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Force majeure in the GCC
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Force majeure in the Gulf Cooperation Council (GCC)— Value Added Tax (VAT) implications businesses should not overlook



The recent increase in force majeure notices across the GCC has brought commercial disruption back into focus. For businesses operating in the region, the challenge is not only managing supply chains, contracts, and operations, but also ensuring that indirect tax outcomes are correctly assessed when performance is interrupted, delayed, or terminated.



Force majeure is primarily a contractual and legal concept. It may excuse, suspend, or delay a party's performance where an event beyond its control makes performance impossible. However, from a VAT perspective, the mere invocation of force majeure does not automatically alter the tax treatment of the underlying transaction. VAT follows the legal and economic substance of the arrangement, the nature of the supply, and the actual flow of consideration. This makes it essential for businesses to assess each impacted contract carefully and to align legal, commercial, accounting, and tax positions.



Why force majeure matters from a VAT perspective

In the GCC, VAT is generally transaction-based. That means the tax treatment depends on whether there has been a supply of goods or services, if consideration has been received, and whether any contractual adjustment changes the nature or timing of the transaction. A force majeure event, by itself, does not erase VAT liability or create an automatic right to reverse output tax. In certain cases, claims for Bad Debt Relief could be considered, which can present some different challenges.

This distinction is particularly important in long-term contracts, project-based arrangements, cross-border service models, and supply agreements involving advance payments or milestone billing. In such cases, businesses may need to determine if the disruption results in a mere delay, a partial supply, a cancellation, a re-performance obligation, or a termination payment. Each outcome may have a different VAT consequence.

For example, where a supplier has already issued a tax invoice and received payment in advance, a later force majeure event may require the parties to consider whether the supply was ultimately made, and if a credit note is needed. Similarly, if the customer pays a cancellation fee or termination charge, the tax treatment will depend on whether that amount is true compensation for loss or, in substance, consideration for a taxable supply.



The contractual position is not always the tax position

A common mistake is to assume that once a contract is suspended or terminated under a force majeure clause, the VAT position follows automatically. A contract may be discharged under governing law, but the tax treatment will still depend on the factual and legal character of the payment or adjustment.

This is especially relevant where the contract provides for liquidated damages, termination fees, standby charges, retention amounts, or mobilization costs. Some of these amounts may be outside the scope of VAT if they are genuinely compensatory. Others may be taxable if they are linked to the right to receive a supply, the availability of goods or services, or the exercise of a contractual option.

A payment described as “damages” is not necessarily outside the scope of VAT. Businesses should not rely solely on labels. They should examine the contractual mechanics, the commercial rationale, and the practical flow of funds.





Key VAT issues to assess

Has a taxable supply been made?

The first question is whether goods or services have been supplied, partially supplied, or not supplied at all. If goods were delivered before the disruption, VAT may already have been triggered, and any later force majeure event may not affect the original tax point. If services were provided over time and the disruption merely delayed completion, the VAT treatment may depend on the billing milestones, contractual performance terms, and the 'time of supply' rules.

Where the supply has not yet been made, the question shifts to whether any advance payment was already received and taxed. In many GCC VAT regimes, VAT can arise upon receipt of consideration or issuance of a tax invoice, depending on the circumstances. If the transaction is later canceled, the business may need to issue a credit note.

What happens if payments become unrecoverable?

A critical consideration for businesses is bad debt relief, particularly where force majeure leads to customer insolvencies, payment suspensions, or protracted disputes that render amounts uncollectible. GCC VAT laws generally provide bad debt relief mechanisms, allowing businesses to recover output VAT previously accounted for on supplies where payment proves irrecoverable after a specified period (typically 6-12 months, depending on the jurisdiction). Notably in the Kingdom of Saudi Arabia the Zakat, Tax and Customs Authority has onerous documentation requirements like initiating legal proceedings for recovery for debts greater than SAR 100,000. This relief is especially relevant in force majeure scenarios where counterparties face financial distress or government interventions disrupt normal payment cycles. Businesses should monitor overdue receivables diligently, maintain evidence of recovery efforts (demand letters, legal notices, insolvency filings), and apply for relief within statutory time limits to reclaim VAT cash flow. Failure to claim timely can result in permanent VAT leakage on disputed amounts.

What is the nature of the payment on termination?

A payment that genuinely compensates one party for loss may be 'outside the scope' of VAT. However, a payment that secures the release of a party from an obligation, or that compensates the supplier for making resources available, may be treated as consideration for a taxable supply.

This distinction often becomes important in force majeure situations where a contract is terminated early, a project is abandoned, or a customer cancels an order after the supplier has already incurred costs. The analysis should focus on whether the payment is linked to a supply or whether it is genuinely a damages payment with no direct connection to a taxable supply.

What is the nature of the payment on termination?

Force majeure can disrupt the normal use of goods or services acquired for the business. This raises questions about input VAT recovery, especially where the related project is delayed, suspended, or cancelled.

In principle, input VAT recovery should be assessed based on the intended use of the cost at the time it was incurred, subject to the applicable local rules. If the expense was incurred for taxable business activities, recovery may still be available even if the project is later interrupted. However, if the underlying activity becomes exempt, non-business, or otherwise outside the scope of VAT recovery, adjustments may be necessary.

This is particularly relevant for sectors such as construction, energy, logistics, manufacturing, and infrastructure, where significant costs are often incurred before revenue is fully realized.

Are cross-border and customs issues involved?

Many GCC businesses operate across borders or rely on imported goods, offshore services, or regional supply chains. A force majeure event may cause goods to be rerouted, delayed at customs, returned to origin, or held in transit. That can create VAT and customs consequences in addition to the commercial impact.

Businesses should review if import VAT was triggered, confirm the validity of export, assess whether goods were re-exported, and evaluate any impact on VAT recovery or refund claims.



Practical areas of risk

The most common risk is delayed action, which may result in penalties, denial of input VAT recovery, or reassessment by the tax authority. Businesses often focus first on the commercial and legal consequences of force majeure and only later consider the VAT implications. By that stage, invoices may already have been issued, payments received, accounting entries posted, and tax returns filed.

That creates several risks:

- Output VAT may have been overdeclared or underdeclared.
- Credit notes may not be raised correctly or on time.
- Bad debt relief claims may be missed or filed late.
- Input tax may be claimed or reversed incorrectly.
- Accounting and tax treatment may diverge.
- Documentation may be insufficient to support the position taken.

A further issue arises where multiple contractual documents interact, such as master service agreements, purchase orders, side letters, and variation orders. In a force majeure scenario, these documents may not all be amended consistently, leading to ambiguity over what exactly was canceled, postponed, waived, or re-priced. That ambiguity can create VAT uncertainty, and inconsistencies across these documents may undermine the defensibility of the VAT treatment adopted.



Governance and documentation

In a force majeure environment, documentation is often the difference between a defensible tax position and a disputed one. Businesses should ensure that the commercial, legal, operational, and tax teams are aligned from the outset.

At a minimum, companies should retain:

- Force majeure notice and response correspondence
- Relevant contractual clause relied upon
- Evidence of the disruptive event and its impact on performance
- Documentation of any renegotiation, suspension, or termination
- Refund, credit note, and payment records
- Bad debt recovery documentation (e.g. demand letters, legal notices, insolvency evidence)
- Accounting entries and management approvals
- Tax analysis supporting the treatment adopted

Where the event affects large contracts or high-value projects, businesses should also create a clear internal memo setting out the tax logic, the facts considered, and the decision taken.

A practical framework for businesses

A disciplined response to force majeure should follow a simple framework.

- 1 Identify** all impacted contracts and classify them by risk level, value, jurisdiction, and VAT sensitivity.
- 2 Determine** whether the disruption has resulted in delay, partial supply, cancellation, suspension, or termination.
- 3 Analyze** the payment profile, including advance payments, deposits, milestone invoices, cancellation charges, potential bad debt exposures and refunds.
- 4 Determine** whether any tax invoice, credit/debit note, return amendment, or bad debt relief is required.
- 5 Validate** the documentation and ensure the legal and tax positions are consistent.
- 6 Consider** whether any cross-border, customs, or input VAT adjustment is needed.

This approach helps businesses move from reactive problem-solving to controlled tax governance. It also reduces the risk of disputes with tax authorities or counterparties.

Conclusion

Force majeure may provide commercial relief, but it does not eliminate VAT responsibility. Businesses operating in the GCC should treat every force majeure event as both a legal and a tax event. The correct VAT outcome will depend on the facts, the wording of the contract, the nature of the payment, and the documentary trail supporting the adjustment.

For indirect tax teams, the priority is clear: Review the contract, test the transaction, assess the payment, monitor bad debt exposures, and align the VAT treatment with the underlying substance. Businesses that act early and document carefully will be better positioned to manage disruption while preserving VAT compliance and protecting cash flow.

About the Indirect Tax Team

Deloitte's Middle East Indirect Tax practice advises businesses across the region on VAT, customs, and related indirect tax matters. We support clients in navigating complex transactions, regulatory change, and compliance risk across all major Middle East jurisdictions.

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