هيئة الزكاة والضريبة والجمارك
Zakat, Tax and Customs Authority

Guideline

Manual of Transition to the International Financial Reporting Standards

and its impact on the Zakat account for the taxpayers who are obligated to keep regular accounts in the Kingdom of Saudi Arabia

"International Financial Reporting Standard 16 Lease Contracts".

Version One November 1 2021

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 of Levying Zakat promulgated by the Ministerial Resolution No. (2216) dated 07 Rajab 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.

This Manual is indicative, and includes a summary of the most important considerations with respect to application of International Financial Reporting Standards (IFRSs) approved in the Kingdom of Saudi Arabia. It is not a statutory document. The provisions thereof are guiding, and it does not eliminate the need to peruse to the International Financial Reporting Standards approved in the Kingdom of Saudi Arabia and other standards and publications approved by the Saudi Organization for Chartered and Professional Accountants. All diagrams and drawings contained herein are for illustrative purposes and may not include all requirements and exceptions to the standards. The Authority expressly disclaims itself for any duties or obligations towards any person or entity that may result from its use of this attached Manual. Please note that this Guideline does not include any conclusion on appropriate accounting processing based on specific facts and does not recommend accounting policies or treatments that the user of this Guideline should choose or apply.

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Introduction

Purpose of Manual:

This Manual aims to provide a summary of the most important effects that resulted from the transition to International Financial Reporting Standards (IFRSs) at the expense of Zakat. It should be noted here that the mentioned standards were adopted by the Saudi Organization for Chartered and Professional Accountants to become applicable by companies listed in the Saudi Financial Market effective from the Fiscal Year January 1st, 2017.

Further, this Manual is intended to contribute to raising awareness on changes in the accounting treatments contained in international standards, which may have changed the Zakat handling for some items. ZATCA aims that the Manual will also contribute to narrowing the gap between the understanding of taxpayers and the Authority's expectations concerning the mechanisms for estimating and calculating Zakat in light of the transition to these standards.

This Manual addresses the following international Standard:
International Financial Reporting Standard 16 "Lease Contracts".
The Manual has been prepared based on the International Financial Reporting Standards approved in the Kingdom of Saudi Arabia issued in 2020 AD.

Overview of the transition to the approved International Financial Reporting Standards in the Kingdom of Saudi Arabia:

International Financial Reporting Standards have been endorsed by the Saudi Organization for Chartered Auditors and Accountants to become applicable by companies listed in the Saudi financial market effective from the fiscal year 1 January 2017.

In the interest of the Zakat, Tax and Customs Authority to keep pace with this fundamental transition, the Authority has listed and formulated the most prominent effects of the transition on the account of Zakat for private sector companies and institutions in the Kingdom of Saudi Arabia.

Overview IFRS No. (16)

IFRS No. (16)

1. Standard objective:

This Standard determines the principles related to the recognition, measurement, presentation, and disclosure of lease contracts. The objective is to ensure that lessees and lessors provide appropriate information that truly reflects that information. This information provides a basis for users of financial statements to evaluate the impact of lease contracts on the entity's financial position, financial performance, and cash flows.

An entity shall consider the terms and conditions of contracts, all relevant facts, and circumstances upon applying this Standard. An entity shall apply this Standard consistently to contracts with similar characteristics and under similar circumstances.

2. Scope Summary:

The Most Significant Exceptions to IFRS 16	Applicable Standard	Standard Name
Leases for the exploration or use of minerals, oil, natural gas and similar non-renewable resources.	IFRS (6)	IFRS 6 "Exploration and Valuation of Mineral Resources and Assessment".
Leases are the biological assets held by the lessee.	International Accounting Standard (41)	IAS 41 "Agriculture".
Public service concession arrangements.	IFRS Interpretations Committee (12)	IFRS Interpretations Committee (12)
Intellectual property licenses granted by the lessor.	IFRS (15)	International Financial Reporting Standard (15) "Revenue from Contracts with Customers"
Rights held by the lessee under license agreements for such terms as: Motion pictures, video recordings, plays, manuscripts, patents, and copyrights.	International Accounting Standard (38)	IAS (38): "Intangible Assets"

Effective Date

January 1, 2019

The international standard that replaced

- IAS 17: Lease Contracts
- IFRIC 4
- Interpretation of SIC 15 Operating Leases - Incentives
- Interpretation of SIC 27 Evaluation of the Substance of Transactions involving Legal Form of a Lease

The Saudi standard that replaced it

Accounting Standard for Leases 14

Overview IFRS No. (16)

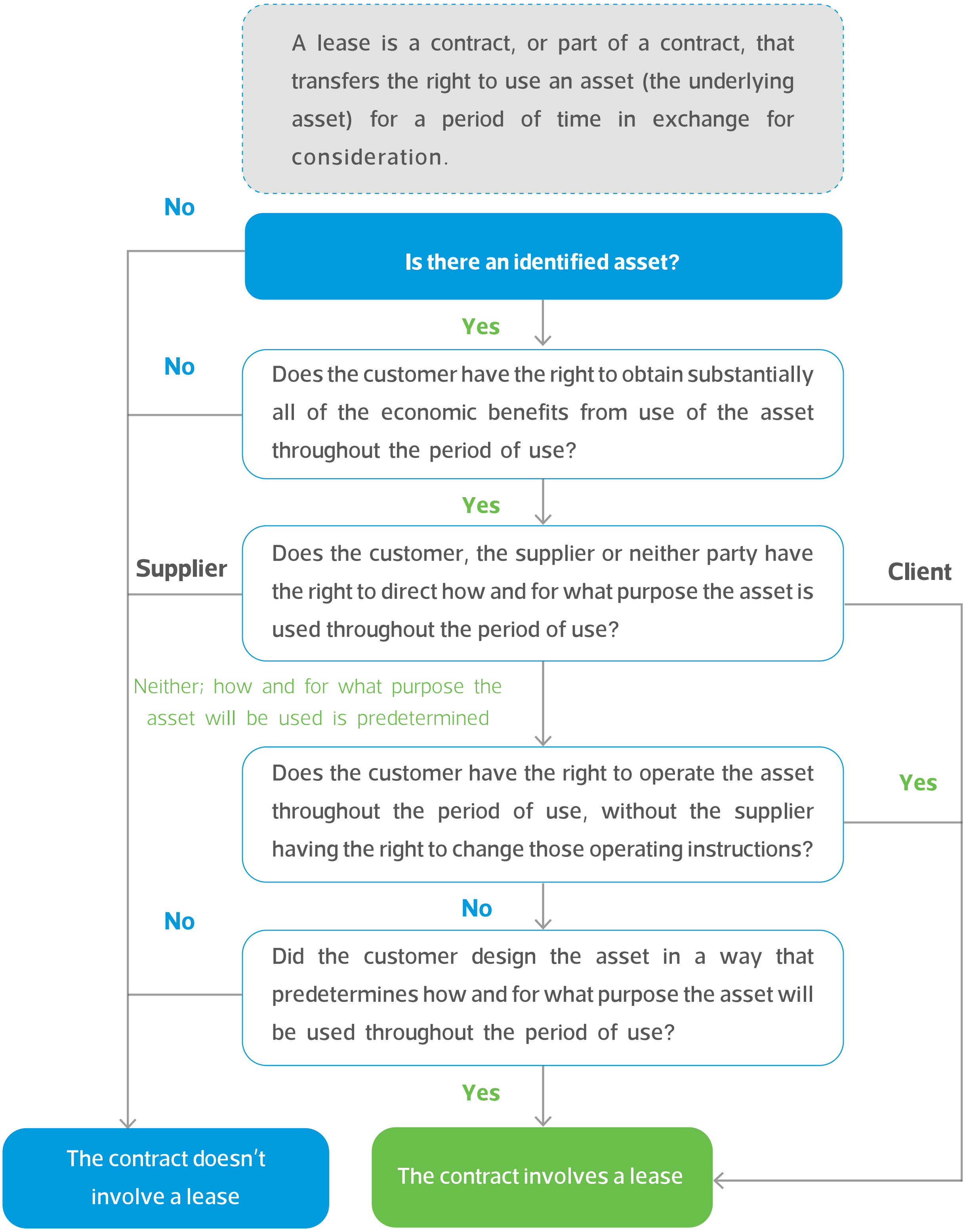
- Accounting Standard 16 addresses lessees as it requires all leases to be capitalized (with some exceptions).
- Standard 16 didn't change the accounting for lessors.
- Lessor's Accounting is still based on the classification of lease as either capital or operational.

Operating leases weren't previously capitalized but grants lease rights and obligations which were not recognized.

Therefore, the operating leases were an off-balance sheet source of financing.

The previous rules of IAS 17 defined the operating and capital leases

Assess whether the Contract is a Lease Contract or Involving a Lease Contract



IFRS 16, Chapter Two, B31: Chart that could help the entities to assess whether the Contract is a Lease Contract or Involving a Lease Contract

The Most prominent requirements according to IFRS (16)

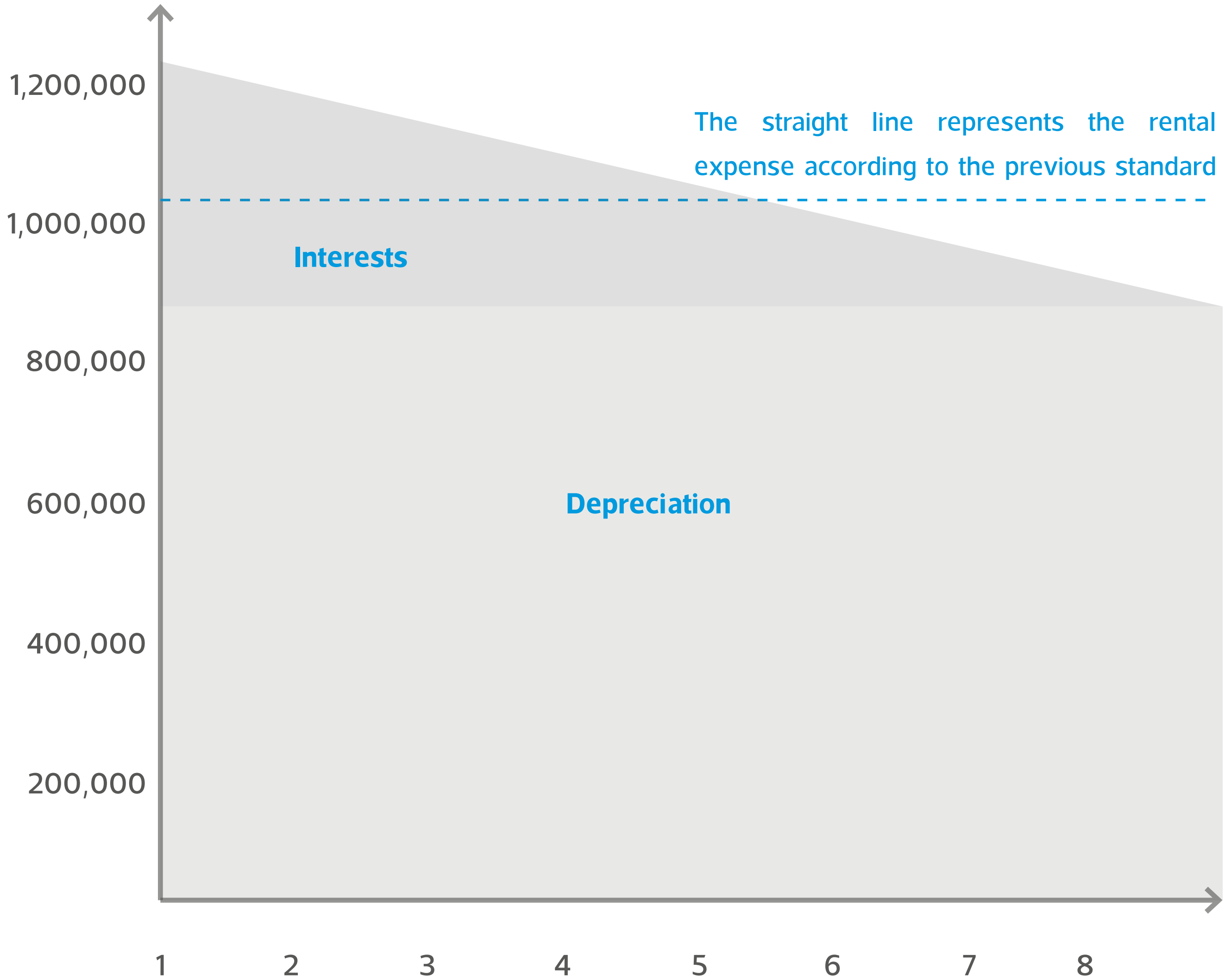
3. Lessee

Subject	Requirement as per IFRS (16)
Recognizing in the financial position	Most leases are recognized in the financial position.
Assets and Liabilities	• Right of Use • Lease obligations
First Measurement	• Right of use = Lease Obligation • Lease Obligation = current value of future lease payments.
Subsequent Measurement	Right of use = Amortized over the life of the contract, or the useful life of the right of use of the asset, whichever is shorter. Obligation: It is increased by interest, and amortized by repayments.
Statement Profits or Losses	• Depreciation expense • Financing expenses
Exceptions of recognizing	Short term contracts (less than 12 months). Low value contracts.

4. Lessor

Subject	IFRS (16) Finance Lease	Operating Lease
Recognizing in the financial position	If the financial lease controls apply.	In no case is operating lease recognized in the financial position
Assets and Liabilities	Net investment.	Not Applicable
First Measurement	At the commencement date of the lease, the lease payments included in the measurement of the net investment in the lease consist of the following payments: A. Fixed payments less any lease incentives payable. B. Variable lease payments that depend on an index or rate. C. Any remaining value guarantees provided to the lessor. D. The purchase-option price if the lessee is reasonably certain to exercise that option E. Payments of penalties for terminating the lease	Not Applicable
Subsequent Measurement	Net investment is increased through interest income, and amortized through payment collections.	Not Applicable
Statement Profits or Losses	Interest income.	Lease Income.

5. The following chart represents the movement of expenses (interest and depreciation) during the lease term - for the lessee



Impact of Transition to IFRS (16) on the Zakat Base

6. Introduction:

In view of the aspects and accounting handling that were addressed in IFRS No. (16) and in view of the differences in the accounting handling of operating lease contracts, which are required to be addressed in accordance with the controls mentioned in the standard after the transition; the elements of these accounting differences shall be viewed together with the following articles provided in the Executive Regulations for Levying Zakat.

6.1. Depreciation Expense and Interest Expense:

Article 8 in Chapter Three (Amendment of Activity Result) of the Executive Regulations for Levying Zakat, as follows:

The following expenses may be deducted to determine the net result of the activity:
Ordinary and necessary expenses required for the activity. The following controls shall be provided:

A. The expense shall be actual and supported by documents and evidence acceptable to ZATCA and verifiable, even if it is related to previous years.

B. To be related to the activity of the taxpayer, and not related to personal expenses or other activities that do not belong to the taxpayer.

C. It may not be of a capitalistic nature. In the event that an expense of a capital nature is included in the expenses; it shall be adjusted as a result of the activity and is added to the fixed assets and consumed within the depreciation of the asset.

The aforementioned article, in paragraph (Four), stipulates the following:

"The annual depreciation premium for the fixed assets owned by the taxpayer and intended for use in the activity according to what is recorded in the commercial books, unless the Authority proves that the taxpayer exaggerated the premium."

6.2. Right to Use the Asset:

Article Five, Paragraph (D) of the first and the sixth items of the aforementioned article:
"The following items shall be deducted from the Zakat Base (ZB) of the taxpayer who keeps commercial books:

Net fixed assets and the equivalent, including but not limited to the following: Net establishment and pre-operating expenses and similar capital expenses".

6.3. Lease Contracts Obligations:

Paragraph (Three) of Article (Four) stipulated the following:

"The taxpayer's zakat base who maintain the commercial books consists of all his funds subject to zakat collection, including the following:

"Debts owed by the taxpayer classified as long-term, and equivalent ، from other components of the base, such as: Government financing, commercial financing, creditors, promissory notes, overdraft account, and loans to owners or partners (including their current accounts), provided that the following shall be 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 may 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 may not exceed the total amount deducted from ZB in accordance with Article 5 of the Regulations."

6.4. Adding Lease Contract Balance against the Right to Use:

Paragraph (Ten) of Article (Four) stipulated the following:
"Any item of liabilities and equity shall be financed from the deducted items from Zakat base."

ZB Financial Impact of the Transition

Referring to the recognition mechanism and accounting handling of operating lease contracts in accordance with IFRS No. (16), it shall be noted that the most prominent differences that result in a financial impact, and thus an impact on the Zakat base, are as follows:

6.4.1. Minimum zakat base (adjusted net profit for zakat purposes or as a result of activity):

After the transition, the depreciation of the right to use the asset and financing expenses will be recognized in the statement of profit or loss as a period expense, which will differ in value either by an increase (or) by a decrease for each year separately, compared to what it was before the transition.

In general, period expenses will be higher in the early years of the contract; due to the high interest expense, it gradually decreases over the remaining years of the contract.

These differences are attributable each year to the amortization of the right to use the asset recognized at the beginning of the lease, after deducting future cash flows (lease payments), and finance charges calculated based on the lease obligations at the beginning of each year. However, these differences each year are only related to timing difference, meaning that the amount of (depreciation and financing expenses) over the years of the contract shall be equal the sum of (actual lease expenses/payments) over the years of the contract.

In light of the above, an effect will appear on the minimum zakat base by decrease (as a result of the increase in interest expenses in the first years of the contract), or increase (as a result of the decreasing interest expense for the remaining years until the interest becomes (zero). Further, the remaining expense shall be represented only by amortization right to use the asset). The cumulative effect of these differences will be zero at the end of the lease.

6.4.2. Other Components of ZB (Additions and Deductions):

In the event that the right to use the asset and the lease obligation are included in the items of deductions and additions (respectively) within the Zakat base; the differences between the two items above will mainly appear; due to the different factors affecting the components of the said lease contracts. For example, the right to use the asset will be affected by the interest rate used to discount the cash flows inversely, i.e. it decreases with an increase in the interest rate, and vice versa. In contrast, lease liabilities will be affected by the payment arrangements (inversely) and interest expense (directly). Accordingly, this will result in an impact on the base when these items are included within the components of the Zakat base (by increase if the balance of liabilities exceeds the deducted principal, and by decrease if the deducted principal exceeds the balance of liabilities). Noting that the difference is mainly attributed to financing expenses, which is considered the basis and reference for handling the difference between the two items. Thus, it may not produce an effect on the Zakat base as a whole (unless) the effect on the opening balance of retained earnings is taken into account as an element of Zakat base.

Similar, when the taxpayer pays zakat according to the zakat base, which includes (adding obligation to the limits of deductions according to the controls for additions contained in Article 4 of the Regulations). This will result in an effect on the base (decrease) as a result of adding obligations to the limits of deductions only. This effect is due to the cumulative effect on retained earnings, which was optimally result by the difference in the lease liability and the deductions. It will be mentioned in the theoretical applications section.

6.4.3. (Other) Special Cases:

In cases where zakat is calculated on the minimum base (net profit adjusted for zakat purposes) over the life of the lease contract, this will result in a decrease in the zakat account in the first years of the contract due to the high interest expense, but it decreases in the following years. At the end of the contract, the impact on Zakat base will be equal to (zero); since the financial impact on profits or losses are only timing differences.

In other cases, the taxpayer may pay the zakat in the first years of the contract at the minimum level, and shift to paying the zakat base, for example in the later years. According to what was mentioned earlier, the first years will witness a higher interest expense and depreciation expense than the actual rental expense, as it was before the transition, which will affect the zakat account. In the last year, no difference should appear in the zakat for the same year due to the accumulated effect on retained earnings (opening balance).

7. Theoretical Examples on the Effect of Transition on ZB

Entity "H" (the Lessee) has signed a three-year lease agreement to lease equipment. Entity "H" agreed to pay the following annual payments at the end of each year:

Subject	IFRS (16) Finance Lease
First Year	12,000
Second Year	12,000
Third Year	12,000

For simplicity, there are no other items for lease payments (e.g.: purchase options, lease incentives from the lessor or upfront direct costs)

Entity "H" uses its borrowing rate of 4,235%, since the implicit interest rate in the lease is not easily determined

Entity "H" amortizes the right-of-use the asset on a straight-line basis over the lease term.

Step One: Initial recognition of a right-of-use asset and lease obligation by calculating the present value of future lease cash flows:

Details		Payment at the end of the first year	Payment at the end of the sec-ond year	Payment at the end of the third year
Agreed upon lease payments rent expense	A	12,000	12,000	12,000
Division	B	(1+4,235%)	2 ^ (1+4,235%)	3^(1+4,235%)
Current Value	D = A + B	11,512	11,045	10,596
The amount of the current value of lease payments	33,153			

First step (continued): Initial recognition of a right-of-use asset and a lease liability by calculat-ing the present value of the future cash flows of the lease:

Details	Right of Use	Lease Contracts Obligations:
Q1: Initial recognition of the right of use	33,153	(33,153)

It is noted that the above accounting entry represents the initial recognition of the right-of-use of the asset, and lease obligations that will be accounted for over the lease period as follows:

Step Two: Amortization of the right-to-use of the asset, and calculation of interest expense for the first year:

Details	Depreciation expense (income statement)	Interest expense (income statement) (1)	Lease obligations (financial position)	Depreciation Accumulation (Account against asset/ financial position)	Cash
Q2: Recognition of depreciation and interest expense for the first year	11,051	1,404	(1,404)	(11,051)	
Q3: Paying the first payment	-	-	12,000	-	(12,000)

(1) Interest rate 4,235% * Book value of lease liabilities 33,153

The balances will be detailed in the statement of financial position for the first year as follows:

Details	Statement of Financial Position	Details	Statement of Financial Position
Right of Use	33,153	Lease Contracts Obligations:	(33,153)
Accumulated depreciation	(11,051)	Interest Expense	(1,404)
Net (non-current assets)	22,102	Payment	12,000
		Lease obligations as at the end of the year	(22,557)

Step Three: Amortization of the right-to-use of the asset, and calculation of interest expense for the second year:

Details	Depreciation expense (income statement)	Interest expense (income statement) (1)	Lease obligations (financial position)	Depreciation Accumulation (Account against asset/ financial position)	Cash
Q4: Recognition of depreciation and interest expense for the first year	11,051	955	(955)	(11,051)	
Q5: Paying the first payment	-	-	12,000	-	(12,000)

(1) Interest rate 4,235% * Book value of lease liabilities 22,557

The balances will be detailed in the statement of financial position for the second year as follows:

Details	Statement of Financial Position	Details	Statement of Financial Position
Right of Use	22,102	Lease Contracts Obligations:	(22,557)
Accumulated depreciation	(11,051)	Interest Expense	(955)
Net (non-current assets)	11,051	Payment	12,000
		Lease obligations as at the end of the year	(11,512)

Step Four: Amortization of the right-to-use of the asset, and calculation of interest expense for the third and last year:

Details	Depreciation expense (income statement)	Interest expense (income statement) (1)	Lease obligations (financial position)	Depreciation Accumulation (Account against asset/ financial position)	Cash
Q6: Recognition of depreciation and interest expense for the first year	11,051	488	(488)	(11,051)	
Q7: Paying the first payment	-	-	12,000	-	(12,000)

(1) Interest rate 4,235% * Book value of lease liabilities 11,512

The balances will be detailed in the statement of financial position for the third and last year as follows:

Details	Statement of Financial Position	Details	Statement of Financial Position
Right of Use of the Asset	11,051	Lease Contracts Obligations:	(11,512)
Accumulated depreciation	(11,051)	Interest Expense	(488)
Net (non-current assets)	0,000	Payment	12,000
		Lease obligations as at the end of the year	0,000

Summary of recognizing the accounting operations for lease contracts:

Item	Reference	Beginning of the contract	First Year	Second Year	Third Year
Rent Payments	A		12,000	12,000	12,000
The recognized rent expense is as follows:					
Interest Expense	b = 4,235% *9		1,404	955	488
Depreciation Expense	C = A ÷ 3 years		11,051	11,051	11,051
Total expenses for the period	D= B + C		12,455	12,006	11,539
Statement of Financial Position:					
Right of Use of the Asset	E	33,153	22,102	11,051	-
Lease Obligations	F = E (beginning of term) - A + B	(33,153)	(22,557)	(11,512)	-

It is noted from the Summary of recognizing the accounting operations for lease contracts, as follows:

1. The right-of-use asset is amortized over the contract period (3 years).
2. Interest expense will be calculated by multiplying the borrowing rate by the carrying amount of the lease liabilities, as at the end of the previous year.
3. It will be noted that the amount of interest expense and depreciation expense for the three years equals the value of the contract (SAR 36,000).
4. The interest expense account for lease liabilities is affected by the increase, while it is affected by the decrease when the lease payments are made.
5. It is noted that the interest expense decreases gradually over the years of the contract coinciding with the obligation of the lease contract, which also decreases when the lease payments are made over the years of the contract.

Possible options for zakat handling of the impact of IFRS No. (16):

In this paragraph and for purposes of clarification only, a set of proposed options were assumed when applying this Standard, and their impact on the Zakat base was clarified if they were applied:

1

Considering the asset depreciable

2

Canceling the impact of IFRS and lease claim based on the actual expense of the lease prior to the transition.

3

Not considering any of the above options: Canceling the effect of the standards while keeping the rent and interest expense unadjusted.

First Option: Consider the asset depreciable, and add the lease liability to the closing balance:

Details	Zakat Handling	First Year	Second Year	Third Year	Total
Total period expenses (depreciation and finance expense)	Deductible Expense	(12,455)	(12,006)	(11,539)	
Right of Use	Deductible from ZB	(22,102)	(11,051)	-	
Lease Obligations	Additions to ZB	22,557	11,512	-	
Net impact on ZB		(12,000)	(11,545)	(11,539)	(35,084)

Option (One) (continued): Consider the asset depreciable, and add the lease liability to the closing balance:

Comparison of impact prior and after transition (minimum base):

Details	First Year	Second Year	Third Year	Total
Total period expenses (depreciation and finance expense)	(12,455)	(12,006)	(11,539)	(36,000)
Rent expense before transition	(12,000)	(12,000)	(12,000)	(36,000)
Difference	(455)	(6)	461	0

It is noted from the above that the minimum zakat base is affected by the decrease in the first years of the contract, due to the high interest rate. It will gradually decrease until it approaches the annual depreciation premium (to become less than the actual interest expense, and it is affected by the increase in recent years). However, these differences are only timing differences on a year-by-year basis, yet, this effect in total (over the years of the contract) is equal to (zero), as the amount of the period expenses for all years will equal the rent expense as it was before the transition.

Comparison of the impact prior and after the transition (elements of zakat base "additions and deductions"):

Details	First Year	Second Year	Third Year	Total
Prior to transition (additions and deductions)	Not Applicable	Not Applicable	Not Applicable	Not Applicable
After transition				
Difference between additions and deductions (lease liabilities, right to use of the asset)	455	461	0	916
Effect on recycled profits or losses	(455)	(6)	461	0
effect on recycled earnings	0	(455)	(461)	(916)
Total	0	0	0	0

It is noted from the above that the differences between additions and deductions to Zakat base are only timing differences in case the impact on retained earnings is taken into account, which is mainly attributed to interest expense.

Second Option: Canceling the impact of IFRS and lease claim based on the actual expense of the lease prior to the transition:

Comparison of impact prior and after transition (minimum base):

Details	First Year	Second Year	Third Year	Total
Total period expenses (depreciation and finance expense)	(12,455)	(12,006)	(11,539)	36,000
Rent expense before transition	(12,000)	(12,000)	(12,000)	(36,000)
Difference	(455)	(6)	461	0

It is noted that canceling the impact of the standards on the net profit or the minimum limit of Zakat base mainly means claiming on the basis of the actual expense of rent on the basis of accrual accounting using the straight-line method. Thus, canceling the timing differences, both in terms of Zakat accounting.

Comparison of the impact prior and after the transition (elements of zakat base "additions and deductions"):

Details	First Year	Second Year	Third Year	Total
Prior to transition (additions and deductions)	Not Applicable	Not Applicable	Not Applicable	Not Applicable
After transition				
Difference between additions and deductions (lease liabilities, right to use of the asset)	0	0	0	0
Effect on recycled profits or losses	455	6	461	0
Effect on retained earnings	0	455	461	916
Total	455	499	922	916

It is noted from the above that canceling the impact of the standards will have an impact as described above compared to the first option, as the asset or the lease contract liability is not included in zakat base items that address with the differences between them, the above difference appears in the retained earnings.

Third Option: Not considering any of the above options: maintaining the expenses of the period without adjustment, and not taking into account any additions or deductions.

Comparison of impact prior and after transition (minimum base):

Details	First Year	Second Year	Third Year	Total
Total period expenses (depreciation and finance expense)	(12,455)	(12,006)	(11,539)	36,000
Rent expense before transition	(12,000)	(12,000)	(12,000)	(36,000)
Difference	(455)	(6)	461	0

As mentioned in the first option, it is noted from the above that the minimum zakat base is affected by the decrease in the first years of the contract, due to the high interest rate. It will gradually decrease until it approaches the annual depreciation premium (to become less than the actual interest expense, and it is affected by the increase in recent years).

However, these differences are only timing differences on a year-by-year basis, yet, this effect in total (over the years of the contract) is equal to (zero), as the amount of the period expenses for all years will equal the rent expense as it was before the transition.

Comparison of the impact prior and after the transition (elements of zakat base "additions and deductions"):

Details	First Year	Second Year	Third Year	Total
Prior to transition (additions and deductions)	0	0	0	0
After transition				
Difference between additions and deductions (lease liabilities, right to use of the asset)	0	0	0	0
Effect on recycled profits or losses	(455)	(6)	461	0
effect on recycled earnings	0	(455)	(461)	(916)
Total	(455)	(461)	0	(916)

It is noted from the above that canceling the impact of the standards will have an impact as described above compared to the first option, as the asset or the lease contract liability is not included in zakat base items that address with the differences between them, the above difference appears in the retained earnings.

Note: The following was considered upon detailing the potential handlings for this example:

1. There are other additions) and (deductions) to/from Zakat base (respectively) to match the market reality of private sector companies, and common practices.
2. In the first option, the lease liability was subject to the closing balance, due to it is funded by a deductible asset (the right to use the asset).
3. Taking into account that the additions to the base may not exceed the total deductions in accordance with Article No. 5 in the Executive Regulations for Levying Zakat (review Article 4 below).
4. In this application, it was taken into account that (retained losses) and (loss of the year) for the purposes of zakat are considered deductions from zakat base in accordance with Article 5 of the Executive Regulations for Levying Zakat. Upon taking this into account, the (deducted) items exceed in their total the additions, and thus the liability lease balance shall be added in full. In light of this, there is no apparent impact on zakat base when calculating the base as a whole or the upper limit.

Summary of zakat impact of the possible options for this example:

Effect on the base minimum	First Year	Second Year
First Option	Decrease or increase over the decade years	No effect
Second Option	No impact since profit is adjusted to reflect actual rental expense	Decrease
Third Option	Decrease or increase over the decade years	Decrease

The previous example included the following assumptions:

1. The company achieved profits for the three years referred to in the previous example.
2. Accordingly, there are retained earnings added to zakat base in the opening balance.
3. The taxpayer pays zakat in the zakat base (net income for the year, plus additions to zakat base, less deductions).
4. The right-of-use of the asset is the only asset recognized in the financial statements.

These shall be considered among the special cases in the light of the assumptions mentioned Zakat handling of this case and the zakat effect are summarized as follows:

In this case, the asset shall be considered as a depreciable asset, and the lease contract obligation shall be added (up to deductions only):

Details	Zakat Handling	First Year	Second Year	Third Year	Total
Total period expenses (depreciation and finance expense)	Deductible Expenses	(12,455)	(12,006)	(11,539)	
Right of Use	Deductible from ZB	(22,102)	(11,051)	-	
Lease Obligations Contract (up to deductions)	Additions to ZB	22,102	11,051	-	
Net impact on ZB for the transition items		(12,455)	(12,006)	(11,539)	(36,000)

Summary of the impact of the lease elements under the assumptions mentioned in this example:

Details	First Year	Second Year	Third Year	Total
Prior to transition (additions and deductions)	0	0	0	0
After transition				
Difference between additions and deductions (lease liabilities, right to use of the asset)	0	0	0	0
Effect on recycled profits or losses	(455)	(6)	461	0
effect on recycled earnings	0	(455)	(461)	(916)
Total	(455)	(461)	0	(916)

It is noted from the above that the effect on profits and losses are only timing differences. However, according to the assumptions mentioned in this example, the difference appears clearly in the retained earnings due to the addition of committing to the deduction's limits. In other words: The impact of the decrease in zakat base will be compensated if the full amount of the obligation is added.

From the foregoing, it is noted that:

1. The lease obligation has been added to the limits of deductions, as a result, the effect appears accumulated in the retained earnings, which will affect zakat base by (decrease) by (SAR 916).

2. Despite there is a shortage in Zakat base in such cases, the provisions of the current regulation don't serve to address the aforementioned difference from a technical point of view. As by taking into consideration the assumptions and (if they rarely occur), it has been considered to add this obligation within the limits of the deductions in accordance with Paragraph (Three) of Article (Four).

External document

This guide has been prepared for educational purposes only, and its content may be modified at any time. It is not considered mandatory by the Authority, nor as a legal advice, and it cannot be relied and acted upon without reference to the relevant statutory provisions. Every person subject to Zakat, Tax, and Customs Laws must check their duties and obligations; they are solely responsible for the compliance with these regulations. ZATCA shall not be responsible in any way for any damages or losses incurred to the taxpayer as a result of not complying with the applicable regulations.