



# Guideline **Input Tax Deduction**



The Zakat, Tax and Customs Authority ("ZATCA", "Authority") has issued this Guide for the purpose of clarifying certain tax treatments concerning the implementation of the statutory provisions in force as of the Guide's issue date. The content of this Guide shall not be considered as an amendment to any of the provisions of the Laws and Regulations applicable in the Kingdom.

Furthermore, the Authority would like to highlight that the clarifications and indicative tax treatments prescribed in this Guide, where applicable, shall be implemented by the Authority in light of the relevant statutory texts. Where any clarification, interpretation or content provided in this Guide is modified - in relation to unchanged statutory text - the updated indicative tax treatment shall then be applicable prospectively, in respect of transactions made after the publication date of the updated version of the Guide on the Authority's website.



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## **1. INTRODUCTION**

### **1.1. IMPLEMENTING A VALUE ADDED TAX (VAT) SYSTEM IN THE KINGDOM OF SAUDI ARABIA**

The Unified VAT Agreement for the Cooperation Council for the Unified Arab States of the Gulf (the "VAT Agreement") was approved by KSA by a Royal Decree No. M/51, dated 3 / 5 / 1438H. Pursuant to the provisions of the Unified VAT Agreement, the Kingdom of Saudi Arabia issued the VAT Law under Royal Decree No. M/113 dated 2 / 11 / 1438H ("the VAT Law") and its corresponding Implementing Regulations were subsequently issued by the Board of Directors of Zakat, Tax and Customs Authority ("ZATCA") by Resolution No. 3839 dated 14 / 12 / 1438H ("the Implementing Regulations").

### **1.2. ZAKAT, TAX AND CUSTOMS AUTHORITY**

ZATCA, also referred to as "the Authority" herein, is the authority in charge of the implementation and administration of VAT (which may be referred to hereinafter as "the tax") in KSA; in addition to the registration and deregistration of Taxable Persons for VAT; the administration of VAT return filing and VAT refunds; and undertaking audits and field visits; ZATCA also has the power to levy penalties for noncompliance with legal provisions relating to VAT.

### **1.3. WHAT IS VALUE ADDED TAX?**

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 imposed 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 until a retailer sells the end-product to a consumer. Unlike other taxes, Persons subject to VAT will both:

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

When Taxable Persons sell a good or service, a 15% VAT charge - assuming a standard case - is assessed and added to the final sales price. The Taxable Persons will account for that 15% that they have collected from all eligible sales separately from its revenue in order to later remit a portion of it to the Authority. The VAT that Taxable Persons collect on their sales is called Output VAT.

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

Further information about VAT can be found in the KSA VAT Manual or at [zatca.gov.sa](http://zatca.gov.sa)

#### **1.4. THIS GUIDELINE**

This guideline is addressed to all natural persons and legal persons practicing economic activities and subject to Tax. The purpose of this guideline is to provide additional clarification with respect to Input Tax deduction and in particular the partial deduction method.

This guideline represents ZATCA'S views on the application and fair treatment of the Unified VAT Agreement, the VAT Law and the Implementing Regulations as of the date of this guideline.

For further advice on specific transactions we encourage you to apply for a ruling or visit the official VAT website ([vat.gov.sa](http://vat.gov.sa)), which contains a wide range of tools and information that is a reference to support the taxpayers and enterprises, as well as visual guidance materials, all relevant information, and FAQs.





## 2. DEFINITIONS OF MAIN TERMS USED

Input Tax is a defined term for VAT purposes in the Unified VAT Agreement as:

“tax borne by a Taxable Person in relation to goods or services supplied to him or imported for the purpose of carrying on the economic activity”<sup>1</sup>.

For the purpose of the KSA VAT Law, only the KSA VAT that is charged in respect of supplies or imports made in the KSA falls within the definition of Input Tax.

Deductible Tax is a defined term for VAT purposes:

“Input Tax that may be deducted from Tax Due on supplies for each Tax Period in accordance with the Agreement and Local Law<sup>2</sup>”.

The term Customer is defined being:

“A Person who receives Goods or Services<sup>3</sup>”.

For the purposes of this guideline, the particular importance of determining the Customer of the supply is to confirm the Person eligible to deduct. A VAT registered Person is only entitled to deduct the Input Tax charged on a supply of goods or services if those goods or services are supplied to him. In most cases, the identity of the Customer is clear. In case of uncertainty, ZATCA considers that the following factors indicate which Person is considered the Customer:

- The Person who instructs the supplier to supply the goods or services;
- The Person to whom the supplier owes obligations
- The Person who enters into a contract with the supplier (or his agent);
- The Person who contractually receives the goods and services from the supplier

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(1) Article 1, Definitions, Unified VAT Agreement

(2) Article 1, Definitions, Unified VAT Agreement

(3) Article 1, Definitions, Unified VAT Agreement



The definition of a Person for VAT purposes is:

“Any natural or legal Person, public or private, or any other form of partnership<sup>4</sup>”.

It is also possible that another Person could receive benefit from a supply of goods or services, although the Person is not the Customer. Such a Person is considered a Beneficiary for the purposes of this guideline.

**Example (1):**

An employer enters into a contract with a private health company to carry out health checks on all employees working at a site to meet its workplace safety requirements. The employer instructs the health company, enters into the contract, and receives the results of the test to satisfy its employer obligations. It is the Customer of the services. The individual employees receive a benefit from the health check, but cannot request additional services. The employees are not the Customer of the services, but they may be referred to as Beneficiaries.

A Tax Invoice is an invoice or similar document issued in respect of a Taxable Supply of goods or services, in line with requirements detailed in the Unified VAT Agreement<sup>5</sup> and Implementing Regulations<sup>6</sup> surrounding when a Tax Invoice should be issued and determine the mandatory contents of the Tax Invoice.

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(4) Article 1, Definitions, Unified VAT Agreement

(5) Article 1, Definitions, Unified VAT Agreement

(6) Article 53, Tax Invoices, Implementing Regulations



A Taxable Supply is a defined term for VAT purposes:

“Supplies on which Tax is charged in accordance with the provisions of the Agreement, whether at the standard rate or zero-rate, and for which associated Input Tax is deducted in accordance with the provisions of the Agreement <sup>7</sup>”.

The Implementing Regulations set out that Taxable Supplies include all supplies made in the KSA under the place of supply rules, including Nominal Supplies and supplies on which VAT is charged under the Reverse Charge Mechanism <sup>8</sup>.

The definition of a Nominal Supply for VAT purposes is:

“Anything that is considered a Supply in accordance with the cases provided for in Article 8 of [the Unified VAT] Agreement <sup>9</sup>.

Based on article (8) of the Unified VAT Agreement, a Taxable Person shall be deemed to have performed a supply of goods when disposing of goods that form part of its assets in any of the following cases:

- The assignment of goods, for purposes other than economic activity, with or without a consideration;
- Changing the use of goods to use for non-taxable supplies;
- Retaining goods after ceasing carrying on an economic activity; and
- Supplying goods without consideration, unless the supply is in the course of business, such as samples and gifts of trivial value as determined by each Member State.

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(7) Article 1, Definitions, Unified VAT Agreement.

(8) Article 14, Taxable Supplies in the Kingdom, Implementing Regulations

(9) Article 1, Definitions, Unified VAT Agreement



Also, a Taxable Person shall be deemed to have made a supply of services in the following cases:

- Use by him of goods that form part of his assets for purposes other than those of an economic activity; and
- Supplying services without consideration

The abovementioned Nominal Supplies of goods and services are only recognized in case the Taxable Person has deducted Input Tax in relation to the listed events.

**Reverse Charge Mechanism** is defined as the mechanism by which the Taxable Customer is obligated to pay the Tax due on behalf of the Supplier and is liable for all the obligations provided for in the Agreement (the Unified Agreement) and the Local Law <sup>10</sup>.

VAT is due under the Reverse Charge Mechanism in cases where a KSA established Taxable Person receives goods or services from a non-resident supplier, provided those goods or services are supplied in the KSA.

A **Taxable Person** is a defined term for VAT purposes. In the KSA, this includes all Persons who are registered or obliged to register for VAT in the KSA (see section 3 for more details on registration) <sup>11</sup>.

**Private use** is not a defined term for VAT purposes. ZATCA considers private use to be any use, consumption or enjoyment of goods or services by a natural Person or a group of natural Persons, where such use does not take part in the course of an economic activity by those Persons.

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(10) Article 1, Definitions, Unified VAT Agreement

(11) Article 2, Taxable Persons required or eligible to register in the Kingdom, 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 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. There are therefore specific rules to determine whether a natural Person falls within the scope of VAT.

Generally, 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.

### 3.2. MANDATORY REGISTRATION

Registration is mandatory for all Persons whose annual turnover exceeds a certain threshold. If a Person's Taxable Supplies over 12 month exceeds SAR 375,000 (the "Mandatory VAT Registration Threshold"), that Person must register for VAT supplies made subject to the transitional provisions provided for in the Implementing Regulations<sup>12</sup>.

Taxable Supplies do not include:

- 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 State; or
- Revenues on sales of capital assets - a capital asset is defined as an asset allocated for long-term business use<sup>13</sup>.

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<sup>12</sup>) Article 3, Mandatory registration - Supplies exceed the Mandatory Registration Threshold, Implementing Regulations

<sup>13</sup>) Article 1, Definitions, Unified VAT Agreement



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

- Persons who are not resident in the Kingdom of Saudi Arabia are required to pay the VAT in respect of supplies made or received by them in the Kingdom of Saudi Arabia and to register for VAT irrespective of the value of the supplies for which they are obliged to collect and pay the VAT<sup>14</sup>.
- During a transitional period up to 1 January 2019, businesses will only be required to register where annual turnover exceeds SAR 1,000,000, and an application for registration must be submitted no later than 20 December 2018<sup>15</sup>.

More information on mandatory registration for VAT is contained at [zatca.gov.sa](http://zatca.gov.sa).

### 3.3. OPTIONAL VAT REGISTRATION

Any Resident Person in the Kingdom of Saudi Arabia 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 voluntary basis<sup>16</sup>.

Optional VAT registration is preferable where a business wishes to claim VAT charged to it on their costs before invoices are raised or the occurrence of an onward supply.

#### **Example (2):**

Al Saqr LLC is a KSA company engaged in the construction of a reinforcing steel factory in Riyadh. It plans to start producing and selling the steel to Customers in January 2020. Nevertheless, the company has incurred high expenses amounting to SAR 2,000,000 to local suppliers during the first quarter of 2018, in connection with the purchase of equipment, and building expenses, before making any supply. In such event, it will be open to Al Saqr LLC to register for VAT voluntarily on the basis of its annual expenditures exceeding the voluntary registration threshold.

More information on voluntary registration for VAT is available at [zatca.gov.sa](http://zatca.gov.sa).

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

(15) Article 79 (9), Transitional provisions, Implementing Regulations

(16) Article 7, Voluntary Registration, Implementing Regulations



## 4. CATEGORIES OF INPUT TAX

### 4.1. GENERAL PROVISIONS

Subject to meeting the criteria for deduction, Input Tax is in principle deductible in respect of the following instances where a Person incurs VAT:

1. Where VAT is correctly charged on a supply of goods or services in the KSA by a VAT-registered supplier;
2. Where VAT is self-accounted by the VAT-registered Person under the Reverse Charge Mechanism on a supply of goods or services in the KSA; or
3. Where VAT is paid to the Customs Department, or reported in the VAT return, on imports of goods into the Kingdom.

This section outlines each of the three categories of Input Tax.

### 4.2. VAT CHARGED BY SUPPLIERS ON GOODS OR SERVICES SUPPLIED IN THE KSA

VAT which is correctly charged on a supply of goods or services in the KSA by a VAT-registered supplier is considered to be Input Tax for the Customer of that supply ("tax borne by a taxable Person in relation to goods or services supplied to him...").

A Customer receiving supplies with VAT charged in KSA has the right to claim deduction in case he can prove the Input VAT amount paid or payable via a Tax Invoice. In this case, the customer should report this Input Tax by reporting in Box 7 of the KSA VAT return (Standard-rated domestic purchases).

In other cases where the Taxable Person does not have a Tax Invoice proving the paid input tax, the Taxable Person can claim deduction when he is able to provide the alternative documents specified in the Implementing Regulations<sup>17</sup>.

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(17) Article (49)(7), Input Tax Deduction, Implementing Regulations.



This category relates to VAT charged (at the standard 15% rate) on domestic supplies only. VAT charged in another GCC State or non-GCC country is not deductible as Input Tax.

VAT incurred on a domestic supply is solely deductible for the Customer (as defined in section 2 of this guideline) who is receiving the good or service. Therefore:

- In case another party than the Customer pays or incurs the VAT due on the supply, this VAT is still only recoverable for the Customer of the supply
- A Beneficiary of a supply is not able to deduct Input Tax on a supply if it is not the Customer of the supply as outlined in section 2. In most cases, it should be clear from the legal arrangements and invoicing party who the Customer of a supply is for the purposes of Input Tax deduction

For Nominal Supplies, the VAT accounted for on these supplies which is not borne by the customer will not constitute Deductible Input Tax of the Customer.

**Example (3):**

Al Ahmed Co, a facilities company, gives a free water cooler to Al Salam Co with a cost price of SAR 10,000 - as a token of thanks for being a loyal Customer. Al Ahmed Co is required to account for VAT of SAR 500 (15% of the cost price) on the Nominal Supply of goods for no consideration. Al Salam Co has not been charged VAT on a supply of goods or services. It is not able to deduct VAT in respect of the Nominal Supply accounted for on Al Ahmed Co's VAT return.

The VAT charged by the KSA supplier must be correctly charged to constitute Input Tax and to be available for deduction. In case a supplier charges VAT incorrectly or without a legal basis, this "VAT" is not deductible for the Customer. It is the supplier's primary responsibility to determine the correct VAT treatment for a supply. However, the Customer should be aware of cases where the VAT paid is clearly not correct - as an Input Tax deduction will not be available in these cases.





#### **Example (4):**

Al Hassan Co purchases goods from a small vendor who charges a 15% "VAT" amount, but does not provide a Tax Identification Number on its invoice and does not appear to be a VAT-registered Person according to the public register of registered VAT payers (at vat.gov.sa). Al Hassan Co must not deduct the "VAT" on its VAT return.

#### **Example (5):**

Al Nuha Co purchases medical equipment from a supplier; such equipment that Al Nuha Co knows to be on the list of Qualifying Medical Equipment published by the SFDA. The supplier charges VAT at 15%, even though the Medical Equipment is clearly required to have VAT charged at 0%. Al Nuha Co must not deduct the VAT on its VAT return.

In all cases, a Customer of a supply of goods or services may wish to seek and retain documentation (such as contracts or additional information from the supplier) to support the validity of the VAT charged, in case of a future query during a GAZT audit or examination.

### **4.3. REVERSE CHARGED VAT**

The second category of deductible Input Tax is VAT which is self-accounted by the Customer of the supply under the Reverse Charge Mechanism:

"A Customer who is obligated to pay Tax pursuant to the Reverse Charge Mechanism may deduct Deductible Tax related thereto provided that he has declared the Tax due under Article 41 (2) of this Agreement<sup>18</sup>."

VAT is due under the Reverse Charge Mechanism in cases where a Taxable Person receives goods or services from a non-resident supplier, provided those goods or services are supplied in the KSA. This does not apply to the import of goods from outside the GCC into the KSA after the end of the transitional period<sup>19</sup>.

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(18) Article 44(3), Tax Deduction Principle, Unified VAT Agreement

(19) Article (79) (6), Transitional Provisions, Implementing Regulations, A Supply treated under the provisions of the Agreement as made in such Member State shall be considered as being made in a third country outside of Council Territory and persons who is a Resident Person in such Member State will be treated as residents of a third country



“In cases where the Agreement provides that a Taxable Customer is obligated to pay Tax on a Supply received from a non-resident Supplier, Tax shall be paid by way of the Reverse Charge Mechanism. The Taxable Customer must report the Output Tax on the Supply and any Input Tax (to the extent that the Customer can benefit from Input VAT deduction) in the Tax Return for that Tax Period<sup>20</sup>.”

VAT is treated as Input Tax only for the Customer who has self-accounted for VAT under the Reverse Charge Mechanism. For Customers who are fully taxable, or who have acquired the goods or services for a taxable use, a full deduction of the VAT under the Reverse Charge Mechanism does not result in any payment of tax in the return. The entry in box 9 of the VAT return - without adjustment - results in VAT payable being fully offset by the Deductible Tax on the supply.

**Example (6):**

An Italian web-hosting provider contracts with a KSA design firm to host its international focussed website. The supplier is not resident in the KSA, but the KSA design firm is VAT registered so it can self-account for the VAT due as the Customer. The web-hosting company is not required to register in respect of this supply. The web-hosting provider issues an invoice on 21 June 2021 for EUR 1,000.

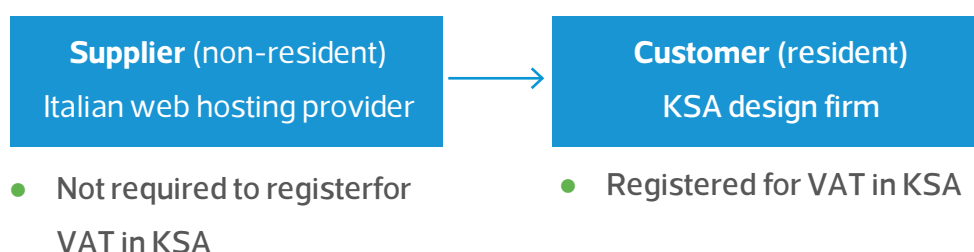
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(20) Article 47(1), Persons liable to pay Tax, Implementing Regulations



### Business to business (B2B)

VAT is paid through the reverse charge mechanism by the KSA tax registered customer



The KSA design firm is required to self-assess VAT on the invoice by way of the Reverse Charge Mechanism. Accordingly, the value of the supply in riyals is SAR 4,500 (equal to Euro 1,000).

The KSA design firm includes this amount in Box 9 of the VAT return for the tax period ended 30 / 6 / 2018. The services are fully used for the purposes of the design firm's taxable economic activities. The VAT return form automatically calculates an Input Tax deduction of the self-accounted VAT, resulting in no VAT payable.

		Amount (SAR)	Adjustment (SAR)	VAT Amount (SAR)
9	Imports subject to VAT accounted through Reverse Charge Mechanism	4,500	-	-



#### 4.4. VAT PAID ON IMPORTS

The importation of goods into the KSA from outside the GCC by any Person is subject to 15% KSA VAT<sup>21</sup>.

VAT is required to be paid on imports by the Person appointed or acknowledged as importer for Customs purposes (under the Common Customs Law). VAT is required to be paid to the Customs Department at the time of entry, but a corresponding deduction is claimed through the Tax Return for the period in which the import is made. Imports are reported in Box 8 of the VAT return (Imports subject to standard VAT rate paid at Customs).

The importer (in accordance with Common Customs Law) is the Person eligible for deduction of VAT charged on import<sup>22</sup>. In some cases, the importer of record will be a different Person to the owner of the goods at the time of import (for example, if a broker imports goods due to import licensing issues, or if a KSA resident Customer imports goods on behalf of a non-resident supplier). In all cases, the Person with the right to deduct/recover is the importer, provided that the goods are used by him in his taxable activity.

##### **Example (7):**

Al Reem Co does not have a license to make imports into the KSA, so it asks a third party to act as importer of specialist equipment. The third party pays the VAT and duty to the Customs Department upon import, and is reimbursed for these costs by Al Reem Co. In this example, neither Person is able to deduct VAT on the import. Al Reem Co is not the importer of the goods, and the third party agent does not import the goods for the purpose of carrying on its economic activity.

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(21) An exemption applies to goods imported in certain circumstances. Refer Article 38, Exemptions on Import, Unified VAT Agreement; and Article 42, Exemptions for imports, Implementing Regulations. More detail is provided in the taxpayer guideline on Import and Export

(22) Article 42, Person Obligated to Pay Tax in respect of Import, Unified VAT Agreement



**Example (8):**

Specialist Equipment Inc. is a company established in the USA. It agrees to supply equipment to Al Etifaq Co, a KSA company, and carry out installation at its premises in Al Khobar. The goods remain the property of Specialist Equipment Inc. until installation and testing is complete. As Specialist Equipment Inc. is not able to act as importer, Al Etifaq imports the goods and pays VAT on import. Al Etifaq is the Person with eligibility to deduct corresponding Input VAT. It is able to do so if it evidences that the goods are used in its economic activity which constitutes making Taxable Supplies.

The VAT paid on imports is deductible in accordance with the general rules for eligibility of Input Tax deduction, discussed in section 5.

A Taxable Person may apply for authorization for the payment of tax on imports to be made through that Person's tax return, instead of being paid to the Customs Department<sup>23</sup>. In cases where this authorization is granted, the procedure for VAT recovery will be the same as for VAT paid under the reverse charge mechanism (described in 4.3 above). Further guidance on the authorization for the payment of tax on imports via the tax return is provided in the import guideline.

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(23) Article 44, Payment of Tax on imports through the Tax Return, Implementing Regulations



## 5. ELIGIBILITY FOR DEDUCTION

A Taxable Person may deduct Input Tax incurred on goods and services it purchases or imports for the purpose of carrying on its economic activity in the course of making Taxable Supplies<sup>24</sup> (including the categories described in section 5.2). 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.

The terms “for the purpose of carrying on the economic activity” and “in the course of making Taxable Supplies” mean that deduction requires supplies purchased to have some link between these supplies and the onwards supplies of the Taxable Person. However, it is not necessary that goods have a direct link to a specific onwards Taxable Supply to qualify for deduction.

### **Example (9):**

Al Saad Co purchases a shipment of 100 electronics products with a purchase price of SAR 1,000 (exclusive of VAT) per unit from a supplier, resulting in a total transaction value of SAR 115,000 (SAR 100,000 for the units and SAR 15,000 VAT). Five of these units will be used as demonstration models in stores, and the remaining 95 units will be held in stock for eventual sale for Customers. It is not known whether any individual item will itself be sold as part of a Taxable Supply. However, the entire shipment is purchased for the purpose of carrying on the economic activity and in the course of making Taxable Supplies. The entire VAT amount of SAR 15,000 is eligible for deduction/recovery.

### **Example (10):**

Al Salwa Co, a wholesale distributor, engages a professional training firm to carry out training for all sales staff on the use of a new Customer relationship management system. The training cannot be linked to any individual Taxable Supply made by Al Salwa Co. However, it is clearly incurred for the purpose of carrying on the economic activity and in the course of making Taxable Supplies. VAT is eligible for deduction.

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(24) Article 46, Proportional Deduction, Unified VAT Agreement



Conversely, VAT incurred on purchases made outside of a Person's Economic Activities, or Input Tax which is related to the taxpayer's VAT exempted activities is not deductible as Input Tax. VAT which relates partly to taxable and exempt activities must be apportioned for deduction purposes.

	<b>Input Tax relates to the Taxable Person's economic activities</b>	<b>VAT relates to the Taxable Person's noneconomic activities</b>	<b>VAT relates partly to economic and partly to non-economic activities</b>
<b>VAT directly attributed to Taxable Person's taxable supplies</b>	Deduct in full		
<b>VAT directly attributed to Taxable Person's exempt supplies</b>	No Deduction	No Deduction	Partial deduction to the extent VAT relates to economic activity and Taxable Supplies
<b>Overheads and all other Input VAT that cannot be directly attributed</b>	Partial deduction based on apportionment		



Section 7 provides more detail on costs incurred that do not relate to the Economic Activity of the Taxable Person, including specifically blocked expenditure types under KSA VAT law.

Input VAT may only be deducted where the Taxable Person holds appropriate documentation (such as a Tax Invoice from the supplier or customs documents showing the amount of tax paid or payable). More details on documentation to support Input Tax deduction is included in section 8 of this guideline.

### 5.1. NON-ECONOMIC ACTIVITIES

A Taxable Person cannot deduct Input Tax if it is for purposes other than Economic Activities<sup>25</sup>. VAT deduction is therefore not available for:

- VAT incurred in respect of a Taxable Person's separate non-economic activities, such as activities carried out in the capacity of a public authority. Please refer to the Economic Activity guideline for more detail;
- VAT incurred in respect of purchases for the private enjoyment of individuals, such as business owners or employees
- VAT incurred on specific types of goods or services deemed by the Implementing Regulations to be received outside the economic activity of the Taxable Person<sup>26</sup>. Further detail surrounding restricted categories of Input Tax are discussed in Section 7 of this Guideline

For the definition of non-economic activities we refer to the Economic Activity guideline.

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(25) Article 45, Restrictions on Input Tax Deductions, Unified VAT Agreement

(26) Article 50, Goods and Services deemed to be received outside of economic activity, Implementing Regulations





## 5.2. TAXABLE SUPPLIES

Taxable Supplies refer to supplies on which tax is charged in accordance with the provisions of the Unified VAT Agreement, whether at the standard rate of 15% or zero-rate, and from which associated Input Tax is deducted in accordance with the provisions of the Agreement, the VAT Law and the Implementing Regulations in KSA.

The concept of Taxable Supplies - for the purpose of Input Tax deduction - refers to the following<sup>27</sup>:

### **Domestic supplies taxable with 15% KSA VAT;**

**Example (11):** A company practicing commercial real estate developing activities established in the KSA, supplies an office building to a consulting company established in the KSA for SAR 10,000,000 (excluding VAT). The Commercial Real Estate Co. will issue an invoice for the supply of the office building amounting to SAR 11,500,000 (including VAT). During the period of construction and fit-out, The Commercial Real Estate Co. incurs costs from KSA suppliers with VAT for the construction of the building. These costs are attributable to the Taxable Supply of the office building and therefore the Commercial Real Estate Co. is eligible to deduct all the KSA Input VAT charged to it for the construction and fit-out costs.

### **Domestic zero-rated supplies, such as supplies of Qualifying Medicines, and exports of goods outside of the GCC Territory;**

**Example (12):** Al Ghanem Co, an electronics company established in the KSA, exports finished goods to a company established in Egypt. The supply of the goods is subject to the zero rate. Al Ghanem Co incurs costs including KSA VAT from a domestic service provider for the testing and packaging of the goods. The KSA VAT charged to the electronics company is attributable to the zero-rated supply of the goods to the Egyptian company; and therefore Al Ghanem Co is eligible to deduct the KSA VAT charged to it as Input VAT.

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(27) Article 49(1), Input Tax Deduction, Implementing Regulations



### **Internal supplies of goods or services made to other GCC States**

These are defined by the Unified VAT Agreement to be “Supplies of Goods or Services by a Supplier who resides in a Member State to a Customer who resides in another Member State”.

During a transitional period, supplies of goods or services to or from another Member State are considered to be exports from or imports to the KSA, equivalent to supplies to or from outside the GCC Territory.

**Example (13):** Al Baraa’ Co, a KSA company, enters into an arrangement to provide consultancy services to UAE LLC, a company established in the UAE and registered for VAT in that State. Services supplied by Al Baraa’ Co. will be considered as exported services to outside GCC in the case that all conditions related to charging zero rate of services to non-GCC residents are fulfilled.

### **Supplies which would have been taxable if they were made in the KSA**

This includes goods and services which are supplied outside the KSA under the place of supply rules, where those underlying goods or services are taxable in nature - so that a supply of those same goods and services in the KSA would have been taxable.

**Example (14):** Al Saeed Co, an electronics company established in the KSA supplies goods which are located in the Netherlands to a Dutch Customer. The supply of the goods takes place wholly outside the territory of the KSA, and is therefore outside the scope of KSA VAT.

The contract of sale is made under KSA law, and Al Saeed Co makes use of a lawyer established in the KSA to agree the contract documentation with the Dutch Customer. The KSA lawyer issues an invoice with KSA VAT for its services to the Al Saeed Co. The services rendered by the KSA lawyer are attributable to the supply of goods in the Netherlands, which would have been taxable if those same goods were supplied in the KSA. Therefore Al Saeed Co is eligible to deduct the VAT charged on the invoice of the KSA lawyer as Input Tax.



### 5.3. TAXABLE PERSONS CARRYING ON FULLY TAXABLE ACTIVITIES

Input Tax directly attributable to the categories of Taxable Supplies listed above is fully deductible for a taxpayer. Many Taxable Persons have economic activities which only involve making Taxable Supplies (they make no exempt supplies of any sort, and have no separate, non-economic, activities).

Provided this is the case, these Taxable Persons are entitled to deduct Input Tax in full on all business expenditure (often referred to as "fully taxable"), and are therefore not required to carry out any exercise to calculate proportional deduction of overheads or other non-attributable expenditure. Note that all Persons must take into account the non-deduction of the VAT relating to the restricted elements listed in Article 50 of the Implementing Regulations.

Taxable Persons whose activities predominantly involve making Taxable Supplies must take care to identify any exempt supplies or non-economic activity. Taxable Persons with any such supplies cannot be considered fully eligible to deduct Input Tax, and must assess the entitlement to VAT deduction for all costs based on their use.



## 6. DEDUCTION OF GENERAL OVERHEADS AND NON-ATTRIBUTABLE COSTS

In case a Taxable Person incurs costs that cannot be directly attributed to either their taxable or VAT exempt supplies, these costs are referred to as general overhead costs or non-attributable costs.

The types of non-attributable costs will vary significantly depending on the economic activities carried out. Examples of overhead costs common to most businesses are rental of commercial premises, utilities such as electricity and water, and fees charged for statutory audit.

Any costs which cannot be attributed to a taxable or exempt activity will in principle be considered non-attributable.

Deduction of VAT charged to a Taxable Person on overhead costs and other non-attributable expenses incurred by the Taxable Person 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 Taxable Person's activities.

"If Input Tax is related to Goods and Services used to make Taxable Supplies and non-Taxable Supplies, then Input Tax cannot be deducted save within the limits of the proportion referable to the Taxable Supplies"<sup>28</sup> .

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(28) Article 46, Proportional Deduction, Unified VAT Agreement



### Example (15):

Al Atlal Co, a real estate company established in the KSA has developed real estate for both commercial and residential leasing. The annual turnover generated with the VAT taxable leasing of commercial real estate amounts to SAR 4,000,000 and the turnover generated with the VAT exempt residential leasing amounts to SAR 2,000,000. ABC Co is charged the following VAT-inclusive costs from suppliers

- Invoice from a construction company for the construction of the commercial real estate: SAR 1,000,000, + SAR 150,000 of KSA VAT;
- Statutory audit fee from a KSA auditor for reviewing and signing off the annual accounts: of SAR 100,000 + SAR 15,000 of KSA VAT.
- Invoice from carpeting company for the carpets to be included in the residential real estate: SAR 40,000 + SAR 6,000 of KSA VAT.

The Input Tax on the invoice issued by the construction company can be directly attributed to the VAT taxable activity (commercial leasing). In this respect, the Input Tax on this invoice can be fully deducted.

The Input Tax on the invoice issued by the carpeting company can be directly attributed to the VAT exempt activity (residential leasing). In this respect, the Input Tax on this invoice cannot be deducted.

The services rendered by the auditor relates to both the VAT taxable and the VAT exempt supplies of the real estate company and is therefore a non-attributable cost.

To determine the portion of the SAR 5,000 KSA VAT which may be deducted, ABC Co must calculate the portion which relates to its Taxable Supplies. Using the default calculation method, this proportion is calculated to be two-thirds (66.67%) of the VAT charged on the invoice of the auditor.



The Implementing Regulations prescribes a default method to determine the portion relating to Taxable Supplies<sup>29</sup>. Further information on the default method for proportional deduction is set out in section 12 of this guideline.

Alternative attribution methods, using other calculation approaches than the value of supplies, may be approved with ZATCA in cases where these better reflect the actual use of VAT incurred. Additional information with respect to the Alternative Methods is provided in section 13 of this guideline.

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(29) Article 51, Proportional Deduction of Input Tax, Implementing Regulations



## 7. RESTRICTED INPUT TAX

### 7.1. PRIVATE USE

In case goods or services are purchased by a Taxable Person, but are used outside of the economic activities of that Taxable Person, Input Tax may not be deducted. The Private (personal) use of goods or services by individuals such as business owners, family of the business owners or employees is a use outside of the economic activities. VAT incurred on any such expenditure is not deductible.

#### **Example (16):**

Khaled owns and manages an office services company in Riyadh which is registered for VAT. Khaled purchases a printer on using the company account, but does not use it in his business and takes it home for use by his family. The printer is not used in the economic activities of the taxable business and Input VAT deduction is not permitted.

#### **Example (17):**

A bank is required by law to provide medical insurance for employees and their immediate families. An insurer provides this statutory cover for a cost of SAR 4,000 (excluding VAT) per insured per year. The insurer offers an addition to the policy for an additional SAR 1,000 per insured per year, providing additional benefits not required under law, of which SAR 150 is VAT.

The bank chooses to cover the cost of the enhanced insurance for its employees, as an additional benefit in order to attract skilled workers. It may deduct VAT on the statutory insurance provided, but must restrict VAT deduction on the SAR 150 of VAT charged on each amount of additional cover incurred.

The application of Private use in the context of benefits provided to employees is discussed in more detail in a separate guideline on Employee Benefits.



## 7.2. RESTRICTED CATEGORIES OF GOODS OR SERVICES

The Implementing Regulations have determined certain categories of goods and services which are in all cases considered to be received outside the economic activity of a Taxable Person<sup>30</sup>. Input VAT on the following expenditures is not eligible for Input Tax deduction; as the nature of these expenditures is a type generally purchased for the private benefit of business owners, employees or affiliated Persons:

### 1. Any form of entertainment, sporting or cultural services;

This category relates to expenses made to enjoy any form of entertainment (e.g. tickets to the cinema), attend sporting events (e.g. football match tickets) or cultural services (e.g. tickets to a museum).

**Example (18):** Omar owns a retail company specialised in the sale of shoes. In his capacity of business owner Omar purchased four tickets for a football match of the national team of Saudi Arabia, to help strengthen business relations with key suppliers. Whilst there may be a business purpose to the expenditure, the VAT paid on the tickets is not deductible for Omar's company as the sporting expenses are specifically restricted in all cases.

### 2. Catering services in hotels, restaurants and similar venues;

**Example (19):** Omar owns a retail company specialised in the sale of shoes. As a reward for securing a large order from a distributor for the supply of a new collection of shoes, Omar takes the account team responsible for the large order out for dinner. During the dinner, the team discusses plans to grow this customer account in future. Whilst the dinner has a connection with the company's economic activities, the company is not allowed to deduct the VAT due on the restaurant bill, as the catering expenses are specifically restricted from deduction in all cases.

### 3. The purchase or lease of restricted motor vehicles; as defined below.

### 4. Repair, alteration, maintenance or similar services on restricted motor vehicles;

### 5. Fuel used in restricted motor vehicles;

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(30) Article 50, Goods and Services deemed to be received outside of economic activity, Implementing Regulations





The Implementing Regulations define a Restricted Motor Vehicle for the purpose of Input VAT deduction. A Restricted Motor Vehicle is deemed to be incurred outside of the Economic Activity, and is not eligible for deduction.

“A Restricted Motor Vehicle is any vehicle designed to be used on the road unless the vehicle is either:

- a. used exclusively by the Taxable Person or by its employees for work purposes, without being made available for any Private use,
- b. primarily intended for resale by the Taxable Person or otherwise for use in an Economic Activity supplying that vehicle<sup>31</sup>”.

Deduction of VAT is not available in respect of a Restricted Motor Vehicle where there is any availability for Private (personal) use: the costs are not apportioned between private and business usage. The Employee Benefits guideline provides additional guidance and interpretation surrounding deduction of VAT on vehicles used in the business.

**Example (20):** An employer signs an agreement with sales representatives that they may use their company vehicle for personal use on Thursday and Friday only, and the vehicle should be used only for business purposes during the remaining days unless specifically instructed by management to use for personal purposes. Although the usage of the vehicle is restricted in part, the vehicle is a Restricted Motor Vehicle, and no deduction is permitted.

It should be noted that ZATCA is not obliged to follow the terms of such contracts, internal labor regulations or any similar document that provides for the conditions of use of the employer’s vehicles and is able to rely on any source to prove whether the vehicles are available for personal use or not.

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(31) Article 50, Goods and services deemed to be received outside of Economic Activity, Implementing Regulations



## 6. Any other goods and services used for a private or non-business purpose.

The last category relates to other expenses incurred by a taxable person which do not fall under the abovementioned categories, but where the nature of the expenses clearly have a private (personal) nature and do not relate to business.

**Example (21):** Al Salah Consulting engages an interior design consultant to assist with the refit of the office. On completion of the project, one of the business owners asks the consultant to provide design advice in respect of his personal home, and to add the services to the invoice issued to the company. In this case, Al Salah Consulting incurs and pays for all of the services, but the services relating to the owner's house are used for a private purpose and the VAT on this element is not deductible.

## 7.3. PROHIBITED GOODS

Any Input Tax charged on goods which are prohibited for sale under KSA law, or incurred in activities which such involve prohibited goods are not eligible for Input Tax deduction<sup>32</sup>.

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(32) Article 45(2), Restrictions on Input Tax Deductions, Unified VAT Agreement



## 8. DOCUMENTS TO SUPPORT DEDUCTION

The Unified VAT Agreement requires that a Person must hold documents as a condition of Input Tax deduction.

“For purposes of exercising the right of deduction, the Taxable Person must hold the following documents:

- a. The Tax Invoice received pursuant to the provisions of this Agreement;
- b. The customs documents proving that he imported the Goods in accordance with the Common Customs Law<sup>33</sup>”.

The requirements for Tax Invoices are prescribed in a KSA context by the Implementing Regulations, a document must include a list of criteria and details in order to be a valid “Tax Invoice<sup>34</sup>”. A Customer should hold a valid Tax Invoice in order to deduct KSA VAT charged by suppliers as Input Tax. The invoice may be held electronically or in physical copy.

In case the VAT supply is self-accounted through the Reverse Charge Mechanism by the Customer of the supply, a valid Tax Invoice will not be issued by the supplier. In order to be eligible for the deduction of Input Tax on such a supply, the KSA Customer should have commercial documents available to evidence the service and the consideration payable on the supply, in addition to the corresponding calculation of tax due on the supply.

**Example (22):** Al Badr Consulting engaged a Japanese legal advisor to provide legal advice for the possible expansion of Al Badr Consulting in Japan. The Japanese legal advisor issued an invoice for the fee of 10,000 yen. This invoice does not comply with the invoice requirements included in the KSA VAT legislation. As the document shows the date of supply and consideration payable, it can however be used to evidence the calculation of the taxable amount to determine the VAT due on the supply.

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(33) Article 48, Conditions for Exercising the Right of Deduction, Unified VAT Agreement

(34) Article 53(5), Tax Invoices, Implementing Regulations.



Where VAT is payable to the Customs Department on importation of goods, the importer of record provides his Tax Identification Number to the Customs Department with the customs entry. The Customs Department provides an electronic summary of the VAT paid on imports by that Taxable Person<sup>35</sup>. This is the only documentation accepted to prove the payment of VAT on imports. In all cases, the date of VAT payment at Customs shall be the date on which paid VAT should be reported in the Tax return, not the date of issuing the customs declaration.

## 8.1. ALTERNATIVE EVIDENCES/DOCUMENTS

The Implementing Regulations have specified other documents which can be used as evidence if the documents prescribed in the Unified VAT Agreement are not held:

- "A simplified Tax Invoice which is correctly issued in accordance with these Regulations<sup>36</sup>;
- In the case of a supply arising on the transfer of Goods to another Member State, a commercial or other document substantiating the value on which VAT is calculated at the transfer date<sup>37</sup>;
- Other commercial documentation permitted at the discretion of the Authority, evidencing that the Taxable Person has received the supply and correctly incurred the VAT in question<sup>38</sup>".

ZATCA considers that a Taxable Person receiving a supply of goods or services should seek and retain a valid Tax Invoice in all cases.

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(35) Article 43, Collection of Tax on imports on entry to the Kingdom, Implementing Regulations

(36) Article 49(7), Input Tax deduction, Implementing Regulations

(37) Article 49(7), Input Tax deduction, Implementing Regulations

(38) Article 49(7), Input Tax deduction, Implementing Regulations



**Example (23):** Tariq is a trader who is registered for VAT. He purchases goods from a small local supplier for SAR 3,000. The supplier issues a VAT invoice which clearly shows the TIN and relevant information surrounding the supply, but does not show the Customer (Tariq's) address or the quantity of parts supplied. Tariq's accountant has requested an updated invoice without success. Whilst the Tax Invoice is not fully complete, Tariq has a document that clearly evidences the particulars of the supply. ZATCA exercises its discretion to accept this as alternative evidence/document. Tariq may deduct Input Tax on this invoice according to the available documents in combination with the document evidencing the payment of VAT.

### **8.1.1 Non-Arabic invoicing**

Tax Invoices must include the relevant details in Arabic, in addition to any other language used. This means that an invoice which is issued without the relevant information in Arabic is not a valid Tax invoice or KSA VAT purposes.

A Taxable Person receiving a supply of goods or services should seek and retain a valid Tax Invoice (in Arabic) in all cases to evidence VAT deduction. However, in case an invoice is held which otherwise meets all invoice requirements listed in the Implementing Regulations, but is issued in another language instead of Arabic, ZATCA will exercise its discretion to allow the Customer to use such invoice as eligible other documentation evidencing that the Taxable Person has received the Supply and correctly incurred the Input Tax in question.



A Taxable Person can therefore use this invoice to exercise its right to deduct Input Tax. However, this is only possible if the following criteria are met:

- The invoice meets all invoice requirements listed in the Implementing Regulations other than being issued in Arabic<sup>39</sup>,
- The Taxable Person has other evidence that VAT has been paid to the supplier (bank statement, receipt from the supplier), and
- Upon request by ZATCA, the Taxable Person must provide a certified translation of any invoice if required during an examination or for any other reason

It is not required for a Taxable Person to request for ZATCA's approval to use non-Arabic invoices as alternative evidence for Input Tax deduction purposes for each individual invoice in case the abovementioned criteria are met.

This discretion only affects the Customer's right to deduct based on an invoice in another language. In all cases the supplier of the goods or services remains obligated to issue invoices meeting the full requirements of the Implementing Regulations, and will violate the provisions of the Law and Regulations where they do not do so.

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(39) The list of items required to be shown on a Tax Invoice is at Article 53(5), Tax Invoices, Implementing Regulations.



## 9. TIMING FOR VAT DEDUCTION

### 9.1. STANDARD TIMING

In the Unified VAT Agreement prescribes that the right to deduct Input Tax for the Customer of a supply is linked to the obligation of the supplier to pay the tax due on the supply - i.e. the date of supply.

“The right to make a deduction arises when a Deductible Tax is due pursuant to this Agreement<sup>40</sup>”.

The standard timing for a Taxable Person (who uses the standard invoice accounting basis to report VAT) to exercise the right to Input Tax deduction is the tax period in which the supply takes place<sup>41</sup>. This is usually the date the goods or services are received and the Tax Invoice or other documentation is issued to the Taxable Person<sup>42</sup>. Deduction cannot be exercised until the Taxable Person who is the Customer in respect of the supply has the appropriate evidence as described in section 8.

It is not required that any specific onwards supply of the goods or services purchased to be able to deduct the Input Tax on a purchased supply.

**Example (24):** Horizon Co, an industrial equipment supplier, purchases a crane from a manufacturer in March 2018 to fulfil an order which is due for delivery to the Customer in May 2018. Horizon Co files VAT returns on a quarterly basis. As the goods have been supplied to Horizon Co during March, and it holds a valid Tax Invoice, it may deduct the VAT charged on the purchase in the VAT return for the first quarter of 2018, although the onwards sale will not take place until a later tax period.

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(40) Article 44, Tax Deduction Principle, Unified VAT Agreement

(41) Article 45, Calculation of Tax, Implementing Regulations

(42) Article 23, Date of Tax Due on Supplies of Goods and Services, Unified VAT Agreement



**Example (25):** Universal LLC, a real estate development company has used the services of an architect for the development of new commercial real estate in Riyadh. The real estate is intended to be constructed and sold in two years. On the invoice issued by the architect KSA VAT has been charged to Universal LLC. Although the real estate has not yet been developed, the KSA Input VAT on the invoice is already deductible for Universal LLC as the services of the architect are directly linked to the intended future taxable sale of commercial real estate in Riyadh.

A Taxable Person using the cash accounting basis shall only make a deduction of Input Tax in respect of Supplies of Goods and services for which and to the extent that payment has been made<sup>43</sup>.

## 9.2. DEDUCTION IN SUBSEQUENT TAX PERIODS

The Implementing Regulations allows a Taxable Person to deduct Input Tax in a tax period subsequent to that tax period including the date of supply, subject to a statutory limitation of five years following the year in which the supply takes place<sup>44</sup>:

“A deduction of Input Tax may be made by a Taxable Person in a Tax Period subsequent to that Tax Period including the date of Supply, provided that the Taxable Person remains eligible to make such deduction under the other provisions of these Regulations. Input Tax may not be deducted in any period which falls more than five calendar years after the calendar year in which the Supply takes place”.

**Example (26):** Al Faris Co receives legal services from a KSA lawyer which are completed on 21 March 2018. The invoice for the services is issued on 31 March 2018 and sent to the commercial manager who instructed the lawyer. The commercial manager takes some time to obtain approval to process the invoice, and it is not sent to the finance team until after the VAT return for the first quarter ending 31 March 2018 is filed. Instead of making an adjustment to the first quarter's return, Al Faris Co is able to include the Input Tax deduction in the VAT return for the second quarter to 30 June 2018.

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(43) Article 46, Cash accounting basis, Implementing Regulations

(44) Article 49 (8), Input Tax Deduction, Implementing Regulations





## 10. ADJUSTMENT OF INPUT TAX DEDUCTION

### 10.1. CHANGE TO THE CONSIDERATION PAYABLE

The right to deduct Input Tax for the Customer of a supply is directly linked to the obligation of the supplier to pay tax due on the supply i.e. the date of supply.

Therefore in case of a change to the consideration payable, this change will have an impact on the VAT due on a supply and therefore also on the deductible Input VAT.

The value of a Taxable Supply by a Taxable Person is adjusted where that supply is cancelled or terminated, or where there is a genuine change to the consideration after the supply has taken place or been treated as taking place, in whole or in part<sup>45</sup>.

As the value of the supply is adjusted, the corresponding amount of deductible Input Tax related to this supply must also be adjusted. If the supplier has already issued a Tax Invoice for the original consideration due, it will be required to issue a credit note or debit note to reflect the change. In case a Customer, being a Taxable Person, has exercised its right to deduct on the original amount of Input Tax charged, this deduction must be adjusted in accordance with the adjustment to the value of the supply.

**Example (27):** Al Majd LLC, a marketing company established in the KSA has purchased ten new printers for the office. The supplier of the printers issues an invoice for the hardware with KSA VAT. This Input VAT is recovered by Al Majd LLC in the tax period corresponding to the date of the supply. After using the printers for three months, it becomes clear that the quality of the printers does not meet the needs of Al Majd LLC, who wishes to use a different supplier with better quality equipment. Therefore the printers are returned to the supplier for a refund, and the supplier issues a credit note. As the supply is cancelled, Al Majd LLC must correct the initially deducted Input VAT.

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(45) Article 27, Adjustment of Tax Value, Unified VAT Agreement



## 10.2. NON-PAYMENT

As the amount of the deductible Input Tax is directly linked to the amount of payable output tax, the Customer of the supply is not entitled to deduct the Input Tax to that supply in cases of non-payment<sup>46</sup>.

In the KSA, the Implementing Regulations prescribe that:

“any Taxable Person who has deducted Input Tax in respect of a supply received, but has failed to make payment in full after a period of twelve months from the date of supply, must reduce the Input Tax deduction by the amount of tax calculated on the consideration not paid at that date<sup>47</sup>”.

This includes cases where the consideration is not yet due for payment to the supplier (for example, if extended payment terms are offered). When the Customer does make payment against the supply, the Input Tax deduction may again be claimed in the period where payment is made<sup>48</sup>.

In certain cases where a Taxable Person does not receive all or part of the consideration for a Taxable Supply, the Taxable Person acting as supplier is - under certain conditions - allowed to reduce the output tax for the tax amount calculated on the supply<sup>49</sup>. This is also referred to as bad debt relief. The adjustment to Input Tax deduction is not linked to the supplier's eligibility to bad debt relief.

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(46) Article 47(1), Adjustment of Deductible Input Tax, Unified VAT Agreement

(47) Article 40(10), Adjustments to value of a supply, Implementing Regulations

(48) Article 40(11), Adjustments to value of a supply, Implementing Regulations



### 10.3. THEFT, DAMAGE OR LOSS

A Taxable Person is not required to adjust the Input Tax where the goods of the Taxable Person are lost, damaged or stolen<sup>50</sup>.

In order to prevent any uncertainty on the status of the goods and to prevent any fraud, the Implementing Regulations require that goods acquired by a Taxable Person, which are lost, damaged or stolen, must be reported as such in the accounting records held by the Taxable Person in order to support deduction of Input Tax on those goods<sup>51</sup>.

The Authority may require further evidence be provided in respect of such lost, damaged or stolen Goods including without limitation police reports and insurance claim documentation.

**Example (28):** In May 2018, Al Hussam Mechanics purchase a stock of 50 interior vehicle lighting parts with a purchase price of SAR 50 (excluding VAT) per unit to use in their vehicle repair business. The total purchase price of the stock is therefore SAR 2,875 (SAR 2,500 for the units, plus SAR 375 of VAT).

Two weeks later, an employee drops the box of parts which become no longer usable. The parts are not sufficiently high value to be insured: the therefore employee records this damage in the register of damaged parts, and this is signed off by management. The damaged parts are recorded in the accounting records by the finance team, and Al Hussam Mechanics is able to deduct the VAT (amounting to SAR 375) charged on the purchase of the damaged parts in the VAT return.

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(50) Article 47 (2), Adjustment of Deductible Input Tax, Unified VAT Agreement

(51) Article 49(5), Input Tax Deduction, Implementing Regulations



## 10.4. CAPITAL ASSETS

There are specific rules for Input Tax deduction related to capital assets. The definition of capital assets is “material and immaterial assets that form part of a business’s assets allocated for long-term use as a business instrument or means of investment<sup>52</sup>”.

Capital assets may therefore include tangible and intangible assets.

Deduction of Input Tax on capital assets is determined based on the purchaser’s intended use of the asset at the date the capital assets are purchased.

**Example (29):** A family business has an investment division carrying on partly exempt financing activities, a retail division and a travel division offering goods and services to Customers. The business purchases new office furniture and fittings to be used exclusively in the office of the travel division. The travel division’s activities are fully taxable. As the business intends the assets to be used long-term in a use which is attributed to Taxable Supplies of travel, the Input VAT is deducted in full on purchase.

The use of the capital assets must be monitored annually over the useful life of the asset. Where usage changes from taxable to non-taxable, or vice versa, the Taxable Person is required to adjust previously deducted Input Tax by way of an adjustment. These changes should be made, as applicable, each 12 months<sup>53</sup>.

Further information about capital assets and the deduction of Input Tax related to capital assets will be provided in a separate guideline.

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(52) Article 1 Definitions, Unified VAT Agreement

(53) Article 52, Capital Assets, Implementing Regulations



## 11. SPECIAL CASES

### 11.1. PRE-REGISTRATION VAT

Taxable Persons are entitled to deduct Input Tax incurred (paid) prior to the date of their effective registration for VAT. This applies to goods and services received in order to be used in the course of practicing an economic activity (to the extent that these goods and services are used for taxable supplies, internal supplies, and supplies that would have been taxable had they been made in the Kingdom)<sup>54</sup>. Pre-registration VAT deduction is subject to other specific conditions and criteria.

The Unified VAT Agreement provides the following conditions regarding the deduction of Preregistration VAT:

1. Goods and Services are received for the purpose of making Taxable Supplies;
2. Capital Assets were not fully depreciated before the date of registration;
3. Goods were not supplied prior to the registration date;
4. Services were received within a specific period of time prior to the date of registration as determined by each Member State;
5. the Goods and Services are not subject to any restriction related to the right to make a deduction stated in this Agreement<sup>55</sup>.

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(54) Article 49(1), Input Tax Deduction, Implementing Regulations

(55) Article 49, The Right to Deduct Input Tax Paid Prior to the Date of the Registration, Unified VAT Agreement



Further interpretation is specified for application of this provision in the KSA in the Implementing Regulations. The additional conditions for the deduction of Input Tax on goods purchased prior to the effective date of registration can be summarized as:

- In cases where the goods are capital assets, these must not have been fully depreciated at the date of registration ( have a positive book value). Therefore, the maximum deductible Input Tax permitted is calculated as if the net book value, determined in accordance with the accounting practice of the Taxable Person, were the Consideration for the Supply
- The goods have not been supplied onwards by the Taxable Person, or used in full by the Taxable Person, prior to the registration date;
- The goods are not of a type which is restricted from deduction, as discussed in section 7 of this guideline<sup>56</sup>.

A Taxable Person is entitled to deduct Input Tax incurred by that Person in respect of services supplied to that Person during the period of the six months before the effective date of registration, provided that:

- The services were purchased for the purpose of using in the course of practicing an economic activity<sup>57</sup>;
- The services have not been supplied onwards, or used in full, by the Taxable Person prior to the registration date;
- The services are not of a type which is restricted from deduction (as included in section 7 of this guideline)<sup>58</sup>.

## 11.2. VAT INCURRED IN OTHER COUNTRIES

Any VAT, or similar transactional tax, incurred by a Taxable Person in another country on supplies of goods and services or on imports cannot be deducted via the tax return in the KSA. A refund system for KSA businesses to obtain refunds of VAT paid in other GCC member states is to be established in due course.

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(56) Article 50, Goods and services deemed to be received outside of Economic Activity, Implementing Regulations

(57) Article 49(1), Input Tax Deduction, Implementing Regulations

(58) Article 50, Goods and services deemed to be received outside of Economic Activity, Implementing Regulations



## 12. PROPORTIONAL DEDUCTION

Input Tax incurred by the Taxable Person which is related to the Taxable Person's VAT exempt activities is not deductible as Input Tax. A person making both taxable and exempt supplies, can only deduct the Input Tax related to the taxable supplies.

For taxable persons who make both exempt and taxable supplies, the deductible Input Tax available to them must be determined using the following process<sup>59</sup>:

1. apportionment of the amount of the tax between the economic and non-economic activities, as set out in section 12.1 below, where the VAT on the economic activities will be the deductible Input Tax
2. apportionment of the Input Tax relating to the economic activity between the taxable supplies and the exempt supplies

For businesses which carry out solely economic activities (and do not have any separate non-economic activity), the first attribution need not be carried out.

### 12.1. APPORTIONMENT BETWEEN ECONOMIC AND NON-ECONOMIC ACTIVITIES

Input VAT deduction is only available to the extent that costs are incurred in the course of an Economic Activity<sup>60</sup>.

**Example (30):** A municipal authority in the KSA acts in its capacity of a public authority. For the purpose of exercising its governmental duties, the municipal authority makes use of a KSA consulting company, Al Asalah Co. Al Asalah Co charges VAT on invoices for its consultancy services. The VAT due on the invoices is directly attributable to the non-economic activities of the municipal authority and cannot be deducted via the VAT return.

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

(60) Article 49(1), Input Tax Deduction, Implementing Regulations



If a Person carries on both Economic Activity and non-economic activity, the Input VAT deduction should be determined based on whether the supply made by the taxable person is in the course of carrying on his Economic Activity, as follows:

After the tax is divided between economic and non-economic activities as described in section 1.12, the Input Tax Deduction related to economic activity is divided between taxable and exempt supplies. The Input Tax for economic activities only is eligible for deduction and attribution.

<b>Input VAT attributed to the supplies made to the taxable person in the course of the carrying on by him of his Economic Activity</b>	Deduct in full, provided this relates to Taxable Supplies
<b>Input VAT attributed to the supplies made to the taxable person in the course of the carrying on of a non-economic activity</b>	No deduction
<b>Other input VAT that cannot be directly attributed to economic or non-economic activities for the taxable Person</b>	Partial deduction based on apportionment

The VAT law does not set out a default method or calculation formula to apportion between economic activities and non-economic activity (as it does for taxable and exempt activities). Taxpayers must use a method that clearly and fairly reflects how the supplies in respect of which VAT has been paid by the taxable person have been used, and the extent to which they have been used in economic activities. The method should be based on verifiable data which can be reviewed by ZATCA.

**The taxable person must specify the amount of tax incurred on supplies received by him in the course of carrying out an Economic Activity, and those received by him outside the Economic Activity, before apportioning input VAT between taxable activities and exempt activities.**





## 12.2. APPORTIONMENT BETWEEN TAXABLE AND EXEMPT ACTIVITIES

VAT incurred which relates to a taxpayer's VAT exempt activities, such as financial services or residential rental, is not deductible as Input VAT. A supplier making both taxable and exempt supplies can only deduct the Input VAT related to the Taxable Supplies.

For taxable persons who make both exempt and taxable supplies, the deductible Input Tax available to them must be determined as outlined in the below table<sup>61</sup>.

<b>Input VAT exclusively and directly related to the taxable supplies</b>	Deduct in full
<b>Input VAT exclusively and directly related to the exempt supplies</b>	No deduction
<b>Overheads, and all other input VAT that cannot be directly attributed to taxable supplies</b>	Partial deduction based on apportionment

The overhead costs/expenses incurred by the Taxable Person 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.

A calculation of the taxable portion of the taxpayer's activities is only required in case a taxpayer makes both Taxable Supplies and exempt supplies. No proportional calculation is required for Taxable Persons who are fully entitled to deduct VAT.



**Example (31):** A municipal authority carries out public activities required of it by the Ministry of Municipal and Rural Affairs. It also owns properties which it rents for residential and commercial usage.

During 2021, the supplies made and received in relation to each activity are as follows:

Description	Supplies made (SAR) - a	Taxable Supplies received (SAR) - b	Input VAT deduction
<b>Public activities</b>	0 No income: centrally funded	4,800,000 (plus VAT of 720,000)	No Input VAT deduction - not incurred in Economic Activity
<b>Taxable commercial rental</b>	200,000 (plus VAT) Output tax 30,000 SAR	50,000 (plus VAT of 7,500)	Input VAT deduction for SAR 2,500
<b>Exempt residential rental</b>	300,000 (no VAT)	150,000 (plus VAT of 22,500)	No Input VAT deduction Non
<b>Non-attributable overheads related to both economic and non-economic activities</b>	N/A	1,000,000 (plus VAT of 150,000)	Requires attribution - Input VAT deduction for SAR 800, please see hereafter



- a. Supplies made refers to all outgoing supplies made by the municipality in the course of their public and economic authority.
- b. Taxable supplies refers to all incoming supplies rendered by Taxable Persons to the municipal authority as a Customer.

The authority's major activity is its public activities - therefore non-attributable overheads relate mostly to Non-Economic Activities, but partly to Economic Activities. The allocation described in section 12.1 must be carried out. The authority allocates this based on the supplies received as a fair and representative proxy for use of the overheads:

$$\frac{\text{Taxable Supplies received for economic activities}}{\text{Taxable Supplies received for economic and non-economic activities}} = \frac{(150,000 + 50,000)}{(4,800,000 + 150,000 + 50,000)} = 4\%$$

The percentage of attributable overheads related to economic activities equals 4% of the overheads, (SAR 40,000) plus (SAR 2,000) of VAT. To calculate the deductible Input VAT, the municipal authority must then attribute these between taxable and exempt supplies, using the following calculation:

$$\frac{\text{Value of Taxable Supplies made in the last calendar year}}{\text{Value of Taxable and exempt Supplies made in the last calendar year}} = \frac{(200,000)}{(300,000 + 200,000)} = 40\%$$

The municipal authority is able to deduct Input VAT for SAR 800, being 40% of the SAR 2,000 of VAT on overheads relating to Taxable Supplies.



### 12.3. DEFAULT METHOD

A prescribed default method of proportional deduction is calculated on the values of supplies made in the year, using of the following fraction<sup>62</sup>:

$$\frac{\text{The value of Taxable Supplies made by the Taxable Person in the last calendar year}}{\text{The total value of Taxable Supplies and Exempt Supplies made by the Taxable Person during the last calendar year}}$$

In this calculation:

Taxable Supplies	Exempt Supplies
Includes the value of all Taxable Supplies made by the Person, and all supplies of goods or services made that would have been taxable if made in the KSA.	0 No income: centrally funded
Excludes the supply of capital assets	200,000 (plus VAT) Output tax 10,000 SAR
Excludes the supplies which take place outside the KSA and are made from an establishment outside the KSA	Includes the value of all exempt supplies made by the Person, and all supplies of goods or services made that would have been exempt if made in the KSA.

(62) Article 51(3), Proportional deduction of Input Tax, Implementing Regulations



**Example (32):** KSA Bank is established in the KSA but also has branches in other countries across the Gulf region. During 2022 its activities include the following:

- KSA Bank supplies finance from its Riyadh head office to a Customer registered for VAT in the UAE, and earns an interest margin. This supply is outside the scope of KSA VAT, as the supply to a Taxable Customer in another State. Assuming the transitional rules for intra-GCC trade have ended, this supply will be outside the scope. However, as it is a supply which would have been exempt if made in the KSA, it counts towards the annual Exempt Supplies in the default proportional calculation
- KSA Bank divests/sell its long term investments in debt securities issued by a Saudi customer. This (the debt security value) is excluded from the default proportional calculation as the supply of a capital asset
- The Bahrain branch of KSA Bank makes a supply of financial advisory services to a Customer in Bahrain. These are supplies which take place outside the KSA under the place of supply rules, and would have been taxable if made in the KSA. However, as the supplies are made from an establishment outside the KSA, they are excluded from the default calculation

## 12.4. ANNUAL CALCULATIONS AND ADJUSTMENTS

The default proportional calculation is carried out based on the annual turnover for the previous Gregorian calendar year.

In case the Taxable Person was not registered for VAT in the previous calendar year, this Taxable Person must calculate the default proportional deduction based on estimated values of the current calendar year.

In either case, following the end of the completed calendar year, the Taxable Person using the default method must carry out an exercise to compare the values used in the fraction during that year (based on the previous year, or an estimate of the current year) with the actual values of supplies made in that calendar year<sup>63</sup>.

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(63) Article 51(6), Proportional deduction of Input Tax, Implementing Regulations



The Taxable Person must then make an adjustment to Input Tax in the final tax return for that calendar year to reflect the correct proportional deduction based on the actual supplies for the entire year<sup>64</sup>.

**Example (33):** Al Madar Co, a real estate company established in the KSA, started its activities on January 1, 2018. Anticipating the expected turnover figures for 2018 to exceed the mandatory registration threshold, the company applied to register in 2017 and has been registered for VAT from January 1, 2018 and Al Madar Co. is filing quarterly VAT returns. Al Madar Co is engaged in the development of real estate for both commercial and residential leasing. In the first three months the turnover generated with VAT taxable commercial leasing amounts to SAR 750,000. The turnover generated with VAT exempt residential leasing amounts to SAR 250,000 in the first three months.

Assuming on the turnover figures of the first three months would remain constant for the whole year, Al Madar Co applied a deduction ratio of 75% on the Input Tax on overhead / general costs and other nonattributable costs.

- Expected annual Taxable Supplies = SAR 3,000,000
- Expected annual Taxable plus exempt supplies = SAR 4,000,000
- Non-attributable costs per quarter = SAR 200,000 plus VAT of SAR 10,000
- VAT deducted in first, second and third quarters = SAR 7,500 per quarter.

At the end of 2018, the actual turnover figures of the entire year are calculated. The turnover generated with VAT taxable commercial leasing over the entire year amounts to SAR 4,000,000. The turnover generated with VAT exempt residential leasing amounts to SAR 1,000,000 over the entire calendar year. Taking the turnover figures into account for the entire year, Al Madar Co. (the Taxable Person) is entitled to an Input Tax deduction of 80% across the year.

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(64) Article 51(7), Proportional deduction of Input Tax, Implementing Regulations



As the company applied a deduction percentage of 75% on the Input Tax on the overhead / general costs during the first three periods (quarters), the company (Taxable Person) can deduct an additional 15% on the Input Tax. In the year 2019, the Taxable Person will take the 80% deduction right as the starting point for the deduction of Input Tax on overhead / general costs.

- Non-attributable costs in fourth quarter = SAR 200,000 plus VAT of SAR 10,000
- VAT deduction for fourth quarter based on actual figures = SAR 8,000
- Adjustment of under-stated VAT deduction in first three quarters =  $3 \times \text{SAR } 500 = \text{SAR } 1,500$



## 13. USE OF ALTERNATIVE METHODS

### 13.1. ALTERNATIVE PROPORTIONAL METHODS

The default proportional calculation uses the value of taxable and exempt supplies as a cost driver to determine how Input Tax is used for taxable and exempt activities. This method may not in all cases be the most accurate method to be used as a proxy for use, because it may give an inaccurate representation of how the VAT incurred proportionally relates to deductible activities<sup>65</sup>.

A Taxable Person may therefore submit an application to use an alternative proportional deduction method to the default method, in cases where that alternative method more accurately reflects the use of goods and services supplied to that Taxable Person.

Alternative attribution methods, using other calculation approaches than the value of supplies, will only be approved by ZATCA in cases where these reflect the actual use of Input Tax incurred better than the default method. In order to be able to apply an alternative method the Taxable Person should be able to demonstrate that the proposed method better reflects the actual use of Input Tax.

ZATCA will only allow an alternative proportional method where the proportional basis is verifiable. The table below gives examples of possible alternatives methods, and where they may be appropriate. This guide does not suggest approval will be given to any one particular method, and does not limit taxpayers to the below alternatives only.

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





Taxable Supplies	Formula	Possible Use
Proportional deduction based on number of transactions	Number of taxable transactions Number of taxable and exempt transactions	Businesses where each transaction uses a similar amount of Inputs, regardless of their value
Proportional deduction based on Inputs	Value of Inputs attributed to Taxable Supplies Value of Inputs attributed to taxable and exempt supplies	Businesses where values of particular supplies are distortive in comparison with relative Inputs
Proportional deduction based on number of employees	Includes the value of all exempt supplies made by the Person, and all supplies of goods or services made that would have been exempt if made in the KSA.	Businesses where a high proportion of Inputs is employee cost, and where employee time can be accurately tracked
Proportional deduction based on floor space	Floor space (m <sup>2</sup> ) used for taxable activities Floor space (m <sup>2</sup> ) used for taxable and exempt activities	Businesses whose rental and associated costs are a high proportion of Inputs
A "sectoral" method (a calculation method which divides the Taxable Person's overall activity into clearly distinct activities or sectors, and then applies a proportional calculation on each sector based on the value of supplies or another cost driver	A number of different sectors with distinct non-attributable Input Tax - each using the default proportional calculation or other calculation above	Businesses with different and distinct sectors, whose Input VAT can be separately measure



### **13.2. APPLYING FOR ALTERNATIVE METHOD**

In case a Taxable Person has the intention to apply an alternative method to calculate the proportional deduction, an application should be filed to ZATCA. In this application the Taxable Person should provide details about the method and its accuracy.

Requests for an alternative method should be submitted to the ZATCA online portal.

The Authority may approve or reject an application to use a method other than the default method by notification. In cases where the application is approved, the Authority shall prescribe a time period during which the alternative method may or must be used: this time provided that this time period does not exceed five years. Following the expiry of the time period, a new application must be submitted, or the Taxable Person may revert to using the default proportional method<sup>66</sup>.

### **13.3. DIRECTION BY ZATCA TO USE ALTERNATIVE METHOD**

The Authority is able to mandate that the Taxable Person use a specific method on a case by case basis. In order to do this, ZATCA will issue a notification to a Taxable Person, directing the use of the default method or an alternative method in case this accurately reflects the Taxable Person's use of goods and services supplied to that Taxable Person. In this case the Authority will also direct the time period for which this method must be used<sup>67</sup>.

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(66) Article 51(9), Proportional deduction of Input Tax, Implementing Regulations

(67) Article 51(10), Proportional deduction of Input Tax, Implementing Regulations



## 14. VAT RELATING TO INCIDENTAL ACTIVITIES

The Implementing Regulations prescribe special rules for VAT incurred in respect of certain transactions which do not form a usual part of a Taxable Person's economic activities, but are instead carried out in order to facilitate the ongoing taxable activities.

"In cases where the Taxable Person incurs Input Tax on Goods and services which are not used to make a Taxable Supply, but are used:

- a. in respect of raising capital for an ongoing Economic Activity to the extent this constitutes the making of Taxable Supplies by way of the issue of share capital or debt,
- b. for a business activity which is treated as outside the scope of VAT, such as a transfer of an Economic Activity or part of an Economic Activity as a going concern within article seventeen of the Regulations,
- c. for another one-off event which is incidental to the Economic Activity to the extent this constitutes the making of Taxable Supplies,

Such Input Tax shall be deductible in accordance with the proportion of the overall Economic Activity of the Taxable Person which constitutes the making of Taxable Supplies, determined using the applicable proportional deduction method determined in accordance with this article<sup>68</sup>".

Under these special rules, the VAT attributable to any of these incidental events is determined as if it were a non-attributable or general overhead cost, following the rules outlined in section 6 of this guideline. The value of any incidental supplies made which are Taxable or Exempt supplies are then not included within the default proportional calculation as outlined in section 12.

These special rules are only applicable for events that fall outside of the usual activities of the business and facilitate the carrying on of an ongoing economic activity in the course of making Taxable Supplies. Taxable Persons who regularly carry out these transactions as part of their business activities must apply the usual rules to determine the eligibility for deduction of VAT related to these supplies

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(68) Article 51(11), Proportional deduction of Input Tax, Implementing Regulations



**Example (34):** Al Barakah Co, a supplier of industrial equipment in Dammam, wishes to significantly expand its business by acquiring premises in other cities in the KSA. Following a detailed offer and tender process, it issues new share capital to existing shareholders and institutional investors. The funds raised from the share issue are used solely in expanding the existing business which is fully taxable for VAT. Al Barakah Co incurs financial advisory and legal costs of SAR 6,000,000 on the share issue. As the costs are for a one-off event which relates to raising capital for an ongoing taxable business, VAT charged by the advisors and lawyers on the costs is deductible as Input Tax, in line with the usual proportional deduction (100% as Al Barakah Co is otherwise fully entitled to deduct VAT).



## 15. VAT OBLIGATIONS OF TAXABLE PERSONS

In your capacity as a Taxable Person, you must know your tax obligations and also comply with the obligations relating to VAT. This includes registering for VAT as necessary, filing in time, 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 [zatca.gov.sa](http://zatca.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

### 15.1. 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 not subject to VAT, by no later than fifteen days following the end of the month in which the supply is made.

Every Taxable Person must issue a simplified tax invoice in the event that the value of the supply is less than SAR 1,000 (not for Internal Supplies or Export of Goods). With regard to supplies made by taxable persons to non-taxable natural persons, or any Person other than the persons mentioned in the preceding paragraph, the taxable supplier must issue an invoice in the same form as the simplified invoice for the supplies. In both cases, the invoice must be issued no later

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(69) Article 53, Tax Invoices, Implementing Regulations

(70) Article 53, Tax Invoices, Implementing Regulations



than 15 days after the end of the month in which the supply took place.

The Tax Invoice must clearly detail certain information such as the invoice date, supplier's tax identification number, taxable amount, tax rate applied, and the amount of VAT charged<sup>69</sup>. If different rates have been applied to supplies, the value of each supplies at each rate must be separately specified, as well as the VAT applicable to each rate. A Tax Invoice may be issued in the form of a commercial document (such as a ticket receipt), provided that that document contains all of the requirements for the issuing of Tax Invoices as set out in the Implementing Regulations to the Law<sup>70</sup>.

Tax invoices are not required for supplies made outside the scope of VAT in the Kingdom of Saudi Arabia.

Further information on the requirements for tax invoicing can be found in the VAT manual or at [zatca.gov.sa](http://zatca.gov.sa).

## 15.2. FILING VAT RETURNS

Each VAT registered Person, or the Person authorised to act on his behalf, must file a VAT return with ZATCA for each monthly or quarterly tax period. The VAT return is considered the Taxable Person's selfassessment of tax due for that period.

Monthly VAT periods are mandatory for Taxable Persons with annual revenues 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.

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(70) Article 53, Tax Invoices, Implementing Regulations



More information on filing of VAT returns is provided 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 after the filing of the VAT return, or at any later time during the next five years by filing a request for a refund to the Authority. ZATCA will review these requests and will pay the amount due on refund requests that have been approved, directly to the taxpayer<sup>71</sup>.

### 15.3. 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 where the conditions specified in Regulations are met - but must be made available to ZATCA on request.

All records must be kept for at least the standard retention period of 6 years. The minimum period for the keeping of records is extended to 11 years in connection with invoices and records relating to movable capital assets, and 15 years in relation to invoices and records relating to immovable capital assets<sup>72</sup>.

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(71) Article 69, Refund of overpaid Tax, Implementing Regulations

(72) Article 66, Records, Implementing Regulations, and Article 52, Capital Assets, Implementing Regulations



#### **15.4. CERTIFICATE OF REGISTRATION WITHIN THE VAT SYSTEM**

A resident Person who is subject to VAT and registered with the Authority in the VAT system must display a 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.

#### **15.5. CORRECTING PAST ERRORS**

If a Taxable Person becomes aware of an error or an incorrect amount in a filed VAT Return, or of any other non-compliance with the VAT obligation, he should notify ZATCA and correct the error by amending VAT the tax return. Errors resulting in a net understatement of VAT (exceeding SAR 5,000) must be made known to ZATCA within twenty (20) days of detecting the error or incorrect amount, and the previous return must be amended. In connection with minor errors resulting in a difference of less than SAR 5,000, the error may be corrected by amending the net tax in the subsequent tax return<sup>73</sup>.

Further information on correcting errors can be found through [zatca.gov.sa](http://zatca.gov.sa).

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(73) Article 63, Correction of Returns, Implementing Regulations





## 16. PENALTIES

The Authority may impose penalties or fines on taxpayers for violations of VAT requirements set out by the Law or Implementing Regulations.<sup>(74)</sup>

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

(74) Chapter Sixteen: Articles (39-47), Tax Evasion and Penalties, VAT Law



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

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

## **17. APPLYING FOR THE ISSUE OF RULINGS (INTERPRETATIVE DECISIONS)**

In the event that you are not sure about the manner of application of VAT to a particular activity or particular transaction that you are doing or intend to do, after referring to the relevant provisions and the relevant guideline, you may submit an application to the Authority to obtain a ruling. The application should set out the full facts relating to the particular activity or particular transaction on which you are asking the Authority to express its view.

Rulings may be in one of the two following forms:

- Public: in which event the Authority will publish details of the ruling, but without referring to any private particulars relating to the individual taxpayer, or
- Private: in which case the Authority will not publish the ruling

Neither a public nor a private ruling issued by the Authority will be treated as binding on it or upon the taxable person in connection with any transaction that he performs, and it shall not be possible to rely on it in any manner.

The Authority is not obliged to respond to all requests for rulings, and it may review all requests and specify priorities on the basis of certain elements, including:

- The level of information submitted by the taxpayer in the request,
- The potential benefit to taxpayers as a whole on the issuing of a general ruling concerning some transaction or activity,
- Whether there is an existing law or guide dealing with this request



## 18. CONTACTING US

For more information about VAT treatment, kindly visit our website: [www.zatca.gov.sa](http://www.zatca.gov.sa); or contact us on the following number: 19993

## 19. Q&A

- 1. My business does not have an import licence but needs to obtain equipment from outside the KSA. Is it able to deduct the VAT paid to the Customs Department on the import of this equipment?**

No, only the Person that acts as importer in accordance with the Common Customs Law, and holds Customs documentation evidencing that he imported the goods, is eligible to deduct VAT paid on import (see 4.4 of this guideline).

- 2. Can a VAT registered business deduct VAT charged on the electricity bill?**

This depends on what the activities of the business are, and what the electricity is used for. If the electricity is used solely for a taxable purpose (such as in a factory producing goods for sale), VAT is likely to be attributed to taxable activities and deductible in full.

- 3. Is VAT deductible on goods, such as food products, which are no longer usable and destroyed?**

Yes, provided the other criteria/conditions for Input Tax deduction are met. There is no requirement to adjust VAT deduction for goods which must be destroyed or disposed of as part of the economic activity.

- 4. Can a business receiving goods and services from a supplier deduct VAT charged if it does not have a VAT invoice but has a supplier statement?**

A Customer must hold a valid Tax Invoice as a condition for deduction of Input Tax. If the supplier statement contains all the required information for a Tax Invoice, it might be sufficient documentation to support deduction based on ZATCA discretion. In all cases, the business should request a correct VAT invoice from the supplier. In exceptional cases, ZATCA may approve the use of alternative evidence (see section 8.1 of this guideline).



**5. How does the business calculate the proportional deduction for 2018, as the business was not registered and no taxable or exempt supplies were made during 2017?**

During 2018, or for any business that was not registered during the previous calendar year, the proportional deduction is based on an estimate of the taxable and exempt supplies for the current calendar year. An adjustment must be made in the last period of the year to reflect the actual values of total supplies for the year.

**6. Will all businesses be partly exempt due to the interest earned on bank accounts?**

ZATCA considers that interest earned on a current account, on which funds are accessible to the Taxable Person, is not viewed as consideration for an exempt supply by the account holder. This means that the account holder is not required to take the interest received from a bank related to the balance on an immediately accessible current account as VAT exempt turnover for the default partial deduction method (see 12.3) The earning of other exempt income from regular financial investments will require the Taxable Person to determine the correct VAT treatment on overheads.

**7. The use of values of exempt supplies is not appropriate for my business, as exempt**

supplies are difficult to value and VAT is incurred predominantly in respect of making Taxable Supplies. A Taxable Person may apply to use an alternative method, which more accurately reflects the use of Goods and services supplied to that Taxable Person.

**8. The business incurs VAT from a hotel in Germany on expenses for a business trip. How is VAT deducted?**

VAT charged in other countries is not deductible through the KSA VAT return. The business may enquire with the tax authorities in the country where VAT has been charged.



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