VAT brief – Oil & gas

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keypoint

Following on from the release of the GCC VAT framework, Saudi Arabia's General Authority of Zakat and Tax (GAZT) has released a draft version of the law as well as a bilingual version of its VAT implementing regulations. All businesses must now be actively preparing for VAT - 1 January 2018 is less than 100 working days away.

What is VAT?

- VAT is a tax on consumption, not income or profits.
- The GCC countries have agreed a standard VAT rate of five percent.
- Goods and services can be exempt, zero-rated or standard-rated.
- Registered suppliers will add VAT to the price of a good or service they supply, collect the tax and pay it to the tax authority on a regular basis.
- Registered businesses should (where the supplies they make are either standard or zero-rated) be able to recover the VAT they have incurred in the course of making those supplies.
- Registered businesses that make supplies that are exempt from VAT will not be able to recover the VAT they have incurred in the course of making those supplies.
- Registered businesses that make supplies that are predominantly zero-rated will usually be in a refund position.

How will VAT affect the oil & gas sector?

- The KSA draft implementing regulations are silent on relief for the oil & gas sector. This means that supplies will be taxable and input taxes should be fully recoverable.
- Long-term contracts that span the introduction of VAT will need to be reviewed to ensure VAT can be passed on to the customer.
- The timing of accounting for VAT could cause a significant cash flow issue. Typically, VAT is accounted for at the earlier of the supply being made or invoice date – so VAT may be payable to the tax authority a long time before payments are collected from customers.
- Subject to certain conditions, supplies of goods and services made under contracts that span the VAT implementation date (1 January 2018 for Saudi Arabia and the UAE) may qualify for zero rating until the earlier of the expiry of the contract or 31 December 2022.
- According to the agreed VAT framework and consistent with general VAT principles, exports will be zero-rated which means that, while VAT is not charged on exported supplies, it is recoverable on purchases. However, cash flow will still be significantly affected. VAT refunds are likely to be the single biggest issue for oil & gas businesses as a large proportion of their sales are likely to be exports.
- VAT incurred on capital expenditure will also significantly impact cash flow. Large-scale capital expenditure is often incurred at the early stages of an oil & gas project while supplies - and so income flow - are likely to occur some years later. Business may be left waiting for VAT refunds.

What should oil & gas companies be doing now?

- Review long-term supply contracts
- Consider the impact of place of supply rules on offshore drilling and production activities
- Examine the impact of VAT incurred on imports on cash-flow - particularly if an exporter in a refund position.

Important note

These briefs are based on a translation of Saudi Arabia's draft VAT laws and general VAT principles and are provided for information purposes only. This document is not a substitute for professional advice. You should seek appropriate professional advice from a tax advisor before making any decision relating to your particular circumstances.

Contact us

Mubeen Khadir
Head of Tax
mubeen.khadir@keypoint.com
+973 1720 6879
+973 3222 6811

George Campbell
Associate Director
george.campbell@keypoint.com
+973 1720 6872
+973 3833 8641

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