Value Added Tax
VAT is an indirect tax applied upon the consumption of most goods and services. As the name suggests, it is charged incrementally based on the value added at each stage of the supply chain and is collected by businesses on behalf of the government. Ultimately the VAT is incurred and paid by the final consumer. UAE VAT is set to come into effect from 1 January 2018. The standard rate of VAT is set at 5%.

GCC VAT Framework and UAE VAT Law
The VAT system in UAE is being implemented as part of a Gulf Cooperation council (GCC) initiative to introduce a common GCC-wide framework, which is to serve as the basis for local VAT legislation in the individual GCC countries. The Federal Tax Authority (FTA) is the UAE government body that is responsible for ensuring implementation and compliance of VAT and Excise Tax laws in UAE.

Reason for VAT introduction
It is part of the GCC’s programme to reduce the regional dependency on oil revenue and create an additional income stream. It is important to note that revenue collected is to be used for infrastructure developments including the development of roads, parks, waste control and other projects. Increased federal revenue will allow governments to continue funding state of the art infrastructural development within the region.

Mechanism of VAT

1. A farmer grows dates, which are picked and sold to a processing factory
2. The factory processes the dates into date syrup, which is sold on to retail chains
3. The retailer places date syrup on the shelves for sale to consumers
4. The retailer collects VAT from the consumer on behalf of the government
   The retailer receives a refund on the VAT paid to the factory


If your businesses’ annual taxable supplies exceeds certain threshold, you are required to be registered for VAT. Businesses should be registered by the last quarter of 2017 so that they are prepared before the implementation date, since they will have to collect, record and report VAT to the government.

VAT’s structure of implementation is different from a sales tax because each supply chain has to apply, collect and report tax. Businesses have to make changes in operations, technology and human resources to ensure that they fully comply with government requirements. This will involve additional cost of doing business. To comply, businesses need to change their book reporting standards and ensure that VAT is collected and reported properly. Failure to do so will result in penalties.

Output VAT
VAT charged by you on your sales to other businesses or ordinary customers. You collect this on behalf of government and are obliged to pay to government on a regular basis.

Input VAT
VAT charged to you by other businesses. Input Vat can be deducted from the VAT payable to the tax authorities.
Categories of VAT

Taxable Supplies

Standard Rated 5%

Zero Rated 0%

Exempt Supplies

Goods and Services

<table>
<thead>
<tr>
<th>Zero Rated Supplies</th>
<th>Exempt Supplies</th>
<th>Standard Rated Supplies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education services</td>
<td>Sale of Bare Land</td>
<td>Supply of all goods and services that are not Zero-Rated or Exempt</td>
</tr>
<tr>
<td>Healthcare services and related medicines and medical equipment</td>
<td>Local passenger transport- buses, taxis, metro</td>
<td></td>
</tr>
<tr>
<td>Means of air, sea and land transportation e.g. ships, aircrafts.</td>
<td>Some financial services (margin based)</td>
<td></td>
</tr>
<tr>
<td>International transportation</td>
<td>Leases on Residential properties</td>
<td></td>
</tr>
<tr>
<td>First sale of new residential property (Within 3 years of construction)</td>
<td>Sale of residential properties as from second sale onward</td>
<td></td>
</tr>
<tr>
<td>Crude oil and natural gas</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Exports outside of GCC states</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment in precious metals such as gold, silver and platinum</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Difference between Zero-Rated and Exempt Supplies

VAT is not charged on both of these supplies. However, zero-rated is a taxable supply, which means that businesses making zero-rated supplies can register for VAT and reclaim VAT on purchases incurred in the making of those supplies.

Businesses solely making exempt supplies cannot register for VAT and cannot claim any Input VAT. However, a business making a mix of taxable and exempt supplies can register for VAT and reclaim Input VAT directly related to taxable supplies.

Out of scope supplies for VAT

These supplies are neither taxable nor exempt. The following are some examples of out of scope supplies:

- Supplies from a non-registered entity
- Sales transacted outside of the UAE e.g. a UAE distributor ships goods from UK supplier directly to a customer in France.
- Certain government activities
- Goods or services provided to a different department within the same business.
VAT Registration Threshold

**MANDATORY**
Taxable Supplies: AED 375,000

**VOLUNTARY**
Taxable Supplies: AED 187,500

**Taxable Supplies**
Standard Rated Supplies + Zero Rated Supplies + Import goods + Reverse Charge Services received. (Provided the taxpayer is responsible for accounting for tax). The items below are not used in calculating the VAT registration threshold.

- Exempt supplies
- Out of scope supplies

**Mandatory Registration**
If the taxable supplies for last 12 months or the anticipated taxable supplies for next 30 days exceeds mandatory registration threshold of AED 375,000.

**Voluntary Registration**
- If the taxable supplies for the last 12 months or the anticipated taxable supplies for next 30 days exceed the voluntary registration threshold of AED 187,500.
- If the expenses that are subject to VAT for last 12 months or for next 30 days exceed that voluntary registration threshold of AED 187,500.

**Group Registration**
Two or more entities carrying on a business are able to apply for a single ‘Group’ VAT registration if

- Each entity has a place of establishment in UAE
- The entities are related parties, and
- Either one entity controls the other, or two or more entities form a partnership to control the others.

Entities within one VAT group are treated as one entity for the VAT purpose. One entity cannot be part of more than one VAT group. Supplies made between members of a VAT group are disregarded for VAT. A VAT group simplifies the VAT return procedures and will also assist with the cash flow management of a qualifying business.

**VAT Liability**
VAT will be due where a taxable supply is being made by a taxable person. All of the categories mentioned on the diagram below need to be met for it to be considered a supply. A ‘consideration’ is anything received in return for a supply such that even a barter transaction will fall under the VAT rules. The consideration is treated as **VAT inclusive**, so the amount received in payment includes an element of VAT for taxable supplies.

A supply of goods or services

- In the course of conducting business
- By any Person
- For Consideration
- In the UAE
Reverse Charge Mechanism
When a VAT-registered business imports goods or services, it may be treated as making taxable supplies to itself and will be responsible for all applicable tax obligations and accounting.

- This reduces the obligations for sellers to register for VAT in the country where supply is made
- The purchaser will have to account and pay the VAT directly to the government instead of paying to the supplier. This ensures that the local and international suppliers are on the equal footing
- The business may be able to claim this VAT on the same VAT return and not wait for the goods to be sold, which will assist with cash flow.

Place of Supply

<table>
<thead>
<tr>
<th>Goods</th>
<th>Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>Place of supply is <strong>UAE</strong> in following cases:</td>
<td>Place of supply is UAE in the following scenarios:</td>
</tr>
<tr>
<td>1. Domestic supplies</td>
<td>1. If the recipient does not have a place of residence in GCC, is outside the UAE at the time of service and the service does not relate to real estate in UAE, it will be zero-rated.</td>
</tr>
<tr>
<td>2. Export outside GCC – Zero-Rated</td>
<td>2. If the service is actually performed outside the GCC or relates to an arrangement of services that is performed outside of GCC, it will be zero-rated.</td>
</tr>
<tr>
<td>3. B2B import into UAE from outside GCC – Reverse charge mechanism to be applied</td>
<td>3. If the supply consists of facilitation of outbound tour packages, it will be zero-rated.</td>
</tr>
<tr>
<td>4. Export to GCC customers that are not VAT-registered and the export amount remains below the mandatory registration threshold.</td>
<td>4. If the supply of service is by a non-UAE resident supplier to a UAE VAT-registered customer, the reverse charge mechanism will be applied.</td>
</tr>
</tbody>
</table>

Place of supply is **outside UAE** in the following cases:
1. B2B exports to GCC customer registered for GCC state VAT – Out of scope
2. Export to GCC customers that are not VAT-registered and export amount exceeds the mandatory registration threshold

Place of supply is one of the GCC states:
1. Supply of service to customer registered for VAT in GCC states (outside UAE)
   - Place of supply varies for following.
   1. Installation of goods- where the service is performed
   2. Restaurant, hotel and catering services- where the service is performed
   3. Real estate services- location of real estate
   4. Transport services- where transport begins
   5. Means of transport to a person not registered for VAT in GCC- where the goods are put at the disposal of the recipient.
   6. Telecommunication and electronic – is where the services are actually used and enjoyed by the recipient.
   7. Cultural, artistic, sporting, educational or similar services – where they are performed.
Time of Supply
Whichever of the following events takes place first:

- Payment is received
- Tax invoice is issued
- Goods are removed (in case of supply of goods with transportation)
- Goods or Services are delivered (in case of supply of goods without transportation)

There is an exception for ‘transitional’ transactions. If the invoice is issued or the amount is paid prior to the date on which VAT came into effect or prior to registration, and supply is made after such date, such bill or payment will be ignored and the actual date of supply will be taken as the tax due date.

However, in the case of ‘continued supplies’ performed partially prior or partially after the date VAT became effective, tax is not applicable on the portion performed prior to the effective date.

Designated Zones
Not all of the free zones will be declared VAT-free zones. Instead, there will be the introduction of ‘designated zones’, which will be considered as outside the UAE for the purposes of VAT. These designated zones are likely to be the fenced free zones like Jebel Ali. Final confirmation will be provided in the executive regulations.

Tax Recovery
Generally, only the VAT incurred on business-related supplies can be claimed back. This will have to be supported by evidence of transaction (invoice with tax) and proof of settlement. However, VAT on the following items may be irrecoverable or only part recoverable.

- Business entertainment
- Gifts to clients and staff above a certain amount.
- Driving expenses for non-business purposes
- Mobile phone usage for non-business purposes.

VAT relief on bad debt
If goods and services have been supplied, invoices have been raised and the due tax has been paid but the invoice remains outstanding for more than 6 months, then the invoice can be written off and a VAT adjustment can be made to get the VAT back on the written off invoices. However, if the invoice does eventually get paid, the VAT amount will also have to be paid.

VAT Invoices
VAT invoices should be drawn up in a specific format or they will not be admissible for VAT purposes. Only a VAT-registered business can issue a tax invoice and the invoice must be issued within 14 calendar days of the time of supply. The main requirements for inclusion are:

- The term ‘Tax Invoice’ in Arabic script
- The VAT registration numbers of both supplier and customer
- Amounts provided in AED
- Net amount, VAT amount and gross amount must be presented separately
- The rate of VAT applicable
- The date of supply if different from the date of invoice issue
- A statement relating to reverse charge mechanism, if applicable
- The rate of exchange applied and the source of that rate.
Record Keeping
There is a strict requirement for the maintenance of all the records for a minimum of 5 years. Annual accounts as well as any additional information necessary to verify entries should be maintained. General ledgers, purchase day books, invoices and credit notes issued and received, VAT ledgers, VAT calculations, adjustments, record of supplies, exports and imports etc. should all be maintained and readily available to be presented to the FTA if the case of any VAT audit.

Federal Tax Authority Audits
The FTA will use risk-based selection criteria to determine any taxpayers subject to audit. The audit can be performed at the business premises or at the FTA office. The FTA can close a place of business for up to 72 hours if there is suspicion of tax evasion.

Penalties
- Administrative non-compliance penalty: Up to 300% of the amount of tax for which the penalty was levied.
- Tax evasion penalty: Potential imprisonment and up to 500% of the relevant tax at stake.

Reporting
- Submission will be online
- The due date will be within the month following the end of the return period as will be announced in the executive regulations.
- Late submission or payment will result in a penalty levied by FTA
- Value of supplies made in each emirate will have to be reported separately on VAT returns.

CONTACT US
Sovereign Corporate Services
26th Floor, The H Hotel Office Tower
One Sheikh Zayed Road
P.O. Box 62201
Dubai
United Arab Emirates

Telephone number: +971 4 270 3400
Local free phone number: 800 SOVEREIGN
Email: accountingdxb@sovereigngroup.com

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