

VAT treatment of the Integrated Single Electricity Market (I-SEM)

This document should be read in conjunction with section 31 of the Value-Added Tax Consolidation Act 2010 (VATCA 2010)

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Introduction

This guidance sets out the VAT treatment of the Integrated Single Electricity Market (I-SEM). The new treatment is effective from the I-SEM go live date of 1st October 2018.

There is existing guidance on the VAT treatment of the Single Electricity Market (SEM) which will continue to apply until activity and settlement under the SEM ceases. This guidance is included in [Appendix 1](#).

This guidance sets out the joint position of the Revenue Commissioners and the HM Revenue & Customs ('HMRC') solely in relation to the VAT treatment of the market functions which will be operated by SEMO under the I-SEM (i.e. settlement of the Capacity Market, the Balancing Market and imbalances). It does not address the forward contracts market, the Financial Transmission Rights Market, Day-Ahead Market or the Intraday Market, none of which will be operated by SEMO.

Market participants may rely on this guidance for their own VAT accounting purposes. However, where both market participants are established for VAT purposes in the same EU Member State (other than Ireland or the UK) or the purchasing party is established in a jurisdiction outside the EU, such participants should seek taxation advice where they have any doubts over the correct taxation treatment to be applied.

The VAT treatment set out in this guidance will be subject to a review five years after commencement of the I-SEM or sooner in the event of any material changes in the meantime.

1. Background

The European Union ('EU') is implementing the European Electricity Target Model ('EETM') which will harmonise the cross-border supply of electricity within the EU with the aim of providing an affordable and secure supply of electricity. In order to meet the requirements of the EETM, the governments of both Ireland and Northern Ireland have requested the development of new wholesale electricity market arrangements which will form the Integrated Single Electricity Market (I-SEM) on the island of Ireland.

1.1. Who operates the I-SEM?

The settlement of the Balancing and Capacity markets and imbalance volumes in the I-SEM will be operated by Single Electricity Market Operator ('SEMO') which is a joint venture between EirGrid plc and SONI Limited.

1.2. What will change?

Many aspects of the existing market will continue in the I-SEM. Under the existing SEM the VAT due on supplies of electricity is accounted for by purchasers on the reverse charge basis in the country of establishment of that purchaser.

Under the I-SEM this will continue to be the case for supplies between vendors and purchasers in Ireland and the United Kingdom ('UK'). The VAT treatment of supplies where one or both participants are established elsewhere other than Ireland or the UK are considered in more detail below.

In the SEM, a generator sells electricity into a gross mandatory pool and a supplier purchases from the pool. In the I-SEM, a generator and supplier will be required to be balance responsible across all trading arrangements and each could become both a vendor and purchaser of electricity. Thus, there are new scenarios to consider regarding the VAT treatment of supplies between participants in the market. The participants will be referred to as vendors and purchasers in this document.

2. Supplies of services by SEMO to market participants

In the I-SEM, SEMO will continue to be registered for VAT as a joint venture in both jurisdictions.

It is accepted that SEMO's role in the I-SEM is restricted to the settlement of the Balancing and Capacity market and imbalance volumes. The role of SEMO will result in it supplying services (referred to as market operator charges) to I-SEM market participants. Invoicing by SEMO for its own services, as distinct from settlement documents issued in respect of the sale and purchase of electricity, will be dependent on the SEMO VAT registration (Ireland or the UK) under which it is issued and by a participant's main place of establishment for VAT purposes. SEMO should obtain confirmation of the main place of establishment for market participants.

The normal VAT place of supply and [invoicing rules](#) relating to the [supply of services](#) will be applied to these services and they will be subject to the rates of VAT applicable in Ireland and the UK, as appropriate.

Should a participant's main place of establishment for VAT purposes be an EU jurisdiction other than Ireland and the UK, the place of supply shall be the EU Member State where the participant's main VAT establishment is located. Accordingly, those supplies will be outside the scope of both Irish and UK VAT. The participant will be required to account for VAT on the reverse charge basis in the country in which the service is received. SEMO will obtain such participant's VAT registration number and quote it on VAT invoices issued and also include an indication that a local reverse charge applies.

Where participants are established outside the EU, the place of supply is outside the EU and no Irish or UK VAT is chargeable.

Such supplies are separate to the transactions for the settlement of the Balancing and Capacity markets and imbalance volumes dealt with in the next section.

3. Supplies of electricity under the Trading & Settlement Code

It is assumed that all market participants are taxable dealers as defined in Article 38 of the Council Directive 2006/112/EC. For ease of reference, Article 38(2) of the Council Directive 2006/112/EC states that **“taxable dealer’ shall mean a taxable person whose principal activity in respect of purchases...electricity... is reselling those products and whose own consumption of those products is negligible.’**

SEMO’s role in the I-SEM is restricted to the settlement of the Balancing and Capacity market and imbalance volumes. SEMO will not take ownership of any of the electricity supplied between participants. Like in the SEM, there will be no direct relationship in the I-SEM between a vendor and purchaser due to the net pool arrangement that is in place under the Trading & Settlement Code.

In the I-SEM, and more specifically the arrangements set out in the Trading & Settlement Code, vendors will sell to the pool and the purchasers buy from the pool. Each vendor will be deemed to have sold proportionately to each purchaser, and each purchaser will be deemed to have purchased proportionately from each vendor. This requires a proportion calculation to be determined for each of sales and purchases to enable VAT calculations.

3.1. The VAT proportion calculation methodology

The VAT proportion calculation methodology takes into consideration the main place of establishment for VAT purposes of both the vendor and purchaser. A purchase proportion is calculated considering all purchases in the balancing/imbalance market grouped by each main place of establishment for VAT purposes. A separate proportion is also calculated for sales on the same basis. It will be based on the monetary value of the transactions between the market participants taking their places of establishment into account and will no longer look at the megawatt-hour (‘MWh’) flows between the two jurisdictions.

The settlement being carried out in I-SEM by SEMO is for the Balancing market and imbalance settlement and so the overall energy volumes and flows on the island are no longer relevant when determining the transactions that have taken place.

3.2. Settlement documents

At the end of each Billing Period (week), participants will be provided with a settlement document. Copy documents are to be held by SEMO and made available to Revenue on request.

As in the SEM, the settlement documents issued by SEMO in relation to supplies and purchases of electricity by I-SEM participants will be acceptable to Revenue as the equivalent of a VAT invoice. There will be no further requirement on participants to issue VAT invoices in relation to supplies covered by the settlement documents.

Participants operating within the pool will use these SEMO settlement documents as the basis for accounting for VAT. The way in which VAT is applied to the settlement document will be governed by the main place where a participant is established for VAT purposes.

As noted above, in the I-SEM, it will be possible for a participant to be both a vendor and a purchaser. This means that a participant could have sales and purchases as a vendor and also separate sales and purchases as a purchaser.

In the I-SEM, the total gross sales and total gross purchases of a participant in any given period will be presented on one settlement document together with an analysis of sales and / or purchases incurred within Local jurisdiction, EU and Non EU. While this is a move away from the current practice of issuing a separate document in respect of each sale and each purchase in the SEM, the change is purely for presentational purposes and will not result in the netting of sales and purchases transactions which would affect the amounts chargeable to VAT in either Ireland or the UK.

On request, SEMO will provide the Revenue Authorities with details of all transactions that have taken place in the I-SEM in the pool.

4. Supplies of capacity

Revenue will continue to treat the sale and purchase of capacity for VAT purposes in the same manner as the sale and purchase of electricity.

The VAT proportion calculation methodology is as detailed above but for the capacity market taking into consideration the main place of establishment for VAT purposes of both the vendor and purchaser.

At the end of each Capacity Period (calendar month), participants will be provided with a settlement document. Copy documents are to be held by SEMO and made available to the Revenue Authorities on request.

As in the SEM, the settlement documents issued by SEMO in relation to supplies and purchases of capacity by I-SEM participants will be acceptable to the Revenue as the equivalent of a VAT invoice. There will be no further requirement on participants to issue VAT invoices in relation to supplies covered by the settlement documents.

Participants operating in the Capacity Market will use these SEMO settlement documents as the basis for accounting for VAT. The way in which VAT is applied to the settlement document will be governed by the main place where a participant is established for VAT purposes.

On request, SEMO will provide Revenue with details of all transactions that have taken place in the I-SEM in the Capacity Market.

5. Electricity supplied outside the pool

Any trading of electricity outside of the pool, in which SEMO is not involved in any part of the transaction, will be subject to the VAT legislation in force in the State.

6. Currency gains and losses

The currency adjustments arising from electricity supplied through the pool will represent pricing adjustments for the electricity. Gains or losses arising in connection with, and reflected in, SEMO charges to participants will similarly represent pricing adjustments in respect of the services provided to the participants. This will not lead to any adjustment to SEMO's input tax credit.

7. Interest

Interest in the I-SEM will be treated as exempt from VAT.

8. Retention of Records

The time limit for retention of records will be six years for both SEMO and I-SEM participants.

9. Supplies received by SEMO

Any supplies made to SEMO by any supplier, will continue to be subject to the normal VAT legislation in force in the State.

Appendix 1 – VAT treatment under the SEM

Background

A Single Electricity Market (SEM) for the entire island of Ireland has been introduced with effect from 1 November 2007. The SEM is a pool-based mechanism for the sale and purchase of wholesale electricity across the island of Ireland. Entities that generate electricity for sale (generators) sell their electricity through the pool, and entities that sell electricity direct to the final consumer (suppliers) buy their electricity from the pool, at the prevailing pool price for any given half-hour trading period. The pool price is determined based on the prices at which generators are prepared to sell their electricity in any given trading period and looking at the predicted demand for that trading period. Financial settlement of the trades in the pool will take place in accordance with the rules set out in the Trading and Settlement Code for the SEM.

The SEM is jointly regulated by the Commission for Energy Regulation (in Ireland) and The Northern Ireland Authority for Utility Regulation (in Northern Ireland). To operate the market, a Single Electricity Market Operator (SEMO) has been established. The SEMO is a joint venture between EirGrid, who is licensed as market operator in Ireland, and SONI Ltd who is licensed as market operator in Northern Ireland. The SEMO will:

- administer the mandatory pooling arrangements created by the SEM Trading and Settlement Code
- manage market operations in both jurisdictions
- have a physical presence in both Ireland and Northern Ireland
- be responsible for calculating the price of electricity and recording all transactions within the SEM between generators and suppliers of electricity.

The introduction of the SEM necessitated joint approval by the Revenue Commissioners in Ireland and Her Majesty's Revenue & Customs (HMRC) in the UK on how VAT is to be operated in relation to generation and supply of electricity on the island of Ireland. Following discussions between the Revenue Commissioners and HMRC, and consultation with relevant stakeholders, agreement has now been reached on the operation of VAT in the SEM. This guidance sets out the agreed VAT treatment.

VAT registration - participants

Participants (generators and suppliers) in the SEM will be registered for VAT on the basis of their place of establishment in either Ireland or Northern Ireland.

VAT registration - SEMO

The role of the SEMO results in it supplying services to SEM participants that are subject to VAT. The SEMO is registered for VAT as a joint venture, in both Ireland and the UK, in respect of these services. The normal VAT rules relating to the supply of services apply to the services supplied by the SEMO and those services are subject to the rates of VAT applicable in Ireland and the UK, as appropriate.

In the context of its operation of the SEM pool, the SEMO receives supplies of goods and services. These supplies are subject to the normal VAT legislation in force in Ireland or the UK, as appropriate.

Supplies of electricity through the pool

The role of the SEMO is restricted to the operation of the pool and it does not take ownership of any of the electricity supplied between participants. As part of that role, the SEMO is responsible for calculating the price of the electricity supplied between the participants.

At the end of each settlement period the SEMO will provide each participant with a settlement document, which will include the VAT amount that is due to be paid by that participant to the Revenue Commissioners or to HMRC depending on the jurisdiction in which the participant is established. The settlement document will be acceptable to both the Revenue Commissioners and HMRC as the equivalent of a VAT invoice, and there will be no further requirement on participants to issue VAT invoices regarding the supply of electricity through the pool.

Participants operating within the pool will use these SEMO settlement documents as the basis for accounting for the output tax due on their supplies or recovering the input tax on purchases, as appropriate.

Information held by the SEMO will be available to the Revenue Commissioners and HMRC on request.

Cross-border supplies

Operation of the SEM will involve cross-border supplies of electricity. In the case of the cross-border supply of electricity from a generator to a supplier, the obligation to account for VAT rests with the recipient who is obliged to self-account, on a reverse charge basis, for the VAT due on the supply at the appropriate rate (reduced rate of VAT where the recipient is established in Ireland; standard rate of VAT where the recipient is established in the UK).

However, the nature of the pooling arrangements in the SEM means that both generators and suppliers will be unable to positively identify the cross-border element of their respective sales and purchases. Of necessity, therefore, the liability of recipient companies to account for VAT on the reverse charge basis in relation to cross-border supplies will be estimated by the SEMO. The production of electricity on the island of Ireland at present is such that, in overall terms, the cross-border element will be from Northern Ireland to Ireland.

For the initial 14 months of operation of the Pool, the SEMO will provide both Revenue authorities with the estimated data to be used for this purpose. This will be based on the projections (used in setting up the SEM) of electricity:

- generated and supplied in Northern Ireland
- generated and supplied in Ireland
- generated in Northern Ireland and supplied to Ireland
- generated in Ireland and supplied in Northern Ireland.

For each subsequent year estimates will be based on the actual trading for the previous year. At year-end the estimates may be compared against the actual energy flows and the rate of VAT applied to settlement documents for that year adjusted as appropriate. Ad hoc year-end settlement documents may be issued to participants reflecting any adjustments in the amount of VAT.

Settlement documents

All SEM transactions will be considered part of the supply of electricity and subject to VAT at the rate in force in either Ireland or UK, as appropriate. A “blended” calculation (being VAT at the Irish reduced rate of VAT / UK standard rate of VAT as appropriate on the domestic element of the supply with no VAT due on the balance as this will be subject to a reverse charge by the relevant participants) will be applied by the SEMO based on the estimated cross border flows and applied to relevant supplies in accordance with the Trading and Settlement Code. An example of a blended computation is contained in Appendix A of this guidance. The settlement document will show the VAT due to be paid to the relevant jurisdiction. The example at Appendix B outlines the entries that are required on the VAT returns of relevant participants.

The SEMO will also, as a temporary measure, issue an additional summary document (bi-monthly to relevant participants in Ireland and monthly to participants in Northern Ireland) identifying the total value of cross-border supplies during the period in question. This information will enable participants to meet their intra-EU VAT accounting obligations, including application of the reverse charge by those receiving cross-border supplies. With the system now live since 1 November 2007, the SEMO will, as a priority, work towards including this information as part of the normal settlement document.

Supplies of electricity outside the pool

Any trading of electricity outside of the Pool, in which the SEMO is not involved in any part of the transaction, will be subject to the VAT legislation in force in Ireland or the UK, as appropriate.

SEMO supplies to participants

Invoices issued by the SEMO for its own services, as distinct from settlement documents issued in respect of the sale and purchase of electricity, will be subject to the VAT legislation in Ireland or the UK, dependant on the VAT registration (Irish or UK, as appropriate) under which it is issued. Generally, these services will be supplied by the SEMO within the relevant jurisdiction – it is not anticipated that a cross border supply of such services will arise. Thus, supplies to a Northern Ireland participant will be supplied under the SEMO's UK VAT registration, while supplies to an Ireland participant will be supplied under the SEMO's Irish VAT registration. In the unlikely event that cross-border supplies of the SEMO's services arise, the VAT position will depend on the nature of the supplies and the VAT treatment will follow the normal place of supply rules.

Retention of records

The time limit for retention of records will be six years for both the SEMO and the SEM participants.

Contracts for differences

A feature of the SEM is that it is anticipated that Contracts for Differences (CFDs) may arise.

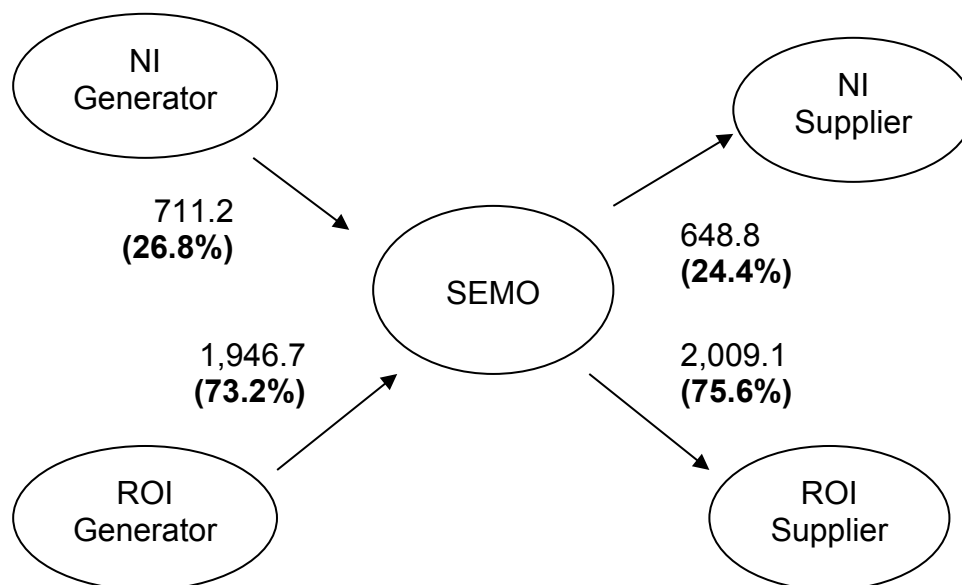
A Contract for Difference is an agreement through which parties can effectively fix the price of a price-volatile commodity, by reference to the difference between the fixed contract price and the market price. That difference is paid after the trading period. In this way the parties can hedge their exposure to price fluctuations.

In the context of the SEM, generators and suppliers may enter into CFDs, which will specify a fixed or indexed price for electricity (strike price) at which the parties have agreed to sell and buy electricity. Where in any trading period the pool price exceeds the strike price, the generator pays the supplier the difference between the two. Similarly, where the strike price exceeds the pool price in any trading period, the supplier will pay any difference to the generator.

CFDs are completely outside the pool trading and settlement arrangements, under which the sale of the electricity itself takes place. CFDs are exempt from VAT on the basis that they are considered a financial transaction and are not connected with the supply of electricity. Thus, it will be necessary for participants who trade in CFDs to apportion the VAT input credit to take account of their exempt income. The apportionment should be agreed with the participant's local Revenue District.

Appendix A - Computation of blended calculation

The diagram below illustrates the flow of electricity, (expressed in € millions), in and out of the SEM pool. The figures in brackets shows the electricity expressed as a percentage of total generation and total supply.



Total Generated = 2657.9m

NI Generator

Assuming that all electricity generated in NI goes first to NI suppliers, the NI generators' position is as follows:

Generates: 711.2

To NI: 648.8

To ROI: 62.4

The amount of cross border supply (to ROI) represents 8.77% of the total amount generated in NI. Therefore 91.23% generated represents local supply. Effectively this means that 91.23% is taxed at 17.5% (local UK rate) and 8.77% is zero-rated as an intra-Community supply. In order to tax the whole amount generated as one, a blended calculation is carried out as follows:

Percentage supplied to NI * Local UK Rate

$$91.23\% \quad * \quad 17.5 = 15.97\%$$

Therefore, the total amount generated by a NI generator is liable to VAT at the blended calculation of 15.97%.

ROI Supplier

Following the same logic as above, an ROI supplier receives 96.9% (1946.7/2009.1) of its electricity from ROI generators and 3.1% from NI generators. Effectively, this means 96.9% of electricity is taxed at 13.5% and 3.1% zero-rated under the reverse charge mechanism. See below for the blended calculation:

Percentage received from ROI * Local ROI rate

$$96.9\% \quad * \quad 13.5 \quad = \quad 13.08\%$$

Appendix B - Completion of VAT return

Below is an example of the VAT treatment and appropriate entries in an ROI VAT return in respect of these transactions.

ROI Generator

- Supplies electricity to the pool.
- SEMO provides document recording sale of €50,000, plus VAT of €6,750 (at local rate of 13.5%; no cross border element).
- SEMO pays the Generator €56,750. Generator declares €6,750 VAT to Revenue Commissioners and retains €50,000.

VAT Return

Box T1: €6,750
Net VAT Payable: €6,750

- Return of Trading Details required annually.*

ROI Supplier

- Purchases electricity from the pool.
- Invoiced by the SEMO for purchase of €40,000 plus VAT of €5,232 (at blended calculation of 13.08%, shown in Appendix 1).
- SEMO also provides a document showing the total value of energy supplied, split between local and cross border acquisitions according to the estimated percentage split; 96.9% local and 3.1% cross-border.
- Supplier pays the SEMO €45,232.
- Supplier calculates VAT on reverse charge element, [$€40,000 * 3.1\% = €1,240$ @13.5% = €167.4]. This amount is declared as output tax in Box T1 and is also added to the actual VAT amount incurred.

VAT Return

Box T1: €167.40
Box T2: €5,399.40
Box E2: €1,240 [$€40,000 * 3.1\%$]
Net VAT Deducted: €5,232

- Return of Trading Details required annually.*

* ROI participants will be required to submit a return of trading details annually on form VAT 3G(A). Details of the VAT-exclusive values for sales, purchases, importations and intra-Community acquisitions and intra-Community supplies made by participant in the period covered by the return must be included. This is an existing requirement for all taxable persons and there is no additional burden for participants in the SEM.