT with a separate and new Tax Identification Number (“TIN”) issued by GAZT to the Tax Group representative on behalf of the Tax Group.

Representative Member: refers to the Taxable Person in the Tax Group that submits the application to GAZT forming the Tax Group. The Tax Group representative member is one of the members of the Group, and is the one authorised by the other members to represent the Tax Group in all its tax affairs, and is responsible with regard to the obligations and rights devolving on the group, on behalf of all its members such as filing VAT returns, without prejudice to the joint liability of the other members of the group.

Legal Person: refers to a company or other entity that has legal personality under the KSA Companies Law. A natural person is not regarded as a legal person, and a legal person does not include a joint venture companies as defined in the KSA Companies’ Law.

Ownership and Control of Capital and Voting rights: One of the requirements for forming a Tax Group is that each legal person should be subject to common financial control. For Tax Grouping purposes, common financial control requires that the same person or group of persons holds a common interest, directly or indirectly, being either:

- 50% or more of the capital of each legal Person being a member of the Tax Group desired to be formed, or
- 50% or more of control over the ownership or the voting rights in both or all of the Legal Persons of the Tax Group desired to be formed⁽²⁾

Joint liability: represents the liability of group members for VAT debts due to GAZT under the VAT law and Implementing Regulations. All members of a Tax Group have joint liability for VAT payments and all the debts related to it which are due to the authority (including penalties) arising whilst they were part of that group. Following issue of notice of non-payment to the representative member of the group, GAZT may issue a notice directly to any other group members requiring payment from them of the relevant amounts due.

(1) Article 4, VAT Group, Unified VAT Agreement

(2) Article 10(2), Group Registration, Implementing Regulations

3. ECONOMIC ACTIVITY AND VAT REGISTRATION

3.1. WHO CARRIES OUT AN ECONOMIC ACTIVITY?

An economic activity may be carried out equally by natural persons or legal persons. It will be presumed that a legal person (such as companies) that has a regular activity making supplies carries on an Economic Activity. It should be stated that natural persons may perform certain transactions as part of their economic activity, or as part of their private activities. Therefore there are specific rules to determine whether or not a natural person falls within the scope of VAT.

Natural persons and legal persons who carry on an economic activity must register for the purposes of VAT if so required, and such persons must collect the VAT applicable to their activities, and pay the tax collected to the Authority.

Holding companies that carry on economic activities in their own right, such as the provision of management services or financing to group members may come within a Tax Group. Meanwhile, the indirect holding of shares and receipt of dividend income is not, in itself, an economic activity.

Further information on economic activity in different situations is provided in the Economic Activity guideline.

3.2. MANDATORY REGISTRATION

Registration is mandatory for all persons whose annual turnover exceeds a certain threshold. If the total value of a person's taxable sales during 12 months exceeds SAR 375,000 (the "mandatory VAT registration threshold") that person must register for VAT for supplies made, subject to the transitional provisions in the Implementing Regulations, relating to the mandatory registration threshold, during the transitional period.⁽³⁾

Taxable supplies do not include⁽⁴⁾:

- Exempt supplies: such as exempt financial services or residential rental which qualifies for VAT exemption;
- Supplies taking place outside the scope of VAT in any GCC member state; or
- Revenues on sales of capital assets: a capital asset is defined as an asset allocated for long-term business use⁽⁵⁾

In certain circumstances, other tests will apply for mandatory registration:

- Non-Resident persons who are obliged to pay VAT in respect of supplies that they make or receive in KSA are obliged to register for VAT irrespective of the value of the supplies in respect of which they are obliged to collect and pay the VAT⁽⁶⁾;
- During a transitional period up to 1 January 2019, registration is only required for persons whose annual turnover exceeds SAR 1,000,000, and the application for registration must be submitted no later than 20 December 2018

More information on mandatory registration for VAT is contained at vat.gov.sa.

(3) Article 50(1)(2), Mandatory Registration, Unified VAT Agreement, and Article 3, Mandatory Registration - Supplies exceed the Mandatory Registration Threshold, Implementing Regulations

(4) Article 52, Calculating the Value of Supplies, Unified VAT Agreement

(5) Article 1, Definitions, Unified VAT Agreement

(6) Article 5(1), Mandatory registration of Non-Residents obligated to pay Tax in the Kingdom, Implementing Regulations

3.3. OPTIONAL REGISTRATION

Any Resident person who has taxable supplies or taxable expenses exceeding the “Optional VAT registration threshold” of SAR 187,500 in a twelve-month period may register for VAT on a voluntary basis⁽⁷⁾. Optional VAT registration may be desirable where a person wishes to claim a refund of VAT charged to it on their costs before invoices are raised or the occurrence of an onward supply.

Example (1): Golden Falcon Company is a Saudi company that has a contract for services in Riyadh, with invoices for its milestone payments able to be raised starting from January 2020. However, it incurs significant costs of SAR 2 million from local suppliers during the first quarter of 2019 in respect of feasibility and planning studies, before any invoices are raised to its customer.

Accordingly, Golden Falcon Company is able to register on an optional basis as its annual taxable expenses exceed the voluntary VAT registration threshold.

More information on voluntary registration for VAT is contained at vat.gov.sa.

(7) Article 7, Voluntary registration, Implementing Regulations

4. JOINING A TAX GROUP

4.1. PERSONS ELIGIBLE TO JOIN A TAX GROUP

Two or more Legal Persons may apply to form a Tax Group provided that the following conditions are met:

- (a) each is resident in the KSA and carries on an Economic Activity;
- (b) ownership by the same person or group of persons, whether directly or indirectly, of 50% or more of the capital in each legal person, or control of 50% or more of the voting or ownership rights in each legal person; and
- (c) at least one prospective member is a Taxable Person who could register for VAT⁽⁸⁾

These criteria are examined in more detail below.

4.1.1. Legal Person carrying on Economic activity in KSA

Tax Grouping is restricted to legal persons, being entities which are incorporated or established and recognized under KSA law as having separate legal personality. Therefore, no individuals or unincorporated joint ventures are eligible to join or form a Tax Group.

A Legal Person must be a resident in the KSA for VAT purposes. This means it must be an entity incorporated in the KSA or have a fixed establishment in the KSA.

Each Legal Person must carry on an Economic Activity, and an Economic Activity is defined as:

"... an activity that is conducted in an ongoing and regular manner, including commercial, industrial, agricultural, or professional activities or Services or any use of material or immaterial property and any other similar activity".⁽⁹⁾

Dormant entities with no activity of their own are therefore unable to join a Tax Group. Holding companies may only join where they carry on an Economic Activity in their own right.

A Legal Person can only be part of one Tax Group at any time. Below is an illustration of instances when Tax Group is not permitted:

| | | |
|---|---|---|
| ✗ Individuals | ✗ Unincorporated joint ventures or partnerships | ✗ Entities that are not resident in KSA |
| ✗ Dormant entities that do not carry on their own economic activities | ✗ Holding companies (without their own separate activity) | ✗ An entity cannot join multiple Tax Groups |

4.1.2. Common ownership or control

One person, or a group of persons, must hold either:

- 50% or more of the capital of each member of the group desired to be formed; or
- control of 50% or more of the voting rights or all ownership of each member of the group desired to be formed

(8) Article 10, Group registration, Implementing Regulations

(9) Article 1, Definitions, Unified VAT Agreement

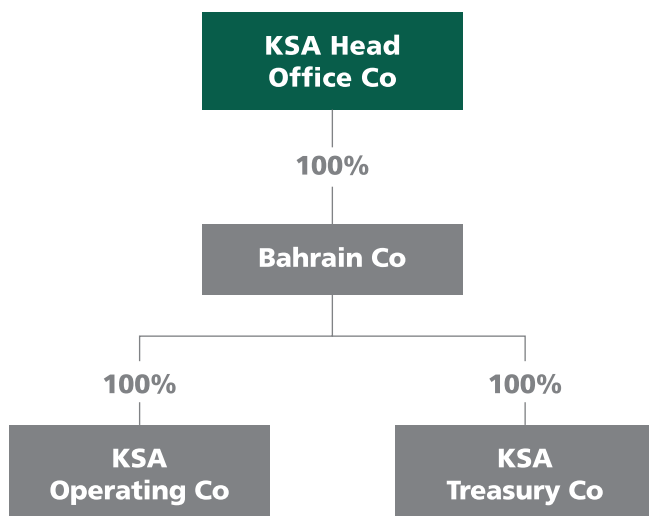
Capital refers to the share capital issued in a company incorporated by shares, or equivalent capital in another legal person.

Ownership or control of the voting rights refers to the ability of the owning person to exercise control over the group members' activity through voting. The percentage of capital owned can differ if the share or other capital has different rights attached.

Ownership or control of the value refers to the owning person having effective control over a certain value of the company, where this differs to the share capital issued. The percentage of capital owned can differ if the share or other capital has different rights attached.

The requirement to hold 50% or more in a company means that evenly held company with two 50% shareholders may join a Tax Group with one of its shareholders. The company may not join two Tax Groups. It is not necessary that the person or persons holding ownership or control in the group members is part of the group, or eligible to join the group. The ultimate owner may, for example, be an individual or a non-resident, provided the group members are themselves eligible to join.

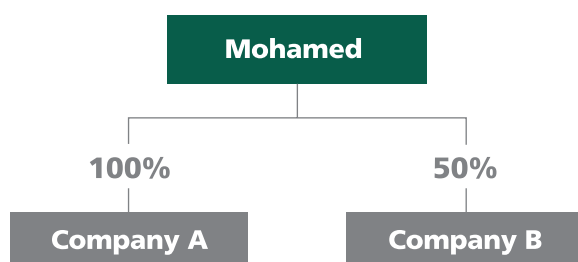
Ownership may be held directly (with the owner himself holding the shares) or indirectly (with an ultimate owner holding effective ownership through an intermediary company). It is not necessary for all eligible entities to join the Tax Group. Tax Grouping is an optional election.



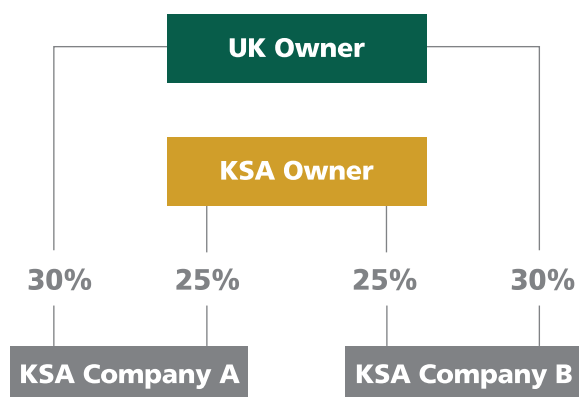
Example (2): KSA Head Office Co holds 100% ownership in Bahrain Co. Bahrain Co holds 100% ownership in (A) KSA Operating Co and (B) KSA Treasury Co.

Provided that each carries on an economic activity in KSA. Therefore the KSA Head Office Co, (A) KSA Operating Co and (B) KSA Treasury Co are eligible to form a Tax Group.

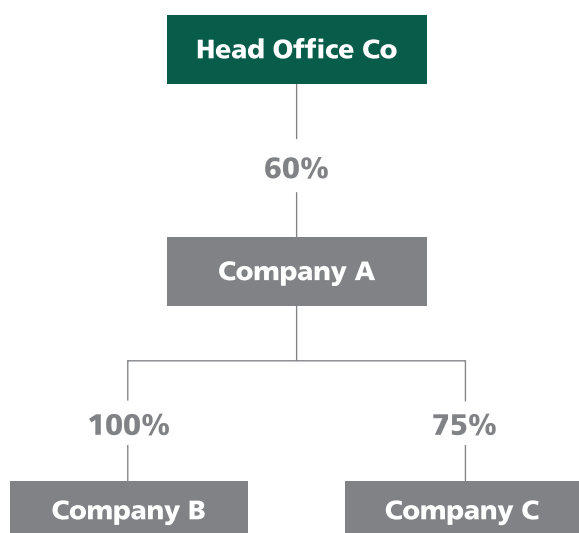
Bahrain Co cannot join the group as a non-resident in KSA – but its intermediary ownership does not preclude the other entities from joining a group in KSA.



Example (3): Mohamed is an individual who holds 100% ownership in (A) Halal Company and 50% ownership in (B) Al Amal Company. Provided that each company is KSA resident and carries on an economic activity, both companies may form a Tax Group.

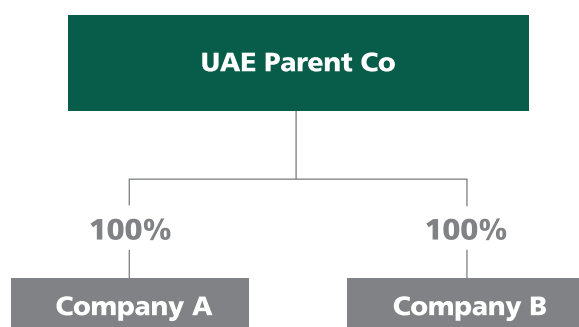


Example (4): A UK investor holds 30% ownership in KSA Company A and KSA Company B. Meanwhile a KSA investor also holds 25% ownership in each company, with the remaining shares being held by individual market investors. The same two investors own more than 50% (a total of 55%) in each company. Therefore, Company A and Company B are eligible to form a Tax Group.



Example (5): Head Office Co owns 60% of Company A. Company A holds 100% in Company B and 75% in Company C. Hence, Head Office Co has indirect ownership of 60% in Company B and 45% in Company C. All companies are KSA resident and carry on an economic activity.

In this situation, Head Office Co may form a group with Company A and Company B. but Head Office Co could not form a Tax Group with Company C as it does not meet the Tax Grouping requirement. Alternatively, Company A may choose to form a group with Company B and Company C only. But all entities cannot join the same group.



Example (6): Two KSA sister entities, Company A and Company B, are wholly owned by a Parent Company in the UAE. The Parent Company has no establishment of its own in the KSA and is therefore a non-resident. In this situation, Company A and Company B may form a Tax Group, even though the ultimate owner (Parent Company) is not eligible to join the group.

4.1.3. At least one member of the Tax Group is a Taxable Person

One group member must be eligible to be registered for VAT (and therefore a “Taxable Person” for KSA VAT purposes).⁽¹⁰⁾ In order to be eligible to register for VAT, that group member must make annual taxable supplies or taxable expenses meeting or exceeding the voluntary VAT registration threshold of SAR 187,500. Hence, one group member is required to meet the voluntary VAT registration threshold criteria. If this is the case, it is not necessary for other group members to measure their respective turnover, provided they all carry an Economic Activity.

Therefore, the supplies of all group members may not be added together to allow the group to register voluntarily.

Example (7): A person owns four companies. These companies had the following taxable revenues during the 2018 calendar year:

| | Annual taxable revenues (SAR) |
|--------------|-------------------------------|
| Company A | 200,000 |
| Company B | 80,000 |
| Company C | 60,000 |
| Company D | 50,000 |
| Total | 390,000 |

Company A is eligible to register in its own right, as its turnover exceeds the voluntary registration threshold. The other companies all carry on an economic activity and may join a Tax Group with Company A, despite not reaching the annual threshold individually and despite the fact that all Companies' annual taxable turnover exceeds the threshold.

The turnover of Companies B, C and D combined is SAR 190,000. Whilst the combined turnover exceeds the voluntary registration threshold, these companies cannot form a Tax Group without Company A as none is a Taxable Person in their own right.

4.2. RESPONSIBILITIES OF THE REPRESENTATIVE MEMBER

The Representative Member will be a member of the Group. That member will be regarded as responsible for the obligations and rights arising out of the Tax Group on behalf of all group members.⁽¹¹⁾ This includes the submission of all returns, correspondence and payments due in respect of the whole group.

By filing returns and correspondence for the group, the Representative Member interacts directly with the Authority on behalf of all group members. All members are bound by those obligations, and jointly liable for the corresponding VAT due. By submitting an application to register, the Representative Member undertakes that he has the authority to bind other group members when dealing with GAZT in respect of VAT.

Whilst the Representative Member has primary responsibility for the VAT obligations of the group, the common liability rules result in all group members having joint responsibility for these obligations.

⁽¹⁰⁾ Article 2, Taxable Persons required to or eligible to register in the Kingdom, Implementing Regulations

⁽¹¹⁾ Article 11 (1), Application to form a Tax Group, Implementing Regulations

4.3. APPLICATION TO FORM A TAX GROUP

An application for group registration must be filed by the representative member on the online portal of GAZT. If group members are not already registered with GAZT, the application must include the relevant details required for VAT registration of each member.⁽¹²⁾

4.3.1. Review of the application

GAZT may request from the Tax Group representative company incorporation, ownership or other documentation to verify the information included in the application for registration and that each member is eligible to join the Tax Group. The Tax Group representative must provide this information within 20 days from the date of the request. Therefore, GAZT will only approve the application where it is satisfied that all members are eligible to join the group.

Upon approval of an application, GAZT will issue a new Tax Identification Number to the group on behalf of the group and suspend existing TINs of members who are individually registered.

GAZT may refuse an application for registration where the information contained is not valid or the legal Persons are not eligible to be registered as a Tax Group.

4.3.2. The Effective Date of the Tax Group registration

The Tax Group takes effect from the first day of the month following the approval date.⁽¹³⁾ Therefore, for example if GAZT approves an application on 20 April, Tax Grouping will take effect from 1 May, and the approval notification will set out the date of effect. GAZT may prescribe a later effective date.

(12) Article 11(1), Application to form a Tax Group, Implementing Regulations

(13) Article 11(5), Application to form a Tax Group, Implementing Regulations

5. AMENDING A TAX GROUP

5.1. COMPULSORY CHANGES

The Representative Member must notify GAZT where any information originally stated in the application changes or any member of the group is no longer eligible to be part of the Tax Group. This notification must be provided within 20 days of the change.⁽¹⁴⁾

Based on the above, if a member is no longer eligible to be in the group or if the group is no longer eligible to exist, the changes will take effect from the date that legal Person is no longer eligible to form part of the Group or from the disbanding date (even if the Authority is notified on a later date).

5.2. OTHER CHANGES

The group may also elect to change the group in other circumstances. The Representative Member may, with the permission of all other group members, file an application to:

- Add a new member or members to the group;
- Remove existing members from the group;
- Substitute the Representative Member; or
- Disband the group

These changes will generally take effect from the date the application is filed, unless the Authority specifies another date.⁽¹⁵⁾

5.3. EFFECT OF REMOVING MEMBERS OR DISBANDING THE TAX GROUP

If one or more members leave the Tax Group, or if the Tax Group disbands, each former member is viewed as a separate legal person from that date. If the exiting group members are required or is eligible to be registered for VAT in its own right, the application form must state this. The individual Legal Person will be registered with a new Tax Identification Number (or any former suspended TIN will be reactivated).

If the exiting member is not required to be registered and does not wish to be voluntarily registered, it must deregister for VAT. A final VAT return must be filed to account for any nominal supplies made for assets (fixed assets and stock) which is owned by that member and held upon deregistration.

A legal person who leaves a Tax Group and is immediately registered as an individual taxable person is not viewed to deregister and does not need to file a final VAT return.

Example (8): Companies A, B and C are all owned by the same individual and are part of the same Tax Group. Their annual taxable revenues are as follows:

| | |
|-----------|---------------|
| Company A | SAR 2,000,000 |
| Company B | SAR 1,500,000 |
| Company C | SAR 85,000 |

Company B is the Representative Member of the group. On 30 June 2019, the owner of the companies divests his ownership in Companies A and B to different purchasers, and retains Company C.

(14) Article 12 (1), Amendments to or disbanding of a Tax Group, Implementing Regulations

(15) Article 12 (2), Amendments to or disbanding of a Tax Group, Implementing Regulations

The three companies are no longer eligible to form part of a Tax Group from that date. Company B, as the Representative Member, must notify GAZT within 20 days of this date with these changes. Company A and Company B exceed the Mandatory Registration Threshold in their own right, so they must immediately apply to be registered individually. Company A and Company B will be issued with new Tax Identification Numbers valid from 30 June 2019.

Company C is not eligible to be registered. It will be de-registered for VAT with effect from 30 June 2019. It holds assets (fixed assets and stock of commodities) valued at SAR 20,000 on this date. The final VAT return for the group must include a nominal supply for SAR 1,000; which is 5% of the value of assets held on deregistration.

6. IMPLICATIONS OF TAX GROUP TREATMENT

6.1. THE TAX GROUP AS WHOLE IS REGARDED AS A SINGLE TAXABLE PERSON

The Tax Group is registered as a single taxable person.⁽¹⁶⁾ As the Representative Member is deemed to carry on the activities of the group on behalf of all group members, all supplies can be seen to be made by the Group (or the Representative Member), rather than by the individual members. All invoices issued by members of the Tax Group should contain the TIN of the Representative Member.

Similarly, all purchases, expenses and supplies to individual group members are treated as supplies to the Tax Group as a whole for VAT purposes. However, the contractual obligations between individual members and third parties are unchanged. Suppliers can issue tax invoices in the name of the group or the Representative Member but it should contain the Tax Group TIN number.

6.2. DISREGARD OF SUPPLYING GOODS AND SERVICES BETWEEN GROUP MEMBERS

As the Tax Group is deemed to act as a single person, it cannot supply to itself for VAT purposes. Therefore, any goods or services supplied from one group member to another is not a supply within the scope of VAT.⁽¹⁷⁾

Supplies made between group members are not reported on the VAT return, and are likewise ignored for purposes of counting taxable or exempt turnover (for example, when calculating the default proportional recovery method of input tax).

Example (9): Companies A, B and C are all financial service providers and members of a Tax Group. Their supplies made during 2020 are as follows:

| | Taxable supplies | Exempt supplies | Intra-group supplies |
|-----------|------------------|-----------------|----------------------|
| Company A | SAR 2,250,000 | SAR 1,800,000 | SAR 30,000 |
| Company B | SAR 1,750,000 | SAR 3,200,000 | SAR 0 |
| Company C | SAR 500,000 | SAR 800,000 | SAR 1,000,000 |

The Tax Group must allocate individual supplies to taxable and exempt activities, following the procedure described in section 8 of this guideline. For deduction of VAT on inputs of the Group as a whole which cannot be allocated to a particular supply or a particular Company, the Tax Group must ignore the intra-group supplies when calculating the proportional deduction.

The proportional deduction should be calculated, ignoring the intra-group supplies, as:

$$\text{Taxable Supplies} / (\text{Taxable Supplies} + \text{Exempt Supplies}) = \\ \text{SAR } 4,500,000 / (\text{SAR } 4,500,000 + \text{SAR } 5,800,000) = 43.7\%$$

6.3. JOINT LIABILITY OF GROUP MEMBERS

Each member is jointly liable for VAT debts and obligations of the entire group arising whilst he was part of the group.⁽¹⁸⁾

In practice, the Representative Member will have the primary obligation for VAT obligations. However, in cases where the Representative Member or another member has not complied with payment or other obligations, GAZT may raise an assessment or demand directly on any group member for VAT or penalties due.⁽¹⁹⁾

(16) Article 4, VAT Group, Unified VAT Agreement

(17) Article 18(2), Supplies by a legal Person to itself, Implementing Regulations

(18) Article 12(6), Amendments to or disbanding of a Tax Group, Implementing Regulations

(19) Article 67, Joint liability for Tax and penalties, Implementing Regulations

7. TAX GROUPING IN SPECIAL CASES

GAZT has special powers to preserve tax revenues in respect of Tax Grouping.

7.1. POWERS OF GAZT TO SET ASIDE TAX GROUPING

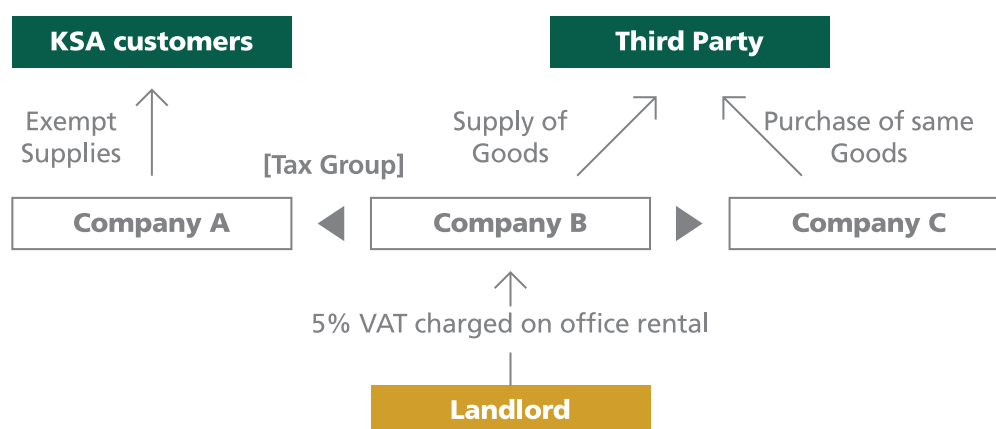
GAZT may issue a notice to the Representative Member removing the status of Tax Group in connection with any intra-group supplies, in case it believes that the existence of the group will result in obtaining tax advantages contrary to the purpose of the Law.⁽²⁰⁾

GAZT may not use these powers where the intra-group supplies represent part of a usual commercial practice, and this provision is only expected to apply very limited circumstances.

The removal of VAT from usual commercial activity between Tax Group members is a tax advantage which the law intends to confer, whereas there may arise out of entitlement to tax benefits agreements and transactions between group members involving artificial transaction which is contrary to the VAT Law.

Example (10): Company A, B and C are members of a Tax Group. Company A makes exempt supplies and is not able to deduct input VAT on its exempt activities. Company B and Company C are created to enter into transactions with a third party where Company B sells goods and Company C purchases these at an artificially inflated value.

Company B acts as contracting party for the office lease and all overhead costs for the group, and attributes a large portion of this to the artificial commercial activity to improve VAT deduction using the default method. Obtaining an advantage of Tax Grouping in this case was the principal purpose of forming the Tax Group.



The Authority will issue a notice to the group representative to set aside the effect of Tax Grouping. This notice may have retrospective effect.

In the above example, following issue of a notice by the Authority, supplies of overheads (including the recharge of the office lease) made from B to A would then need to include VAT.

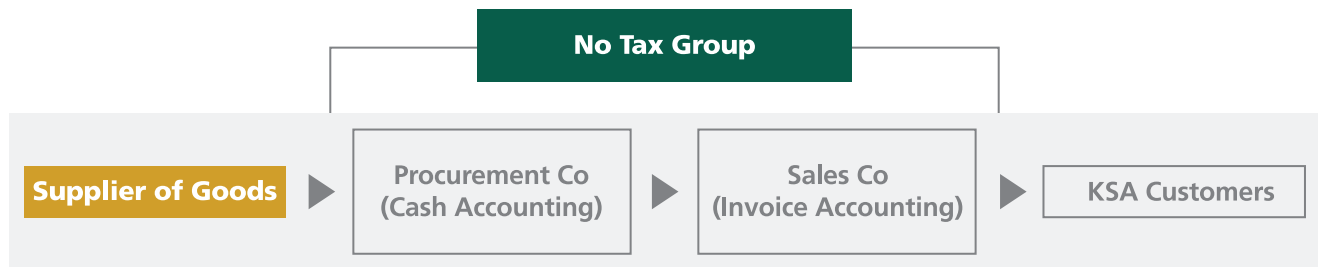
Powers of GAZT to request for two persons to join Tax Grouping In other cases, GAZT may require two or more persons to form a Tax Group, where it believes the registration of either of them as a separate person would result in a tax advantage which is contrary to the purpose of the Law.⁽²¹⁾

These powers will not be applied to usual commercial practice, but are generally aimed to counter artificial schemes which are designed in order to produce a tax advantage.

(20) Article 12(7), Amendments to or disbanding of a Tax Group, Implementing Regulations

(21) Article 12(8), Amendments to or disbanding of a Tax Group, Implementing Regulations

Example (11): Al Iman Procurement Company is a separate legal entity set up to purchase goods for use in the wider Al Iman corporate group. It is not part of any Tax Group. Al Iman Procurement Company is registered on the cash accounting basis and claims an immediate input VAT deduction for goods purchased for cash. Al Iman Sales Company is registered on an invoice accounting basis, and do not make payment for 9 months. Al Iman Sales Company is able to recover input VAT on purchases from Al Iman Procurement Company despite not paying.



If Al Iman Procurement Co purchases equipment and sells this onwards to Al Iman Sales Co in January, but payment is not received until September, the following VAT consequences occur:

| Procurement Co | Sales Co |
|---|--|
| Pays output VAT - September (cash accounting basis) | Uses equipment – no output VAT |
| Deducts input VAT - January (cash accounting basis) | Deducts input VAT - January (invoice accounting basis) |

By registering these entities separately and flexing payment terms to suit the cash accounting and invoice accounting regimes, there is an excessive cash flow advantage for the corporate group, which is contrary to the purpose of the cash accounting regime in the Law.

If both Al Iman Procurement Company and Al Iman Sales Company are qualified with one another to form a Tax Group, GAZT may issue a notice to both of them that they are to be treated as a Tax Group on any date specified by the Authority, in the event that the registration of either of the companies as a separate person will or might result in tax advantages in conflict with the purpose of the VAT Law.

8. INPUT VAT DEDUCTION

8.1. GENERAL PROVISIONS

A VAT registered person may deduct Input VAT charged on goods and services it purchases or received in the course of carrying on its Economic Activity. Input VAT may be deducted on:

- VAT charged by a VAT-registered supplier in the KSA;
- VAT self-accounted by the VAT-registered person under the Reverse Charge Mechanism;

As a rule, input VAT which is related to the Group's VAT exempted activities, is not deductible as input VAT.

In addition, input VAT may not be deducted on any costs not incurred as part of the Economic Activity (including some blocked expenditure types such as entertainment and motor vehicles⁽²²⁾), or on any costs which relate to exempt supplies.

This input VAT is a credit entered on the VAT return which is offset against the VAT charged on supplies (output VAT) made during that period.

Input VAT may only be deducted where the taxable person holds a tax invoice or Customs documents proving the amount of VAT due (or any alternative document proving the amount of input tax paid or due for payment, with the consent of the Authority). The invoice received from the supplier should show the name of either the Representative Member or a current VAT group member as the recipient of the supply.

8.2. PROPORTIONAL DEDUCTION: ATTRIBUTION OF INPUT VAT

VAT incurred which relates to a taxpayer's VAT exempt supplies, such as financial services or residential rental, is not deductible as Input VAT. A taxable person making both taxable, and exempted supplies, can only deduct the Input VAT related to the taxable supplies. If a taxable person incurs general costs or expenses in respect of the making of taxable supplies, and other exempt supplies, he must in that case allocate the costs and expenses precisely and specify those costs relating to the taxable part. Input tax will be determined in accordance with the following provisions⁽²³⁾:

Supplies between group members will be disregarded and are not included as taxable or exempt supplies for input VAT deduction purposes.

For Tax Groups whose activities include partly exempt activities, the Input VAT available to them must be determined using the following process.

| | |
|---|---|
| Input VAT directly attributed to taxable VAT sales | Deduct in full |
| Input VAT directly attributed to exempt sales | No deduction |
| Overheads, and input tax that cannot be directly attributed to taxable supplies | Partial deduction based on apportionment |

The overhead costs/expenses incurred by the Tax Group for making both taxable and exempted supplies must be apportioned to most accurately reflect the use of those costs in the taxable portion of the taxpayer's activities correctly. The Tax Group will be regarded as a single person for tax purposes, and the taxable part will be based on the combined activities of all of the members of the group (or a proportional deduction for each member individually), and they will be amalgamated in the combined tax return submitted by the Group Representative.

(22) A detailed list of the blocked expenditures is listed under article 50 of the Implementing Regulations

(23) Article 51, Proportional deduction of Input Tax, Implementing Regulations

The calculation of the proportional deduction in respect of the value of the taxable supplies made during a particular year will be done using the following default method:

The value of **Taxable Supplies** made by the Taxable Person
(all members of the group) in the last calendar (Gregorian) year

The total value of **Taxable Supplies** and **Exempt Supplies** made by the Taxable
Person (all members of the group) during the last calendar (Gregorian) year

The above method does not include supplies of Capital Assets made by the taxpayer, as these distort the use of input VAT.

In the case of Tax Groups, the expenses that cannot be directly linked to taxable supplies or exempt supplies are usually distributed on the basis of all overheads incurred by each member of the group individually and the equivalent of the supplies made by the member company of the group. In that event, the method of calculation “according to the amount incurred by each sector” will permit the deduction of input tax in accordance with the activities of each company individually (individual business) and it will be treated as a sector separate from the Tax Group, and will consequently constitute best practice for the use of overheads.

Example (12): A family group owns three different companies, and it decides to form a tax group between them. Company A imports and sells cigarettes, Company B leases out long-term residential units and leases out short-term furnished flats, and Company C is an investment company making some financial supplies subject to VAT, and others that are exempt.

The three companies are operated separately from one another, but there are joint costs of low value. The supplies for the company’s in 2020 were as follows:

| Company | Taxable supplies (SAR) | Exempt supplies (SAR) | Default proportion | Unallocated overheads | Expenses deductible for each company (sector) individually |
|------------------------------------|------------------------|-----------------------|--------------------|-----------------------|--|
| A | 14,000,000 | 0 | 100% | 50,000 | 50,000 |
| B | 2,000,000 | 3,000,000 | 40% | 350,000 | 140,000 |
| C | 500,000 | 2,000,000 | 20% | 200,000 | 40,000 |
| Total proportion for the tax group | 16,500,000 | 5,000,000 | 77% | 600,000 | 230,000 |

Company A has the highest amount of taxable supplies and the lowest amount of overheads that cannot be allocated; in the event that the default mode is used, the group would be permitted to deduct its proportion of 77% from the total overheads of the group (SAR 462,000), and that will result in a distortion in the cost deduction for both Company B and Company C. For that reason, the “per sector” method of calculation must be used, and the overheads must be calculated for each company individually.

Alternative attribution methods, using other calculation approaches than the value of supplies, may be approved with GAZT in cases where these better reflect the actual use of VAT incurred. More information will be provided in what is related to the VAT Deduction and VAT Proportional Refund in a separate guideline. ⁽²⁴⁾

(24) Article 51(8) Proportional deduction Of Input Tax, Implementing Regulations

9. OBLIGATIONS OF THE TAXABLE PERSON

In your capacity as a taxable person, you must evaluate your tax obligation and also comply with the conditions and obligations relating to VAT. This includes registering for VAT as necessary, and exactly calculating the net amount of VAT payable, and paying the tax at the time due, as well as keeping all necessary records and cooperating with officials of the Authority on demand.

If you are not sure of your obligations, you must contact the Authority through its website at vat.gov.sa or by other means of communication, and you may also seek external consultation through a qualified consultant. There follows below a review of the most important tax obligations provided for in the Law and the Implementing Regulations.

9.1. TAX IDENTIFICATION NUMBER

GAZT will issue a Tax Identification Number to the group, and will suspend any existing TINs for individual group members who had previously been separately registered.

The Tax Group's TIN should be used on tax invoices and any correspondence relating to VAT.

9.2. ISSUING INVOICES

A supplier must issue a tax invoice for each taxable supply made to any VAT-registered person or to any other legal person, or issue a simplified tax invoice in the event that the value of the supplies is less than SAR 1,000, or issue a simplified invoice for supplies made to an end consumer, by no later than fifteen days following the end of the month in which the supply is made. The invoices must clearly mention some information and data for example the date of the invoice, the TIN of the supplier, the taxable amount, the tax percentage applicable and the VAT amount charged.⁽²⁵⁾

If different rates are applied for the supplies, the value of each item must be separately specified, as well as the VAT applied to that item. A VAT invoice may be issued in the form of a commercial invoice, provided that that document contains all of the requirements for issuing tax invoices as set out in the Implementing Regulations to the Law.⁽²⁶⁾

So far as concerns the Tax Group, the tax invoice issued by the group or any member of the group must include the Group's TIN, and the tax invoice may include the name and address of the member company in the group as being the actual supplier.

Further information on the requirements for tax invoicing can be found in the VAT manual published at the GAZT website, vat.gov.sa.

9.3. FILING VAT RETURNS

Each VAT registered person, including a Representative Member of a Tax Group, must file a VAT return with GAZT for each monthly or quarterly tax period. The VAT return is considered the taxable person's self-assessment of tax due for that period.

Monthly VAT periods are mandatory for businesses or Tax Groups with an annual turnover exceeding SAR 40 million. For all other VAT registered persons, the standard tax period is three months.

The VAT return must be filed, and the corresponding payment of net tax due made, no later than the last day of the month following the end of the tax period to which the VAT return relates.

(25) For more detail on the requirements for issuing tax invoices, refer to Article 53 (5) of the Implementing Regulations

(26) Article 53, Tax Invoices, Implementing Regulations

Further details concerning the filing of the tax return will be given in a separate guideline.

If the VAT return results in VAT due to the taxpayer, or if the taxpayer has a credit balance for any reason a request for a refund of this VAT may be made with the filing of the VAT return, or at any later time during the next five years or by filing an application for a refund to the Authority. GAZT will review these requests and will make payment of on approved refund requests directly to the taxpayer.⁽²⁷⁾

For a Tax Group, the VAT return has the same form as for an individual taxpayer, but must combine the supplies made by and to all group members (other than supplies between group members). The members of the Tax Group will consolidate the values of their VAT returns in order to reflect their input and output tax for that period, and will then submit them to the representative member of the group for inclusion in the Tax Group's consolidated return, as a practical measure for gathering information from the Tax Group Representative for filling in the consolidated VAT return for the group. If the Authority so requires, the representative member may have access to the relevant records, and provide the Authority with them.

Further information can be found in the VAT manual at vat.gov.sa.

9.4. KEEPING RECORDS

All taxpayers are required by law to keep appropriate VAT records relating to their calculation of VAT for audit purposes. This includes any documents used to determine the VAT payable on a transaction and in a VAT return. This will generally include:

- Tax invoices issued and received;
- Books and accounting documents;
- Contracts or agreements for large sales and purchases;
- Bank statements and other financial records;
- Import, export and shipment documents; and
- Other records relating to the calculation of VAT

Records may be kept in physical copy, or in some cases electronically – but must be made available to GAZT on request.

All records must be kept for at least the standard retention period of 6 years. That minimum period for retention is extended to 16 years in connection with invoices and records relating to movable capital assets.

9.5. VAT REGISTRATION CERTIFICATE

A resident person who is subject to VAT and registered with the Authority in the VAT system must display the certificate to the effect that he has been registered in the VAT system in a place visible to the public at his main place of business and at all his branches.

In the event of a contravention, the person in breach will be liable to the penalties provided for in the Law.

9.6. REQUESTING AN EXPLANATORY RULING

If, having consulted the relevant law and guidance, you are unsure on how VAT applies to a particular activity or transaction that you carry out or intend to carry out, you may apply to GAZT for an explanatory ruling. The request should contain the full facts of the particular activity or the particular transaction that you wish the Authority to consider.

(27) Article 62, Tax Returns, Implementing Regulations

The reply to the request for a ruling may be made as follows:

- Public: in which case GAZT will publish details of the ruling, without any taxpayer-specific information;
or
- Private: in which case GAZT will not publish the ruling

The explanatory ruling request may include all information on the activity or transaction that you request a ruling for and a description of the specific area of uncertainty in the law or guidance which you have considered. You may choose to describe the alternatives and what you consider to be the correct treatment.

GAZT is not obliged to respond to all requests for explanatory rulings. It will consider and prioritize requests based on factors such as:

- The level of information presented by the taxpayer in the request;
- The benefit to the wider taxpayer community in issuing a public explanatory ruling on the transaction or activity; and
- Whether there is existing law or guidance which addresses the request

A public or private explanatory ruling issued by GAZT is not binding on GAZT or on any taxpayer in respect of any transaction carried out and it cannot be relied upon in any way.

9.7. CORRECTING PAST ERRORS

If a tax payer is aware of an error or an incorrect amount in a filed VAT Return, or of any other VAT obligation which he has not complied with, he should notify GAZT and correct the error by amending the tax return. Errors resulting in a net understatement of VAT exceeding SAR 5,000 must be notified to GAZT within twenty days of becoming aware of the error or incorrect amount.

For small errors, resulting in an understatement of the net VAT of less than SAR 5,000, the tax payer may instead correct the error by adjusting the net tax in the following VAT return.

With regard to Tax Groups, the rectification of errors will be done at group level through its VAT returns. Further information on correcting errors can be found through vat.gov.sa.

10. PENALTIES

Penalties or fines may be imposed on taxpayers for violations of VAT requirements set out by the Law or Implementing Regulations:

| Description of offence | Associated fine |
|--|--|
| Submitting false documents with the intent of evading the payment of the VAT due or to reducing its value | <ul style="list-style-type: none"> • At least the amount of the VAT due • Up to three times the value of the goods or services |
| Move goods in or out of the Kingdom without paying the VAT due | <ul style="list-style-type: none"> • At least the amount of the VAT due • Up to three times the value of the goods or services |
| Failure to register for the VAT in the allotted timeframe | SAR 10,000 |
| Filing incorrect tax return, amend a tax return after submission or filing any document with the authority relating to VAT resulting in a lower amount due | 50% of the value of the difference between the calculated Tax and Tax due |
| Failure to file VAT return in time | 5-25% of the VAT in respect of which the return should have been submitted |
| Failure to pay the VAT in time | 5% of the VAT due for each month or part of a month |
| Collecting VAT without being registered | Up to SAR 100,000 |
| Failure to maintain books and records as stipulated in the regulations | Up to SAR 50,000 |
| Preventing GAZT employees from performing their duties | Up to SAR 50,000 |
| Violating the provisions of the VAT regulations or the VAT law | Up to SAR 50,000 |

In all cases, if a violation is repeated within three years from the date of issuing the final decision of the penalty, the fine for the second offense may be doubled.

The level of the penalty or fine imposed is set by GAZT with regard to the taxpayer's behaviour and compliance record (including taxpayers meeting their requirements to notify GAZT of any errors and provide co-operation to rectify mistakes).

11. CONTACTING US

For more information about VAT treatment, kindly visit our website: vat.gov.sa; or contact us on the following number: 19993

APPENDIX: FREQUENTLY ASKED QUESTIONS

1. Can persons resident in KSA form a Tax Group if the ultimate owner is not VAT registered?

Yes, provided that the entities are under common control and the remaining conditions for grouping are met.

2. Is it mandatory for all commonly owned companies to join the Tax Group?

No, Tax Grouping is optional. In limited circumstances GAZT may require companies to join or form a Tax Group to prevent avoidance.

3. The entities in my group carry on different business types. Can they join a single Tax Group?

Yes, the Tax Group will be viewed as a single taxable person carrying on different business types.

4. Does each intended group member need to be a registered person to apply?

No, at least one member of the group must be eligible to register for VAT in its own right.

5. What changes must be made to invoicing once I join a Tax Group?

Tax invoices issued for sales must show the TIN of the Tax Group. A member may continue to issue invoices in his own name, provided that he includes the Group TIN with his name, and states that he is a member of the Tax Group.

6. Is a tax invoice required for supplies made to another Tax Group member?

No. VAT should not be charged on supplies made to another group member, and there is no requirement to issue a formal tax invoice.

7. Can I apply for retrospective Tax Grouping?

No, Tax Grouping may only apply prospectively from a date on or after approval by GAZT.

8. What portion of VAT does each group member pay?

Each member of the group is jointly liable for all debts of the group whilst they are a member. The actual payments are a matter for agreement between the parties, but this is often calculated from the Output VAT on sales by each group member less the Deductible Input VAT on purchases by that group member.

9. How is VAT deduction applied to the group?

The right to VAT deduction is in the name of the Representative Member. The standard rules to determine deduction by attributing Input VAT to taxable supplies or exempt supplies made by the group will apply. Non-attributable VAT should be deducted in accordance with a proportional deduction method.



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