

VAT brief | Utilities

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Saudi Arabia and the UAE implemented VAT on 1 January 2018. Bahrain has confirmed implementation on 1 January 2019, with the other GCC countries expected to follow over the next 12 months. Business leaders should now be more aware than ever that we have entered a new tax era. Key decision makers in the UAE, Saudi Arabia and Bahrain need to ensure their processes and systems are - and remain - 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.
- The GCC countries have agreed a standard VAT rate of five percent.
- The supply of goods and services can be exempt, zero-rated or standard-rated (five percent), or out of scope.
- The mandatory registration threshold is the equivalent of US\$100,000 - as set out in the GCC VAT treaty. The voluntary registration threshold is the equivalent of US\$50,000.
- Registered businesses account for VAT on the price charged for the goods or services they supply 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 or out of scope with recovery) 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 cannot recover the VAT they have incurred in the course of making those supplies.
- Registered businesses may not be able to recover the VAT they have incurred on certain purchases that are deemed to have a private element.
- Registered businesses that make supplies that are predominantly zero-rated are likely to be in a VAT refund position.
- Businesses that make both exempt and taxable supplies can only recover a proportion of their input VAT.

How does VAT affect utility companies?

- Supplies of utilities are likely to be standard-rated (5%), meaning suppliers will have to charge VAT to customers. The UAE and Saudi Arabia have applied VAT on utilities – with Bahrain expected to adopt similar approach. However, clarification (expected in the implementing regulations) on the application of Bahrain's zero-rating to the oil and gas sector may affect how VAT applies to the utilities sector.
- Utility companies should evaluate pricing strategies to take VAT into account, choosing between passing on VAT costs by increasing the price by the VAT amount, maintaining their prices (effectively absorbing the VAT impact), or something in between. Any pricing decision will have to balance profit margins, sales volumes and market share.
- Utility companies that decide to pass VAT to customers will need to be wary of regulatory constraints and the impact pricing may have on their competitiveness.
- Utility providers typically make continuous supplies to customers where VAT is charged and collected on a periodic basis. Affected suppliers will need to be aware of how time of supply rules affect them, ensuring VAT is accounted for at the correct time - which may differ from the standard time of supply rules for discrete, one-off supplies.



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- Utility suppliers that import oil and gas will want to ensure any import VAT is recoverable and does not become a sticking cost – which can occur when another party imports and is named on the relevant customs documentation as the importer of record, but is neither supplier nor recipient in the supply chain.
- Importers must ensure their documentation is correct to facilitate input tax recovery. In Saudi Arabia, import VAT is recoverable as input tax, subject to the normal conditions and as long as a valid customs *bayan* is held in the name of the party seeking to recover the VAT.
- The GCC treaty allows states some discretion on the treatment of oil & gas:
 - The UAE has zero-rated the supply of crude oil and natural gas
 - Supplies of crude oil and natural gas are taxable at 5% in Saudi Arabia
 - Bahrain is zero-rating oil, oil derivatives and gas
- Special rules apply to the cross-border supplies of goods and services between businesses within the GCC. In essence, a reverse charge may apply.
- Utility providers may be required to perform complex VAT accounting and must understand the impact of operating within international supply chains.

What should utility businesses do now?

- Consider the impact of VAT on pricing – should the cost of VAT be passed on to consumers?
- Assess whether price capping or competition will hamper price increases.
- Understand the impact of VAT on purchases - particularly imports - and when VAT can be recovered.
- Review customer contracts to understand whether prices can be changed - and how quickly.

Important note

The information in this document is based on translations of the draft Bahrain VAT law, the VAT laws and regulations of the UAE and Saudi Arabia, the GCC VAT framework and general VAT principles. It is provided for information purposes only. As the draft Bahrain VAT law has been recently released and is still being reviewed in detail, any comments on this law are preliminary in nature and are likely to change. Any omissions or errors are inadvertent. This document should not be relied upon in making any decisions. You should seek appropriate professional advice from a tax advisor before making any decision relating to your particular circumstances.