VAT in the UAE

2016

Introduction

This series will explore the fundamentals of value-added tax ("VAT") in the United Arab Emirates ("UAE") and consider the legal impact of the regime, as well as the effect on businesses and residents.

In February 2016 the Ministry of Finance announced the introduction of VAT in the UAE. The tax-free status of the UAE has previously been a major appeal to foreign investors and individuals. However, the well-known benefits afforded by this largely tax-free status are soon to change with the introduction of a VAT regime.

At present, it is uncertain exactly which VAT model will be implemented in the UAE. However, there is little time for businesses to consider the implications of VAT being introduced into the UAE and to make the necessary changes to their commercial contracts and current terms and conditions of sale in order to comply with the new regime.

What, Why, When, Who, How?

What is VAT?

VAT is a general consumption tax, which will apply to most goods and services within the UAE. VAT is a fiscally neutral tax and is levied on a destination basis, where the tax rate is based on the location of the customer.

What will the applicable rate be?

The expected rate of VAT to be introduced is 5% for both goods and services, which appears low when compared to other countries i.e. European countries, which charge between 17-27% of value. Despite this considerably lower rate, VAT should generate significant revenue and reduce any governmental dependency on income from oil and gas. It is expected that the VAT regime will allow for more stability by creating steady income for the government.

What will VAT be charged on?

VAT will be charged on all goods and services supplied in the UAE at point of sale such as cars, smart phones, electronics, jewellery, eating out and entertainment. Goods imported into the UAE may also be subject to VAT.

Whilst no official guidance or publications have been released, the Ministry of Finance has indicated there will be some exemptions, which are driven by socio-economic policy considerations. For example, it is contemplated that basic foods will be charged at 0% and potential areas such as health care and education to be completely exempt. If some goods and services are subject to 0% tax or completely exempt, this should avoid a significant increase in the cost of living for residents and encourage exports.

What does this mean for UK businesses trading within the UAE?

As VAT has not previously been an issue in the UAE, those supplying goods and services may be supplying on contractual terms that do not include provisions and mechanisms in relation to price adjustment where VAT is chargeable, or account for the possible change in law. The supplier is generally responsible for VAT and those contracts that remain silent in relation to VAT could expose businesses to penalties and potentially heavy costs. There have been concerns in relation to the cost of doing business and the readiness of businesses to facilitate the introduction of VAT. However, for UK based suppliers it is likely that implementing VAT should be less complicated, in comparison to businesses that have not previously dealt with the administrative nuances of tax.

To ensure the smooth transition of the VAT regime and to mitigate compliance costs, businesses should keep up to date with the changes and regulations. Legal advice should be considered by those party to existing supply contracts, as well as those due to undertake the supply of goods and services in the UAE. We will consider this further in our next series.

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Why is VAT being introduced?

With the collapse of the oil price, countries whose economy is largely based on oil production have seen a shift in focus to vary income sources.

It is estimated that the UAE will generate more than AED 12billion additional revenue in the first year following implementation of this new tax.

When will VAT be introduced and when should businesses register for VAT?

It is expected that the UAE will implement VAT from 1st January 2018, with other GCC countries to follow by 1st January 2019. It is understood that the UAE has also prepared a draft law that is under discussion internally, and is subject to the final approval of a GCC VAT legal framework, which is yet to be agreed.

The finance ministers of the GCC member states met in June to approve, in principle, the treaties, for the collection of excise tax and VAT. It is expected the common treaties should be announced in the last quarter of the year.

Once the framework agreement regarding implementation of VAT is reached, GCC countries will have one year from 1st January 2018 to implement it within the time frame. It is expected that registration for VAT should be made available to businesses that meet the requirements criteria three months before the launch of VAT.

Who will charge VAT?

VAT will be introduced in the UAE in two phases. The UAE Ministry of Finance recently confirmed that under phase 1 of implementation, businesses with an annual turnover of between AED 1.87million and AED 3.75million would have the option to register for VAT. Companies with a turnover above the AED 3.75million threshold will be obliged to register under the system. Details of phase 2, which will apply to all companies operating in the UAE, have not yet been revealed. However, it is envisaged that it may eventually become a requirement that all companies register for VAT.

Businesses that are registered for VAT will be able to charge VAT. As such, businesses will need to amend their systems, processes and procedures and will need to ensure they comply with the new requirements. Businesses will be required to keep records which will enable the authorities to identify the details of the business activities and review transactions. This will be discussed further in our next series.

How does it work?

VAT is charged by adding the rate of VAT to the charge for the supply of goods and services. Moreover, excise tax is usually levied on specific goods during import or manufacture and is often included in the price of the product. In any event, those involved in the import and/or local manufacture of goods (that are subject to excise tax) and the supply of goods and services will be required to submit to the tax authority the necessary VAT and excise tax returns.

Output VAT: This means businesses registered for VAT will be required to charge on their taxable sales i.e. the VAT businesses charge on their own sales of goods and services both to other businesses and ordinary consumers which companies will collect for customers on behalf of the government.

Input VAT: This is VAT chargeable on most goods and services acquired by businesses. If the company is registered for VAT, this can be deducted from the output tax owed.

It is expected that registered businesses will need to submit VAT returns on the default period for filing, VAT returns should be three months for the majority of businesses. Businesses will need to consider their eligibility for input/output tax recovery, as well as a range of matters such as registration with the competent tax authorities and administration of payments.

VAT-registered businesses should consider the following: to charge VAT on taxable goods or services they supply; potential reclaim for any VAT they've paid on business-related goods or services; and to keep business records to allow the government to check compliance.

Next time:

We consider the effect and impact of the VAT regime on businesses and residents in the UAE.

Who we are and how we can help:

The Gateley Dubai Corporate team is one of the leading corporate teams in the MENA. We can assist our clients with a range of tax structuring issues. We understand local laws and customs and can help our clients overcome any issues they might experience undertaking business in the UAE, as well as internationally.

Once implemented, VAT will likely affect all functions within a business. There is little time for companies to consider the implications of VAT being introduced into the UAE and to make the necessary changes to their commercial arrangements, current terms and conditions of sale and internal procedures and processes to ensure compliance with the new regime. It is essential to consider the impact now and for businesses to determine their ability to accommodate the introduction of VAT.

For further information please get in touch with Jonathan Burton at JBurton@gateleyae.com or Tania Diab at TDiab@gateleyae.com.