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VAT

Electricity and Utilities: Guideline

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1. Introduction

1.1. Implementing a Value Added Tax (“VAT”) system in the Kingdom of Saudi Arabia (“KSA”)

The Unified VAT Agreement for the Cooperation Council for the Unified Arab States of the Gulf (the “VAT Agreement”) was approved by KSA by a Royal Decree No. M/51, dated 31438/5/ H. Pursuant to the provisions of the Unified VAT Agreement, the KSA issued the VAT Law under Royal Decree No. M/113 dated 21438/11/ H (“the VAT Law”) and its corresponding Implementing Regulations were subsequently issued by the Board of Directors of the General Authority of Zakat and Tax (“GAZT”) by Resolution No. 3839 dated 141438/12/ H (“the Implementing Regulations”).

1.2. General Authority of Zakat & Tax (“GAZT”)

GAZT, also referred to as “the Authority” herein, is the authority in charge of the implementation and administration of VAT (which may be referred to hereinafter as “the tax”) in KSA. In addition to the registration and deregistration of Taxable Persons for VAT, the administration of VAT return filing and VAT refunds; and undertaking audits and field visits. GAZT also has the power to levy penalties for non-compliance with legal provisions relating to VAT.

1.3. What is Value Added Tax (“VAT”)?

VAT is an indirect tax, which is imposed on the Importation and Supply of Goods and Services throughout the supply chain, with certain limited exceptions. VAT is imposed in more than 160 countries around the world.

VAT is a tax on consumption that is paid and collected at every stage of the supply chain, starting from when a manufacturer purchases raw materials until a retailer sells the end-product to a consumer. Unlike other taxes, persons registered for VAT will both:

- Collect VAT from their customers equal to a specified percentage of each eligible sale; and
- Pay VAT to their Suppliers equal to a specified percentage of each eligible purchase.

When Taxable Persons sell a Good or provide a Service, a 5% VAT charge – assuming a standard case – is assessed and added to the sales price. The Taxable Persons will account for that 5% that they have collected from all eligible sales separately from its revenue in order to later remit a portion of it to the Authority. The VAT Taxable Persons collect on their sales is called Output VAT.

That same will apply to purchase transactions done by Taxable Persons, in that VAT will be added at the rate of 5% to purchases of Goods or Services from other Taxable Persons (on the assumption that the basic rate applies to those Supplies). The VAT a business pays to its Suppliers is called Input VAT.

Further general information about VAT can be found in the KSA VAT Manual or at vat.gov.sa

1.4. This Guideline

This guideline is addressed to all natural persons and legal persons who carry on an economic activity and who will be required to register for VAT. The purpose of this guideline is to provide further clarification to taxpayers regarding the VAT implications of transactions involving electricity and other utilities such as water, heating, cooling, and air conditioning.

This guideline represents GAZT's views on the application and fair treatment of the Unified VAT Agreement, the VAT Law and the Implementing Regulations to the sector as of the date of this guideline. This guide amounts to a guideline, and does not include, or purport to include, all the relevant provisions in relation to the sector from those laws. It is not binding on GAZT or on any taxpayer in respect of any transaction carried out and it cannot be relied upon in any way.

For further advice on specific transactions you may apply for a ruling, or visit the official VAT website at (vat.gov.sa), which contains a wide range of tools and information that has been established as a reference to support persons subject to VAT, as well as visual guidance materials, all relevant information, and FAQs.

2. Definitions of Key Terms

Goods is a defined term for VAT purposes, being “All types of material property (material assets), including water and all forms of power including electricity, gas, lighting, heating, cooling and air conditioning.”⁽¹⁾

Whilst the term “Goods” are often viewed as tangible assets, the definition clearly intends that electricity and similar utilities will also be considered as Goods for applying VAT rules.

Supply of Electricity – Electricity is not a defined term for VAT purposes, but signifies a type of supply with distinct VAT Place of Supply rules⁽²⁾. GAZT views this to have its everyday meaning – that is, power generated from any source and transmitted for use in powering devices. All activity connected to electricity in the KSA is regulated by the Electricity Law⁽³⁾ and its Implementing Regulations. The Supply of Electricity is any transfer or other form of supply of electricity or the right to use electricity, and is considered a Supply of Goods.

The term “supply” is often used in the utility sector to denote the provision of utilities such as water or electricity to consumers. This term is often used with similar meaning to the defined term of a “Supply” for VAT purposes, but please note that the industry usage may differ to the VAT definition in some cases.

Supply of Gas, Water and Oil through the pipeline distribution system is not a defined term for VAT purposes, but signifies a type of Supply with distinct VAT Place of Supply rules⁽⁴⁾.

The **pipeline distribution system** is not a defined term for VAT purposes. GAZT considers that this includes any integrated network of pipelines or similar infrastructure, such as transmission networks, distribution networks, and associated facilities connected to those networks whereby gas, water or oil are distributed to producers, distributors or consumers of those utilities.

In respect of electricity, the Electricity Distribution System is not a defined term for VAT purposes, but is defined in electricity regulation in the KSA:

“Subject to the specific provisions of the relevant Distribution Licence, a system consisting of cables, overhead lines, and electrical apparatus having such design voltage(s) as may be specified in the relevant Distribution Licence used for the distribution of electricity from connection points within the Transmission System or within Generating Stations to point of delivery to Consumers or other Distribution Systems and includes any electrical installations and meters owned or operated in connection with the distribution of electricity, but shall not include any part of a Transmission System.”⁽⁵⁾

Taxable Trader is a defined term for VAT purposes, being “any taxable person, whether natural or legal person, in any Member State whose main activity is the distribution of Oil, Gas, Water and Electricity⁽⁶⁾.”

Place of Residence is a defined term for VAT purposes. The main definition is “The location where Place of Business or any other type of Fixed Establishment is.”⁽⁷⁾

(1) Article 1, Definitions, Unified VAT Agreement

(2) Article 14, Supply of Gas, Oil, Water and Electricity, Unified VAT Agreement.

(3) Royal Decree No. M/56 dated 20 / 10 / 1426 H (22 November 2005)

(4) Article 14, Supply of Gas, Oil, Water and Electricity, Unified VAT Agreement.

(5) Article 1, Definitions, Implementing Regulations to the Electricity Law

(6) Article 1, Definitions, Unified VAT Agreement.

(7) Article 1, Definitions, Unified VAT Agreement.

This definition has additional qualifications, applying in certain circumstances:

- “In the case of a natural person, if he does not have a Place of Business or Fixed Establishment, it will be his usual place of residence.
- If a Person has a Place of Residence in more than one State, the place of residence will be considered to be in the place most closely connected with the Supply.”⁽⁸⁾

Place of Business is a defined term for VAT purposes as “The Place where a business is legally established; or where its actual management center is located where key business decisions are made if different from place of establishment.”

Fixed Establishment is a defined term for VAT purposes as “Any fixed location for a Business other than the Place of Business, in which the business is carried out and is distinguished by the permanent presence of human and technical resources in such a way as to enable the Person to supply or receive Goods or services.”⁽⁹⁾

Place of Actual Consumption is the place where the Customer actually consumes the Goods. In the context of a Supply of electricity, gas, oil, water or other utilities through a pipeline distribution system, GAZT considers the Place of Actual Consumption is the registered premises or delivery point to which the Goods are delivered.

Supply of Services is any form of Supply that does not constitute a Supply of Goods⁽¹⁰⁾.

Import of Goods is defined for VAT purposes as “The entry of Goods into any Member State from outside the GCC Territory in accordance with the provisions of the Common Customs Law”⁽¹¹⁾. During the transitional period, the receipt of Goods into the Kingdom from another Member State by a Taxable Person is also treated as an Import of Goods to the KSA⁽¹²⁾.

Export of Goods is defined for VAT purposes as “Supply of Goods from any Member State to the outside of the Council Territory in accordance with the provisions of the Unified Customs Law”.⁽¹³⁾

The Export of Goods therefore must involve a Supply of those Goods. A movement of a person’s own Goods outside of the GCC Territory is not a Supply for VAT purposes, other than in the case of a Nominal Supply.

During the transitional period, a Supply of Goods involving transport of the Goods from the KSA to another GCC Member State shall be treated as an Export of the Goods for VAT purposes.⁽¹⁴⁾

Note that the Export of Goods is a separate concept to the industry concept of a customer “exporting” electricity from his premises to the Electricity Distribution System.

Licensee is a term defined in domestic electricity regulation in the KSA. This is every person holding a valid License issued by the relevant Authority to carry out an Electricity Activity; being generation, cogeneration, transmission, distribution, supply, and trading of electricity⁽¹⁵⁾.

(8) Article 1, Definitions, Unified VAT Agreement.

(9) Article 1, Definitions, Unified VAT Agreement

(10) Article 7, Supply of Services, Unified VAT Agreement

(11) Article 1, Definitions, Unified VAT Agreement.

(12) Article 79(7), Transitional provisions, Implementing Regulations

(13) Article 1, Definitions, Unified VAT Agreement.

(14) Article 79(7), Transitional provisions, Implementing Regulations

(15) Article 1, Terms, Electricity Law

3. Economic Activity and Registration

3.1 Who carries out an Economic Activity?

An Economic Activity may be carried out by natural persons or legal persons.

It will be presumed that a legal person (company) that has a regular activity making Supplies carries on an Economic Activity. Natural persons may perform certain transactions as part of their Economic Activity, or as part of their private activities. There are therefore specific rules to determine whether or not a natural person falls within the scope of VAT.

Natural persons and legal persons who carry on an Economic Activity must register for the purposes of VAT if the registration requirements are fulfilled, and such persons must calculate the VAT applicable to their activities, collect and pay the tax to the Authority through their periodic returns.

3.2. Mandatory registration

Registration is mandatory for all persons whose annual Taxable Supplies exceed a certain threshold. If the total value of a person's Taxable Supplies during any 12 months exceeds SAR 375,000, (the "mandatory VAT registration threshold"), that person must register for VAT⁽¹⁶⁾ on the Supplies made, subject to the transitional provisions provided for in the Implementing Regulations.

Taxable Supplies do not include:

- Exempt Supplies– such as exempt financial Services or residential rental which qualifies for VAT exemption;
- Supplies taking place outside the scope of VAT in any GCC state; or
- Revenues on sales of capital assets – a capital asset is defined as an asset allocated for long-term business use⁽¹⁷⁾.

In certain circumstances, other tests will apply for mandatory registration:

- Persons who are not resident in the Kingdom of Saudi Arabia are required to pay the VAT in respect of Supplies made or received by them in the Kingdom of Saudi Arabia and to register for VAT irrespective of the value of the Supplies for which they are obliged to collect and pay the VAT⁽¹⁸⁾.
- During a transitional period up to 1 January 2019, businesses will only be required to register where annual turnover exceeds SAR 1,000,000⁽¹⁹⁾. Starting from the year 2019, the mandatory registration threshold amounting to SAR 375,000 will be applied as stipulated in the Unified VAT Agreement. For persons whose Taxable Supplies are expected to exceed this amount in the year commencing 1 January 2019, an application for registration must be submitted on or before 20 December 2018.

More information on mandatory registration for VAT is contained at vat.gov.sa

(16) Article 3, Mandatory registration - Supplies exceed the Mandatory Registration Threshold, Implementing Regulations

(17) Article 1, Definitions, Unified VAT Agreement.

(18) Article 5(1), Mandatory registration of Non-Residents obligated to pay Tax in the Kingdom, Implementing Regulations.

(19) Article 79 (9), Transitional provisions, Implementing Regulations

3.3. Optional VAT registration

Any Resident person in the Kingdom of Saudi Arabia who has Taxable Supplies or taxable expenses exceeding the “Optional VAT registration threshold” of SAR 187,500 in a twelve-month period may register for VAT on a voluntary basis⁽²⁰⁾.

Optional VAT registration may be desirable where a business wishes to claim VAT charged to it on their costs before invoices are raised or the occurrence of an onward Supply.

Example (1): Best Solar Company decides to enter into the developing renewable energy generation market. It obtains a generation licence and Imports an array of photovoltaic cells to install at sites around the KSA. It also enters into power purchase agreements with distribution companies in the KSA to sell the generated energy, on which it will charge VAT.

The installation of the first solar array is due to be operational for making Taxable Supplies by April 2020. However, Best Solar incurs SAR 500,000 in costs during 2019 in preparatory costs, such as obtaining licences, design costs, as well as Import and installation. As the taxable expenses exceed SAR 187,500, Best Solar is able to register for VAT in 2019 and deduct VAT on the costs that relate to the future Taxable Supplies from generation of electricity.

More information on voluntary registration for VAT is contained at vat.gov.sa

(20) Article 7, Voluntary Registration, Implementing Regulations

4. Place of Supply

An important concept to determine the application of VAT is the Place of Supply: this identifies in which country the Supply is deemed to take place for VAT purposes, and which country's VAT rules and obligations apply to that Supply. This is determined in accordance with Place of Supply rules set out in the Unified VAT Agreement.

In most circumstances, the Place of a Supply of Goods depends on the physical location of the Goods at a defined time⁽²¹⁾. As it is difficult in practice to determine the physical location of an exact quantity of electricity, gas, oil or water supplied through a pipeline, there are different rules to determine the Place of Supply.

4.1. Place of Supply of Electricity and Gas, Oil, or Water through a Distribution System – Customer is a Taxable Trader

The Place of Supply for electricity and for the Supply of gas, oil, or water through a pipeline distribution system by a Taxable Person who is established in a Member State to a Taxable Trader established in another Member State shall be the place where the Taxable Trader is established.⁽²²⁾

VAT is chargeable at the rate of 5% on all Supplies of water, electricity, oil, gas and any form of power, that are made in the KSA for VAT purposes, including those made to a Person that is a Taxable Trader.⁽²³⁾

If the Supply is made by a non-resident to a Taxable Trader in the KSA, the Taxable Trader will be required to account for the VAT on the Supply through the Reverse Charge Mechanism. This is entered by the Taxable Trader in field 9 of the VAT return (this field is named "Imports subject to VAT accounted for through reverse charge mechanism", but is used for all Supplies where a resident Customer self-accounts for VAT upon receiving a supply from a non-resident).

Example (2): RAK Generation Company generates electricity at its facilities in the UAE. It enters into a spot power transaction to sell 20 MW of electricity to Al-Fahad Energy Trading, which is a KSA company licensed to trade electricity in the GCC states for SAR 10,000. Al-Fahad intends to sell this electricity to a distribution company in the UAE. The electricity is not physically transmitted across the country border to the KSA.

In this case, whilst the electricity remains in the UAE, the Place of Supply is deemed to take place in the KSA, as the recipient is a Taxable Trader established in the KSA. RAK Generation does not charge VAT on its invoice. Al-Fahad must apply VAT due (5% of the sale price) under the Reverse Charge, which is done by including the purchase in Box 9 of its VAT return.

4.2. Place of Supply of Electricity and Gas, Oil or Water through a Distribution System – Customer is not a Taxable Trader

This could include a Supply to Taxable Person, such as a factory wishing to consume the power or water as part of its Economic Activities, or to a Non-Taxable Person such as an individual under a domestic supply contract.

(21) Article 10, Supply of Goods without Transportation, Unified VAT Agreement.

(22) Article 14 (1), Supply of Gas, Oil, Water and Electricity, Unified VAT Agreement.

(23) Article 2, Scope of Tax, Unified VAT Agreement.

In all cases, where electricity is supplied or where gas, oil, or water is supplied through a pipeline distribution system to a Person who is not a Taxable Trader, the Place of Supply shall be the Place of Actual Consumption.⁽²⁴⁾ In practice, this is determined by the premises to which the delivery takes place.

As is the case for Supplies to a Taxable Trader, VAT is chargeable at the rate of 5% on all Supplies of water, electricity, oil, gas and any other form of power, that are made in the KSA for VAT purposes (other than those made to customs duty suspended zones as described in section 4.3).⁽²⁵⁾

Example (3): The Electricity Supply Company (ESC) is an entity established in the KSA licensed to generate, transmit and distribute electricity. It supplies power to various Taxable and non-Taxable Persons (such as factories, plants and residential homes) for consumption in the KSA.

For Supplies made from ESC's distribution division, ESC's practice is to use the address of the metered supply point, where delivery from the Electricity Distribution System takes place, to determine the premises at which the electricity is consumed. For all customers with a point of delivery from the Electricity Distribution System in the KSA, VAT is applied to the Supply at 5%.

4.3. Supply to a Customs-suspended premises

A business established in location that is controlled by Saudi Customs as a customs duty suspension situation, such as a free zone or duty free shop, is subject to special rules.

All Supplies of Goods (including electricity, water and other utilities) to a delivery point of the Electricity Distribution System within a customs duty suspension situation are zero-rated for VAT purposes.⁽²⁶⁾

Example (4): ESC has an electricity supply contract with King Logistics Company. King Logistics has operations in an office building in Riyadh, and a separate distribution centre within a customs suspended free zone area.

The Supply of power to the metered supply point at the office building is subject to VAT at 5%. The Supply of power to the metered supply point in the customs suspended free zone is subject to VAT at 0%. ESC issues Tax Invoices to King Logistics with Supplies made to the different locations separately identified, and applying the appropriate VAT rates for each premises.

4.4. Place of Supply of Gas, Oil or Water outside of a Distribution System

All Supplies of gas, oil or water which do not take place through a pipeline distribution system (such as Supplies of product transported in bottles, cylinders, tanks or other containers, or product directly pumped into a vehicle or machine) are subject to the standard rules to determine the Place of Supply of those Goods.

In these cases, the Place of Supply is determined as follows

- If the Supply of Goods occurs without transportation or dispatch of those Goods (for example, the customer uplifts the Goods at the Supplier's premises), the Place of Supply is where the Goods are located on the date they are placed at the Customer's disposal⁽²⁷⁾.
- If the Supply of Goods occurs with transportation or dispatch of those Goods by the Supplier or otherwise to the account of Customer, the Place of Supply is where the Goods are located when the transportation or dispatch commences⁽²⁸⁾.

(24) Article 14 (2), Supply of Gas, Oil, Water and Electricity, Unified VAT Agreement.

(25) Article 2, Scope of Tax, Unified VAT Agreement.

(26) Article 34 (1), Supplies to Outside the GCC Territory, Unified VAT Agreement.

(27) Article 10, Supply of Goods without Transportation, Unified VAT Agreement.

(28) Article 11, Supply of Goods with Transportation, Unified VAT Agreement.

VAT is chargeable at the rate of 5% on all Supplies of Oil, Gas and Water, which are made outside of a network or pipeline distribution system in the KSA for VAT purposes, whether the consumer is a Taxable or non-Taxable Person.

Example (5): Sham'ah Gas Company produces 3.5 million standard cubic metres of methane gas. It sells 3 million standard cubic metres into the KSA's Master Gas System, but also ships 500,000 standard cubic metres by truck to a desalination plant, which is not connected to the system. The Place of Supply to the desalination plant takes place where the truck transport commences, at Sham'ah's production facility in the KSA.

Example (6): A water supply company has a storage tank in a rural area holding 250,000 litres of water. In April, it agrees to sell the water to a local farmer, with the water held in storage tanks (so that the farmer is able to collect the water when he wishes in the coming months). There is no transportation of the Goods. The Place of Supply is where the Goods are made available to the customer (at the storage tank) – regardless of the status of the Customer.

Any Supplies involving the Import of Goods from outside the GCC, or Export of Goods to a place outside the GCC, are subject to rules for Imports and Exports. Please see the Import and Export guideline, for more detail. Chapter 5 of this guideline discusses the rules applying to Imports and Exports within a pipeline or electricity distribution system.

For completeness, please note that special Place of Supply rules may apply to Supplies of Goods which are transported to another GCC State (outside of a pipeline system), after the introduction of an Electronic Services System and the full implementation of VAT rules for intra-GCC trade. Further details will be provided upon the introduction of the Electronic Services System.

4.5. Transportation of Electricity, Gas, Oil or Water

The transmission of electricity is a licensed activity in the KSA, to convey electricity from generation facilities to the Electricity Distribution System through the Transmission Network. The transmission of electricity is considered as the transportation of Goods for VAT purposes.

Similarly, in cases where consideration is paid to a Person to transport gas, oil, water from one place to another – whether through a pipeline distribution system or shipped using a means of transport – this consideration relates to the Transportation of those Goods.

The Place of Supply of any Goods transportation Services is the place where that transport starts.⁽²⁹⁾ This rule applies regardless of the residence or VAT registration status of the Supplier or Customer.

In the case of transportation Services which start at a location in the KSA and have a destination outside of KSA territory (including another GCC State, a third country state, or any other destination outside of the KSA's sovereign territory), the zero rate (0%) of VAT applies⁽³⁰⁾.

Transport Begins	Transport Ends (Destination)	KSA VAT treatment
In the KSA	In the KSA	VAT at 5% - local transport
In the KSA	Outside the KSA: - another GCC State - outside of GCC Territory	VAT at 0% - intra-GCC or international transport
Outside the KSA	In the KSA	Not subject to KSA VAT
Outside the KSA	Outside the KSA	Not subject to KSA VAT

(29) Article 18, Supply of Goods and Passenger Transportation Services, Unified VAT Agreement.

(30) Article 32, Intra-GCC and International Transportation, Unified VAT Agreement

Transactions with a Place of Supply outside the KSA will not be subject to KSA VAT. The country where the Place of Supply takes place may however seek to impose VAT or a similar transactional tax.

Please see the taxpayer guideline on Transportation for further general information about the application of VAT to transport and transport-related Services.

4.6. Other Services

Utilities providers, and other businesses in the sector, may provide other Services to customers, which relate to the Supply of electricity, gas or water under their utility contract. Examples of such Services might include:

- Waste water disposal Services;
- Network connection, re-connection or disconnection;
- Installation of equipment such as meters; and
- Repair and maintenance to a customer's equipment.

If the Taxable Person makes a charge for these Services, it is conceptually necessary to determine if:

- The Services provided are a necessary and inseparable element for the underlying Supply of Goods – and are therefore additional consideration for the single Supply of electricity/utilities; or
- The Services are separate and additional to the electricity, water or gas being provided.

For most domestic supply contracts, the distinction does not affect the overall VAT treatment – as the Place of Supply of both the Goods and the Services would take place in the KSA and be subject to VAT at 5%.

4.6.1. Services related to Real Estate:

Real Estate-related Services are those which affect or are related to a specific area of Real Estate or to a specific site of immovable property.⁽³¹⁾ In these cases, VAT applies in the country where the real estate is situated, regardless of the residence of the Supplier or Customer.

GAZT's view is that most additional and separate Services provided in connection with a utility supply contract to a specific premises in the KSA will be real-estate related Services for the purpose of establishing the Place of Supply.

Any Services relating to specific generation, transmission, distribution or similar assets will also be considered as real-estate related Services.

Example (7): Al-Harbi LLC is a KSA resident contractor, who carries out work for the installation of electricity lines for a mall in Dammam according to the electrical drawings provided by the Engineer. Al-Harbi carries out its electrical installation work as a subcontractor for a Kuwaiti company, who is the lead contractor for the construction project. The installation Services are related to Real Estate located in the KSA. Therefore, the Place of Al-Harbi's Supply is in the KSA for VAT purposes, regardless of the residence of its customer.

(31) Article 23 (2), Real Estate related services, Implementing Regulations.

5. Imports and Exports through Distribution Systems

5.1. Background

Increasingly, commodities such as electricity and gas are physically transported between countries through international distribution systems in order to facilitate trade and maintain the security of supply. Examples of such distribution systems within the GCC are gas pipelines, and electricity interconnectors between countries.

In respect of electricity, the GCC Interconnector Authority has been established to link the States' domestic power systems and develop an efficient power market across the GCC.

Interconnector facilities allow the transfer of electricity from one country to another, to support in events of power generation loss and shutdowns. Transfer through the interconnector could also be used in future to facilitate trading within a broader power market, across GCC states and to any other neighbouring countries connected to the network.

This section describes the VAT consequences of a physical transfer of Goods to or from the KSA through a gas pipeline or at an electricity interconnector connecting with another State. For information on Imports or Exports outside of a distribution system (for example, in a vessel), please refer to the guideline on Imports and Exports.

5.2. Import of Goods into KSA

VAT is chargeable at 5% on the physical Import of Goods as a separate event to any Supply of those Goods, including for example electricity, water, oil, or gas.

The imposition of VAT upon the Import of Goods therefore applies separately, and in addition to, any VAT imposed on the Supply of those same Goods:

- For Goods Imported into the KSA, the **Place of Import** is the KSA.
- The **Place of Supply** is determined in accordance with the Place of Supply rules in section 4 (depending on whether the Supply is made to a Taxable Trader, or for consumption).

VAT is imposed on the Importer of the Goods – being the licensed person who submits the customs declaration to Saudi Customs (together with any additional regulatory requirements for the receipt of electricity or gas through the interconnector or pipeline respectively). VAT is applied whether the Importer is a Taxable Person or a non-Taxable Person.

The physical receipt of electricity, gas or other Goods from a GCC State to the KSA is also considered to be an Import which is subject to VAT, during the transitional period in place before the introduction of the Electronic Services System⁽³²⁾. VAT will be applied based on the statistical Import declaration submitted to Saudi Customs.

Import VAT is only applied to a physical transfer of the Goods into the KSA. The purchase of electricity, gas, oil or water situated in a distribution system outside of the KSA does not result in an Import for VAT purposes (although the Place of Supply of the Goods may be in the KSA).

(32) Article 79(7), Transitional provisions, Implementing Regulations

Returning to example (2): RAK Generation Company generates electricity at its facilities in the UAE. It enters into a spot power transaction to sell 20 MW of electricity to Al-Fahad Energy Trading, which is a KSA company licensed to trade electricity in the GCC states for SAR 10,000. Al-Fahad intends to sell this electricity to a distribution company in the UAE. The electricity is not physically transmitted across the country border to the KSA. Therefore, there is no Import of the Goods (electricity) into the KSA.

However, Al-Fahad applies KSA VAT to the Supply – which is deemed to take place in the KSA – based on the reverse charge mechanism.

Example (8): An industrial gas Supplier does not have sufficient reserves to make a Supply to one of its large manufacturing Customers. In order to fulfil the customer's requirements, it purchases gas from a Supplier in Kuwait and Imports this through a newly established gas pipeline. At this time, there is no Electronic Services System in place, and intra-GCC trade remains subject to transitional VAT rules. The Supplier files a statistical customs declaration to Saudi Customs to Import the Goods. It pays VAT at 5% on the Import into the KSA.

5.3. Export of Goods from the KSA

The Export of Goods is a Supply that involves the physical movement of Goods to a place outside the GCC territory as a consequence of that Supply. An Export made from the KSA is subject to KSA VAT at the zero rate.⁽³³⁾

During the transitional period before the introduction of the Electronic Services System, a Supply involving the movement of Goods outside of KSA territory to other GCC member states is also considered an Export subject to the zero rate.⁽³⁴⁾

In standard cases, an Export of Goods involves both:

- The completion of an Export declaration by the exporter as required under the Common Customs Law; and
- Transport of the Goods outside of the GCC territory.

An exporter must hold evidence that the Goods have been transported from Council Territory within 90 days of the Supply taking place⁽³⁵⁾.

In the case of a Supply through a gas pipeline or electricity via the interconnector, the Supplier should ensure the operator of the pipeline or interconnector provides evidence of the transport outside of the KSA. There may also be additional regulatory requirements connected with Exports through a pipeline or interconnector.

(33) Article 34, Supplies to Outside the GCC Territory, Unified VAT Agreement

(34) Article 79(7), Transitional provisions, Implementing Regulations.

(35) Article 32(1), Exports of Goods from the Kingdom, Implementing Regulations

6. VAT in the Domestic Electricity Sector

6.1. Background to the KSA Electricity Sector

The electricity industry is a regulated sector in the KSA. It includes the "Electricity services that Persons undertake or intend to undertake, including electricity generation, cogeneration and transmission of electricity, its distribution, supply and Trading."⁽³⁶⁾ Whilst the Electricity Law refers to "electricity services", a Supply of electricity is a Supply of Goods for VAT purposes.

The licensed activities are described in Regulations to the Electricity Law:

Generation	(a) developing or extending the capacity of a Generating Station for the purposes of generation of electricity at such Generating Station; (b) generation of electricity at a Generating Station.
Cogeneration (The simultaneous production of electricity and desalinated water, or steam used in other production processes, or both.)	a) developing or extending the capacity of a Generating Station for Cogeneration for the purposes of Cogeneration at such Generating Station; (b) Cogeneration at a Generating Station.
Transmission	(a) developing or extending any part of a Transmission System; (b) transmission of electricity over a Transmission System.
Distribution	(a) developing any part of a Distribution System; (b) distribution of electricity over a Distribution System for the purpose of enabling a supply to be given to any Consumer, including sale of electricity to Consumers within the authorized area of the Distribution Licence.
Trading The sale, purchase, import or export of a product or service included in an Electricity Activity.	Trading of electricity or Cogeneration products either to other Trading Licensees or to Retail Licensees, or to Distribution Licensees where they sell such electricity to Consumers within their authorized areas.
Retail	Sale of electricity to Consumers.
Preparatory work	Preparatory work (including the developing of plans and the carrying out of studies) prior to the commencement or extension of an Electricity Activity.

(36) Article 1, Terms, Electricity Law.

6.2. VAT Considerations for Preparatory work and Generation Sector

6.2.1. Expenditure incurred before Generation

For VAT purposes, the preparatory activities carried out before a generation or other activity which are intended to take place on an ongoing and regular manner constitute an economic activity for VAT purposes.

A KSA resident business carrying on preparatory work, and incurring taxable expenses of SAR 187,500 or more in a year, is eligible to register for VAT on an optional basis. Provided that the intended economic activity constitutes making Taxable Supplies of power or transmission, VAT charged on expenditure should be deductible as Input VAT. It is not necessary to make a specific onwards Supply in order to deduct the Input VAT as credit. Deduction of Input VAT is based on intended use at the time of purchase.

Example (9): Red Sea Power establishes a company to construct a small generation facility near a large industrial facility. It registers for VAT and deducts Input VAT charged on construction expenses. Before the generation facility begins production, the industrial facility closes down and the generation facility is no longer commercially viable.

Red Sea has correctly registered and deducted Input VAT based on the intended use at the time of purchase, and is not required to make an adjustment to reflect the plant not operating.

6.2.2. Construction activities

All construction Services performed in the KSA, or any contract to construct a generation facility in the KSA – including the activities of sub-contractors on any such project - is a Supply of Services which is subject to VAT at the rate of 5%.

This includes combined contracts to design and construct a facility, such as Engineering, Procurement and Construction contracts (EPC) and Lump Sum Turn Key (LSTK) contracts.

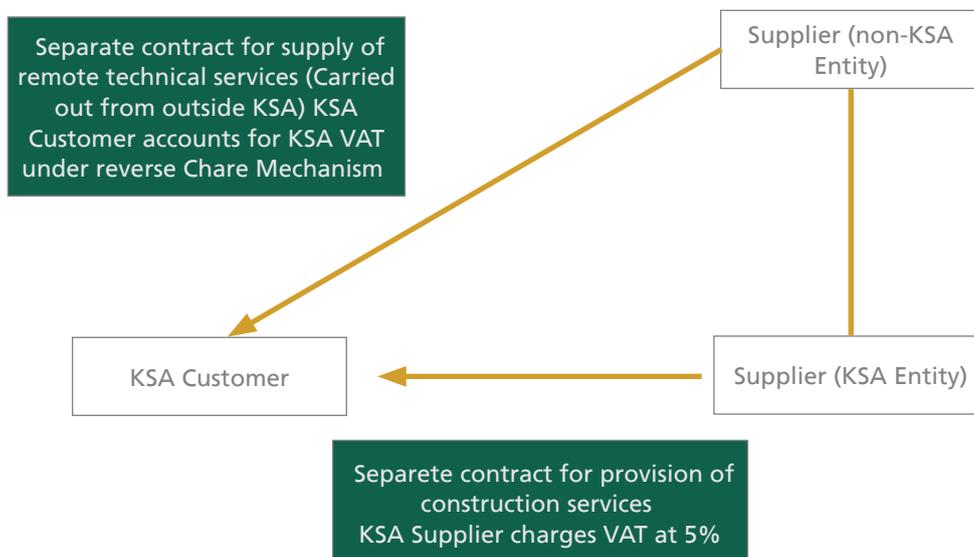
Whilst these contracts involve the provision of tangible materials and equipment, they are in most cases seen in totality as one contract for a single Supply of construction Services. The Place of Supply of the Services takes place in the country where the facility is located.

An EPC or LSTK contract is typically entered into by a local Supplier, or by a KSA branch or subsidiary company of a multinational construction business. In these cases, the resident Supplier must charge VAT on the Supply.

In some cases, a multinational Supplier may agree with the customer to split the contract and Supply certain "remote" or "Outside Kingdom" Services from another group entity. Typically, these are specialist Services carried out remotely by staff or contractors of a non-resident entity, which can be provided without physical presence in the KSA (typically Services such as design, off-site engineering and procurement).

In these cases, if the recipient of the Services enters into a separate contract with a distinct non-resident Supplier for the provision of clearly distinguishable Services, VAT can be applied based on the residence of each different Supplier in each case. The Services concerning a specific facility will be related to Real Estate in the KSA and subject to VAT at 5% regardless of the residence of the entity acting as Supplier. However, the Taxable Customer will be liable to self-account for VAT under the Reverse Charge Mechanism on receipt of the Services provided directly by the non-resident.

Diagram: Two distinct suppliers from same multinational group



Example (10): Red Sea Power entered into an agreement with Ichigawa KSA Limited for the construction of its generation facility in the KSA. It enters into a separate agreement with Ichigawa Japan for the provision of remote Services in connection with the facility. Both Supplies are Services connected to the facility located in the KSA.

Ichigawa KSA Limited issues an invoice for the first milestone payment of the contract

Ichigawa KSA Limited TIN 30000 74174 00003	Date: 30 September 2020
EPC Milestone 1	SAR 600,000
VAT at 5%	SAR 30,000
Total due for payment	SAR 630,000

Ichigawa Japan issues a separate invoice to reflect the remote Services directly provided to Red Sea KSA Limited under its contract, for SAR 120,000. This invoice does not include KSA VAT, but Red Sea KSA Limited is required to account for VAT of SAR 6,000 under the Reverse Charge Mechanism, in its VAT return.

It is not possible for a Supplier with a KSA branch and foreign head office to split its Supplies in this way for VAT purposes. If a Supplier has Fixed Establishments both in the KSA and in another country, it will be viewed as resident for that Supply in the country that is most closely connected to the Supply⁽³⁷⁾. For the provision of an EPC or similar contract, it is very likely that the Supplier's KSA Fixed Establishment will be the Establishment most closely connected to the Supply, and will be required to issue the Tax Invoice as the Supplier.

(37) Article 21 (4), Taxable status of Supplier and Customer, Implementing Regulations.

6.2.3. Application of VAT to Supplies of generated electricity

The Supply of electricity generated from a generating station is a Supply of Goods, which is subject to VAT at 5%, provided the Supply takes place in the KSA.

The Supply of a certain amount of electricity on a set date (such as a spot power trade of a defined quantity to a defined delivery point, or an energy trade made up of electricity delivered during hourly periods on the same date) is a one-off Supply of Goods. The Supply of Goods takes place on the date the electricity is made available, unless VAT has already become due on an earlier date (by virtue of the Supplier issuing a tax invoice, or receiving payment in respect of that Supply).⁽³⁸⁾

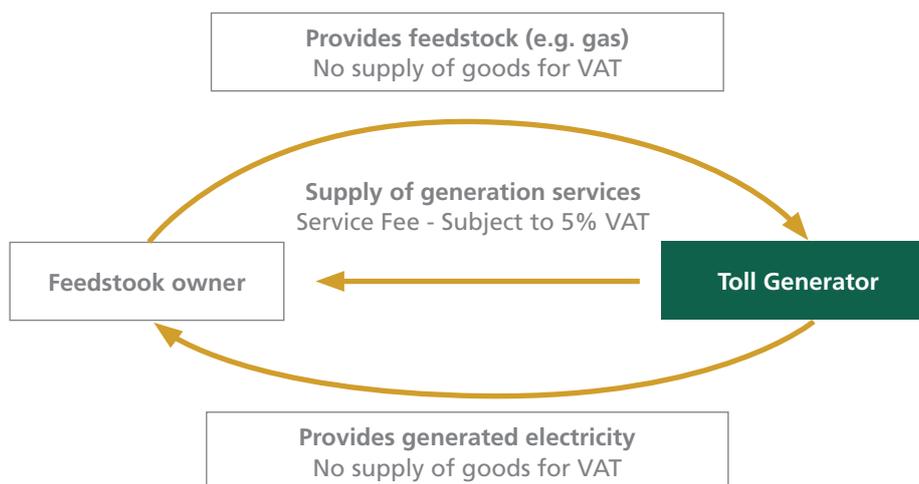
An agreement to Supply all generated electricity across a defined long-term period (such as a power purchase agreement under which all power is delivered to one "offtaker"), could be considered as a "continuous" Supply of Goods.

In the case of a "continuous" Supply of electricity, VAT becomes payable based on each progressive payment, according to the following rules:

- Where contracts have specified payment due dates at set milestones (e.g. periodical installments), VAT becomes payable on the due date or the date of actual payment, whichever comes first.⁽³⁹⁾
- In all other cases, VAT becomes payable for each progress payment at the date of issuing the invoice or the date of actual payment, whichever comes first.⁽⁴⁰⁾

6.2.4. Toll generation

Toll generation is a process whereby a generation facility is provided with feedstock (for example gas) by a Customer, and charges a fee to convert that feedstock to electricity, which is made available to the same Customer.



In these cases, the generation activity is a Supply of Services carried out for the Customer, and the fee collected will be subject to VAT at 5%, in the same manner as other Services or work carried out on Goods in the KSA. There is no Supply of the underlying Goods (feedstock or electricity) in these cases for VAT purposes.

(38) Article 23, Date of Tax Due on Supplies of Goods and Services, Unified VAT Agreement

(39) Article 20 (1), Date of Supply in specific circumstances, Implementing Regulations.

(40) Article 20 (2), Date of Supply in specific circumstances, Implementing Regulations.

6.3. VAT Considerations for Small Generation Facilities

Small generation facilities include facilities with a capacity less than 30MW, and are subject to different regulatory requirements⁽⁴¹⁾. These are often cogeneration facilities, renewable facilities or other onsite power generation facilities, which may be directly connected to a specific facility (rather than providing electricity to the Electricity Distribution System).

Cogeneration is the simultaneous production of electricity and by-products (such as steam, heat or the use of these products in desalination process). Renewable Generation projects rely more on the use of natural energy sources to generate power such as the wind, solar energy and waste-to-energy technology. These technologies are important to diversify generation sources and maximise efficiency of electricity generation.

Electricity consumers who own onsite renewable or other small generation facilities will generally consume the energy produced, but in some cases may also be able to Supply excess electricity back to the Electricity Distribution System.

6.3.1. Application of VAT to onsite generation

As for other generation methods, VAT is charged on the Supply of electricity generated from a Generation or Cogeneration facility. If a Generation facility makes a charge to a third party for a by-product of Cogeneration, this is also a Taxable Supply of that by-product.

The consumption of power generated by a Taxable Person who generated it, or the consumption of by-products from a Cogeneration facility by the owner of that facility, is not a Supply for VAT purposes and does not result in VAT consequences.

If a generating facility is wholly operated for the owner's consumption, the eligibility for deduction of VAT incurred on the costs of generation will be determined based on whether that electricity is used for taxable purposes. See chapter 8 for general information on Input Tax deduction.

Example (11): An industrial factory in the Eastern Province builds a small gas-powered generating facility next to its premises. The generating facility will connect directly to the factory, and will Supply all power for the factory's own consumption. The factory is used to manufacture products which are sold as Taxable Supplies in the KSA.

The factory does not make a Supply when it consumes the power generated by its own facility. It is able to deduct VAT incurred on the construction and operational costs of the generating facility, as these costs form part of the business's overall Economic Activity which constitutes making Taxable Supplies.

6.3.2. Supply of Electricity by Consumers to the Electricity Distribution System

Electricity consumers who have an excess of electricity from onsite generation facilities may, subject to regulatory considerations conveyed by the competent Authority, be able to Supply (referred to in the sector as "export") this energy from their premises to the Electricity Distribution System, for use by other consumers. Note that the term "export" in this case is different from the defined VAT term of an "Export of Goods" (concerning a movement of Goods to a place outside of the KSA).

(41) Article 6, Implementing Regulations to Electricity Law

The VAT consequences of this will be as follows:

- If the consumer is paid a monetary consideration for the “exported” electricity, this will be consideration for a Supply of Goods by that consumer. If the consumer is a Taxable Person, he will be required to charge VAT.
- If the consumer is allowed a reduction or offset to the invoice for electricity supplied to him from the Electricity Distribution System, this is an example of a barter transaction. In this case, both the electricity Supplier and the electricity consumer make Supplies of Goods. If the consumer is a Taxable Person, he must charge VAT on the Supply of Goods.

Example (12): Ahmed installs solar panels at his home. His utility provider agrees to provide an offset to any excess renewable power, at SAR 0.27 per KWh, a rate determined by the competent Authority.

During October 2021, Ahmed incurs regular supply charges of SAR 130 (excluding VAT) for connection charges and energy consumed from the Electricity Distribution System. These must be subject to VAT in full, and the Supplier must report Output VAT of SAR 6.50. Ahmed also generates 160 KWh of excess solar energy. However, Ahmed is not a Taxable Person as the value of his Supplies of solar energy do not exceed the Mandatory Registration Threshold, and therefore he is not required to charge VAT on the excess energy supplied.

This can be displayed on the invoice as follows:

Supply charges, 1/10/21 to 31/10/21	SAR 130.00
VAT at 5%	SAR 6.50
Sub-total	SAR 136.50
Offset for excess solar power generated 160KWh @ SAR 0.27	(SAR 43.20)
Total due for payment	SAR 93.30

6.4. VAT Considerations for Transmission

The Supply of the transmission of electricity is the transportation of Goods for VAT purposes, whether this is carried out by a Transmission Licensee through the Transmission System, or locally from a small generating facility to a consumer.

The transmission of electricity within in the Kingdom by a Taxable Supplier shall be treated as a Supply of transportation Services and shall be subject to VAT at the rate of 5%. Please refer to section 4.5 above for more details on the Place of Supply in other cases.

A company acting as a transmission Supplier may make other charges, such as for transmission capacity or for access to the Transmission Network. These charges are also treated as Supplies of Services for VAT purposes, and are subject to VAT at 5%.

6.5. VAT Considerations for Trading

Trading activities involve the purchase and sale of electricity on the wholesale market by persons who do not generate or consume the electricity.

An electricity trade generally involves the delivery of a certain quantity of power on a specified

date (for example, a spot trade under which the power is transferred on the agreement date). The consideration paid for the power is subject to VAT, on the earlier of the date of delivery of power, the date of issuance of the Tax invoice or upon partial or full receipt of the Consideration, whichever is earlier, and to the extent of the received amount.⁽⁴²⁾

6.5.1. Trading of Electricity Derivatives

Commodity derivative contracts can also be entered into with electricity being the underlying commodity. This could include, for example, a forward or futures contract, or an option. Commodity derivatives are often entered into by a trader as a financial derivative, without any intention of the trader purchasing or selling the underlying commodity.

Any explicit fee (or “premium”) paid to enter into a commodity derivative contract is consideration for a Taxable Supply, provided that contract allows for delivery of the electricity to take place at a delivery point in the KSA.

A forward or futures contract remains in place until:

- The contract is exercised – at which point the power is physically supplied on the nominated date. VAT is due on the Supply of the power if delivered in the KSA.
- The contract is cancelled, either by cancellation of the original contract, or entering into an equal and opposite contract to offset the trade. In this case, no Supply of the underlying Goods takes place. Any Output VAT already accounted for regarding the Supply of power may be adjusted in accordance with the adjustment rules for a cancelled Supply⁽⁴³⁾. Any premium paid to enter the contract is not cancelled.

A financial derivative contract may have a commodity such as electricity as its base price, but its terms do not allow for the electricity to be delivered. Any consideration paid to enter these “non-deliverable” contracts are not for the underlying Goods. Profits earned by traders on a financial derivative are exempt from VAT.

Traders who enter into financial contracts must also consider the effect of Exempt Supplies on Input Tax deduction and the appropriate method for proportional deduction. Please see the guidelines on financial Services and Input Tax deduction for further information.

(42) Article 23, Date of Tax Due on Supplies of Good or Services.

(43) Article 27, Adjustment of Tax Value, Unified VAT Agreement

7. Common issues under Distribution or Retail contracts

This section covers some of the major issues for electricity and other utilities provided to consumers.

7.1. Application of VAT to Supplies of Goods and Services

The provision of Goods and associated Services for consumption under a utilities contract over a defined period is considered to be a “continuous” Supply. Therefore, VAT becomes payable based on each progressive payment, according to the following rule:

- Where a utility contract includes a set installment amount with a due date for each period’s installment, VAT becomes payable on the due date or the date of actual payment, whichever comes first.⁽⁴⁴⁾
- In all other cases, VAT becomes payable on the date of issuing the invoice or the date of actual payment, whichever comes first.⁽⁴⁵⁾

In general, the Supply of the underlying utility (such as electricity, water, gas) and associated Services under Distribution contracts by a Taxable Supplier to a Customer in KSA shall be subject to VAT at the rate of 5%. Examples of associated services are:

- Additional charges for provision of secure supply capacity, or emergency supply capacity;
- Periodic supply charges (e.g. a daily or monthly charge not linked to the volume of consumption)
- Waste water disposal Services;
- Network connection, re-connection or disconnection;
- Installation of equipment such as meters; and
- Repair and maintenance to a customer’s equipment.

7.2. Retrospective discounts

If a discount to the Consideration payable is provided after a Tax Invoice has been issued by the Supplier, the Supplier must issue a credit note to record the change to Consideration (subject to the special cases outlined in section 7.3 below). A retrospective discount may also be described as a “cash rebate” – in cases where the Supplier repays any Consideration initially paid by the Customer.

In the event a credit note is issued, this will affect the calculation of the Supplier’s Output Tax and Customer’s Deductible Input Tax (in cases where the Customer is a Taxable Person). Please see the guideline on Invoicing and Records for more details.

(44) Article 20(1), Date of Supply in Specific Circumstances, Implementing Regulations.

(45) Article 20(2), Date of Supply in Specific Circumstances, Implementing Regulations.

7.3. Special case: Adjustments reflected in current invoices

Often, a Supplier of electricity, water or other utilities will issue a Tax Invoice for a period based on the estimated usage during that period. Estimated billing may arise where the Supplier does not have exact usage data from the customer's meter reader for a completed billing period. The estimate of the Customer's usage for that period is often based on its property's previous usage pattern.

In the utilities sector, an adjustment may also be made to a current utilities invoice in cases where an earlier invoice was issued based on incorrect data (such as from an incorrect meter reading or incorrect pricing information). This is instead of issuing a credit note or debit note to adjust the consideration payable for the earlier Supply.

7.3.1. Estimated billing

The invoice based on estimated consumption remains due for payment, but the actual consumption will be monitored at the next time the Supplier obtains exact usage data (for example, on the next meter reading). In order to reflect this actual usage, it is common commercial practice in the utility sector to make an adjustment to the consideration payable in the invoice raised for the next billing period, instead of correcting the tax invoice already raised for the earlier billing period:

- This may take the form of a credit or debit to the next bill to adjust the difference between actual and estimated usage; or
- If meter readings are taken over a longer period (and less frequently than each billing period), the tax invoice issued after the actual meter reading is taken will be based on the actual usage during the longer period, less the estimated usage to date.

7.3.2. Correction of Output Tax for adjustments

For VAT purposes, if VAT has already been reported on the Supply in a prior Tax return based on the original consideration, an adjustment to Output Tax should be made:

For an upwards adjustment to Output Tax	In the Tax Period in which the change to consideration occurred ⁽⁴⁶⁾
------------------------------------------------	---------------------------------------------------------------------------------

Provided that the tax invoice for the initial period is based on an accurate estimate based on the information held at the time, and creates an obligation for the Customer to make payment based on that estimated amount, GAZT accepts that the change to consideration takes place when the Supplier obtains the actual or updated data and advises the Customer of the change to consideration.

In these cases, Output Tax on the Supply of utilities in the earlier billing period should therefore be adjusted in the Tax Period in which the billing adjustment is made.

For a downwards adjustment to Output Tax	In the Tax Period in which the change to consideration occurred, or the credit note was issued to the Customer, whichever is later ⁽⁴⁷⁾ .
-------------------------------------------------	------------------------------------------------------------------------------------------------------------------------------------------------------

(46) Article 40 (4), Adjustment to value of a Supply, Implementing Regulations.

(47) Article 40 (5), Adjustment to value of a Supply, Implementing Regulations.

If the downwards adjustment to consideration is carried out through an adjusted invoice for a subsequent billing period (instead of by issuing a credit note to adjust the earlier period), the Output Tax is effectively adjusted when the Output Tax is reported in respect of that adjusted invoice.

Example (13): The Electricity Supply Company (ESC) supplies electricity under a contract to the business office of Crown Office Services in Dammam. Due to a technical problem, ESC is unable to take a meter reading of actual consumption in the month of September 2019. In line with its supply contract, it therefore issues an electricity bill on 30 September 2019 based on estimated usage for the month of 120KWh, (calculated from previous usage by Crown Office Services in previous months). The bill is for SAR 360, plus VAT of SAR 18.

On 31 October, ESC is able to take a meter reading of the actual electricity consumption for the two months of September and October 2018, being a total of 150KWh in that two-month period. From this data, it is likely that usage for the September bill was over-estimated. However, in line with commercial practice, ESC effectively reflects adjustments into the October bill (it charges for the additional 30 KWh only) and does not adjust the estimated invoice issued in September.

In this case, the Taxable Supplier (ESC) is not required to retrospectively adjust the Output VAT in the September Tax Return. Instead, it applies VAT to the October invoice as usual, at the standard rate of 5%. This way, the actual electricity consumption for the two months of September and October 2018 is subject to VAT in line with the existing commercial practice for estimating actual usage and issuing invoices.

If the Customer is a Taxable Customer and receives a credit note to reflect a downwards adjustment to consideration, the Taxable Customer must adjust any Input Tax deduction made on the original invoiced amount.

7.4. Discounts for Prompt Payment

A Supplier may offer a discount to Customers on a Supply of Goods or Services, on the condition that the Customer makes payment for the Supply before a certain date. In cases where the Customer makes early payment and the discount is given, the Output VAT reported and the tax invoice documentation issued by the Supplier should reflect the discounted Consideration paid.

If a Tax Invoice has already been issued showing VAT based on the non-discounted Consideration, a credit note must be issued to reflect the discount to Consideration.

7.5. Late payment charges

A utilities Supplier may often impose an additional charge or administrative fee to a Customer who does not make payment of their invoice within the time specified.

This charge will generally be consideration for Goods or Services provided by the Supplier. Depending on the exact arrangements, this may be:

- An increased charge for the Goods and Services provided under the utilities contract – this is additional consideration for the underlying Supplies, which is subject to VAT at 5%.
- An administrative charge for the Supplier to pursue, collect and administer overdue amounts – this is a separate Service, which is subject to VAT at 5%.
- An explicit amount (such as a fixed fee or fixed percentage of the amount due) for the extension of the repayment facility – this is a financial Service with an explicit fee, which is subject to VAT at 5%.

In some cases, a Supplier may charge an implicit margin on an overdue amount (this will be VAT exempt), or may seek compensation for actual or punitive damages caused by the late payment (this would not be subject to VAT). These cases are not expected to be common in practice within the sector. GAZT expects that late payment charges will be charged with 5% VAT: a Supplier adopting a different treatment should retain clear evidence to support this treatment.

7.6. Security Deposits

A security deposit is a common commercial arrangement in the sector whereby an amount of money is held by a Licensed Distributor or Retailer as a security measure (for example, against Customer default or damage).

The treatment of deposits is not explicitly considered within KSA VAT laws, but any payment of an amount which is Consideration for a Supply results in the Date of Supply occurring, and the corresponding tax becoming due (to the extent of that payment)⁽⁴⁸⁾.

GAZT's interpretation is that a security deposit that is available for use by the Supplier and is able to be applied to Taxable Supplies of utilities is consideration for future Taxable Supplies. VAT should be applied to the deposit at 5% and reported as Output VAT.

However, if the Supplier:

- holds the security deposit with a third party or in another separate account; and
- is not contractually able to use the security deposit funds, or apply these to Taxable Supplies, until a specified default event;

GAZT accepts that the payment of the security deposit is not consideration for the Taxable Supplies. In these cases, VAT will only become due from the time the deposit becomes available for use by the Supplier.

If a separately held security deposit of this type is returned without being applied to Taxable Supplies, the return of the funds does not have VAT effects for the Supplier or Customer.

Example (14): The Electricity Supply Company (ESC) takes a security deposit of SAR 500 from a new residential customer on 1 January 2020. Under its contract, it must hold these funds in a separate account and is unable to use these unless the customer is in default by 20 days or more, or the customer agrees for these to be applied against ESC's Supplies.

The receipt of the security deposit is not consideration for a Supply by ESC. At the end of a twelve-month period, ESC agrees to remove the security deposit. On 3 January 2021, the customer agrees to offset the next invoice payable (SAR 315 for electricity usage in December), and have the rest repaid in cash. For VAT purposes, the payment of SAR 315 consideration by the Customer takes place on 3 January 2021. The return of the remaining SAR 185 to the Customer is not subject to VAT.

(48) Article 23(1), Date of Tax Due on Supplies of Goods and Services, Unified VAT Agreement

7.7. Prepayment meters

Prepayment meters are a method of paying for energy whereby customers put credit on their account before using energy, instead of receiving periodic invoices after the usage.

The payment of credit on a prepayment meter, or any similar mechanism whereby the customer is required to pay in advance for future Taxable Supplies, is consideration for the Taxable Supplies made by the Supplier.

The Supplier must account for the corresponding VAT amount on the date the payment is made, and issue a tax invoice within fifteen days of the month in which payment takes place.

7.8. Payment of additional consideration

In cases where a Customer makes multiple payments against a Supplier invoice in error, or in other cases where a customer makes payment of additional consideration to the Supplier which cannot be attributed to a future Supply, the receipt of this payment is not consideration for a Supply.

Example (15): On 2 January 2020, the Water Supply Company issues an invoice for SAR 420 to Samir Clothing Company for water supply during the fourth quarter of 2019. The finance clerk receives the invoice and makes payment in full on 6 January. The business owner sees the charge on his online account and makes another full payment on 7 January. There are no other amounts due to the Water Supply Company, so the Supplier retains the credit balance on the account until an invoice is issued in the next quarter.

The second payment is made in error and is not a deposit for a future Supply. VAT becomes due at the time the next tax invoice is issued.

7.9. Compensation paid to customers

A Supplier may choose to offer a discount to customers as a gesture to reflect a small inconvenience, such as an incorrect invoice or small disruption to Supply. These are generally treated as an adjustment to consideration for the Supply.

However, in other circumstances, Customers may be contractually entitled to claim compensation for losses caused by a fault or error of the Supplier, such as lost revenues from power outages, or damages to property caused by a power surge. For VAT purposes, such claims are not subject to VAT as they do not constitute a Taxable Supply. Further, the payment of compensation by the Supplier does not reflect an adjustment to the consideration payable for Goods or Services provided by the Supplier in the past or in future.

Example (16): Advanced Laboratories has a power supply contract with the Electricity Supply Company. In April 2021, Advanced Laboratories has suffered lengthy power disconnection and damages to its electrical hardware due to a power surge. The entity has submitted a claim to the Taxable Supplier for actual damages incurred. In May 2021, ESC agrees to compensate the Customer SAR 2,500 for all the damaged electrical equipment.

This payment of compensation should not be subject to VAT as it is not consideration for a Taxable Supply made by either Advanced Laboratories or ESC for VAT purposes. This does not result in any adjustment to ESC's Output VAT on Supplies of utilities.

7.10. Adjustment for non-payment ('Bad Debts')

In cases where a Taxable Supplier does not receive all or part of the Consideration for a Taxable Supply made by him, a Supplier who has taken usual commercial measures to collect the debt

might elect to “write off” the amount owed by the Customer as a “bad debt” for accounting purposes. This is an accounting process, which does not change the Consideration payable for the Supply: the debt will technically remain owing by the Customer.

A relief exists for debts that are written off by a Supplier in this way. The Taxable Supplier may reduce his Output VAT for the VAT amount calculated on the Consideration not paid in the Tax Return in which all of the following conditions are met:

- “the Taxable Person has previously included Tax calculated on the Taxable Supply as Output Tax on a Tax Return and made payment of the Tax due,
- the Consideration is in respect of a Supply of Goods or services made to a Person who is not a Related Person,
- a period of at least twelve months has passed from the date of the Taxable Supply,
- the Taxable Person holds a certificate from his certified accountant indicating that the unpaid Consideration has been written off in his books,
- in cases where the total amounts unpaid by the Customer exceed one hundred thousand (100,000) riyals, formal legal procedures have been taken to collect the debts without success and the Taxable Person can provide evidence of these procedures, such as the issuance of a judicial ruling, evidence of the debtor’s bankruptcy or a court order initiating any other formal recovery procedure.⁽⁴⁹⁾”

The adjustment should be recorded in the VAT return for the first Tax Period in which all of the conditions specified are met.

If, subsequent to an adjustment to the Supply value is made according to the above conditions, the Taxable Supplier receives the full or part of the Consideration, the VAT calculated on the subsequent Consideration will become payable and must be accounted for in the VAT return for the Tax Period in which the payment occurs. A new Tax invoice must be issued to reflect the additional amount received.⁽⁵⁰⁾

(49) Article 40 (7), Adjustment to value of Supply, Implementing Regulations. This relief is not available for any supplier using the cash accounting basis to report VAT.

(50) Article 40 (9), Adjustment to value of Supply, Implementing Regulations.

8. Input VAT Deduction

8.1. General Provisions

A VAT registered person may deduct Input VAT charged on Goods and Services it purchases or receives in the course of carrying on its Economic Activity. Input VAT may be deducted on:

- VAT charged by a VAT-registered Supplier in the KSA;
- VAT self-accounted by the VAT-registered Taxable Person under the Reverse Charge Mechanism; or
- Import VAT paid to the Customs Department on Imports of Goods.

As a rule, input VAT which is related to the taxpayer's VAT exempted activities, such as Residential Real Estate, is not deductible as input VAT.

In addition, input VAT may not be deducted on any costs not incurred as part of the Economic Activity (including some blocked expenditure types such as entertainment and motor vehicles), or on any costs which relate to making Exempt Supplies.⁽⁵¹⁾

This input VAT is a credit entered on the VAT return which is offset against the VAT charged on Supplies (output VAT) made during that period.

Input VAT may only be deducted where the Taxable Person holds a tax invoice, or sufficient evidence of the amount of Input VAT paid or payable if approved by GAZT.⁽⁵²⁾

8.2. Proportional Deduction Relating to Input VAT

VAT incurred which relates to a taxpayer's VAT exempt activities, such as exempt financial Services or residential rental, is not deductible as Input VAT. A person making both Taxable and Exempted Supplies, can only deduct the Input VAT related to the Taxable Supplies. If a Taxable Person incurs general costs or expenses (overheads) in the making of Taxable Supplies, and others that are exempt from VAT, he must in that event split the costs and expenses precisely so as to specify those costs that relate to the Taxable Supplies. The input tax will be determined in accordance with the following rules:⁽⁵³⁾

Input VAT directly attributed to taxpayer's Taxable Supplies	Deduct in full
Input VAT directly attributed to taxpayer's Exempted Supplies	No deduction
Overheads and all other input VAT that cannot be directly attributed to Taxable Supplies	Partial deduction based on apportionment

A Prescribed default method of proportional deduction is calculated on the values of Supplies made in the year, using the following fraction:

(51) Article 50 (1), Goods and services deemed to be received outside of Economic Activity, Implementing Regulations.

(52) Article 49 (7), Input Tax Deduction, Implementing Regulations.

(53) Article 51, Proportional deduction of Input Tax, Implementing Regulations.

$$\frac{\text{The value of **Taxable Supplies** made by the Taxable Person in the last calendar year}}{\text{The total value of **Taxable Supplies** and **Exempt Supplies** made by the Taxable Person during the last calendar year}}$$

The fraction for the default method does not include Supplies of Capital Assets made by the taxpayer, as these distort the use of input VAT.

Alternative attribution methods, using other calculation approaches than the value of Supplies, may be approved with GAZT in cases where these better reflect the actual use of VAT incurred. Further information about deduction of VAT and proportional VAT recovery are provided in a separate guideline.

9. VAT obligations of the Taxable Person

A Taxable Person must evaluate its tax obligations and comply with the conditions and obligations relating to VAT. This includes registering for VAT as necessary, and exactly calculating the net amount of VAT payable, and paying the tax at the time due, as well as keeping all necessary records and cooperating with officials of the Authority on demand.

If a Taxable Person is not sure of its obligations, it must contact the Authority through its website at vat.gov.sa or by other means of communication, and may also seek external consultation through a qualified consultant. There follows below a review of the most important tax obligations provided for in the Law and the Implementing Regulations.

9.1. Issuing Tax Invoices

A Supplier must issue a Tax Invoice for each Taxable Supply made to any VAT-registered person or to any other legal person, or issue a simplified invoice in the event that the value of the Supply is less than SAR 1,000, or for Supplies made to the end consumer, by no later than fifteen days following the end of the month in which the Supply is made.

The Tax Invoice must clearly detail information such as the invoice date, Supplier's tax identification number, taxable amount, tax rate applied, and the amount of VAT charged⁽⁵⁴⁾. If different rates have been applied to Supplies, the value of each Supply at each rate must be separately specified, as well as the VAT applicable to each rate. A Tax Invoice may be issued in the form of a commercial document, provided that document contains all of the requirements for the issuing of Tax Invoice as set out in the Implementing Regulations to the Law⁽⁵⁵⁾.

9.1.1. Third party billing

A third party may issue Tax Invoices for Taxable Supplies provided when the following conditions are met:

- A Taxable Supplier should provide the Taxable Supplies to their Customer. In this case, the third party issues the invoice on behalf of the Taxable Supplier.
- The details of the Supplier, including the Tax Identification Number, must be disclosed on the invoice, and it should be clear that that Supplier issues the Tax Invoice in respect of a Supply. The third party should not include its Tax Identification Number on the invoice (and is not required to disclose any of its details on the invoice).
- The Taxable Supplier must not issue a Tax Invoice for a Supply if a third party has issued a Tax Invoice on its behalf for the same Supply.
- Obtaining the approval of the concerned Tax authority and provided that all the obligations provided for in the Unified VAT Agreement and the Local Law are fulfilled⁽⁵⁶⁾. For Supplies made in the KSA, GAZT approves the use of billing by third parties provided that the conditions in this notice are met unless it rejects the notification provided to it by the Supplier and third party.
- The Supplier shall be responsible for the accuracy of the information shown on the Tax Invoice and for reporting Output Tax on the Supply⁽⁵⁷⁾.

(54) For more details on the requirements for issuing tax invoices, refer to the published Invoicing & Records guideline and Article 53, Tax Invoices, Implementing Regulations

(55) Article 53, Tax Invoices, Implementing Regulations

(56) Article 58(2), Special Provisions, Unified VAT Agreement

(57) Article 53(3), Tax Invoices, Implementing Regulations

- Both the Supplier and the third party (if registered for VAT purposes) should notify GAZT with their agreement through the procedure as specified by GAZT and subject to any further conditions as GAZT may determine. If GAZT rejects this notification, the third party must not issue tax invoices on behalf of that Supplier.

Further information on the requirements for tax invoicing can be found in the Taxpayer guideline on Invoicing and Records.

9.2. Filing VAT Returns

Each VAT registered person, or the person authorised to act on his behalf, must file a VAT return with GAZT for each monthly or quarterly tax period. The VAT return is considered the Taxable Person's self-assessment of tax due for that period.

Monthly VAT periods are mandatory for Taxable Persons with annual revenues exceeding SAR 40 million. For all other VAT registered persons, the standard tax period is three months.

The VAT return must be filed, and the corresponding payment of net tax due made, no later than the last day of the month following the end of the tax period to which the VAT return relates.

More information on filing of VAT returns is provided in a separate guideline.

If the VAT return results in VAT due to the taxpayer, or if the taxpayer has a credit balance for any reason a request for a refund of this VAT may be made after the filing of the VAT return, or at any later time during the next five years by filing a request for a refund to the Authority. GAZT will review these requests and will pay the amount due on refund requests that have been approved, directly to the taxpayer⁽⁵⁸⁾.

9.3. Keeping records

All taxpayers are required by law to keep appropriate VAT records relating to their calculation of VAT for audit purposes. This includes any documents used to determine the VAT payable on a transaction and in a VAT return. This will generally include:

- tax invoices issued and received;
- books and accounting documents;
- contracts or agreements for large sales and purchases;
- bank statements and other financial records;
- import, export and shipment documents; and
- other records relating to the calculation of VAT

Records may be kept in physical copy or in some cases electronically – but must be made available to GAZT on request.

All records must be kept for at least the standard retention period of 6 years. That minimum period for retention is extended to 11 years in connection with invoices and records relating to movable capital assets, and 15 years in connection with invoices and records relating to non-movable capital assets⁽⁵⁹⁾.

(58) Article 69, Refund of overpaid Tax, Implementing Regulations

(59) Article 66, Records, Implementing Regulations, and Article 52, Capital Assets, Implementing Regulations

The Taxable Person may appoint an Agent or other third party to comply with its record storage requirements. The Taxable Person in all cases remains directly responsible for such compliance⁽⁶⁰⁾.

9.4. Certificate of registration within the VAT system

A resident person who is subject to VAT and registered with the Authority in the VAT system must display a certificate to the effect that he has been registered in the VAT system in a place visible to the public at his main Place of Business and at all his branches.

In the event of a contravention, the person in breach will be liable to the penalties provided for in the Law.

9.5. Correcting past errors

If a Taxable Person becomes aware of an error or an incorrect amount in a filed VAT Return, or of any other non-compliance with the VAT obligation, he should notify GAZT and correct the error by amending VAT the tax return. Errors resulting in a net understatement of VAT (exceeding SAR 5,000) must be made known to GAZT within twenty (20) days of detecting the error or incorrect amount, and the previous return must be amended. In connection with minor errors resulting in a difference of less than SAR 5,000, the error may be corrected by amending the net tax in the subsequent tax return⁽⁶¹⁾.

Further information on correcting errors can be found through vat.gov.sa and in the separate guideline on examination, assessment and correction.

(60) Article 66(4), Records, Implementing Regulations

(61) Article 63 [Correction of Returns], Implementing Regulations.

10. Penalties

The Authority may impose penalties or fines on taxpayers for violations of VAT requirements set out by the Law or Implementing Regulations.⁽⁶²⁾

Description of offence	Associated fine
Submitting false documents with the intent of evading the payment of the VAT due or to reducing its value	<ul style="list-style-type: none"> • At least the amount of the VAT due • Up to three times the value of the goods or services
Moving goods in or out of the Kingdom without paying the VAT due	<ul style="list-style-type: none"> • At least the amount of the VAT due • Up to three times the value of the goods or service
Failure to register for the VAT in the allotted timeframe	SAR 10,000
Filing incorrect tax return, amend a tax return after submission or filing any VAT document with the Authority resulting in a lower amount due	Equal to 50% of the value of the difference between the calculated Tax and Tax due
Failure to file VAT return in time	5%-25% of the VAT in respect of which the return should have been filed
Failure to pay the VAT in time	5% of the VAT due for each month or part thereof
Collecting VAT without being registered	Up to SAR 100,000
Failure to maintain books and records as stipulated in the regulations	Up to SAR 50,000
Preventing GAZT employees from performing their duties	Up to SAR 50,000
Violating of any other provision of the VAT regulations or the VAT law	Up to SAR 50,000

In all cases, if a violation is repeated within three years from the date of issuing the final decision of the penalty, the Authority may double fine for the second offense.

The level of the penalty or fine imposed is set by GAZT with regard to the taxpayer's behaviour and compliance record (including taxpayers meeting their requirements to notify GAZT of any errors and provide co-operation to rectify mistakes).

(62) Chapter Sixteen: Articles (39), (40), (41), (42), (43), (44), (45), and (47), [Tax Evasion and Penalties], VAT Law.

11. Applying for the issue of rulings (interpretative decisions)

In the event that you are not sure about the manner of application of VAT to a particular activity or particular transaction that you are doing or intend to do, after referring to the relevant provisions and the relevant guideline, you may submit an application to the Authority to obtain a ruling. The application should set out the full facts relating to the particular activity or particular transaction on which you are asking the Authority to express its view.

A reply to a request for a ruling may be either:

- Public, in which event the Authority will publish details of the ruling, but without referring to any private particulars relating to the individual taxpayer, or
- Private, in which case the Authority will not publish the ruling.

Neither a public nor a private ruling issued by the Authority will be treated as binding on it or upon the taxpayer in connection with any transaction that he performs, and it shall not be possible to rely on it in any manner.

The Authority is not obliged to respond to all requests for rulings, and it may review all requests and specify priorities based on certain elements, including:

- The level of information submitted by the taxpayer in the request,
- The potential benefit to taxpayers as a whole on the issuing of a general ruling concerning some transaction or activity,
- Whether there is an existing law or guide dealing with this request.

12. Contacting us

For more information about VAT treatment, kindly visit our website: vat.gov.sa; or contact us on the following number: **19993**

13. Common Questions & Answers

1. Can input VAT incurred on utility Supplies such as electricity and water be deducted?

Yes, to the extent these utilities are used for Taxable activities.

The VAT charged may be deducted in the Tax Return if it is incurred in the course of carrying out the economic activity which constitutes making Taxable Supplies. Any Goods and Services intended for personal use and not for the business or economic activity should not be deducted. To correctly evidence the deduction, the utility bill should be in the name of the Business.

2. Are water and electricity service bills from a State-owned supply company subject to VAT?

Yes, utility bills from a public or private Supplier are subject to 5% VAT.

3. Is a new generation company able to register for VAT before generation commences?

Yes, if the company's expenses exceed the Optional VAT Registration threshold. Input VAT deduction is available on any expenditure intended for use in making Taxable Supplies of electricity.

4. A generation company has an Import licence, and therefore Imports equipment on behalf of its Supplier, who will install the equipment as part of its Supply. Can the generation company deduct the VAT?

Yes, the generation company may deduct VAT on the Import of the Goods, on the assumption that the Goods are used to make Taxable Supplies of electricity. VAT is also likely to apply on the Supply of the Goods in the KSA: VAT deduction in respect of the Supply will also be determined based on the generation's company.

5. A supply company issues a tax invoice based on an estimated meter reading. Later, it takes an actual meter reading and is required to charge an additional amount in the next billing cycle. How does the supply company charge and report the VAT?

On the basis the first invoice (using estimated data) was issued in line with usual commercial practice, the supply company is able to charge VAT on the higher amount in the tax invoice for the next billing cycle. No adjustment is required for the Tax Return in which the original tax invoice was reported.

6. A manufacturing company builds a small electricity generation facility to use as backup and during peak load periods. It consumes all the power generated and does not make any Supply of electricity to other businesses. What are the VAT consequences?

The manufacturing company does not make any Supply of power for VAT purposes. It is entitled to deduct VAT incurred on construction and operating of the facility, provided the power is used in the course of making Taxable Supplies.



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