VAT brief | Oil & gas

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Saudi Arabia and the UAE implemented VAT on 1 January 2018, with the other GCC countries expected to follow in the next 12 months. Key decision makers should now be more aware than ever that we are entering into a new tax era. Key decision makers at businesses in the UAE and Saudi Arabia need to ensure their processes and systems are VAT-compliant, while their counterparts in the other GCC states need to start preparing now for the implementation of VAT.

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 (five percent), or out of scope.
- Registered suppliers need to account for VAT out of the price charged for a good or service they supply and pay that tax to the tax authority on a regular basis.
- Registered businesses should (where the supplies they make are either standard- or zero-rated or out of scope) 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 zero-rated will usually be in a refundable position.

How will VAT affect the oil & gas sector?

- The UAE has zero-rated the supply of crude oil and natural gas. Suppliers of these products are likely to almost always be in a VAT refund position, as their primary sources of revenue will be zero-rated and they are entitled to full recovery on their costs.
- The Saudi implementing regulations (IRs) are silent on relief for the oil & gas sector, meaning supplies will be taxable at 5% and input tax should be fully recoverable.
- Long-term contracts that span VAT introduction will need to be reviewed to ensure VAT can be passed on to the customer.
- Timing of VAT accounting could significantly impact cash flow. Typically, VAT is accounted for at the earlier of the supply being made or invoice date – so VAT may be payable a long time before payments are collected.
- Both the UAE and Saudi rules have special transitional relief provisions for contracts which span implementation. However, the operation of these rules and the criteria which must be met before they can be applied are different. In the UAE, suppliers who meet the criteria are entitled to add the VAT amount on top of the agreed contract price. In Saudi Arabia, suppliers can zero-rate until the earlier of the expiry of the contract or 31 December 2018.
- Consistent with general VAT principles, exports to outside the GCC will be zero-rated which means that VAT is recoverable on purchases although it is not charged on exported supplies. 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.

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What should oil & gas businesses 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 you expect to be in a refund position.

Important note

These briefs are based on a translation of the UAE and Saudi Arabia's VAT legislation, the relevant regulations and general VAT principles and are provided for information purposes only. Saudi Arabia and the UAE implemented VAT on 1 January 2018 and the other GCC countries continue – as of the date of release of this brief – to work towards implementation in the next 12 months. This brief 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.

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