UAE VAT Law – Overview of the new Legislation

Introduction
On November 21st, 2017, a Technical Workshop was delivered on the new UAE VAT Law and the expected implications on the construction industry. The workshop was facilitated by Adrian Low, Partner at Clyde & Co Law Firm. Topics covered included overview of the VAT Law, methods of compliance, and relevant impacts on construction industry.

Due to the full tax legislation not being fully available at the time of the workshop, the UAE VAT Law was discussed at a high level rather than details specific to the construction sector.

What is VAT?
VAT (Value Added Tax) is a consumption tax paid by the end consumer, which will be imposed on all goods and services. The Federal Tax Authority (FTA) has announced the supplies that will be subject to VAT as of January 1, 2018, revealing selected sectors that will be assigned zero-rated tax, such as education, healthcare, oil and gas, transportation and real estate [1].

Supplies Subject to VAT
Selected supplies in sectors such as transportation, real estate, and financial services will be completely exempt from VAT, whereas certain government activities will be outside the scope of the tax system (and, therefore, not subject to tax). These include activities that are solely carried out by the government with no competition with the private sector, as well as activities carried out by non-profit organizations [1]. The UAE Cabinet is expected to issue a Decision to identify the government bodies and non-profit organizations that are not subject to VAT [1].

This FTA website outlines all supplies that will be subject to the 5% Value Added Tax, as well as zero-rated supplies and exempt supplies: https://www.tax.gov.ae/fta-announces-supplies-subject-to-vat.aspx
**What is the VAT process?**

VAT will be charged at every step of the supply chain whereby the seller collects VAT on behalf of the FTA. It will be imposed on all goods and services within the UAE and potentially on the import and export of goods and services. There are, however, exceptions and terms and conditions which one must refer to at the FTA or with qualified lawyers or other financial advisors.

The factors that suppliers/purchasers need to consider in relation to VAT are shown below and reflected in Figure 1:

- Supply of goods or services in the conduct of business
- Place of supply – is supply within or outside the state
- Time of supply – when the tax needs to be paid
- Value of supply – amount on which VAT is charged

![Diagram of VAT process](image)

**Figure 1 Outgoing and incoming VATs**

VAT process has three main categories depending on the legislation applicability. First, the Standard Rate, which is the general category. Secondly is the Zero Rate, which is applicable to selected entities such as Schools. And finally, the Exempt category, which is applicable to exempt entities such as Banks. Figure 2 to 4 illustrate the process for each of these three arrangements.

Zero Rated arrangement will be applicable to:

- Export of goods and services to outside of GCC (initially states who implement VAT)
- International transportation and related supplier
- Supplies of certain sea, air and land means of transportation (such as aircraft and ships)
- International air passenger transport
- Certain investment grade precious metals (gold, silver of 99% purity)
- Newly constructed residential properties, that are supplied for the first time within 3 years of their construction
- Supply of certain education services, and supply of relevant goods and services
- Supply of certain healthcare services, and supply of relevant goods and services

Exempt category will be applicable to:

- Supply of some financial services
- Residential property
- Bare land
- Local passenger transport

*Figure 2 VAT Process of the Standard Rate (General) Category. The end consumer will carry the overall tax price*
Figure 3 VAT Process of the Zero Rate Category. Students will not carry the VAT costs and schools will be able to recover the VAT costs associated with their material purchases from the supplier. Nonetheless, suppliers will charge VAT normally as in the Standard Rate category.

Figure 4 VAT Process of the Exempt Category
Further Details

Reverse Charge: occurs when contracts are being conducted with an overseas company that is not registered within the UAE. This means that the purchaser (in the UAE) would potentially pay less. However, this will not be the case since it will be controlled via a reverse charge paid by the purchaser. This act ensures fairness and competition control within the UAE. As an example, developers will not be able to avoid VAT fees by hiring an Architect from abroad instead of within the UAE. Figure 5 illustrates this process:

**Figure 5 Reverse Charge VAT Process**

Capital Asset Scheme (CAS): reduction of amount reclaimed as Input Tax over life of an asset. If you acquire or create an expensive capital asset, or already have one when you register for VAT, you may have to adjust the amount of VAT you reclaim. You do this by using the Capital Goods Scheme, which allows you to spread the initial VAT claimed over many years [1]. This is applicable to:

- Assets supplied with large capital value and long useful life:
  - AED 5m
  - 10 years building (or part)
  - 5 years other than buildings (or part)
- Expenditures cumulatively more than 5m with stage payments:
  - Purchasing of buildings
- Construction of building
- Extension, refurbishment, fit out work on building
- Purchase construction, assembly or installation of goods or immovable property where components supplied separately for assembly

Designated Zone: consist of areas within the UAE, such as free-zones, that are decided by the cabinet to be exempt from VAT. Cross activities, such as the transportation of a good from one designated zone to another, will be taxed.

VAT Group: aids a single owner with multiple subsidiaries to file an application with FTA to pay the VAT in totality and not for any supplies that are made within the group.

**Transitional Arrangement (2017-2018)**
For activities occurring in 2017 but are delivered in 2018, regardless whether they are a service or a good, will be taxed. Therefore, it’s highly recommended to include a statement in invoices about the applicability of VAT. One could then choose to indicate the VAT within the main invoice or via separate VAT invoice.

**Impact on Construction Contracts**
Based on the FIDIC (International Federation of Consulting Engineers) 1999 (Red Book):
- 1.41(b): Contractor to pay all taxes, duties, and fees and contract price not adjusted except under 13.7.
- 13.7: Contract Price adjusted to take account of any increase or decrease resulting from a change in laws

But unless otherwise stated in the Conditions (14.1), therefore need to check specific terms. Dubai Municipality (and other large employers) all have specific terms passing risk onto the Contractor, so no automatic ability to pass on VAT costs.

**VAT Invoicing**
Two prevailing invoices will be appearing in 2018. “VAT Invoice” is a detailed invoice highlighting all aspects of the purchase that will be seen for example when signing a design consulting contract. “Simplified VAT Invoice” is a concise and short invoice which will be provided in cases such as buying groceries from the supermarket.

**Conclusion and Advice**
VAT, in summary, will be a cashflow rather than a cost problem. End consumers will take the burden of the price increase, whereas most of the B2B activities will be a simple transfer of the VAT from the incoming onto the outgoing invoices. Any delays or nonconformity of stakeholders will not be tolerated by the FTA. Hence, each company
will have to pay the VAT dues in time regardless of any external difficulties in the supply chain.

References
