Corporate Income Tax

Corporate Income Tax is payable on the shares of income of corporations and limited liability companies pro rata to the participations of non-GCC nationals. Partnerships are treated as pass-through entities, and their participants who are not GCC nationals are therefore subject to Income Tax on their shares of the partnership income, and GCC nationals are liable for Zakat on their shares of the same income.

(i)Tax Rates

According to Article 7 of the Income Tax Law the tax rates for corporate income of foreign companies are as follows:

20% of the Saudi Tax Base for all taxpayers (other than as follows);

30% for a taxpayer engaged in the natural gas investment field;

85% for a taxpayer engaged in the production of oil or hydrocarbons;

Any withholding that may be applicable to such taxpayers (as discussed above).

(ii) Gross Income

Saudi Arabian Tax Law does not distinguish between different categories of income. Gross income consists of all gains, profits or other net income arising from business transactions carried out within Saudi Arabia. If transactions are carried out in part or in whole inside Saudi Arabia all income derived from the transactions will be considered part of the Saudi Tax Base and potentially taxable in Saudi Arabia.

Capital gains are treated as ordinary income. The same principle applies to gains derived from the sale of shares in partnerships or companies registered in Saudi Arabia. Usually, profits from sales are calculated by subtracting the re-evaluated book value (or the market price, if it is lower) of the shares from the sale price. In the case of recently established corporations sometimes only the historical book value is subtracted from the sale price. The law does not, however, prescribe any particular method.

Interest earned on capital in Saudi Arabia is considered part of gross income. The same applies to rents, licence fees or royalties for the use of patents, copyrights, secret processes, formulae, goodwill, and trademarks, etc., registered in Saudi Arabia. Dividends on shares in corporations registered in Saudi Arabia are added to gross income, unless corporate tax or Zakat has already been charged. Income derived by Saudi-resident companies from operations outside Saudi Arabia is also assessed as gross income.

(iii) Calculation of taxable income

Taxable income is calculated by reference to the audited financial statements of an enterprise.

If a foreign legal entity does not file a tax return, and/or does not submit audited financial statements any payments made to it from Saudi Arabian residents will be subject to withholding.

(v) Deductions

Net taxable income is calculated by deducting allowable expenses from gross income. In principle, necessary business expenses are deductible from gross income. In practice it is, however, often difficult to determine whether or not certain expenses are deductible. Numerous decisions of the DZIT and rulings of the PTAC and the ACZTA have been issued on the subject.

Salaries and wages are considered ordinary business expenses and are thus deductible from gross income. The DZIT requires companies to provide detailed payroll information with their tax returns. Social security contributions are deductible only to the extent of the employer's share, as are contributions to certain pension funds operated in Saudi Arabia are deductible. Agency fees paid by a foreign company are also deductible, subject to certain conditions and restrictions.

As a general rule, provisions and termination benefits are not deductible, except for employment termination benefits required by the labour law. Administrative costs incurred by the head office of a company outside Saudi Arabia are not deductible, with the exception of technical costs directly related to business activities in Saudi Arabia.

(vi) Depreciation

Assets of a company may be written off within the limits of depreciation rates established by the DZIT, which accept accelerated depreciation of certain equipment, such as computers subject to the depreciation allowances and schedules set forth in the Income Tax Laww.

(vii) Losses

Losses previously could not be carried forward until the entry into effect of Council of Ministers' Resolution No. 3 of 1422 H. [2001 G.], which allows losses to be carried forward indefinitely. In return, the former exemption periods ('tax holidays') for joint-venture investment projects (5 or 10 years depending on the nature of the project) have been terminated. However, companies which enjoyed exemptions under the previous investment law continue to enjoy them under the current law until their expiry.

(viii) Tax exemptions

Under the tax system, tax guarantees or incentives are rare. Certain foreign entities may be exempted from the Corporate Income Tax by Royal Decree.

There are no tax-free zones in Saudi Arabia.