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ADVANCES IN TRANSFER PRICING

Zain Satardien and Aakriti Sharma of Hourani and Partners look at how ZATCA in Saudi Arabia has been refining their approach to Transfer Pricing with new guidance on Advance Pricing Agreements (APAs).

"The Zakat, Tax and Customs Authority (ZATCA) in Saudi Arabia has recently released a guideline on Advance Pricing Agreements (APAs)," states Zain Satardien.

"This guideline helps to formalise Saudi's transfer pricing framework as well as aligning the Kingdom more closely with international best practice in transfer pricing and the Organisation for Economic Co-operation and Development (OECD) guidance on this area."

"This is a significant move which should help bolster investor confidence and also help enhance tax certainty"

"The Guideline details the process taxpayers should follow in order to apply for an Advance Pricing Agreement with ZATCA which establishes relevant criteria (such as the transfer pricing method (TPM), selection of comparables, and any necessary adjustments) for Controlled Transactions," Satardien continues.

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WHAT ARE ADVANCE PRICING AGREEMENTS?

"Broadly speaking, Advance Pricing Agreements are pre-emptive arrangements between a taxpayer and the tax authority which fix the method used for pricing intercompany transactions over a specific period," states Aakriti Sharma. "In most cases this period will typically be three years."

"Article 23 of the Saudi Arabia Transfer Pricing Bylaws explicitly includes Advanced Pricing Agreements," Satardien continues. "They aim to establish (in advance) the criteria which will be applied to specified Controlled Transactions to ensure that they adhere to the arm's length principle which applies in Transfer Pricing."

"Controlled Transactions are defined as any Transaction involving Related Persons or Persons Under Common Control. Controlled

Transactions include any notional Transactions or consideration exchanged between a Person and its Permanent Establishment, to the extent that these Transactions are recognised for the purposes of the Law," Sharma adds.

"These criteria which will be applied must have regard to Critical Assumptions about the future economic and operational conditions of each taxpayer," Satardien states.

"The new Guidelines explain that Critical Assumptions are the underlying business conditions and assumptions relied on for purposes of the Advance Pricing Analysis which, if significantly changed during the Advance Pricing Period, would affect the substantive terms of the APA and may potentially invalidate the APA itself."

WHY ARE ADVANCE PRICING AGREEMENTS USEFUL?

"Advance Pricing Agreements are useful as they can help to avoid future tax disputes as having an agreement in advance with the tax authority can assist in providing certainty on tax and Zakat treatment for both ZATCA and the taxpayers," states Sharma.

"However, it is important to note the limitations within these new Guidelines. At present the Guidelines only outline the procedures for entering into unilateral APAs (between the taxpayer and ZATCA specifically). There are no bilateral and multilateral APAs (involving other tax authorities)," Sharma adds. "Although, the Guideline does suggest that these may be considered in the future."

"Advance Pricing Agreements cover future years' transactions and cannot be applied retrospectively once they have been issued."

WHO IS ELIGIBLE?

"Taxpayers who engage in related party transactions are eligible to apply for Advance Pricing Agreements provided the value of each transaction in the APA reaches at least SAR 100 million annually," states Satardien.

"However, it is important to note that ZATCA has discretion to waive this threshold for complex transactions (which are defined by the use of sophisticated TP models, uncertainty around the appropriate TPM, or where there is a lack of reliable comparables)."

APPLICATION STAGES

1. The Introductory Meeting
A pre-filing meeting between the taxpayer and ZATCA.

2. Submission of the Application
The taxpayer submits a request via ZATCA's ERAD e-portal at least 12 months before the start of the first APA year.

3. Application processed
ZATCA conducts a preliminary assessment and then a comprehensive review.

4. Conclusion of the agreement
ZATCA finalises its position.

THE APPLICATION PROCESS

"The first stage when making an application to ZATCA for an Advance Pricing Agreement is the introductory meeting," states Sharma. "Taxpayers must first have a pre-filing meeting with ZATCA's APA team. This is their opportunity to explain their present business operations, their related party structures (in this respect they should focus on Covered Transactions), the proposed TPM they wish to take and its impact both on the taxpayers' Saudi tax and/or Zakat position," Satardien adds. "Taxpayers may be asked to provide organisation charts to explain their structure as well as functional and risk profiles of the taxpayer and related parties involved in the APA."

"No commitments will be made at this stage. The purpose of this meeting is to establish an early dialogue between the taxpayer and ZATCA, and most importantly to ensure all information has been properly understood by ZATCA," Sharma adds.

"The second stage is to actually submit the Advance Pricing Agreement application," Satardien continues. "All APA requests must be filed via ZATCA's ERAD e-portal at least 12 months before the start of the first APA year."

"Applications must include detailed justifications for the selected TPM and should also show how it would apply over historical and forecast periods," Sharma states. "All documents provided in the application must be in Arabic or in English where appropriate."

"Once the application has been submitted ZATCA will begin processing it," Satardien explains. "ZATCA conducts a preliminary assessment within 90 days of receiving the application and at this point may request further information from the taxpayer."

"There is then a comprehensive review stage," Satardien continues.

"This includes site visits and functional interviews, and there can also be additional documentation requests. This stage can take up to nine additional months."

"It is important to note that where additional information is requested if it is not provided within the required timeframe, ZATCA may discontinue the APA process."

THE ADVANCE PRICING AGREEMENT

"After all these steps have been completed, ZATCA will then draft the Advance Pricing Agreement and submit it to the taxpayer for approval and further discussion," Sharma states.

"When ZATCA is handling requests for Advance Pricing Agreements it may impose limits on the proposed scope of the agreement or could even require an expansion in the agreement's coverage."

"ZATCA has stated that they will aim to finalise their position on an Advance Pricing Agreement within 12 months of receiving the complete application," Satardien adds.

ONCE THE AGREEMENT IS ACTIVE

"Once an Advance Pricing Agreement is active, a taxpayer will also have to submit an Annual Compliance Report (ACR) within 120 days of each fiscal year-end," Sharma states. "This report has to cover all required items specified in the APA, including any requests for revisions or cancellations."

"Those who fail to submit this report within the required deadline or fail to submit it at all may find their Advance Pricing Agreement has been cancelled by ZATCA."

"In addition, once an Advance Pricing Agreement is in place the taxpayer also has a number of additional responsibilities," Satardien states.

"For example, they must maintain detailed records which substantiate their transfer pricing outcomes. They must submit timely and accurate ACRs. In addition, they must notify ZATCA of any changes which are affecting the Advance Pricing Agreement. Failure to comply with these requirements could also lead to cancellation or retroactive revocation of the APA."

REVISIONS, RENEWALS AND TERMINATION

"Advance Pricing Agreements may be revised if Critical Assumptions change," Sharma states. "They can also be renewed for another term under similar conditions, and may can be cancelled or revoked if non-compliance, fraud, or material misrepresentations are discovered."

"Renewal requests have to be submitted at least 12 months before the beginning of the first fiscal year concerning the new agreement," Satardien continues.

OTHER GCC STATES

"At present Saudi Arabia is the only GCC state to have formalised its approach to Advance Pricing Agreements," states Satardien.

"The UAE Corporate Tax Law (Federal Decree-Law No. 47/2022) and UAE Transfer Pricing Guidelines require detailed documentation on transfer pricing to be provided. However, at the time of writing Advance Pricing Agreements were not available in the UAE."

"Despite this it should be noted that the UAE stated in its Decision on Clarifications and Derivatives Federal Tax Authority Decision No. 5/2021 (which was issued and came into force on 8 December 2021) applications for unilateral Advance Pricing Agreements would be received from the fourth quarter of 2025," Sharma adds.

"However, it should be noted at present there has been no specific date provided and additional guidance on this area."