



# Asset management review 2023

Trends and themes shaping  
the industry in Saudi Arabia

October 2023  
KPMG Professional Services

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# Strong growth and asset diversification

The asset management industry acts as a catalyst for economic activity as it attracts liquidity from investors with appetite for wide-ranging assets. This has facilitated domestic investors to take on exposure in the global financial markets and for many years now, it has attracted foreign investors to equities and bond markets of Saudi Arabia. More recently, also more innovative products were introduced to cater to the increased funding requirements of corporates and banks.

The industry offers an increase in wealth over time through acquiring, maintaining, or trading assets or portfolios while maintaining an acceptable level of risk for unique investors. The industry serves high-net-worth individuals, institutional investors, government organizations, like pension funds, and retail investors.

In line with Vision 2030, the government of Saudi Arabia is undoubtedly fostering a favorable environment in Saudi Arabia for the industry to grow. Especially for its ambitious agenda of giga and mega projects, financing will be increasingly needed. The Financial Sector Development Program (FSDP) was also designed to further develop and internationalize the industry.

The Capital Market Authority (CMA) has taken initiatives to increase the depth of the capital market in line with Vision 2030's FSDP. Real estate continues to be the primary form of alternative investment in Saudi Arabia to provide a stable stream of income and capital appreciation over the medium to long-term. Real estate investment trusts and private real estate funds have gained popularity. CMA is working to facilitate fintech by developing the necessary infrastructure and supporting entrepreneurs and startups.

Important developments in the space of and Zakat include an approval by the Ministry of Finance of new Zakat rules for investment funds, effective since 1 January 2023. Despite not being subject to Zakat, funds must register with ZATCA and submit an information declaration within 120 days. Also, the Transfer Pricing Bylaws have been amended to include Zakat paying entities, starting in 2024..

With experience built on a wealth of knowledge accumulated through its audit, tax and advisory work for asset management firms around the globe and in



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the Kingdom, KPMG has the depth of expertise to help investment managers through the challenges that lie ahead for long-term growth and to support them as they look to grow revenue and increase efficiency.

To provide a directional overview of how the asset management industry has performed, this publication presents a detailed analysis of the cumulative performance of twelve large asset management firms, as well as an overview of the emerging themes and regulatory landscape of relevance for the sector. This is our second edition on this subject and we look forward to your feedback.



**Ovais Shahab**  
Head of Financial Services

# Industry performance analysis

## Market overview

In recent years, the capital markets of Saudi Arabia have become more appealing to both regional and international investors as a result of its high level of liquidity, improved infrastructure and transparency, and diverse range of investment offerings. The inclusion of Tadawul into global indices, such as MSCI Emerging Markets Index, FTSE Russell, and S&P Dow Jones, has also helped.

To create more opportunities for companies to raise capital and enable investors to access new markets, the Saudi Tadawul Group and the Saudi Exchange have been forming agreements with other international exchanges. Currently, there are discussions with the Shenzhen Stock Exchange in China for dual listings. In 2019, an agreement was signed with the Abu Dhabi Securities Exchange (ADX) resulting in Americana Restaurants becoming the first dual listing in 2022. There are other agreements in place with the Swiss Stock Exchange (SIX) in 2021 and the Muscat Stock Exchange (MSX) in 2022, with dual listings expected in the future.

With the vast scale of mega and giga project underway in the Kingdom, there will be financing needed beyond what the domestic banking sector can provide. Considering these significant investment requirements, capital markets will play a crucial role. For example, the IPO of NEOM is expected to take place in 2024.

According to the International Competitiveness Yearbook issued by the International Institute for Management Development (IMD) for the financial year 2022, the Kingdom has achieved advanced ranks with the indicators associated with the capital market. Saudi Arabia's ranking increased in nine indicators out of twelve associated with the capital markets, while three indicators maintained the same ranking as compared to the prior financial year 2021. The factors that most improved included training and education, regulatory framework, and adaptive attitudes.

The capital market reached record levels of foreign ownership in the financial year 2022, as net foreign investment in the main market amounted to about SAR184 billion. Further, we have observed that from 2019 to June 2023, foreign investors' ownership in the Saudi equities and debt markets grew by a compound average growth rate (CAGR) of around 17.4 percent – from SAR198 billion to SAR376 billion driven by reforms and international presence.

To expand the capital market and align with Vision 2030, Tadawul and CMA have implemented several reforms as part of the wider Financial Sector



**Foreign participation in the Kingdom's markets is also rising, with international investors representing 15 percent of the free-float shares that are publicly traded.**

Development Program (FSDP) aiming to increase the stock market capitalization (excluding Saudi Aramco) to 80.8 percent of GDP. These have included measures such as market liberalization for foreign investors, post-trade reforms, Tadawul's own transformation into Saudi Tadawul Group, improved corporate governance standards and transparency, streamlining the listing process and expanding product offerings.

The IPO drive in Saudi Arabia has moderated in 2023, though the pipeline in the second half of 2023 and beyond remains firm with more than 25 companies currently working on their IPO submissions. In October, the IPO of Ades International Holding Company, a PIF-backed oil & gas drilling company, is with SAR3.4 billion funds raised the largest of the year so far.

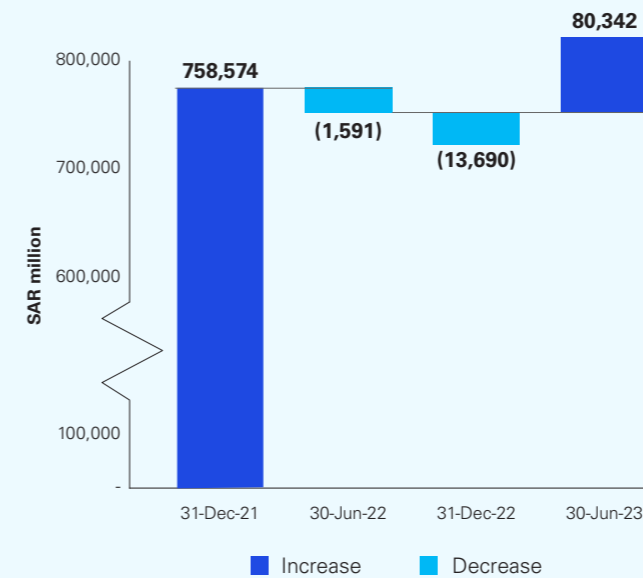
## Financial performance

Based on our analysis of the most recent available financial information of twelve large asset management firms in Saudi Arabia, we noticed a remarkable increase in their financial performance. The net income of these companies grew from SAR5.3 million for the year ended 31 December 2022 to SAR6.2 million for the year ended 31 December 2023, representing growth rate of 16.5 percent.

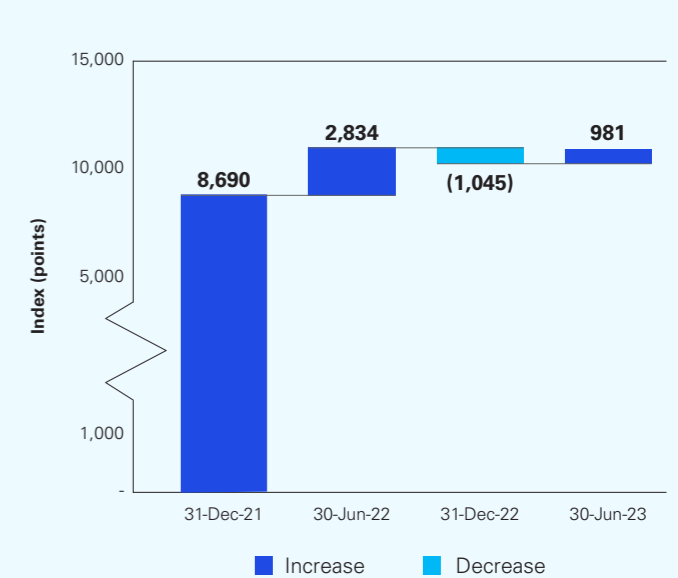
We also observed a surge of 35.7 percent year-on-year in the number of investment funds, rising from 839 to 1,130 and significant growth of the number of public and private investment fund subscribers reported from 675,465 to 901,896, representing a 33.5 percent year-on-year increase. Additionally, the size of AUM reached SAR823 billion as of 30 June 2023, from SAR756 billion as of 30 June 2022. We evaluate this shift is on account of better opportunities offered in the capital market and an increased number of funds.

Lastly, there has also been a remarkable surge in the number of subscribers to both public and private investment funds, from 675,465 to 901,896, or 33.5 percent, during this same period.

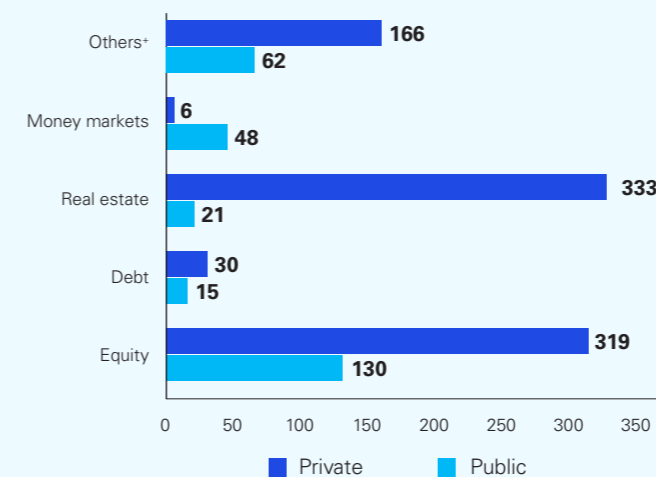
## Assets under management\*



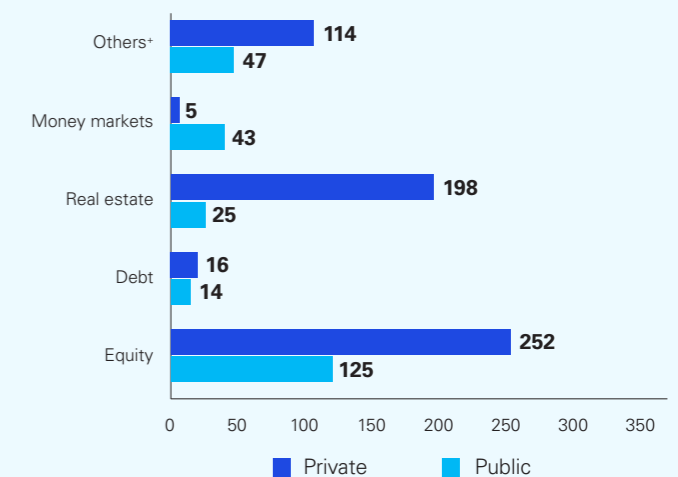
## TASI performance\*



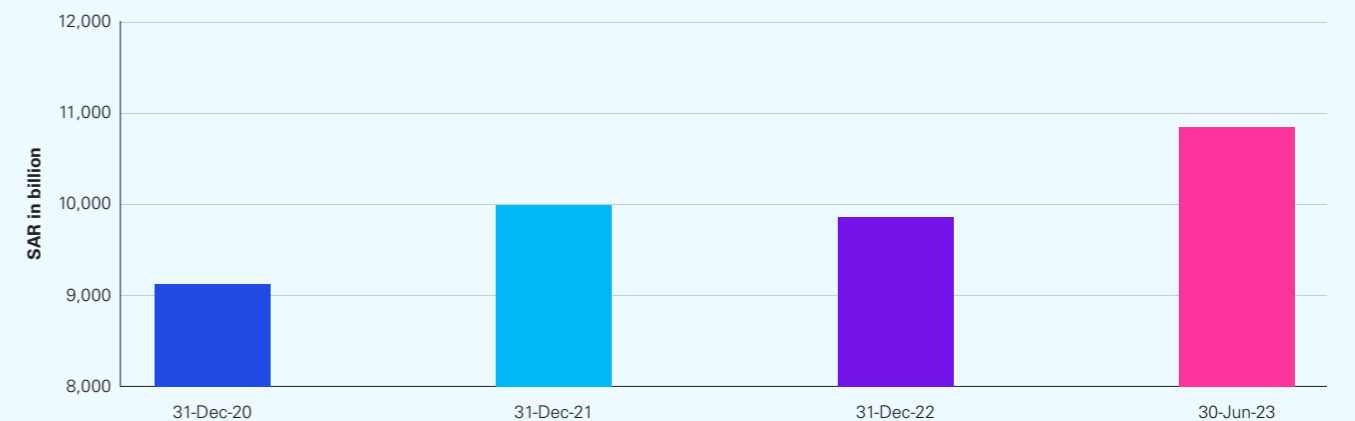
## Number of funds as of 30 June 2023\*



## Number of funds as of 30 June 2022\*



## Market capitalization\*

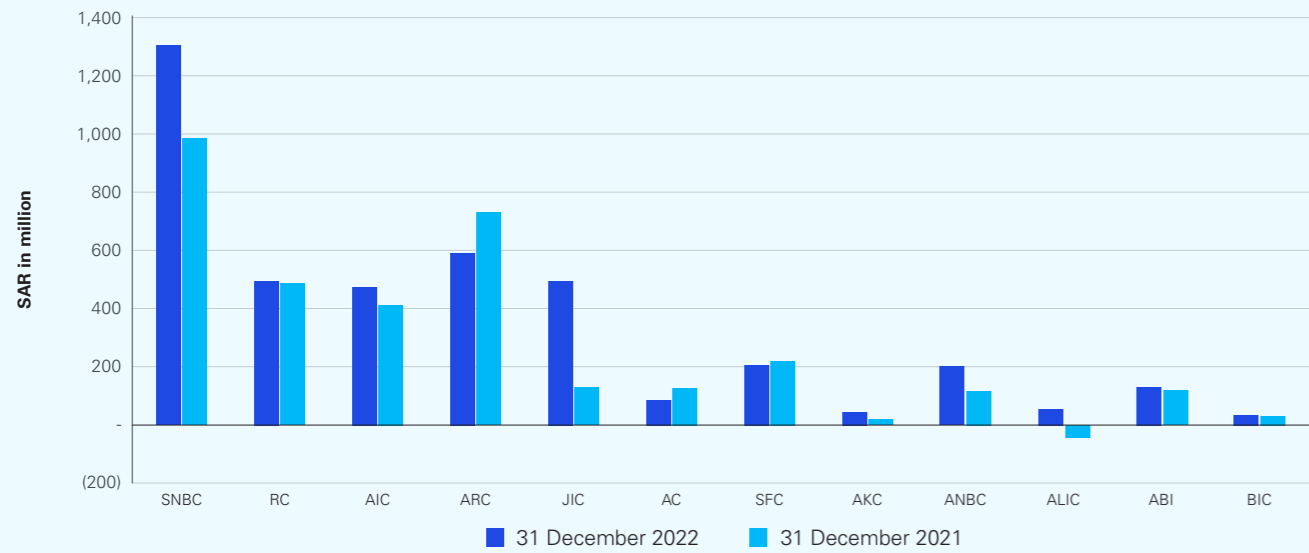


\*Capital Markets Authority, website.

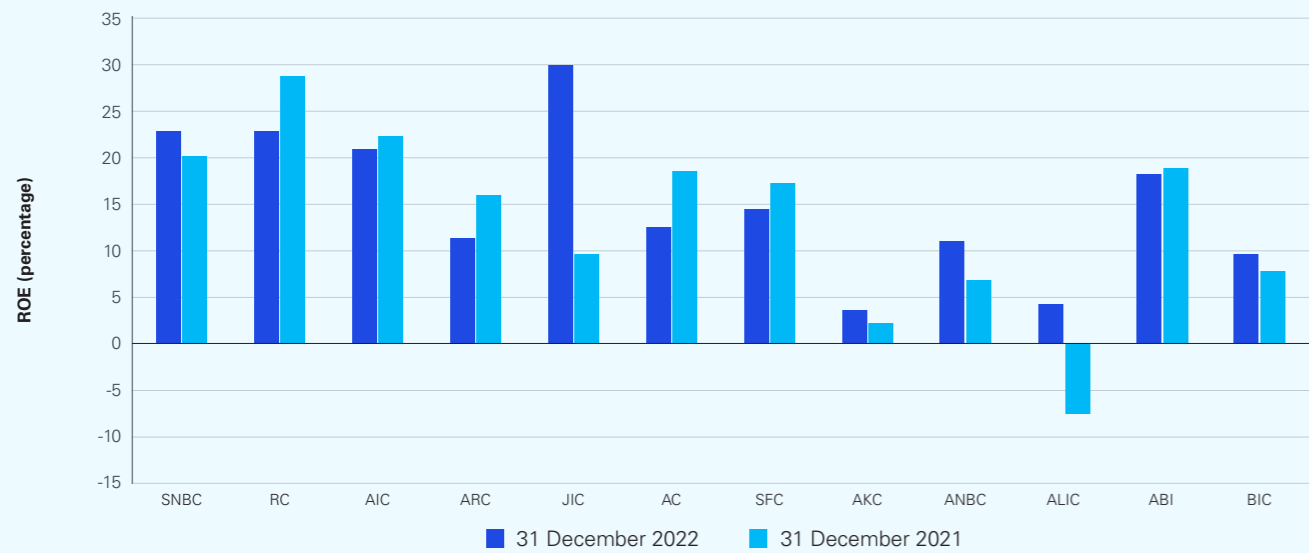
\* Fund of funds, exchange-traded funds (ETFs), multi-assets, endowments, feeder funds, closed-ended funds (CEFs) and commodities funds.

**Note:** All amounts on this page are presented in SAR and are rounded off to a million unless otherwise stated.

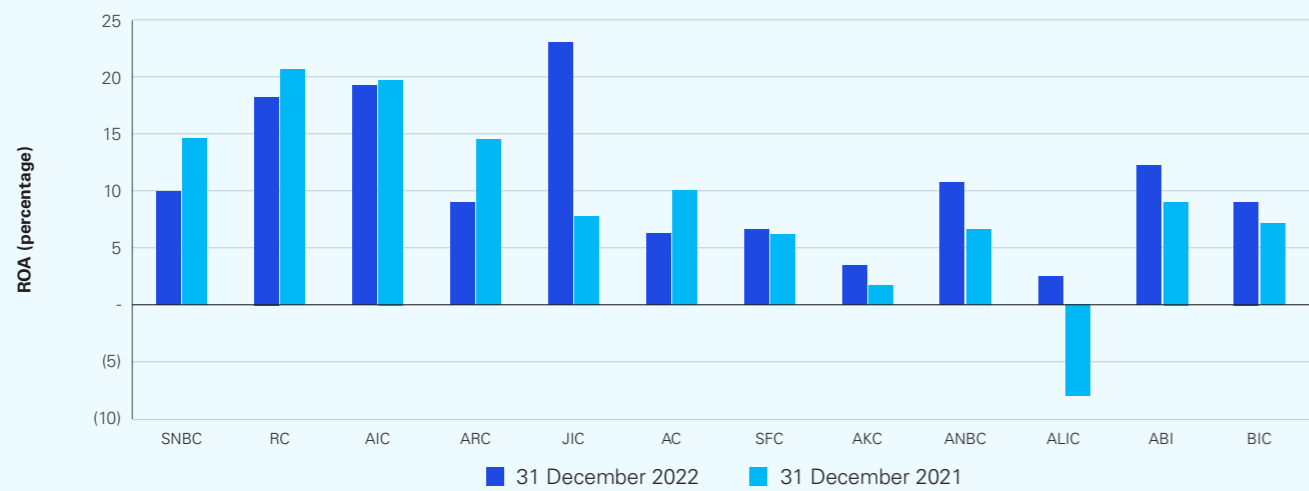
### Net income



### Return on equity

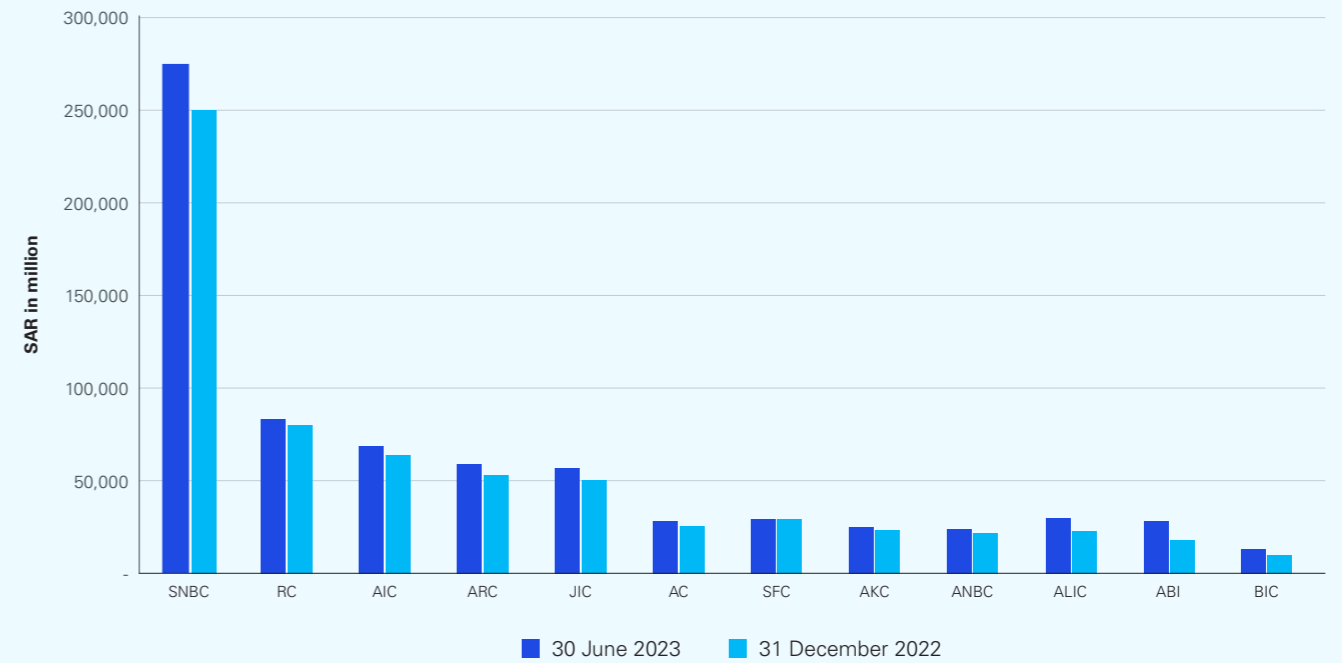


### Return on assets



**Note:** All amounts on this page are presented in SAR and are rounded off to a million unless otherwise stated.

### Assets under management\*



### Legend

SNB Capital Company	SNBC	Jadwa Investment Company	JIC	ANB Capital Company	ANBC
Riyad Capital Company	RC	Alistithmar Capital Company	AC	Alawwal Investment Co	ALIC
Alinma Investment Company	AIC	Saudi Fransi Capital Company	SFC	AlBilad Investment Co	ABI
Al Rajhi Capital Company	ARC	AlKhair Capital Company	AJC	Blominvest Company	BIC

\* Capital Markets Authority, website.

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# Emerging themes

The Saudi Stock Market (Tadawul) is the world's tenth largest stock exchange in terms of market capitalization and the largest in the Gulf Cooperation Council (GCC) region.<sup>2</sup>

CMA has been taking various initiatives to increase the depth of the capital market in line with Vision 2030's FSDP. This has included listing more companies on both the main market and parallel market (Nomu), establishing initiatives to develop the sukuk and debt

instruments, as well as the derivatives market, and broadening the liquidity and investor base. In this section, we highlight the most relevant updates across the asset management landscape that are impacting the industry.



## Open-ended funds and exchange

A significant portion of assets under management (AUMs) with fund managers in Saudi Arabia are routed through open-ended fund vehicles, which allows investors flexibility in redeeming and subscribing units. The product and solution offering suite by the fund managers in Saudi Arabia has broadly stayed consistent over the years.

Saudi Arabia has the largest number of ultra-high-net-worth individuals (UHNWI) in the region, a base that continues to grow and become more sophisticated, in turn requesting asset managers to offer more bespoke investment solutions and products.

The open ended funds market is growing rapidly as we have observed the funds number have increased from 254 as of 30 June 2022 to 276 as of 30 June 2023.

## ETFs

Currently, there are eight ETFs listed in Saudi Arabia, with a rapidly growing number of subscribers – more than 50 percent between 2022 and 2023. This trend, shifting from the historical open-ended funds towards more exchange-centered funds is expected to grow, further contributing to the depth of the capital markets in Saudi Arabia.

China and Saudi Arabia's stock exchanges are in talks to allow ETFs to list on each other's bourses as the countries look to deepen financial ties amid warming diplomatic relations. Beijing and Riyadh are currently in the early stages of talks, which could represent a major first step towards expanding cooperation beyond the energy, security, and sensitive technology sectors.<sup>3</sup>

## Real estate

Real estate continues to be the primary form of alternative investment in Saudi Arabia, providing opportunities for retail investors to participate in the Kingdom's rapidly expanding property market. The objective has usually been to provide a stable stream of income and capital appreciation over the medium to long-term, while properties have included various diversified income-generating properties and properties under construction. Real estate investment trusts (REITs), structured and traded, have gained popularity in recent years.

The biggest number of public and private investment funds subscribers were in the operating funds in the real estate sector. The real estate funds market is growing rapidly as we have observed the real estate funds increasing from 204 as of June 2022 to 337 as of 30 June 2023.<sup>4</sup>



**With a growing non-oil economy and a strategic vision for the future, Saudi Arabia is paving the way for a vibrant startup ecosystem.**

## Fintech

CMA is working to follow the best practices in regulating and facilitating fintech, coming from its legislative role, which contributes to the national economy and in achieving the FSDP goals. Its Saudi FinTech Initiative supports stimulating the fintech environment by developing the necessary infrastructure and supporting entrepreneurs and startups.

There are currently 38 companies licensed as financial technology companies in Saudi Arabia, which has facilitated the availability of new types of financing that were not previously available, such as crowdfunding, which has boosted the financial system.<sup>5</sup>

The number of authorized fintech in the equity crowdfunding platforms amounted to five companies in Q4 of 2022, and the aggregated funds through equity crowdfunding platforms reached SAR25.50 million.<sup>6</sup>

## Venture capital

Saudi Arabia achieved a growth rate of 72 percent in 2022 for venture capital (VC) funding, the highest compared to countries in the MENA region and registering an all-time high of US\$987 million. With that the Kingdom maintains its position as the second largest country in the region in terms of the volume of venture funding during the year 2022, and owning 31 percent of the total amounts invested in the region compared to 21 percent in 2021.<sup>7</sup>

We are continuing to observe in Saudi Arabia that fund managers are increasing their pursuit of VC investments, particularly around fintech and other disruptive technology companies that are domiciled in Saudi Arabia and the wider Middle East.

VC funds provide the necessary (and early) funding to these companies, and thereby, we are observing an uptick in simple agreement for future equity (SAFE) type instruments, i.e., convertible financial instruments, being used by asset managers to invest in these start-ups. Such financial instruments provide the investees early financing without the administrative

burden of going through a formal fundraising round. On the other hand, investors get early exposure to start-ups and, in turn, preferential conversion terms when the investee companies raise equity financing. We expect these financial instruments to gain popularity in Saudi Arabia as the start-ups/fintech market scales and more VC investors enter this space.

During 2022, Saudi Arabia recorded three large deals, a US\$170 million series C by Foodics, a US\$100 million series B by FinTech Tamara, and a US\$100 million series C by TruKker, and captured 37 percent of the total funding. In terms of industry breakdown, the VC ecosystem in the Kingdom mirrored its peer MENA markets and saw most of the capital being deployed in fintech, which captured 24 percent of the total funding.

The government has been introducing a range of initiatives to foster entrepreneurship and innovation. Funding programs, regulatory reforms, and infrastructure development have created an enabling environment for startups to thrive. The Kingdom recorded major deals worth US\$289 million in the first six months of 2023, driven by two transactions of US\$156 million and US\$133 million by e-commerce/retail startups Floward and Nana, respectively. Further, Saudi-based regional fintech Hala has acquired UAE's payment startup Paymennt.com as it aims to expand its foothold in the SME sector.<sup>9</sup>

With a growing non-oil economy and a strategic vision for the future, Saudi Arabia is paving the way for a vibrant startup ecosystem. It crossed the US\$1 billion mark for the first time in 2022 while it has slowed down a bit in 2023, partly due to the high interest environment. The VC ecosystem of the Kingdom has grown at a compound annual growth rate (CAGR) of 74 percent between 2018 and 2022.<sup>9</sup>

Recently, the Financial Times reported on how Silicon Valley investors are increasingly visiting the Middle East, particularly Saudi Arabia, to build relationships and seek funds at a time of market cooldown. PIF's venture arm, Sanabil, recently disclosed its partnerships with nearly 40 US VC firms, including 500 Global. In June 2023, Silicon Valley-based investor Plug and Play Tech Center aimed, in discussion with Jada, to raise US\$100 million to support Saudi startups.<sup>10</sup>

#### Credit-related funds

Credit funds or direct financing investment funds are categories of alternative investment funds that either extend a variety of loans (original lending business) or acquire them (derivative lending business). The operational challenges for the financial investment



### Attracting foreign investors to the market and increasing their ownership as a percentage of the total market value of free float shares will help to reach 16.5 percent by the end of 2023.

management company in the management of credit funds, such as the classification and early detection of risks by minimum requirements for risk management, also require a corresponding organizational structure and workflows.

The strategic objective of CMA is to develop an advanced capital market and empower financial institutions to support the private sector while improving financial planning. Therefore, CMA has implemented regulations for direct financing investment funds in 2022. These regulations aim to govern the issuance of units in investment funds established specifically for conducting direct financing activities and managing the operations of such funds.

The launch of these funds represents a significant achievement of the FSDP to enhance and diversify alternative financing sources. Particularly for key economic sectors like startups, entrepreneurs, and nongovernmental organizations, by promoting the growth of investment funds focused on financing.

This will support the private sector and introduce an initiative to foster the expansion and proliferation of investment funds involved in financing activities. Moreover, the program ensures alignment between regulations and the interests of relevant stakeholders, as it aims to create an additional financing avenue for infrastructure development within the economy.

During the year 2023, the number of funds has increased from 4 to 9 funds which means it almost doubled from the prior year.

#### Savings sukuk

In terms of providing various financial products that meet the needs of the sector, citizens and residents, the Ministry of Finance and the National Debt Management Center signed a memorandum of understanding with SNB Capital to develop and launch savings sukuk for individuals and motivate them for a better saving plan for the future.



#### ESG and sustainability

ESG and sustainability continue to gain further prominence and stakeholders' attention in Saudi Arabia. Recently, CMA issued ESG disclosure guidelines for listed companies, and we are observing increased sustainable financing activity through the advent of green sukuk issuances, enhanced sustainable reporting being done by blue chip companies, and increased green initiatives being launched by the government to support net-zero ambitions.

The PIF is leading the charge around ESG in line with its vision, and there is an expectation that this would drive the asset management sector to begin embedding ESG in their investment strategies, particularly when it is expected that CMA will play a vital role in the advancement of ESG in Saudi Arabia. ESG trends in the Kingdom are expected to converge with those observed globally, where some of the largest asset managers are convinced that sustainable investing will become the new norm. This would require asset managers to develop robust strategies that integrate ESG considerations into their investment and management practices. Currently, there is discretionary submission of these reporting figures, which may change with the introduction of new framework and standards.

#### Emergence of ESG-oriented investment funds

We are observing that asset managers in Saudi Arabia are launching ESG-oriented funds aimed at appealing to investors who want to play a vital part in supporting those entities that are sustainability-oriented. The asset managers typically apply ESG scoring criteria, whereby scoring potential investee entities based on ESG factors when screening investments. The ESG scoring criteria adopted can be proprietary, or in the case of passive investment funds, simply track a global index based on ESG-scored investments.

#### Uptick in green bond issuances

Financial markets globally are increasingly prioritizing companies and business practices that create value in a way that helps improve the world in the process. Tadawul is a partner exchange supporting the UN Sustainable Stock Exchanges Initiative to promote ESG awareness initiatives and encourage sustainable investment in collaboration with market participants such as issuers and investors. To date, Tadawul has engaged with listed companies, standards-setters, index providers, rating providers, investors, and other stock exchanges through a myriad of mediums to help advance ESG disclosure in the capital market.

This has led to a growing trend in the issuance of green bonds (sukuk) in Saudi Arabia. As a result, entities are establishing defined sustainable finance frameworks aligned with global standards, which encompass green debt issuances. Such sustainable finance frameworks specify that the proceeds from these green issuances can only be used in green-oriented investments/projects, etc. These green sukuk present institutional investors, such as asset managers, an important avenue to channel their investments towards a larger, sustainability-oriented cause. Given Saudi Arabia's emission targets by 2060, asset managers in Saudi Arabia have a vital role to play in providing the necessary funding to drive the country's sustainable future.

As part of that, the Saudi Green Initiative works on increasing Saudi Arabia's reliance on green and renewable energy, offsetting emissions, and protecting the environment, in line with Vision 2030. It



**Asset managers in Saudi Arabia are launching ESG-oriented investment funds aimed at appealing to investors who want to play a vital part in supporting entities that are sustainability-oriented.**

aims to improve the quality of life and protect future generations. On 23 October 2021, the first wave of over 60 programs and projects that contribute to the overarching targets were announced, representing more than SAR700 billion of investment supporting the growth of the green economy.



In February 2023, the PIF completed its second international green bond issuance amounting to US\$5.5 billion, nearly double the amount of its first one of US\$3 billion in October 2022 – both with a maturity period of a hundred years.

*Sovereign wealth fund leading the way*

The PIF is leading the way around sustainability in line with its vision to make impactful investments through the following recent activities to name a few:

- Ongoing building of a completely sustainable city, NEOM.
- Investments in the development of alternative energy through its strategic investments in ACWA Power.
- Establishing a voluntary carbon market to facilitate the sale and purchase of carbon credits.
- Investments in electric vehicle making through Lucid and CEER.

According to a recent report issued by the United Nations Principles for Responsible Investment (UNPRI), there is a significant gap in the amount of funding needed to meet the UN sustainable development goals in emerging markets, estimated to be as much as US\$3.7 trillion annually. Asset managers, therefore, have a pivotal role, particularly in bridging the funding gap.

**ICFR**

In response to several audit and accounting incidents and subsequent increased regulatory focus in many geographies around the world, organizations are considering the benefits of a proactive versus a reactive system for internal controls – and, as part of that, improve their internal control over the financial reporting (ICFR) program. Various countries and jurisdictions have enacted new and more stringent legislation to protect stakeholders from accounting fraud, concealing or distorting financial status, and lacking transparency and regaining stakeholders' confidence. Such ICFR frameworks, aiming at enhancing corporate governance, can lead to reform for more transparent reporting protocols, risk mitigation, and sound internal controls.

In Saudi Arabia, most companies have reached the maturity level where they can have an edge by reaping the benefits of ICFR. These benefits can include a collaborative and effective internal control culture with error correction in real-time opportunities to improve internal practices.

The importance of ICFR for registered entities – including asset management firms – in the Kingdom is growing. In recent years, we have witnessed a series of

high-profile business collapses in private equity, financial services, healthcare and construction sectors across the region. This alerted other companies in the region to delve deeper into the quality of their financial reporting.

There are, however, several challenges associated with the implementation of new ICFR frameworks, which include costs. As with any paradigm shift, the upfront investment can be higher than was accounted for. Further, as there are usually short time windows for implementation, it can be hard to go beyond basic compliance. It is also critical to maintain a balance between flexibility for governance to be adaptable to suit all those adopting it and enough direction to make it effective. Lastly, this will put more pressure on the regulator to monitor and enforce compliance.

Therefore, it is important to highlight the benefits that can be obtained from ICFR. For example, it will likely become part of the continuous improvement cycle in financial reporting. Further, it will reduce the need for restatements and improve the company culture around its risk and control function. Lastly, implementation in other geographies investors has indicated that it can have a positive impact on investor confidence and auditor independence.

**Going forward**

New types of investments are likely to gain prominence in Saudi Arabia as the government, in line with their Vision 2030, is undoubtedly creating a conducive environment in Saudi Arabia not only for attracting VC investments but also to support start-ups across a range of fields to positively disrupt the market and flourish. These start-ups will require funding and thus will present good opportunities for investors who have a higher risk appetite to invest in this segment.

Attracting foreign investors to the market and increasing their ownership as a percentage of the total market value of free float shares will help to reach 16.5 percent by the end of 2023.

Further, deepening the market for sukuk and debt instruments and raising the volume of the debt instruments market as a percentage of the GDP will also help to reach 20.1 percent by the end of 2023.<sup>11</sup>

Lastly, through promoting institutional investment in the capital market, deepening the investment funds sector, increasing its attractiveness to investors, and raising its effectiveness as an institutional investment channel, it is likely to reach a rate of 27.4 percent AUM as percentage of GDP by the end of 2023.

# Evolving tax and Zakat landscape

Over the past twelve months, several tax and Zakat updates issued by the Ministry of Finance and the Zakat, Tax and Customs Authority (ZATCA) of Saudi Arabia have impacted the asset management industry – the most critical ones are summarized below.

## Introduction of Zakat rules for investment funds

In December 2022, the Ministry of Finance approved Zakat rules for investment funds to be effective from 1 January 2023. While the Zakat collection on funds will be applied to the fund's unitholder, under these rules, investment funds are required to register with ZATCA, even though funds are not subject to Zakat. Funds approved by CMA before 1 January 2023 must register with ZATCA before the end of their fiscal year, and funds approved on or after 1 January 2023 must register with ZATCA before the end of their first fiscal year from the date of approval of incorporation. Funds will also need to submit an information declaration to ZATCA within 120 days from the end of their fiscal year, including audited financial statements, records of related party transactions and any other data requested by ZATCA during the filing period. Furthermore, funds must notify ZATCA within 60 days from liquidation, and Transfer Pricing Bylaws and amendments will apply to the transactions between related parties and the fund.

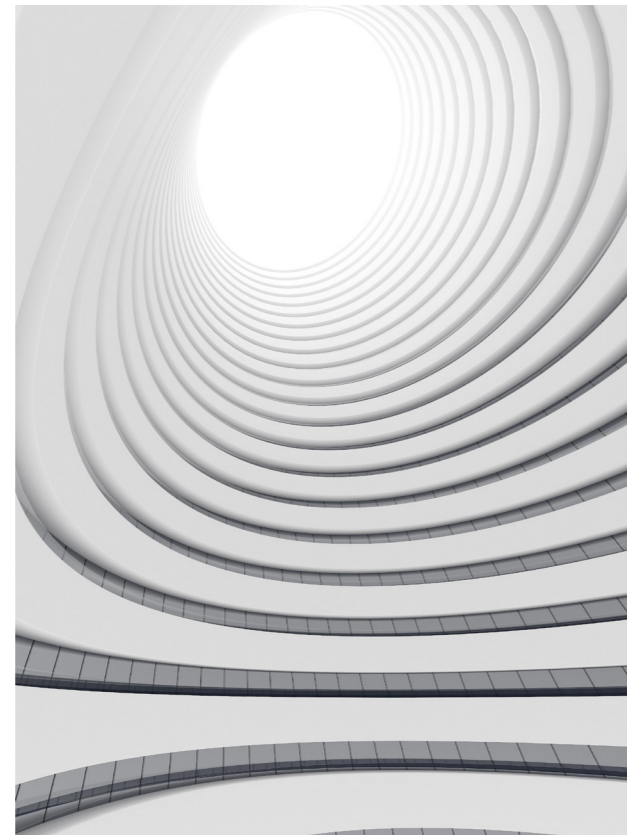
## Amendments to the rules for calculating Zakat on financing activities

On 22 August 2023, the Ministry of Finance approved additions and amendments to the rules for calculating Zakat on financing activities. The definition of "financing activities" is amended to include direct and indirect financing funds licensed by CMA, besides banks and financing companies licensed by SAMA.

## Key considerations applicable to investment fund unitholders

The unitholder in the investment fund may deduct the value of investment in the fund from the Zakat base provided that the investment is for non-trading purposes and the calculation of Zakat due on funds is

certified by chartered accountants or supported by audited financial statements. The rules do not apply to holders of units in finance funds or to holders that own the entire fund and submit a consolidated Zakat return, including the fund. The rules have also provided a formula for calculating the Zakat due from a unit holder: the product of the Zakat base of the fund, the unitholder ownership percentage in the fund, and the Zakat rate according to Zakat regulations. The minimum Zakat base for the unitholder will be equal to the unitholder's share in the net adjusted profit of the fund, regardless of whether the profit is distributed or not.



## Applicability of transfer pricing regulations to Zakat payers

On 20 March 2023, ZATCA approved amendments to the Transfer Pricing Bylaws to extend their applicability from entities subject to corporate income tax (full tax-paying and mixed entities) to include Zakat paying entities for fiscal years 1 January 2024 onwards. Zakat payers will need to ensure that their related party transactions are executed at arm's length prices and will be required to evidence this through compliance with transfer pricing requirements (Transfer Pricing Disclosure Form and Transfer Pricing Affidavit, to be submitted along with the Zakat return). Zakat payers will also need to prepare transfer pricing documentation (master file and local file) subject to exemptions. Phase 1 (FY2024-FY2026) will exempt Zakat payers with related party transactions less than SAR100 million, and phase 2 (FY2027 onwards) will exempt Zakat payers with related party transactions less than SAR48 million. Financing funds are excluded from phase 1 but included in phase 2.

## Introduction of Advanced Pricing Agreements (APA) provisions for tax and Zakat payers

Under Article 23 of the revised Transfer Pricing Bylaws, the APA program was introduced in March 2023. An APA is an agreement between the tax authority and a taxpayer which determines in advance the arm's length price of a transaction or manner of determining the same between related parties. The benefits of such a program include improved certainty, reduced compliance costs and reduced risk of controversy. APAs can be unilateral (between taxpayer and tax authority), where it is akin to a tax ruling. They can also be bilateral (between taxpayer and tax authorities of both countries involved in related party transactions) or multilateral (between taxpayer and multiple tax authorities). APAs are generally valid for a specified period ranging from three years to five years. Additional details are anticipated from ZATCA in due course with regard to APAs.

## Update on Service Permanent Establishment

The Model Taxation Convention issued by the United Nations states that a Service Permanent Establishment (Service PE) is deemed to exist where a service provider furnishes services in a state for a duration longer than the threshold under the applicable double tax treaty. Under ZATCA's historic interpretation of the Service PE concept, a "Virtual Service PE" could be triggered based solely on the duration of the contract rather than the service provider's actual activities and even without the physical presence of employees in the country.

Non-resident companies struggled with this interpretation of the Service PE concept as it could potentially lead to double taxation. On 17 May 2023, ZATCA issued a circular on the Taxation of Permanent Establishments (PE) in the context of a Double Tax Agreement (DTA), which clarifies the conditions that need to be fulfilled to trigger a Service PE. An activity needs to pass three tests to be considered a Service PE; the company must provide relevant services through employees, these employees must be physically present in Saudi Arabia while providing these services, and the physical presence should be, in aggregate, more than 182 days in any twelve-month period. If a Service PE is created in Saudi Arabia, the non-resident service provider is deemed to be subject to tax according to the applicable DTA and under the terms of the Saudi Arabian tax regulations. In case the activity of the non-resident service provider does not pass all three tests, the profits generated from that activity will only be subject to tax in the home country of the service provider. However, in certain cases, the activity of the non-resident service provider could be subject to withholding tax in Saudi Arabia.

## Tax amnesty extended until 31 December 2023

ZATCA had issued a waiver of the Fines and Penalties Initiative, which was meant to expire on 31 May 2023 but has now been extended to 31 December 2023. The tax amnesty extension applies to penalties relating to corporate income tax, withholding tax, value-added tax (VAT), excise tax and real estate transaction tax. It will cover late registration fines, payment delay fines, delay in filing tax returns fines, VAT returns amendment fines, VAT field detection and e-invoicing regulations violations fines. The incentives are applicable for the amendments of any tax returns, either made by the taxpayer under the tax amnesty initiative or by ZATCA through assessments or reassessments. Tax amnesty initiative excludes tax evasion fines and fines associated with returns due after 1 June 2023. Taxpayers looking to benefit from this tax amnesty should register their business with ZATCA for the applicable taxes and submit outstanding returns along with payment of due tax liability.

## Amendments to implementing regulations on Zakat collection

On 28 April 2023, key amendments were introduced in the Zakat implemented regulation concerning the deductibility of some items for Zakat purposes. Under these amendments, the issuer may treat the sukuk and bonds issued as capital without considering their classification in its financial statements, and in this case, sukuks and bonds shall be deducted from the Zakat base of the investees under certain conditions.



# Regulatory updates



## Recent revisions to prudential rules

CMA revised its prudential rules for asset managers in April 2023, with key updates being around capital adequacy in terms of methodology and reporting. The regulator updated the methodology used to calculate the minimum limit of capital adequacy and provided requirements for investment management, arranging transactions and advisory activities to be based on expenses, in line with the nature of such activities. Such revisions are aimed at boosting the confidence of the capital market participants and creating an attractive investment environment to support the growth ambitions of the economy.



## Revised rules on foreign investment

The capital markets in Saudi Arabia continue to open up for foreign investors. In March 2023, CMA in Saudi Arabia issued rules for foreign investment in securities listed in the local main market, debt instruments and investment funds. The rules formally now define who are the eligible foreign investors, what the required qualifications, investment restrictions and other terms and conditions need to be complied with. The rules intend to facilitate foreign investment into Saudi Arabia, particularly to attract large global asset managers.



## New rules around establishment of direct financing funds

We are seeing a growing trend of establishing direct financing funds whose primary purpose is to carry out direct financing for legal persons or other investment funds. Such funds are established by asset managers, providing the unitholders with direct exposure to the risks and rewards of a lending business. CMA has issued specific instructions around direct financing investment funds during 2022, which set out specific conditions for establishing such funds, investment limitations and additional duties, particularly around credit sanctioning and monitoring, that an asset manager must comply with when managing such financing funds. While there are unique risks to consider when operating outside of the traditional banking sector, there are several potential benefits around direct financing, such as providing alternative sources of funding to customers, increased credit availability to boost economic growth, increased liquidity in the market, and the resilience of the financial markets is further enhanced to create more market depth. These direct financing funds will attract sophisticated investors who are cognizant of the credit risks associated with a lending business yet would want to gain exposure, particularly in a rising interest rate environment that currently prevails in Saudi Arabia.



## Establishing of a real estate exchange

In August 2023, the Ministry of Justice launched the Real Estate Market application, a digital platform developed in cooperation with the Ministry of Municipal and Rural Affairs and SAMA, to facilitate real estate transactions and provide e-services to property owners and buyers such as those relating to managing of portfolios and title deeds. This digitization drive is a significant initiative, one which will bring transparency to the market and play a vital role in further developing the depth and breadth of the real estate market in Saudi Arabia. Real estate investments are still a primary alternative investment class for asset managers, and thus, this initiative will further attract investor flows.



## Equity crowdfunding

CMA established the regulatory framework in 2022 for equity crowdfunding, aiming to determine the requisite authorization for capital market institutions and to enable companies that have a Fintech Sandbox license to obtain the appropriate authorization to practice it as a capital market institution. CMA, through the amended regulations, account for crowdfunding businesses and the custody of clients' funds. There are currently five companies that have received licenses to experiment from CMA about testing their equity crowdfunding model, with the hopes of obtaining permanent crowdfunding licensees at the end of the trial period. The aggregated funds through equity crowdfunding platforms reached SAR142.5 million by 30 June 2023.<sup>12</sup>



## Securities depository

CMA approved the securities exchanges and depository center regulations in July 2022, effective from 1 January 2023. These regulations aim to develop the regulatory framework for the authorization and supervision of securities exchanges and depository centers for the efficient performance of their duties and obligations. On the one side, these regulations set out the authorization and capital requirements and on the other, it is the regulation relating to the requirements for the conduct of business and systems and control.



## Shariah governance

CMA also set forth a new document related to instructions for Shariah governance in capital market institutions, approved in July 2022 by the board. This set of instructions aims to provide rules and standards for Shariah governance in capital market institutions that provide, wholly or partially, products or services that are compliant with the rules and principles of Shariah. It critically relates to the responsibilities of the board of directors (or equivalent) and the executive management in capital market institutions, the work of a Shariah committee and their independence and reporting structure and procedures for the development process of products and services.

<sup>1</sup> 'Saudi IPOs are best in world' say experts as Kingdom lines up 23 offerings this year - Arabian Business.

<sup>2</sup> <https://cdn.saudiexchange.sa/>.

<sup>3</sup> Exclusive: China, Saudi in talks for ETF cross-listings to bolster financial ties | Reuters.

<sup>4</sup> Capital Markets Authority, Quarterly Statistical Bulletin, Q4 2022: Capital Market Authority Issues QSB for Q4 2022 ([cma.org.sa](https://cma.org.sa)).

<sup>5</sup> Capital Markets Authority, annual report 2022: [cma.org.sa/en/Market/Reports/Documents/cma\\_2022\\_report-en.pdf](https://cma.org.sa/en/Market/Reports/Documents/cma_2022_report-en.pdf).

<sup>6</sup> Capital Markets Authority, Quarterly Statistical Bulletin, Q4 2022: Capital Market Authority Issues QSB for Q4 2022 ([cma.org.sa](https://cma.org.sa)).

<sup>7</sup> FY2022 KSA Venture Investment Report | MAGNiTT.

<sup>8</sup> H1 2023 Saudi Arabia Venture Capital Report | MAGNiTT.

<sup>9</sup> Is Saudi Arabia Your Next Best Bet? | MAGNiTT.

<sup>10</sup> Silicon Valley VCs tour Middle East in hunt for funding | Financial Times ([ft.com](https://ft.com)).

<sup>11</sup> Capital Markets Authority, annual report 2022: [cma.org.sa/en/Market/Reports/Documents/cma\\_2022\\_report-en.pdf](https://cma.org.sa/en/Market/Reports/Documents/cma_2022_report-en.pdf).

<sup>12</sup> CMA Statistical Bulletin Q2 2023.

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