



Guideline

Manual Zakat Handling of Debts of Taxpayers who Maintain Statutory Accounts



Table of contents

1. INTRODUCTION	5
1.1 About Zakat	5
1.2 Collection of Zakat	5
1.3 Zakat Collection in the Kingdom of Saudi Arabia	5
1.4 Zakat, Tax and Customs Authority (ZATCA)	7
1.5 ZATCA's Tasks	8
1.6 About the Debt Handling Manual	9
2 Debts and the Like	9
2.1 Provisions of the Executive Regulations for Levying Zakat that Addressed the Zakat Handling of Debts	9
2.2 Types of Debt	10
2.2.1 Debts to Taxpayer	10
2.2.1.1 Types of Debts to Taxpayer	10
2.2.2 Debts by Taxpayer	15
2.2.2.1 Bank Financing (Loans, Facilities, and Other Related Banking Products)	15
2.2.2.2 Non-Bank Financing	20
2.2.2.3 Implications of the Following Processes:	40



Table of contents

2.2.2.4 Other Cases	42
3 Controls for Additions to ZB	44
Practical Example	50
Zakat Handling of Debts Owed by Taxpayer	57
Annex: FAQs	60



Disclaimer

This Manual is indicative and constitutes the concept and interpretation of the Zakat, Tax and Customs Authority (ZATCA) with regard to the implementation of the Executive Regulations for Levying Zakat promulgated by the Minister of Finance's Resolution No. (2216) dated 07/07/1440 AH. It is not a statutory document, and its provisions are indicative, non-binding to ZATCA, and it does not eliminate the need to peruse the Executive Regulations for Levying Zakat and the relevant rules and resolutions.



1. Introduction

1.1 About Zakat

Zakat is the third pillar of Islam. It is the most important financial way of worship at all. Therefore, it was mentioned repeatedly in the Glorious Qur'an. Allah Almighty has associated it with prayer in more than eighty verses. It is one of the key pillars that distinguishes a Muslim community from others, and a manifestation of the supremacy of Islamic legislations. It represents a successful way to fight poverty, alleviate the suffering of the needy, which lead to achievement of social solidarity.

1.2 Collection of Zakat

What evidences the great regard of Zakat in Islam is assigning its management and supervision to the State. In fact, the State is the entity responsible to collect Zakat on funds and spend it on those entitled, by assigning some personnel (Zakat Employees) to visit the owners of funds throughout the Islamic State, calculate the amount of their Zakat, then collect it from them, and supervise the disbursement and distribution of it to the beneficiaries.

ZACTA undertakes the task of levying Zakat. It undertakes all procedures related to the taxpayer's Zakat calculation, starting with the registration of the taxpayer, through the process of calculating the amount of Zakat for the taxpayer, which includes supervision of the taxpayer's submission of Zakat Reports, payment procedures, examination of the submitted statements, and verification of them with systems by well-trained personnel working at ZATCA, and ending with the issuance of the Final Zakat Certificate. This may also include examining the resulting taxpayers' objections to ZATCA's Zakat amounts assigned thereto.

1.3 Zakat Collection in the Kingdom of Saudi Arabia

The collection of Zakat and its disbursement to those entitled is one of the basic tasks of the State, as stipulated in the Basic Law of Governance in Article 21, wherein the following is set forth: (Zakat shall be collected and disbursed in its disbursement channels). Article 7 set forth evidence of the State's attention to the duties of Sharia and its commitment thereto in general, which includes collecting Zakat and disbursing it to the beneficiaries. It stipulates as follows:



(Government in Saudi Arabia derives power from the Holy Qu'ran and the Prophet's tradition. They are the rulers governing the Law as well as all State laws).

In confirmation of the foregoing, during the reign of the Founder King Abdul-Aziz -may Allah have mercy on him- Royal Decree No. (17/2/28/8634) dated Jumada Al-Thani 29, 1370 AH corresponding to April 06, 1951 AD, was issued containing the order to collect Zakat. The said Royal Decree was followed by many royal decrees confirming it as well as executive ministerial resolutions, in addition to the regulations and circulars, including: Royal Decree No. (M/40) dated Rajab 02, 1405 AH, and the Executive Regulations for Levying Zakat promulgated by Ministerial Resolution No. (2082) dated Jumada Al-Thani 01, 1438 AH corresponding to (February 28, 2017 AD), and the Executive Regulations for Levying Zakat promulgated by Ministerial Resolution No. (2216) dated Rajab 07, 1440 AH corresponding to (March 14, 2019 AD), which is applied to the Zakat Years (ZY) commencing from January 01, 2019 AD for all taxpayers, except for those who are treated under the discretionary method in accordance with Chapter Four of the Regulations, for whom the Regulations shall apply to their reports submitted after December 31, 2019 AD. Therefore, the Executive Regulations for Levying Zakat promulgated on Rajab 7, 1440 AH do not apply to the fiscal years prior to the said date, but rather those years shall be treated in accordance with the previous regulations and instructions prior to the said date.

The Executive Regulations for Levying Zakat has been particularly concerned with clarifying the provisions for levying commercial activities, besides other zakat funds, the requirements for submitting the Zakat Declaration, procedures for examination, assessment, and payment, and their respective terms. The Zakat proceeds collected by ZATCA are received and deposited firsthand in the Social Security Account, which is responsible for disbursement to the poor and needy in accordance with Royal Decree No. (16/5/1) dated Muharram 05, 1383 AH corresponding to (May 28, 1963 AD), wherein Paragraph (1) provides for: "Zakat shall be collected in full from all joint stock companies, and others, and individuals who are subject to Zakat." In addition, Paragraph (2) stipulates: "All amounts collected shall be returned to the Social Security Fund."



1.4 Zakat, Tax and Customs Authority

- ZACTA is the authority entitled to collect Zakat in the Kingdom of Saudi Arabia (KSA). It was entrusted with the collection duties in implementation of the Royal Decree No. (17/2/28/8634), dated 29/06/1370 AH, which stipulates that Zakat shall be collected from Saudis.
- It was established pursuant to the Ministerial Resolution No. (394), dated Shaaban 07, 1370 AH, as one of the government entities affiliated with the Ministry of Finance, and it was entrusted with the task of collecting the Zakat
- Then, the Royal Decree No. (61) was issued on Muharram 05, 1383 AH, which included the order to collect zakat in full and supply it to the Social Security Corporation
- A number of royal decrees and ministerial resolutions followed regulating the works of levying Zakat, key of which are: Royal Decree No. (M/40) issued on Rajab 02, 1405 AH, which included the order to collect Zakat in full from all companies, institutions, and others, and individuals who are subject to Zakat. Then, the Executive Regulations of the Royal Decree (M/40) was issued under Ministerial Resolution No. (2082), dated Jumada al-Akhirah 01, 1438 AH, and the Executive Regulations for the collection of Zakat was issued by virtue of the Ministerial Resolution No. (2216) issued on Rajab 07, 1440 AH, which is effective from January 01, 2019 AD.
- On Rajab 20, 1438 AH, ZATCA was formed under the Council of Ministers' Resolution No. (465), which contains approval of ZATCA's Regulations.
- On Ramadan 23, 1442 AH corresponding to May 04, 2021 AD, a Council of Ministers' Resolution was issued merging the General Authority for Zakat and Income with the former General Authority of Customs under the name of the Zakat, Tax and Customs Authority (ZATCA).



1.5 ZATCA's Tasks

ZATCA's Regulations defined the tasks of ZATCA in Article (3) thereof, which include the following:

- Collecting Zakat and taxes as well as custom fees from taxpayers in accordance with the relevant regulations and instructions.
- Providing high-quality services to taxpayers to support them in fulfilling their duties.
- Liaising with taxpayers and taking the necessary measures to ensure the collection of dues.
- Raising awareness among taxpayers, enhancing the degree of understanding and voluntary commitment to compliance and ZATCA.
- Leveraging modern technology in implementing, monitoring, and facilitating ZATCA's operation, and in enhancing the security role in combating customs smuggling.
- Cooperating with the private sector in the implementation and management of some supportive works.
- Developing the necessary plans to organize, manage, and invest the facilities of customs ports in coordination with the relevant authorities.
- Setting standards for following up on the performance indicators of ZATCA's works and plans, which ensure the development of its performance and services. ZATCA may coordinate in this regard with whomever it deems appropriate from the relevant authorities.
- Cooperating and exchanging experience and best practice with regional and international bodies and organizations.
- Representing KSA in regional and international forums and conferences.



1.6 About the Debt Handling Manual

This Manual provides guidelines and basic information regarding the Zakat Handling of the Debt Item, for those who are subject to Zakat (taxpayers) operating in various sectors. It helps form a clear vision and provides guiding instructions regarding the practical applications of debt accounting.

This Manual constitutes ZATCA's concept and interpretation regarding the implementation of the Executive Regulations for Levying Zakat promulgated on Rajab 07, 1440 AH. It is worth noting that this Manual is not a legal document, and its contents are only of a guiding nature, and it does not aim to contain all relevant provisions of the Executive Regulations for Levying Zakat. Although these guidelines are not binding on ZATCA or the taxpayer with respect to any transaction to be carried out; they provide general guidelines on how ZATCA treats zakat-related procedures on a practical level.

To check the instructions on any transaction, you can visit the official website of ZATCA at (zatca.gov.sa), which contains a wide range of tools and information specially-developed to assist the taxpayer, including visual guidance materials and all relevant data, as well as responses to the Frequently-Asked Questions (FAQs).

2. Debts and the Like

2.1 Provisions of the Executive Regulations for Levying Zakat that Addressed the Zakat Handling of Debts

The Executive Regulations for Levying Zakat, in its Second, Third, and Tenth Paragraphs of Article 4, addressed the zakat handling of debts, as follows:

Paragraph No. (2) of Article (4) sets forth the following: "Revenues and advance payments of the taxpayer shall be at the beginning or end of ZY, whichever is less."

Paragraph No. (3) of Article 4 sets forth the following: "Debts owed by the taxpayer, classified as long-term and similar components of ZB, such as government finance, commercial finance, creditors, notes payable, overdraft account, owners' or partners' loans (including their current accounts), provided that the following is observed:



- A. In case the debts owed by the taxpayer or other sources of funding have a period of three hundred and fifty-four (354) days or more overlapping during ZY and the year following the same, then it shall be added to the Zakat Base (ZB) for each year in proportion to the number of days in each ZY.
- B. ZY of debts shall not be interrupted by renewal or rescheduling of debts with the creditor itself, or by substitution of said debts or other funding sources that finance what was previously-financed by said debts.
- C. The mounts added as contained in this Paragraph shall not exceed the total amount deducted from ZB in accordance with Article 5 of the Regulations."

Paragraph No. (10) of Article (4) sets forth the following: "Any item of liabilities and equity shall be financed from the deducted items from ZB."

2.2 Types of Debt

2.2.1 Debts to Taxpayer

These are the amounts owed to the taxpayer by third parties as a result of dealing therewith, and the taxpayer has become a creditor to others in their value. These are classified under current assets or non-current assets according to their nature.

Zakat handling of said debts to the taxpayer is that they are not deducted from ZB because they are zakat assets. They were not mentioned amongst the deductible assets set forth in Article (5) of the Executive Regulations for Levying Zakat.

2.2.1.1 Types of Debts to Taxpayer

Trade Receivables

These are the receivables owed by third parties as a result of dealing with the taxpayer, and the taxpayer has become a creditor of others in its value as a result of deferred (credit) sales.

Trade receivables are zakat assets that are not deducted from ZB.



Advance Payments to Companies

These are amounts paid to the invested-in companies.

Payments made to companies are deemed zakat assets that are not deducted from ZB, in implementation of the Principle of Legal Personality, and that each company has an independent financial liability.

Loans to Subsidiaries and Associate Companies

These are the values of amounts paid to subsidiaries and associate companies.

Loans paid to subsidiaries and associate companies are deemed zakat assets non-deductible from ZB, which did not represent an investment in the subsidiary company, and the subsidiary company did not include the same as equity in its lists.

Accrued Revenues

These are the amount of revenues such as the receivables that have been recognized but not received.

The accrued revenues are deemed zakat assets that are not deducted from ZB.

(Positive) Derivative Financial Instruments

These are contracts made between two parties. These contracts derive their value from the price of an underlying asset. These contracts are restricted to a specific time and price in the contract with regard to delivery of the underlying asset, or until settlement is made in cash at a future date. Derivatives derive their price from the asset, which can be a stock, an index, or others.

(Positive) derivative financial instruments are zakat assets that are not deducted from ZB.

Partners' Current Debit

These are the value of the amounts owed from the partners.

Partners' current debits are deemed zakat assets that are not deducted from ZB, in implementation of the Principle of Legal Personality.

Other Receivables

These are other receivables owed by others (such as advances and custodies of employees, owed by government entities, etc.).

Other receivables are zakat assets that are not deducted from ZB.



Staff Housing Finance

These are the values of the amounts paid to subsidies the home ownership programs for the employees of the establishment.

The employees' housing item (or the like) is deemed a non-deducted asset, regardless of the method of financing, because the establishment classifies it as a debt owed thereto by the employee.

The foregoing shall be subject to the following conditions:

1. The units may not be registered as part of the fixed assets of the establishment.
2. The unit shall be depreciated in accordance with the depreciation of the rest of the fixed assets of the establishment.
3. The Subsidy Contract shall provide for granting the employee the benefit of the unit, and that the protection and maintenance of the asset shall be the responsibility of the establishment.
4. The unit's ownership may not be transferred to the employee for any reason.
5. There shall be no correlation between the premium and the value of the asset.

ZATCA may, upon examining the documents of the item, not accept its deduction when one of the conditions is not met.

Investments in Government Sukuk and Bonds

Sukuk or bonds are securities issued by governments or companies to raise money from investors for a specified period of time under a specified repayment date.

Pursuant to the Minister of Finance's Resolution No. (2218) dated Rajab 07, 1440 AH, as amended by the Ministerial Resolution No. (1343) dated Rabiul-Awwal 28, 1441 AH: "The State shall bear the zakat and income tax resulting from investing in sukuk and bonds issued locally by the Ministry of Finance in Saudi Riyals until their maturity date."



Controls for State's Bearing of Zakat and Income Tax Resulting from Investing in Sukuk and Bonds Issued by the Ministry of Finance:

1. The holder of the suk/bond shall submit his/her declaration within the statutory period in accordance with the procedures of ZATCA, and shall pay the amount due to ZATCA accordingly.
2. The holder of the suk/bond shall be one of those who are accountable according to their financial statements in accordance with the procedures of ZATCA.
3. The holder of the suk/bond shall not be one of the entities exempted from zakat or income tax.
4. The State shall not bear an amount greater than what the taxpayer paid to ZATCA.

Calculation Mechanism of State's Bearing of Zakat and Income Tax Resulting from Investing in Sukuk and Bonds Issued by the Ministry of Finance

First: The amount incurred by the State for zakat on sukuk and bonds shall be calculated by calculating two bases for the taxpayer; from one of which sukuk and bonds shall be deducted, and sukuk and bonds shall not be deducted from the other base, then the difference between the two bases shall be multiplied by the zakat percentage stipulated in the Executive Regulations for Levying Zakat, and the outcome is the incurred amount that can be recovered from the Ministry of Finance, except for the following cases:

1. If ZB reaches the minimum level, whether the investment in government sukuk has been deducted from ZB or not, the amount incurred shall be the zakat of annual returns on sukuk and bonds, calculated according to the following equation:

$$\text{(Adjusted Net Profit} \div \text{Gross Profit)} \times \text{Return on Sukuk and Bonds} \times \text{Zakat Percentage}$$

2. If ZB reaches the minimum when deducting the investment in sukuk and bonds, and does not reach it when it is not deducted, so the deduction amount shall be the outcome of the difference between the two bases, minus the share of the sukuk and bond returns from the net profit, multiplied by the zakat percentage, calculated according to the following equation:

$$\text{[Difference between the Two Bases} - \text{(Net Profit} \div \text{Gross Profit)} \times \text{Return on Sukuk and Bonds]} \times \text{Zakat Percentage}$$



Second: The amount incurred by the State for income tax shall be calculated on the net proceeds of sukuk and bonds according to the following equation:

$$(\text{Adjusted Net Profit} \div \text{Gross Profit}) \times \text{Return on Sukuk and Bonds} \times \text{Tax Percentage}$$

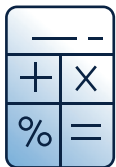
Third: This deduction applies to the fiscal years beginning on and after January 01, 2019 AD, and the deduction ceases for any government debt instrument except for the sukuk issued within the Saudi Riyal Sukuk Issuance Program at the Ministry of Finance starting from January 01, 2020 AD.

Example (1):

ZB for a company as on December 31, 2020 AD, amounted to SAR 10,000,000, and the investment value in the government sukuk and bonds issued by the Ministry of Finance, amounted to SAR 2,000,0000.

How is the State's Bearing of Zakat and Income Tax Resulting from Investing in Sukuk and Bonds Issued by the Ministry of Finance Calculated?

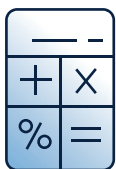
First: Zakat is calculated on ZB without deducting the value of the investment in sukuk and bonds



$$10,000,000 \times 2.5847\% (366 / 345 \times 2.5\%) = 258,470$$

Second: Zakat is calculated on ZB upon deducting the value of the investment in sukuk and bonds

$$10,000,000 - 2,000,000 = 8,000,000$$



$$8,000,000 \times 258,470 = 206,776$$

The difference between the zakat amount of the two bases is SAR (258,470 - 206,776 = 51,694) is calculated, and the difference in zakat between the two bases, which is SAR 51,694, is recovered from the Ministry of Finance.



2.2.2 Debts by Taxpayer

These are the amounts payable (obligations) to third parties as a result of said third parties' dealings with the taxpayer, and the taxpayer has become indebted thereto. These are deemed sources of external financing, which are classified as short-term or long-term obligations according to their nature.

Long-term obligations are added to ZB according to the value of the deductible assets. Furthermore, short-term liabilities that have financed a deduction for ZB are added in full.

2.2.2.1 Bank Financing (Loans, Facilities, and Other Related Banking Products)

Bank financing is one of the forms of external financing sources that an establishment resorts to to obtain funds for the purpose of using them in operational, investment, or production operations.

Loans

Loans are one of the sources of bank credit granted by banks that provide liquidity to the establishment through obtaining short-term or long-term loans for the purpose of using them in operational, investment or production operations.

Short-Term Loans

These are the funds granted to the establishment in order to finance its operating activities, through its use in the production cycle, obtaining cash, or financing investment activities through the purchase of productive assets, whose term is one year or less.

Short-term loans are deemed obligations and are therefore added to ZB according to the following controls:

1. Debts classified as short-term liabilities -including accrued expenses- are not added to ZB (even if they exceed 354 days), except in the following cases:
 - A. If the debt is renewed or rescheduled with the same creditor, or if the debt is replaced by another debt or source of financing that finances what was financed by the previous debt.
 - B. If it becomes known that it financed a deducted item.
 - C. If it is part of equity (e.g. profits under distribution).
 - D. If it is the current portion of a long-term loan.



2. With regard to the recycling or replenishment of the short-term debt, it shall be added to ZB when the following controls apply:
 - A. It shall be classified under short-term liabilities.
 - B. If the balance between the taxpayer and the lender has reached the value of (zero) during ZY for a period of more than ten days, it shall not be added to ZB. In the event that the balance does not reach the value of (zero), or has reached it for ten days or less; it shall be added to ZB under its value at the beginning or end of the year, whichever is less.
 - C. When these descriptions are fulfilled; in revolving loans, the upper threshold for adding external sources of funds shall be observed, which is the sum of what is deducted in accordance with Paragraph (3/C) of Article (4) of the Regulations.

Example (2)

A company has signed promissory notes that are due for payment in (less than 354 days) and are as follows:

1. SAR 6,000,000 as the value of a promissory note in return for financing the purchase of a plot of land.
2. SAR 4,000,000 as the value of a promissory note in return for financing the purchase of goods.
3. SAR 2,000,000 as the value of a promissory note in return for financing the payment of multiple obligations in the activity.

How much should be added to ZB in each case?

1. An amount of SAR 6,000,000 shall be added to the entire promissory note to ZB, as it was used in a deducted financing (fixed asset).
2. An amount of SAR 4,000,000 shall not be added to the value of the promissory note for ZB, as the promissory note is short-term and was not financed as a deduction (fixed asset).



3. An amount of SAR 2,000,000 shall not be added to the value of the promissory note for ZB as long as it is a short-term promissory note, and was used to pay off multiple obligations in the activity, and did not include deducted financing. In addition, it did not replace a previous commitment.

Example (3)

A company obtained a new short-term loan in an amount of SAR 10,000,000 on April 30, 2020 AD, due to be repaid on December 31, 2020. On April 19, 2020 AD, an existing short-term loan was repaid with the same amount from the same bank, knowing that the end of the fiscal year is on December 31, 2020 AD, how to determine what shall be added to ZB?

As for the new loan, it is not added to ZB because the new loan is short-term and not linked to the old loan; because the old loan is short-term and was repaid first, while the new loan was obtained after the old loan was repaid, and it did not finance what the previous loan was financing.

Example (4)

A company obtained a loan of SAR 6,000,000 on May 20, 2020 AD, due to be repaid on May 10, 2021 AD in return for repayment of an existing loan of the same amount, and it finances what was financed by the previous loan, knowing that the end of the fiscal year is on December 31, 2020 AD, how to determine what is added to ZB in 2020 AD?

The loan classified as short-term shall be added to ZB in its entirety because the conditions of addition apply thereto.

Long-Term Loans

These are the funds granted to the establishment to finance its investment assets, which require the availability of large liquidity for long periods of time (more than a year), which are repaid over long periods, and they are classified under long-term (non-current) liabilities.

Long-term loans are deemed debts and are therefore added to ZB according to the following controls:

1. The debts classified as long-term that arose during previous years shall be added to the balance of the ending term, including the additions thereto during the year, up to the maximum deductions.



2. If a long-term debt arises during the year and its duration is 354 days or more, it shall be added to ZB from the debt in relation to the year in proportion to the number of days, unless it is known that it was financed for a deducted item, in which case it shall be added up to a maximum of deductions.
3. The total of the debts added to the components of ZB shall not exceed the value of the deductions therefrom, including Paragraph (10) of Article (4) where they are added to the maximum deductions.

The following table shows how long-term and overlapping loans are processed during one year:

Long-Term Loans are Processed in the First Year

$$\frac{\text{Number of Days Left until End of the Fiscal year}}{\text{Number of Days of the Year (366)}} \times \text{Debt Value} = ****$$

Example (5)

A company obtained a long-term loan of SAR 4,000,000 on June 20, 2020 AD, knowing that the end of the company's fiscal year is December 31, 2020 AD, how to determine what loans shall be added to ZB?

For a long-term loan, it shall be added to ZB based on the number of days for ZY as follows:

Long-Term Loans are Processed in the First Year

$$\frac{\text{Number of Days Left until End of the Fiscal year}}{\text{Number of Days of the Year (366)}} \times \text{Debt Value} = ****$$



$$\frac{165}{366} \times 4,000,000 = 2,131,148$$



Example (6)

The total debts of the taxpayer classified as long-term obligations during the year ending December 31, 2020 AD amounted to SAR 50,000,000, while the total deductions from ZB amounted to SAR 35,000,000, how to determine what shall be added to ZB?

The debts by the taxpayer that are classified as long-term or financed deductible assets shall be added to ZB at the end of the year within the limits of deductions in an amount of only SAR 35,000,000.

Other Banking Facilities and Products

Other banking facilities and products shall be deemed financial facilities provided by financial institutions to companies such as financing the issuance of letters of credit, financing issuance of letters of guarantee, overdraft accounts, and other financial financing services.

Other banking facilities and products obtained from banks shall be deemed debts and are therefore treated, with regard to zakat, according to the following controls:

1. Debts classified as short-term liabilities -including accrued expenses- are not added to ZB (even if they exceed 354 days), except in the following cases:
 - A. If the debt is renewed or rescheduled with the same creditor, or if the debt is replaced by another debt or source of financing that finances what was financed by the previous debt.
 - B. If it becomes known that it is a deducted financing.
 - C. If it is part of equity (e.g. profits under distribution).
 - D. If it is the current portion of a long-term loan.
2. With regard to the recycling or replenishment of a debt, it shall be added to ZB, while observing the following:
 - A. It shall be classified under short-term liabilities.
 - B. If the balance between the taxpayer and the lender has reached the value of (zero)



during ZY for a period of more than ten days, it shall not be added to ZB. In the event that the balance does not reach the value of (zero), or has reached it for ten days or less; it shall be added to ZB under its value at the beginning or end of the year, whichever is less.

C. When these descriptions are fulfilled; in revolving loans, the upper threshold for adding external sources of funds shall be observed, which is the sum of what is deducted in accordance with Paragraph (3/ of Article (4) of the Regulations.

3. The debts classified as long-term that arose during previous years shall be added to the balance of the ending term, including the additions thereto during the year, up to the maximum deductions.
4. If a long-term debt arises during the year and its duration is 354 days or more, it shall be added to ZB from the debt in relation to the year in proportion to the number of days, unless it is known that it was financed for a deducted item, in which case it shall be added up to a maximum of deductions.
5. The total of the debts added to the components of ZB shall not exceed the value of the deductions therefrom, including Paragraph (10) of Article (4) where they are added to the maximum deductions.

2.2.2.2 Non-Bank Financing

Non-bank financing is one of the forms of external financing sources that the establishment resorts to to obtain funds for the purpose of using them in operational, investment, or production operations, such as government financing, commercial financing, creditors, notes payable, and loans of owners or partners (including current accounts).

Partner's Current Account and Dues Financing to Related Parties

These are the funds that an establishment obtains from partners or related parties in return for financing operational or investment activities.



Financing obtained from partners or related parties is deemed a liability and is therefore added to ZB according to the following controls:

1. Partners' current account financing classified under short-term obligations shall not be added to ZB (even if it exceeds 354 days), except in the following cases:
 - A. If it becomes known that it is a deducted financing.
 - B. If it is part of equity (e.g. profits under distribution).
 - C. If it is the current portion of a long-term financing.
2. The partners' current account financing classified as long-term that arose during previous years shall be added to the balance of the ending term, including the additions thereto during the year, up to the maximum deductions.
3. If the partners' current account financing arises during the year and its duration is 354 days or more, it shall be added to ZB from the debt in relation to the year in proportion to the number of days, unless it is known that it was financed for a deducted item, in which case it shall be added up to a maximum of deductions.
4. The total of the partners' current account financing added to the components of ZB shall not exceed the value of the deductions therefrom, including Paragraph (10) of Article (4) where they are added to the maximum deductions.

Example (7)

A company obtained financing from a partner (less than 354 days) and it was as follows:

1. An amount of SAR 1,000,000, which was used to finance the purchase of equipment for the plant.
2. An amount of SAR 2,000,000, which was used to finance the purchase of raw materials.
3. An amount of 3,000,000, which was used to pay employees' salaries.

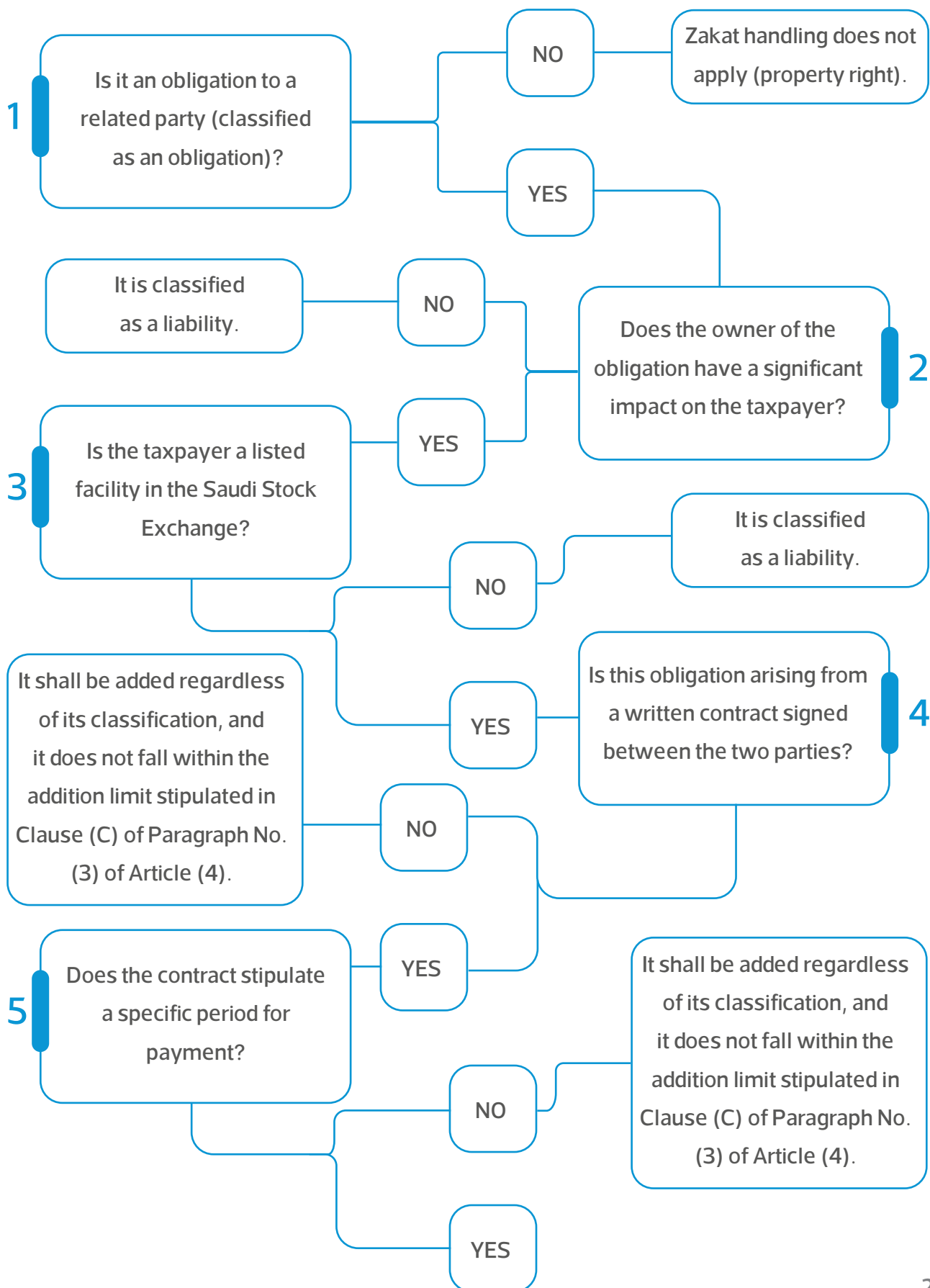


How much should be added to ZB in each case?

1. An amount of SAR 1,000,000 shall be added to ZB, as it was used in a deducted financing (fixed asset).
2. An amount of SAR 2,000,000 shall not be added because it is a short-term loan and it was not used in a deducted financing.
3. An amount of SAR 3,000,000 shall not be added as long as it is a short-term loan and is used to pay the salaries of employees.

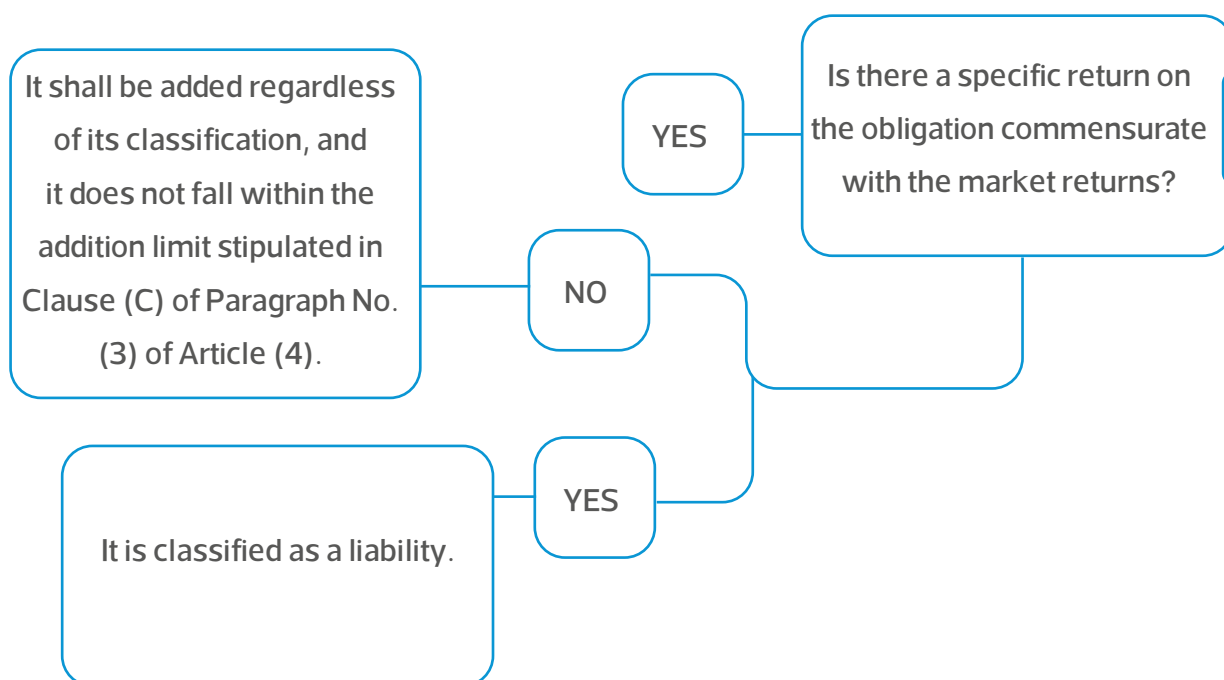
Zakat Handling of Debts by the Taxpayer with a Related Party:

Cases of Considering Debt (Obligations) with a Related Party as External Sources of Funds and
Cases of Considering it as Internal Sources of Funds (Property Rights)





6



Advance Payments

Payments received in advance for contracts obtained as part of a project, which are used to disburse on the project.

Payments received in advance for contracts shall be deemed external sources of funds, obtained as part of the project, which are used for disbursement on the project, and shall be added to ZB by comparing the balance of the beginning or end of ZY, and the lesser balance is added, in accordance with Paragraph No. (2) of Article (4) of the Executive Regulations for Levying Zakat.

- In the event that there is a debit balance to the same entity from which the advance payments were received, a set-off is then made between the debit balance and the credit balance of the received advance payments of the same entity. In the event that the set-off process results in a credit balance for the advance payments, it shall be deemed amongst advance payments; thus it shall be added to ZB as per the control above.

Example (8)

A company working in the field of contracting received an advance payment from one of its clients for a contract to implement a project in an amount of SAR 6,000,000 on October 22, 2020 AD, knowing that the balance of the advance payment remained the same at the end of



the year (December 31, 2020 AD), and during 2021 AD, the company doesn't expect to issue invoices or claims, especially with regard to this payment, before the date of December 31, 2021 AD.

How much should be added to ZB from the balance of the payment for 2021 AD?

An amount of SAR 6,000,000 shall be added to ZB at the end of 2021 AD, based on Article (4), Paragraph (2) of the Zakat Implementing Regulations.

Loan Securitization

Loan securitization is the value of the loan of bonds or sukuk issued by the company in return for obtaining large cash flows according to the terms of the issue.

Loan securitization is one of the external sources of funds that are obtained from the exchange of the bonds issued. It is the value of the bond loan and is deemed one of the obligations, and therefore it shall be added to ZB according to the following controls:

1. Loan securitization classified under short-term obligations shall not be added to ZB (even if it exceeds 354 days), except in the following cases:
 - A. If the loan is securitized or rescheduled with the same creditor, or if the debt is replaced by another debt or source of financing that finances what was financed by the previous debt.
 - B. If it becomes known that it financed a deducted item.
 - C. If it is the current portion of a long-term loan.
2. The loan securitization classified as long-term that arose during previous years shall be added to the balance of the ending term, including the additions thereto during the year, up to the maximum deductions.
3. If a loan securitization arises during the year and its duration is 354 days or more, it shall be added to ZB from the debt in relation to the year in proportion to the number of days, unless it is known that it was financed for a deducted item, in which case it shall be added up to a maximum of deductions.
4. The total of the loan securitization added to the components of ZB shall not exceed the value



of the deductions therefrom, including Paragraph (10) of Article (4) where they are added to the maximum deductions.

Example (9)

On March 15, 2020 AD, a joint stock company issued 10,000 bonds with a return of 6% annually, and the nominal value of the bond was SAR 2,000 due to be repaid after five years, and offered it for public subscription during a period ending on March 15, 2025 AD, and all bonds were subscribed and paid in one payment.

What amount should be added to ZB for the year ending December 31, 2020 AD?

Value of the Bond Loan Obtained

$$\text{Number of Bonds Issued} \times \text{Nominal Value} = \text{Bond Loan Amount}$$

$$10000 \times 200 = 20,000,000$$

The amount of the bond loan obtained is added to ZB (SAR 20,000,000) in proportion to the number of days on the basis that it is one of the other financing sources, and it is deemed a long-term obligation on the taxpayer, and therefore, an amount of SAR 15,901,639 shall be added, as calculated below, with the obligations not exceeding the amount of deductions from ZB as follows:

$$\frac{\text{Number of Days Left until End of the Fiscal year}}{\text{Number of Days of the Year (366)}} \times \text{Bond Loan Amount} = ****$$



$$\frac{291}{366} \times 20,000,000 = 15,901,639$$

For the years 2021, 2022, 2023, and 20249, the amount is added to the maximum deductible assets of ZB. As for 2025, no amount is added to ZB as there is no balance for the loan at the end of the period.



Government Dues

Government dues are amounts owed to the State, such as government grants, government loans, and government payables that are granted by the State to companies based on specific conditions depending on the nature and objectives of the activity.

Government dues are deemed sources of external funds and are among the obligations of the taxpayer, and are added to ZB in accordance with the Executive Regulations and based on the following controls:

1. Government dues classified under short-term obligations shall not be added to ZB (even if it exceeds 354 days), except in the following cases:
 - A. If the government dues are renewed or rescheduled with the same entity, or if the debt is replaced by another debt or source of financing that finances what was financed by the previous debt.
 - B. If it becomes known that it financed a deducted item.
 - C. If it is the current portion of a government dues is long-term.
2. The government dues classified as long-term that arose during previous years shall be added to the balance of the ending term, including the additions thereto during the year, up to the maximum deductions.
3. If long-term government dues arise during the year and its duration is 354 days or more, it shall be added to ZB from the debt in relation to the year in proportion to the number of days, unless it is known that it was financed for a deducted item, in which case it shall be added up to a maximum of deductions.
4. The total of the government dues added to the components of ZB shall not exceed the value of the deductions therefrom, including Paragraph (10) of Article (4) where they are added to the maximum deductions.



Example (10)

An agricultural company obtained government grants in an amount of SAR 30,000,000 on October 10, 2020 AD, due to be paid after (10) years, knowing that the end of the company's financial year is December 31, 2020 AD, how to determine the amount to be added to ZB for 2020 of government grants?

For a long-term loan, it shall be added to ZB based on the number of days for ZY as follows:

$$\frac{\text{Number of Days Left until End of the Fiscal}}{\text{Number of Days of the Year (366)}} \times \text{Debt Value} = ****$$

∨

$$\frac{82}{366} \times 30,000,000 = 6,721,311$$

Expenses Payable

These are expenses that pertain to the current financial period but have not been paid until the end of the financial period. The expenses payable are deemed sources of external funds, and they are amongst the obligations of the taxpayer. To add them to ZB, it is stipulated that they be classified as long-term according to the provisions of the Regulations, or be short-term, and are known to have financed one of the deductions.

Example (11)

The balance of expenses payable classified under long-term liabilities amounted to SAR 20,000, and the balance of the expenses payable classified under short-term liabilities was SAR 70,000, what amount should be added?

An amount of SAR 20,000 shall be added to ZB because it is classified as long-term obligations, in accordance with Paragraph No. (3) of Article (4) of the Executive Regulations for Levying Zakat.



Trade Creditors

These are the receivables owed by the taxpayer to third parties as a result of deferred (credit) purchases.

Trade creditors are deemed sources of external funds and are among the obligations of the taxpayer, and are added to ZB in accordance with the Executive Regulations and based on the following controls:

1. Trade creditors classified under short-term obligations shall not be added to ZB (even if it exceeds 354 days), except in the following cases:
 - A. If the debt is renewed or rescheduled with the same creditor, or if the debt is replaced by another debt or source of financing that finances what was financed by the previous debt.
 - B. If it becomes known that it financed a deducted item.
2. If a long-term debt arises during the year and its duration is 354 days or more, it shall be added to ZB from the debt in relation to the year in proportion to the number of days, unless it is known that it was financed for a deducted item, in which case it shall be added up to a maximum of deductions.
3. The total of the debts added to the components of ZB shall not exceed the value of the deductions therefrom, including Paragraph (10) of Article (4) where they are added to the maximum deductions.

Example (12)

A company made purchases on credit during the year in an amount of SAR 20,000,000 on March 1, 2020 AD, as follows:

1. An amount of 6,000,000 for the purchase of goods, due to be paid on January 31, 2021 AD.
2. An amount of 10,000,000 for the purchase of a new production line, due to be paid on January 31, 2021 AD.



3. An amount of SAR 4,000,000 for the purchase of raw materials used in production operations, due to be paid on February 28, 2021 AD.

What amount should be added to ZB for 2020 AD?

1. An amount of SAR 6,000,000 shall not be added to ZB because it is classified as short-term obligations, and it did not finance a deduction, in accordance with Paragraph No. (3) of Article (4) of the Executive Regulations for Levying Zakat.
2. An amount of SAR 10,000,000 for financing the purchase of a completely new production line, shall be added to ZB because it financed deductible assets.
3. The amount for purchase of the raw materials (SAR 4,000,000) shall be added in proportion to the number of days on the basis that it exhausted (354) days, and it is deemed a long-term obligation on the taxpayer, and therefore, an amount of SAR 3,344,262 shall be added, as calculated below, with the obligations not exceeding the amount of deductions from ZB as follows:

$$\frac{\text{Number of Days Left until End of the Fiscal}}{\text{Number of Days of the Year (366)}} \times \text{Increase Amount} = ****$$



$$\frac{306}{366} \times 4,000,000 = 3,344,262$$



Provisions

These are funds allocated to provide for a possible loss of unknown amount. This is with the exception of the provision for employees' benefits, as it is an invertible provision.

Types of Provisions, Including But Not Limited To, the Following:

1. Provision for Employees' Benefits

This is a provision to face cases of quitting work, expiry of the term of service for some employees, or retirement.

2. Provision for Bad Debts

This is a provision to meet the shortfall in the debts of customers and debtors as a result of their inability to pay their debts to the company.

3. Provision for Damaged and Slow-Moving Inventory

This is a provision to meet the decrease in the value of inventory resulting from damage and slow-movement or stagnation of inventory.

4. Provision for Declining Exchange Rates

This is a provision to counteract to the depreciation of exchange rates in cases of dealing with foreign currencies.

5. Provision for Zakat and Taxes

This is a provision to meet a zakat or tax amount for years that the Authority has not assessed or approved its submitted returns, whether zakat or tax.

6. Provision for Lawsuits or Damages

This is a provision to face certain losses of unknown amount in return for judicial compensation from the company towards third parties.



- Provisions shall be added to ZB according to the following controls:
 1. To be (added/deducted) to the (adjusted profit/adjusted loss) provision formed during ZY, as it is among the items in the income statement.
 2. The first of term balance shall be added to ZB minus the used balance during the year, as it is among the items in the financial position.
 3. If ZB is less than the adjusted profit, it shall not be allowed to deduct the used provisions from the adjusted profit because it is a deduction from the provisions of first term balance when it is added to ZB.
 4. When the provisions are added to ZB, it shall not be compared to the deductions from ZB.

Example (13)

The adjusted profit balance amounted to SAR 1,000,000 at the end of the year, which is the minimum base for ZB. In addition, the used balance of provisions is SAR 100,000.

Is it allowed to deduct the used balance from the provisions from the adjusted profit in case of calculating Zakat on the minimum base?

It is not allowed to deduct the used amount from the provisions from the adjusted profit (the minimum for ZB) because the used amount has been deducted from the provisions balance at the beginning of the year within ZB.



Example (14)

The table below shows the movement of provisions during the year:

Item	First of Year Balance	Accrual During the Year	Used During the Year	End of Year Balance
	SAR	SAR	SAR	SAR
End-of-Service Indemnity	4.000.000	1.000.000	600.000	4.400.000
Provision for Bad Obligations	2.000.000	400.000		2.400.000
Total	6.000.000	1.400.000	600.000	6.800.000

What amount should be added to modify the activity result?

Item	Amount
Amount of Provisions Made During the Year	1.400.000

What amount should be added to ZB?

Item	Amount
First of Year Provisions Balance	6.000.000
Deducting: Used Provisions During the Year	600.000
Provisions Balance Added to Base	5.400,000



Financial Derivatives:

Financial derivatives are defined as financial instruments that derive their value from a real asset (such as commodities, like gold) or a financial asset (such as stocks or bonds) or one of the market indicators. Such tools are used in managing financial risks and hedging and for purely speculative purposes and others.

In general, financial derivatives are characterized by the following:

- Their value changes when the underlying asset (i.e. an agreed-upon clause in the contract, such as an interest rate), exchange rates, or the price of a particular commodity (such as oil or gold) changes.
- Financial derivatives do not need an initial net investment when entering into the contract, or small amounts of premium may be paid when the contract is concluded.
- They are settled in the future.

Key examples of financial derivatives are the following:

- Future Contracts
- Forward Contracts
- Contracts for Difference (CFD)
- Option Contracts
- Swap Contracts



The accounting aspect of derivatives can be summarized as follows:

Companies must recognize changes to derivatives in their financial statements.

Changes to the fair value of financial derivatives are recognized either in the statement of profit or loss, or in equity, depending on their purpose, as follows:

1. **Financial Derivatives for Trading Purposes:** Changes to the fair value of such derivatives are recognized in profit or loss.
2. **Financial Derivatives for Hedging or Risks Mitigation:** For the purposes of hedge accounting, hedges are classified into two categories:
 - A. Fair value hedges, which hedge the risk of change to the fair value of recognized assets and liabilities.
 - B. Cash flow hedges, which hedge the risks of changes to cash flows associated with either a specific risk relating to a recognized asset or liability or a forecast transaction.

Financial derivatives are included at fair value as derivatives with positive market values are included in the (assets) while derivatives with negative market values are included within (other liabilities) in the statement of financial position.

In both sides (positive derivatives and negative derivatives), recognizing them in the financial statements entails the formation of a revaluation reserve, which is often at the same value as the derivatives. In the event that the derivatives that the entity has enlisted in its financial statements are negative derivatives, the revaluation reserve shall be shown at the negative value, and if the item appears at the positive value; the value of the revaluation reserve shall be shown as positive.



Cash	×××		Negative Fair Value of Derivatives	600	
Investments	×××	Revaluation Reserve	Revaluation Reserve for Positive Derivatives	1000	400
Positive Fair Value of Derivatives	1000		Revaluation Reserve for Positive Derivatives	(600)	
		Term Loans			×××
		Capital			×××

Zakat Handling of Debts of Taxpayers who Maintain Statutory Accounts Other Than Financing Activities

The financial derivatives recognized in the financial statements are not deemed deductible items from the components of ZB, as the Regulations did not address financial derivatives in the provisions related to the items that can be deducted in Article (5) of the Regulations. Therefore, the positive value of the financial derivative recognized as an asset in the financial statements is not deemed amongst the deductions from the components of ZB.

As regards the aspect recognized in profit or loss; the result of the activity is not modified in line with the provisions of the Regulations, which require observing changes to the fair value when calculating ZB.



As for the negative value of financial derivatives recognized as (liabilities); they are treated in terms of zakat according to the following:

1. The negative value of the derivatives is added at their full value, regardless of their classification or term; and the ruling does not differ, with regard to adding them, whether they are classified under short-term obligations or otherwise.
2. In addition to the negative value of the derivatives, the value of the valuation reserve that is created against the derivatives shall be added.
3. When adding the negative value of the derivative, they do not fall within the upper threshold of the addition; which does not exceed the value of the deductions.

To clarify the foregoing, given the previous example, the zakat handling shall be applied to the derivatives according to the following:

Addition Items:	
Capital	x x x
Term Loans - Up to the Maximum Amount of Deductions	x x x
Negative Fair Value of Derivatives	600
Revaluation Reserve for Positive Derivatives	1000
Revaluation Reserve for Positive Derivatives	(600)
Deduction Items:	



Investments	xxx
Nondeductible Items:	
Cash	xxx
Positive Fair Value of Derivatives	xxx

Zakat Handling of Taxpayers Subject to Calculating ZB under the Ministerial Resolution No. 2215 (Taxpayers of Financing Activities)

The Ministerial Resolution No. 2215 dated Rajab 07, 1440 AH required taxpayers practicing financing activities to treat the positive or negative value of derivatives as follows:

- The positive value of financial derivatives recognized in the assets shall be treated as non-zakat assets for the part due after one year or more (said treatment does not apply to the rest of the taxpayers, as this item is not deemed amongst the deductions from ZB).
- The negative value of financial derivatives recognized as (liabilities) shall be added as sources of funds subject to zakat for the part due after a year or more.

Other Debts

These are the receivables owed by the taxpayer to others as a result of operations other than deferred purchase and access to services, such as receivables to employees, deferred tax liability, and others.

Other debts are deemed sources of external funds, and they are amongst the obligations of the taxpayer. To add them to ZB, it is stipulated that they be classified as long-term according to the provisions of the Regulations.



Example (15)

The balance of accrued expenses for employees classified under short-term liabilities at the end of the year amounted to SAR 70,000, noting that the balance includes an amount of 10,000 from the beginning of the year.

How much should be added to ZB?

An amount of SAR 70,000 shall not be added to ZB because it is classified under short-term liabilities.

Deferred Tax

International Standard No. (12) adopted by the Kingdom of Saudi Arabia clarifies the accounting for the current and future tax implications of accrued or recoverable income tax in relation to taxable profit or loss for future periods as a result of past transactions or events. Deferred tax arises from the differences (known as temporary differences) between the book values of assets and liabilities in the statement of financial position and the corresponding tax bases. Deferred tax is classified under long-term liabilities or long-term assets. The Standard above applies to tax and mixed companies.

When calculating ZB, the deferred tax liability shall be added to ZB, and the debt is handled according to the provisions of the Regulations, while the deferred tax asset is not deemed amongst the deductible items according to the provisions of the Regulations.

Example (16)

The balance of the deferred tax liability classified as non-current liabilities at the end of the year amounted to SAR 12,000. In addition, the balance of the deferred tax assets classified as non-current assets at the end of the year amounted to SAR 8,000. What is the amount that should be added to ZB?

An amount of SAR 12,000 shall be added to ZB within the obligations, not exceeding the amount of deductions from ZB, while an amount of SAR 8,000 is not deducted from ZB.



2.2.2.3 Implications of the Following Processes:

Reclassification of Debt Following Reclassification of Asset

When building ZB, the obligations of the taxpayer (external sources of funding) shall be added initially, assuming its priority in financing the deducted items before the internal sources of funding, according to the following order:

- External Sources of Funds (Maximum Deductible Assets):
 1. Obligations that are known to have financed deductible assets, such as: (A promissory note for the purchase of a fixed asset).
 2. Long-term obligations.
- Internal sources of funds:

Property rights, such as: (capital reserves and retained earnings).

Example (17)

The following statements for a company as at the end of the fiscal year:

Statement of Financial Position			
Assets		Liabilities and Equity	
Item	SAR	Item	SAR
Current Assets	4,000	Current Liabilities	1,500
Long-Term Assets (Property and Equipment)	3,000	Long-Term Liabilities	3,500
		Equity	2,000
Total	7,000	Total	7,000



Base Calculation:

Item	SAR
Long-Term Liabilities (Not Exceeding the Deductions)	3,000
Equity	2,000
Minus: Deducted Assets	(3,000)
Total	2,000

The external sources of financing shall be added to ZB first to meet them with deductions, not exceeding the total value of the deductions, and then the internal sources of financing shall be added, and thus the long-term liabilities in the example above were added to ZB within the limits of the deductible assets, and then the equity is added.

Converting Debt into Equity and Converting Equity into Debt

- In the event of converting debt into equity, the following rules shall be observed:

Debt transferred shall be added to equity during the whole year.

Example (18)

A company increased its capital during the year by an amount of SAR 14,000,000 on August 01, 2020 AD by transferring the item of current partners' account into the capital, of which SAR 10,000,000 were used to purchase a new production line, and SAR 4,000,000 were used to finance the purchase of goods and raw materials.

What amount should be added to ZB for 2020 AD?



1. The full amount of SAR 14,000,000 shall be added to ZB.

- In the event of converting equity into debt:

The amount converted from equity to debts during the whole year is added to ZB as one of the internal sources of funds.

Example (19)

The balance of dividends in one of the companies at the beginning of the year amounted to SAR 20,000,000, as the partners decided to distribute profits in the amount of SAR 5,000,000 on July 01, 2020 AD, at the end of the year it was found that the dividends had not been paid to the partners, and the amount was listed as current liabilities under the item of non-paid dividends.

What amount should be added to ZB?

The total amount of dividends amounting to SAR 5,000,000 shall be added to ZB.

2.2.2.4 Other Cases

Bad Debts

There are the amounts owed from clients, which the taxpayer has written off from his/her records because it was not possible to collect them from the client. Bad debts are deemed amongst the expenses that may be deducted to reach the result of the activity in accordance with the following controls:

1. The revenues that resulted from said obligations have been previously declared within the taxpayer's revenues in the year of the repayment entitlement.
2. Bad debts shall be the result of the activity.
3. The taxpayer shall submit a certificate certified by a chartered accountant licensed in the Kingdom of Saudi Arabia, stating that the cancellation of said obligations was carried out by a decision of the authorized person, upon the Authority's request for that certificate.
4. The obligations shall not be on parties associated with the taxpayer.
5. The taxpayer shall declare what will be collected from those debts in the future.

Liabilities Against a Finance Lease



It is the value of the contractual obligation resulting from the finance lease contract resulting from the use of an asset, as it is recognized based on International Financial Reporting Standards (IFRS) 16.

Liabilities against the financial lease contract are deemed external sources of funds and are amongst the obligations of the taxpayer, and they shall be added to ZB to fulfill the deductible assets.

Example (20)

On December 31, 2020 AD, the balance of the liabilities against a finance lease; the current part amounted to SAR 2,000,000, and the balance of the liabilities against a finance lease; the non-current part amounted to SAR 12,000,000.

What amount should be added to ZB?

The total amount of liabilities against a finance lease contract, the current part, shall be added to ZB, in addition to the non-current part in full, amounting to SAR 14,000,000, within the obligations, not exceeding the amount of assets deducted from ZB.

Deferred Revenues

These are the amount of payments received for the provision of a service or product that have not yet been fulfilled.

Deferred revenues shall be deemed external sources of funds, and shall be added to ZB by comparing the balance of the beginning or end of ZY, and the lesser balance is added, in accordance with Paragraph No. (2) of Article (4) of the Executive Regulations for Levying Zakat.

Example (21)

A company working in the field of equipment manufacturing received an advance payment from one of its customers in exchange for manufacturing equipment in an amount of SAR 10,000,000 on September 05, 2020 AD, as it was classified within deferred revenues, noting that the balance of deferred revenues was at the beginning of the year on January 01, 2020 AD an amount of SAR 5,000,000, while at the end of the year, on December 31, 2020 AD, it reached SAR 15,000,000.



How much should be added to ZB from the balance of the deferred revenues for 2020 AD?

An amount of SAR 5,000,000 shall be added to ZB at the end of 2020 AD, based on Article (4), Paragraph (2) of the Zakat Implementing Regulations.

3. Controls for Additions to ZB

General Rule for Adding Debts to ZB and Zakat Handling

Debts by the taxpayer are deemed sources of external funds and are among the obligations of the taxpayer, and are added to the base in accordance with the Executive Regulations and based on the following controls:

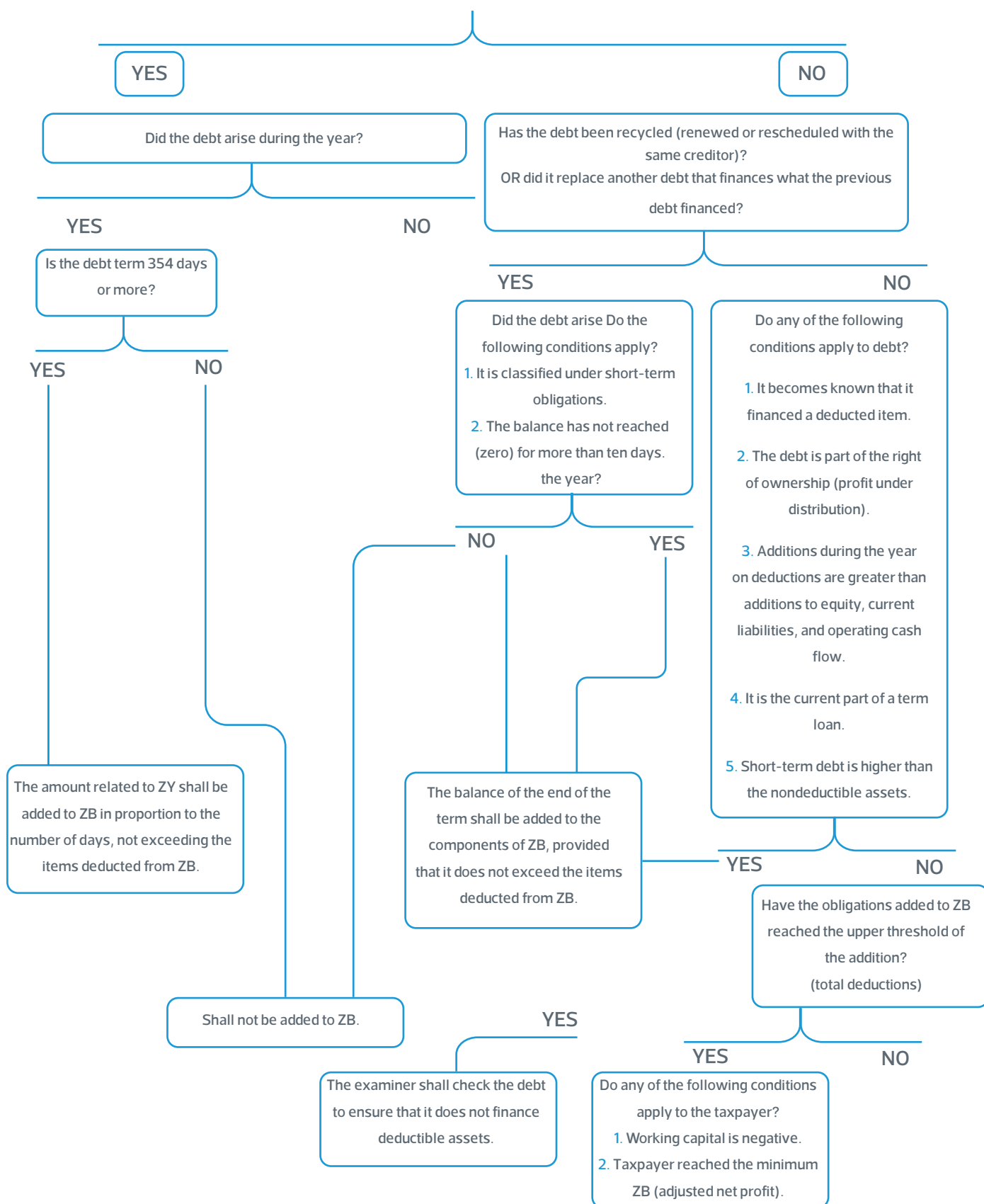
1. Debts classified as short-term liabilities -including accrued expenses- are not added to ZB (even if they exceed 354 days), except in the following cases:
 - A. If the debt is renewed or rescheduled with the same creditor, or if the debt is replaced by another debt or source of financing that finances what was financed by the previous debt.
 - B. If it becomes known that it financed a deducted item.
 - C. If it is part of equity (e.g. profits under distribution).
 - D. If it is the current portion of a long-term loan.
2. With regard to the recycling or replenishment of a debt, it shall be added to ZB, while observing the following:
 - A. It shall be classified under short-term liabilities.
 - B. If the balance between the taxpayer and the lender has reached the value of (zero) during ZY for a period of more than ten days, it shall not be added to ZB. In the event that the balance does not reach the value of (zero), or has reached it for ten days or less; it shall be added to ZB under its value at the beginning or end of the year, whichever is less.



- C. When these descriptions are fulfilled; in revolving loans, the upper threshold for adding external sources of funds shall be observed, which is the sum of what is deducted in accordance with Paragraph (C/3) of Article (4) of the Regulations.
2. The debts classified as long-term that arose during previous years shall be added to the balance of the ending term, including the additions thereto during the year, up to the maximum deducted assets.
 3. If a long-term debt arises during the year and its duration is 354 days or more, it shall be added to ZB from the debt in relation to the year in proportion to the number of days, unless it is known that it was financed for a deducted item, in which case it shall be added up to a maximum of deducted assets.
 4. The total of the debts added to the components of ZB shall not exceed the value of the deductions therefrom, including Paragraph (10) of Article (4) where they are added to the maximum deducted assets.



Is debt classified as long-term obligations?





Applying the Concept of Upper Threshold of Additions when Calculating ZB

This concept is based on adding the external sources of funds to ZB first, which include long-term obligations, and obligations that are known to have financed a deduction, not exceeding the total value of the deductions, and then the internal sources of funding shall be added (capital allocations, retained earnings, etc.).

Example (22)

The following statements for a company as at the end of the fiscal year:

Statement of Financial Position			
Assets		Liabilities and Equity	
Item	SAR	Item	SAR
Current Assets	10,000,000	Current Liabilities	2,000,000
Long-Term Assets (Property and Equipment)	30,000,000	Long-Term Liabilities	35,000,000
		Capital	5,000,000
		Carried-Forward Losses	(2,000,000)
Total	40,000,000	Total	40,000,000

Base Calculation:

Item	SAR
Long-Term Liabilities (Not Exceeding the Deductions)	32,000,000
Capital	5,000,000
Minus: Deductions (Long-Term Assets + Carried-Forward Losses)	(32,000,000)
Total	5,000,000



The external sources of financing shall be added to ZB first to meet them with deductions, not exceeding the total value of the deductions, and then the internal sources of financing shall be added, and thus the long-term liabilities in the example above were added to ZB within the limits of the deductible assets, and then the capital is added.

Revolving Loans:

Revolving Loans means: Renewing or replacing obligations with other obligations or funding sources that finance what these obligations were financing, or rescheduling obligations with the same creditor.

Based on the provisions of Paragraph No. (3/B) of Article (4) of the Executive Regulations for Levying Zakat; recycling the debt by renewing it, or replacing obligations with other obligations, or sources of funding that finance what said obligations were financing, or rescheduling the same with the same creditor; all of the foregoing may not be deemed debt revolving, and when adding them, the following descriptions shall be materialized:

1. It shall be classified under short-term liabilities.
2. If the balance between the taxpayer and the lender has reached the value of (zero) during ZY for a period of more than ten days, it shall not be added to ZB. In the event that the balance does not reach the value of (zero), or has reached it for ten days or less; it shall be added to ZB under its value at the beginning or end of the year, whichever is less.
3. When these descriptions are fulfilled; in revolving loans, the upper threshold for adding external sources of funds shall be observed, which is the sum of what is deducted in accordance with Paragraph (3/ of Article (4) of the Regulations

Example (23)

A company obtained a loan of SAR 30,000,000 on August 01, 2020, in return for the payment of an existing obligation of the same amount on the same date and from the same lender and on the same terms as the old loan.

How much should be added to ZB at the end of 2020 AD?

An amount of SAR 30,000,000 shall be added to ZB at the end of 2020 AD within the obligations, not exceeding the amount of deductions from ZB.



Practical Example

Statement of Financial Position

As on December 31, 2020 AD

Amounts in (SAR)

Assets	2020 AD	2019 AD
Current Assets		
Cash in Hand and at Banks	250,000	300,000
Cash Held	150,000	100,000
Murabaha Term Deposits with Banks	100,000	150,000
Other Receivables and Trade Receivables	450,000	400,000
Advance Payments to Contractors	100,000	150,000
Unbilled Revenues	50,000	100,000
Prepaid Expenses and Other Debit Balances	250,000	450,000
Total Current Assets	1,350,000	1,650,000
Non-Current Assets		
Property and Equipment	2,800,000	3,000,000
Dues from Related Parties	1,200,000	800,000
Accounts Receivable from Employees	400,000	500,000
Government Bonds	850,000	800,000
Advance Payments	800,000	800,000
Under-Construction Projects	750,000	700,000
Investment Real Estate	2,000,000	1,500,000
Treasury Bills	300,000	300,000
Other Long-Term Assets	150,000	300,000
Total Assets	10,600,000	10,350,000



Liabilities and Partners' Equity	2020 AD	2019 AD
Current Liabilities		
Liabilities Against a Finance Lease - Current Part	200,000	450,000
Short-Term Loan	200,000	400,000
Advance Payments from Customers	250,000	100,000
Deferred Revenue	400,000	150,000
Accounts Payable	250,000	200,000
Dividends	550,000	0
Accrued Expenses and Other Credit Balances	450,000	350,000
Zakat Provision	94,654	200,000
Tradable Part of a Term Loan	100,000	250,000
Total Current Liabilities	2,494,654	2,100,000
Non-Current Liabilities		
Liabilities Against a Finance Lease	1750,000	2150000
End-of-Service Indemnity Provision	500,000	650,000
Term Loan	500,000	600,000
Advance Payments for Rental Contracts	750,000	550,000
Total Liabilities	5,994,654	6,050,000
Partners' Equity		
Capital	2,500,000	2,500,000
Statutory Reserve	1,250,000	1,250,000
Retained Earnings	855,346	550,000
Total Partners' Equity	4,605,346	4,300,000
Total Liabilities and Partners' Equity	10,600,000	10,350,000



Income Statement

For the Period Ending on January 01, 2020 AD to December 31, 2020 AD

Amounts in (SAR)

	2020 AD
	SAR
Revenues	15,000,000
Cost of Revenues	(12,500,000)
Gross Profit	2,500,000
Sale and Marketing Expenses	(700,000)
General and Administrative Expenses	(600,000)
Other Losses (Net)	(150,000)
Income from Operations	1,050,000
ROI in Government Bonds	50,000
Financing Expenses (Net)	(150,000)
Profit before Zakat and Income Tax	950,000
Zakat	(94,654)
Profit for the Year	855,346



Additional Notes

1. There are expenses not related to the activity, amounting to SAR 200, which represent entertainment expenses for employees and others not related to the activity.

2. The company has short term loans. The movement of short-term loans during 2020 AD was as follows:

Item	First of Year	Withdrawals During Year	Payments of Year	Balance at End of Year
Short- and Long-Term Loans	400,000	200,000	400,000	200,000

Noting that no withdrawals were used during the year to finance the purchase of assets or items deducted from ZB. The company also expects to repay the year's loan withdrawals within the next (12) months.

3. The movement of provisions was as follows:

Item	First of Year	Accrual During Year	Payments During Year	Balance at End of Year
Zakat Provision	200,000	90,777	(200,000)	90,777
End-of-Service Indemnity Provision	650,000	50,000	(200,000)	500,000
Bad Debts Provision	50,000	10,000	(15,000)	45,000



Zakat Calculation:

Item	First of Year
Modification of Activity Result	SAR
Net Profit before Zakat and Income Tax	950,000
Added: End-of-Service Indemnity Provision Accrued During Year	50,000
Bad Debts Provision Accrued During Year	10,000
Added: Non-Deductible Expenses	200
Total Modification of Activity Result	1,010,200



Additions to ZB	
Item	SAR
Capital	2,500,000
Statutory Reserve	1,250,000
Retained Earnings	550,000
Distribution of Dividends	(550,000)
End-of-Service Indemnity Provision	450,000
Bad Debts Provision	35,000
Under-Distribution Dividends	550,000
Advance Payments from Customers	100,000
Deferred Revenue	150,000
Advance Payments for Rental Contracts	650,000
Total Additions Subject to ZB Without the Upper Threshold of Deductions	5,685,000
Obligations of Taxpayer within the Limits of Deductions	
Liabilities Against a Finance Lease (Classified as Long-Term and Current Part)	1,950,000
Term Loan (Classified as Long-Term and Current Part of Loan)	600,000
Total External Sources of Funds Subject to Limits of Deductions	2,550,000
Total Additions to ZB	8,235,000



Additions to ZB	
Item	SAR
Capital	2,500,000
Property and Equipment	2,800,000
Under-Construction Projects	750,000
Investment Real Estate	2,000,000
Total Deducted Assets	5,550,000
ZB without Adjusted Profit for Year	2,685,000
Zakat at 2,5847% of ZB without Adjusted Profit	69,399
Adjusted Profit	1,010,200
Zakat at 2,5% without Adjusted Profit	25,255
Total Zakat	94,654



Zakat Handling of Debts Owed by Taxpayer

Item	Item Nature	Zakat Handling according to the Rules	Rule
Current Liabilities			
Liabilities Against a Finance Lease - Current Part	These are the value of a contractual obligation as a result of a finance lease arising from the use of an asset.	External source exhausted in a deduction	To be added to ZB to account for the deductible assets.
Long-Term Loans - Current Part	These are the current part of financing assets or of a long-term loan.	External financing source exhausted in a deduction	To be added to ZB to account for the deductible assets.
Advance Revenues	These are the value of the payment received from clients as a percentage of the value of the project/services.	External Funding Source	The lesser shall be added to the balance at the beginning or end of ZY.
Short-Term Loans	These are the value of obligations as a result of loans that are due to be repaid within less than one year.	External source not exhausted in a deduction.	It shall not be added to ZB if it becomes known that it financed a deducted item or one of the conditions for adding the short-term debt has been fulfilled.
Deferred Revenue	These are the amount of payments received for the provision of a service or product that have not yet been fulfilled.	External Funding Source	The lesser shall be added to the balance at the beginning or end of ZY.



Advance Payments from Customers	These are the payments received on contracts.	External Funding Source	The lesser shall be added to the balance at the beginning or end of ZY.
Other Current Financial Obligations	These are various liabilities classified under current liabilities.	External finance source not exhausted in a deduction.	It shall not be added to ZB if it becomes known that it financed a deducted item or one of the conditions for adding the short-term debt has been fulfilled.
Trade Payables	These are the commercial liability within the activity of the establishment.	External finance source not exhausted in a deduction.	It shall not be added to ZB if it becomes known that it financed a deducted item or one of the conditions for adding the short-term debt has been fulfilled.
Accruals and Other Current Liabilities	These are a variety of liabilities.	External finance source not exhausted in a deduction.	It shall not be added to ZB if it becomes known that it financed a deducted item or one of the conditions for adding the short-term debt has been fulfilled.
Trade Creditors and Others	These are the commercial liability within the activity of the company.	External finance source not exhausted in a deduction.	It shall not be added to ZB if it becomes known that it financed a deducted item or one of the conditions for adding the short-term debt has been fulfilled.
Murabaha Financing and Long-Term Loans - Current Part	These are the current part of financing assets.	External finance source exhausted in a deduction.	To be added to ZB to account for the deductible assets.



Non-Current Liabilities			
Loans and Notes Payable	These are long-term obligations to finance fixed assets.	External finance source exhausted in a deduction.	To be added to ZB to account for the deductible assets.
Long-Term Loans - Non-Current Part	These are not the current part of financing assets.	External finance source exhausted in a deduction.	To be added to ZB to account for the deductible assets.
End-of-Service Provision	These are the non-current part of financing assets.	External finance source exhausted in a deduction.	It shall be added to ZB based on the balance of the beginning of the term minus the used during the year.
Finance Lease Obligations - Non-Current Part	These are the non-current part of the contractual obligations arising from the use of an asset.	External finance source exhausted in a deduction.	To be added to ZB to account for the deductible assets.
Deferred Government Grants	These are deferred balances that are depleted over the useful life of the financed assets.	External finance source exhausted in a deduction.	To be added to ZB to account for the deductible assets.
Deferred Tax Liabilities	These are tax differences.	External finance source exhausted in a deduction.	To be added to ZB to account for the deductible assets.
Obligations of an Operating Lease Contract	These are lease payments owed.	External finance source exhausted in a deduction.	To be added to ZB to account for the deductible assets.
Long-Term Sukuk	These are financing instruments with fixed period and other controls.	External finance source exhausted in a deduction.	To be added to ZB to account for the deductible assets.



Annex: FAQs:

Is it permissible to deduct the debts of the taxpayer that are classified as long-term, such as long-term notes, from ZB?

Notes are deemed amongst the debts of the taxpayer, and they are zakat assets that are not deducted from ZB.

In the event of purchasing machinery on credit from a supplier, is the balance of the supplier at the end of the year added to ZB, noting that the balance shall be repaid within a period of less than 354 days?

Machines are deemed items deductible from ZB, and based on the Regulations, the entire balance of the supplier shall be added to ZB.

Is it permissible for an establishment to deduct bad debts from ZB? What are the controls for that?

Bad debts are deemed amongst the expenses that may be deducted according to the following controls:

1. It shall have been previously declared within the establishment's revenues in the year the revenues are due.
2. Bad obligations shall result from the exercise of the activity, and the following are required for said obligations:
 - A. The establishment shall submit a certificate from a chartered accountant stating that said obligations have been written off from the books by virtue of a decision from the authorized person.
 - B. The obligations shall not be on parties associated with the taxpayer.
3. The establishment shall declare the obligations within its income when they are collected.



In the event that an establishment obtains a new loan in return for the payment of other obligations, is the loan amount added to ZB?

Pursuant to the Executive Regulations, obtaining a new loan in return for the payment of other existing obligations is deemed a part of the substitution of obligations with other obligations or sources of funding that finance what was previously financed by such obligations, thus the loan balance shall be added to ZB.

How is the capital increase that did not fund a deductible item calculated?

The increase in the capital shall be added in full to ZB if its source is equity. Also, the increase that did not fund a deductible item shall be added in proportion to the number of days on the basis that it is amongst other funding sources, and shall be treated as the obligations of the taxpayer, and therefore shall be added without exceeding the amount of deductions from ZB.

Is the part of the long-term loan, repaid within the last year, added to ZB?

It shall not be added to ZB because it was paid during the year.

 External document

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