

# VAT FAQs

## What is Tax?

Tax is the means by which governments raise revenue to pay for public services. Government revenues from taxation are generally used to pay for things such as public hospitals, schools and universities, defence and other important aspects of daily life.

There are many different types of taxes:

- A direct tax is collected by government from the person on whom it is imposed (e.g., income tax, corporate tax).
- An indirect tax is collected for government by an intermediary (e.g. a retail store) from the person that ultimately pays the tax (e.g., VAT, Sales Tax).

## What is the difference between VAT and Sales Tax?

A sales tax is also a consumption tax, just like VAT. For the general public there may be no observable difference between how the two types of taxes work, but there are some key differences. In many countries, sales taxes are only imposed on transactions involving goods. In addition, sales tax is only imposed on the final sale to the consumer. This contrasts with VAT which is imposed on goods and services and is charged throughout the supply chain, including on the final sale. VAT is also imposed on imports of goods and services so as to ensure that a level playing field is maintained for domestic providers of those same goods and services.

Many countries prefer a VAT over sales taxes for a range of reasons. Importantly, VAT is considered a more sophisticated approach to taxation as it makes businesses serve as tax collectors on behalf of the government and cuts down on misreporting and tax evasion.

## Who can or will be able to register for VAT?

A business must register for VAT if their taxable supplies and imports exceed the mandatory registration threshold of AED 375,000.

Furthermore, a business may choose to register for VAT voluntarily if their supplies and imports are less than the mandatory registration threshold, but exceed the voluntary registration threshold of AED 187,500.

Similarly, a business may register voluntarily if their expenses exceed the voluntary registration threshold. This latter opportunity to register voluntarily is designed to enable start-up businesses with no turnover to register for VAT.

## What are the VAT-related responsibilities of businesses?

All businesses in the UAE will need to record their financial transactions and ensure that their financial records are accurate and up to date. Businesses that meet the minimum annual turnover requirement (as evidenced by their financial records) will be required to register for VAT. Businesses that do not think that they should be VAT registered should maintain their financial records in any event, in case we need to establish whether they should be registered.

### **VAT-registered businesses generally:**

- must charge VAT on taxable goods or services they supply;
- may reclaim any VAT they've paid on business-related goods or services;
- keep a range of business records which will allow the government to check that they have got things right

If you're a VAT-registered business you must report the amount of VAT you've charged and the amount of VAT you've paid to the government on a regular basis. It will be a formal submission and it is likely that the reporting will be made online.

If you've charged more VAT than you've paid, you have to pay the difference to the government. If you've paid more VAT than you've charged, you can reclaim the difference.

## What does a business need to do to prepare for VAT?

Concerned businesses will have time to prepare before VAT will come into effect in January 2018. During that time, businesses will need to meet requirements to fulfil their tax obligations. Businesses could start now so that they will be ready later. To fully comply with VAT, We believe that businesses may need to make some changes to their core operations, their financial management and book-keeping, their technology, and perhaps even their human resource mix (e.g., accountants and tax advisors). It is essential that businesses try to understand the implications of VAT now and once the legislation is issued make every effort to align their business model to government reporting and compliance requirements. We will provide businesses with guidance on how to fully comply with VAT once the legislation is issued. The final responsibility and accountability to comply with law is on the business.

## When are registered businesses required to file VAT returns?

Taxpayers must file VAT returns with the FTA on a regular basis (quarterly or for a shorter period, should the FTA decide so) within 28 days from the end of the tax period in accordance with the procedures specified in the VAT legislation. The Tax returns shall be filed online using eServices.

## What kind of records are businesses required to maintain, and for how long?

Businesses will be required to keep records which will enable the Federal Tax Authority to identify the details of the business activities and review transactions. The specifics regarding the documents which will be required and the time period for keeping them will be stated in the relevant legislation.

The taxable person shall keep the following records of:

All supplies and Imports of Goods and Services.

- Tax Invoices and alternative documents related to receiving Goods or Services.
- Tax Credit Notes and alternative documents received.
- Tax Invoices and alternative documents issued.
- Tax Credit Notes and alternative documents issued.
- Goods and Services that have been disposed of or used for matters not related to Business, showing Taxes paid for the same.
- Goods and Services purchased and for which the Input Tax was not deducted.
- Exported Goods and Services.
- Adjustments or corrections made to accounts or Tax Invoices.
- Records relating to capital assets for at least 10 years
- Tax Record that includes the following information:
  - Due Tax on Taxable Supplies.
  - Due Tax on Taxable Supplies pursuant to the reverse charge mechanism.
  - Due Tax after the error correction or adjustment.
  - Recoverable Tax for supplies or imports.
  - Recoverable Tax after the error correction or adjustment.

Taxable persons for VAT must retain the above-mentioned records for at least 5 years. The Executive Regulation of the Decree-Law on VAT shall specify further details on restrictions and conditions with respect to maintaining the records listed above.

## How long must a taxable person retain VAT invoices for?

Any taxable person must retain VAT invoices issued and received for a minimum of 5 years.

## How should a business determine the place of supply?

The place of supply will determine whether a supply is made within the UAE (in which case the UAE VAT law will apply), or outside the UAE for VAT purposes.

For a supply of goods, the place of supply should be the location of goods when the supply takes place with special rules for certain categories of supplies (e.g. water and energy, cross border supplies).

For the supply of services, the place of supply should be where the supplier is established with special rules for certain categories of supplies (e.g. cross border supplies between businesses).

## What sectors will be zero rated?

VAT will be charged at 0% in respect of the following main categories of supplies:

- Exports of goods and services to outside the GCC;
- International and intra GCC transport;
- Air passenger transport;
- Supply of air, sea and land means of transport as would be specified in the executive regulations;
- Supply of aircraft or vessels for specific purposes;
- Supply of goods and services related to transfer of goods or passengers;
- Supply or import of investment grade precious metals (e.g. gold, silver, of 99% purity);
- Newly constructed residential properties, that are supplied for the first time within 3 years of their construction;
- First supply of buildings to be used specifically for charities for sale or lease/buildings converted from non-residential to residential;
- Supply of crude oil and natural gas;
- Supply of educational services and related goods and services for specific institutions as would be specified in the executive regulations;
- Supply of preventive and basic healthcare services and related goods and services as would be specified in the executive regulations.

## What sectors will be exempt?

The following categories of supplies will be exempt from VAT:

- The supply of some financial services (clarified in VAT legislation);
- Residential properties;
- Bare land; and
- Local passenger transport

## Will there be VAT grouping?

Businesses that satisfy certain requirements covered under the Legislation (such as being resident in the UAE and being related/associated parties) will be able to register as a VAT group. For some businesses, VAT grouping will be a useful tool that would simplify accounting for VAT.

## Will there be bad debt relief?

VAT registered businesses will be able to reduce their output tax liability by the amount of VAT that relates to bad debt which has been written off by the VAT registered business. The legislation will include the conditions and limitations concerning the use of this relief.

## Will there be a margin scheme?

To avoid double taxation where second hand goods are acquired by a registered person from an unregistered person for the purpose of resale, the VAT-registered person will be able to account for VAT on sales of second hand goods with reference to the difference between the purchase price of the goods and the selling price of the goods (that is, the profit margin). The VAT which must be accounted for by the registered person will be included in the profit margin. The legislation will include the details of the conditions to be met in order to apply this mechanism.

## How will partial exemption work?

Where a VAT registered person incurs input tax on its business expenses, this input tax can be recovered in full if it relates to a taxable supply made, or intended to be made, by the registered person. In contrast, where the expense relates to a non-taxable supply (e.g. exempt supplies), the registered person may not recover the input tax paid.

In certain situations, an expense may relate to both taxable and non-taxable supplies made by the registered person (such as activities of the banking sector). In these circumstances, the registered person would need to apportion input tax between the taxable and non-taxable (exempt) supplies.

Businesses will be expected to use input tax (ratio of recoverable to total) as a basis for apportionment in the first instance although there will be the facility to use other methods where they are fair and agreed with the Federal Tax Authority.

## What are the cases that would lead to the imposition of penalties?

Penalties will be imposed for non-compliance.

Examples of actions and omissions that may give rise to penalties include:

- A person failing to register when required to do so;
- A person failing to submit a tax return or make a payment within the required period;
- A person failing to keep the records required under the issued tax legislation;
- Tax evasion offences where a person performs a deliberate act or omission with the intention of violating the provisions of the issued tax legislation.

## Will there be any special schemes for SMEs?

No special rules are planned for small or medium sized enterprises. However, the FTA will provide materials and resources available for these entities to assist them in their enquiries.

## Will there be transitional rules?

Special rules will be provided to deal with various situations that may arise in respect of supplies that span the introduction of VAT. For example:

- Where a payment is received in respect of a supply of goods before the introduction of VAT but the goods are actually delivered after the introduction of VAT, this means that VAT will have to be charged on such supplies. Likewise, special rules will apply with regards to supplies of services spanning the introduction of VAT.
- Where a contract is concluded prior to the introduction of VAT in respect of a supply which is wholly or partly made after the introduction of VAT, and the contract does not contain clauses relating to the VAT treatment of the supply, then consideration for the supply will be treated as inclusive of VAT. There will, however, be special provisions to allow suppliers to charge VAT in situations where their recipient is able to recover their VAT but where there is no VAT clause.

## How will insurance be treated?

Generally, insurance (vehicle, medical, etc) will be taxable. Life insurance, however, will be treated as an exempt financial service.

## How will financial services be treated?

It is expected that fee based financial services will be taxed but margin based products are likely to be exempt.

## How will Islamic finance be treated?

Islamic finance products are consistent with the principles of sharia and therefore often operate differently from financial products that are common internationally.

To ensure that there are no inconsistencies between the VAT treatment of standard financial services and Islamic finance products, the treatment of Islamic finance products will be aligned with the treatment of similar standard financial services.

## Can UAE nationals claim VAT?

A scheme will be introduced to allow a UAE national who is not registered for VAT to reclaim VAT paid on goods and services relating to constructing a new residence which will be privately used by the person and

his family. This will allow the recovery of VAT on such expenses as contractor's services and building materials.

### How quickly will refunds be released?

Refunds will be made after the receipt of the application and subject to verification checks, with a particular focus on avoiding fraud.

### Will FTA issue rulings or provide tax advice?

In the course of its interaction with taxpayers, the FTA may provide its views on various matters in the law. Taxpayers may choose to challenge these views. It should be noted that penalties may be imposed on taxpayers who are found to violate any tax laws and regulations.

### Will it be possible to issue cash receipts instead of VAT invoices?

A supplier registered or required to be registered for VAT must issue a valid VAT invoice for the supply. To be considered as a valid VAT invoice, the document must follow a specific format as mentioned in the legislation. In certain situations the supplier may be able to issue a simplified VAT invoice. The conditions for the VAT invoice and the simplified VAT invoice are mentioned in the legislation.

### Will there be any VAT that businesses are not allowed to claim?

VAT will not be deductible in respect of expenses incurred for making non-taxable supplies. Furthermore, input tax cannot be deducted if it is incurred in respect of specific expenses such as entertainment expenses e.g. employee entertainment.

### Under which conditions will businesses be allowed to claim VAT incurred on expenses?

VAT on expenses that were incurred by a business can be deducted in the following circumstances:

- The business must be a taxable person (the end consumer cannot claim any input tax refund).
- VAT should have been charged correctly (i.e. unduly charged VAT is not recoverable).
- The business must hold documentation showing the VAT paid (e.g. valid tax invoice).
- The goods or services acquired are used or intended to be used for making taxable supplies.
- VAT input tax refund can be claimed only on the amount paid or intended to be paid before the expiration of 6 months after the agreed date for the payment of the supply.

## Will non-residents be required to register for VAT?

Non-residents that make taxable supplies in the UAE will be required to register for VAT unless there is any other UAE resident person who is responsible for accounting for VAT on these supplies. This exclusion may apply, for example, where a UAE business is required to account for VAT under a reverse charge mechanism in respect of a purchase from a non-resident.

## Will VAT be paid on imports?

VAT is due on the goods and services purchased from abroad.

In case the recipient in the State is a registered person with the Federal Tax Authority for VAT purposes, VAT would be due on that import using a reverse charge mechanism.

In case the recipient in the State is a non-registered person for VAT purposes, VAT would be paid on import of goods from a place outside the GCC. Such VAT will typically be required to be paid before the goods are released to the person.

## How will Government Entities be treated for VAT purposes?

Supplies made by government entities will typically be subject to VAT. This will ensure that government entities are not unfairly advantaged as compared to private businesses.

Certain supplies made by government entities will, however, be excluded from the scope of VAT if they are not in competition with the private sector or where the entity is the sole provider of such supplies. It is likely certain government entities will be entitled to VAT refunds – this is designed to avoid budgeting issues and provide a level playing field between outsourced and insourced activities.

For the supplies provided for government entities, the treatment of such supplies shall depend on the same supply and not on the recipient of the supply. Therefore, if the supply is subject to the standard tax rate, the treatment would remain the same even if it is provided to a government entity.

## Will Businesses have to report on their business in each of the Emirates?

It is expected that businesses will need to complete additional information on their VAT returns to report revenues earned in each Emirate. Guidance will be provided to businesses with regards to this.

It is expected that the rules will be relatively straightforward for most businesses and will be based, for example, for B2C transactions, on the location of the transaction (e.g. in a retail environment, the location of the shop).

## Will the goods exempt from customs duties also be exempt from VAT?

Not necessarily. Some goods that are imported may be exempt from customs duties but subject to VAT.

### Will tourists also pay VAT?

Yes, tourists are a significant source of revenue for the UAE and will pay VAT at the point of sale. Nevertheless, we have set the VAT rate deliberately low so that VAT is a limited burden on all consumers.

### Will visiting businesses be able to reclaim VAT?

It is intended that we will allow foreign businesses to recover the VAT they incur when visiting the UAE. This is important as it encourages them to do business and also, because a lot of other countries have VAT systems, it protects the ability of UAE businesses to recover VAT when visiting other countries (where the rates are a lot higher).