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Value Added Tax
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GCC VAT Fundamentals in the Oil and Gas Sector

The introduction of VAT is a landmark event for the region and marks the true beginning of VAT implementation across the GCC. The VAT Treaty signed by the GCC states establishes the common principles of the VAT system which is to apply in each GCC State and provides a structure on which domestic VAT legislation will be developed. We are gradually getting clarity over the principles which every State will be required to enact and can start to confirm our understanding of how businesses will be impacted by the introduction of VAT within the region. The Treaty however leaves certain decisions to the discretion of the individual GCC States, so whilst we now have a greater understanding of how the VAT system will operate there remain many 'grey' areas which can only be resolved once each of the countries have released their VAT laws.

VAT will be relatively straightforward conceptually

- Registered suppliers charge VAT (output tax) in most instances (i.e. typically added to current prices)
- Registered business customers recover the VAT (input tax) in most instances
- End consumer suffers the total VAT cost; flows through businesses to a great extent
- Standard VAT rate will be 5% across the GCC

Zero-rated

- No VAT charged to customers but can recover input tax
- Zero-rated traders usually in a repayment position – need to manage cash flow effects of VAT and refunds from tax authorities

Exempt

- No VAT charged but no input tax recovery
- Exempt traders have a higher cost base and often increase prices as a result

What will be the VAT liability of the oil and gas industry?

In accordance with Article 29 of the Treaty every GCC State may choose to apply the **zero-rate to oil, oil derivatives and the gas sector** *BUT* the exact conditions of the zero-rating and the definition of supplies covered by the provisions are left up to each State to determine:

- Exports will be treated as **zero rated** under Article 34 of the Treaty, meaning no VAT charged on the supply, but VAT recoverable on costs
- **Most costs** and **imports** are likely to be subject to VAT. Warehousing and temporary movements have special rules
- **Cash flow** is impacted as VAT is charged on purchases but recovery from the authorities can take months and can affect **working capital** but this may be alleviated by **zero-rating on purchases of oil etc.** under Article 29
- Transactions involving **swapping of supply or loaning of goods** are likely to result in a VAT impact, even where no payments are made
- Offshore exploration and production activities (in a country's Exclusive Economic Zone) may fall outside of the VAT territory
- **Loss in storage, import or transit** may have a VAT impact
- **Contracts** that straddle the start of VAT implementations are often ill prepared for the introduction of VAT, is the **price inclusive or exclusive of VAT?**
- VAT may not be able to be recovered on **staff accommodation**

There will be issues...

- There will be VAT implications of inter-company transactions *BUT* **VAT Grouping** could allow for transactions between connected companies to be disregarded, subject to certain criteria
- **Joint Ventures and cost sharing arrangements are common:** upfront planning of contractual arrangements can reduce VAT inefficiencies

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