

UAE VAT Health Check

*What Every Business Should Review
Before the FTA Does*

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VAT compliance in the UAE has moved well beyond filing returns on time. The Federal Tax Authority (FTA) has significantly enhanced its audit capabilities deploying data analytics and AI-driven cross-verification tools to identify discrepancies that may not be visible on the surface of a business's filings. In 2024 and 2025, audit activity intensified across key sectors including real estate, financial services, retail, and logistics.

The uncomfortable reality is that most businesses that fail FTA audits do not do so because they applied the wrong VAT rate. They fail because of weak documentation, incorrect timing of supply recognition, missing invoices, or undisclosed errors. These are all issues that a structured VAT Health Check is designed to catch before the Authority does.

This article walks through what a VAT Health Check involves, what it typically uncovers, and why it matters, illustrated through real-world scenarios from industries operating in the UAE.

Compliance is King

1. Why Does a VAT Health Check Matter?

Under Federal Decree-Law No. 28 of 2022 on Tax Procedures, the compliance burden rests entirely with the business. The FTA does not verify filings before accepting them; it audits after the fact, often years later. By that point, penalties, and reputational impact have compounded significantly.

Key obligations every UAE business must meet include:

- ▶ Accuracy of VAT returns and all disclosures made to the FTA
- ▶ Maintaining complete accounting records, commercial books, and VAT-related documentation
- ▶ Retaining all invoices, contracts, correspondence, and working papers for at least 5 years (7 years for real estate transactions, 10 years in case of capital assets scheme data)
- ▶ Correcting errors proactively through Voluntary Disclosure before the FTA identifies them
- ▶ Responding to FTA information requests within the specified window commonly 10 business days from notification of audit procedures

That last point is often underestimated. Businesses that cannot compile complete, accurate, audit-ready documentation within a short FTA response window face extended audit cycles, additional penalties, and increased scrutiny across all tax periods.

2. The Cost of Non-Compliance Key Penalties

Cabinet Decision No. 40 of 2017 (as amended, effective 14 April 2026) sets out the administrative penalties applicable to VAT violations:

Violation Type	Penalty	How to Mitigate
Incorrect VAT return	15% fixed + 1% per month on tax difference (if no VD before audit)	File accurate returns on time; submit VD proactively
Failure to issue a tax invoice	AED 2,500 for each detected case	Implement invoice compliance checks
Failure to maintain required records	AED 10,000 (first); AED 20,000 (repeat)	Structured record-keeping with 5-year retention
Failure to notify record changes	AED 1,000 (first); AED 5,000 (repeat)	Immediate update with any changes in record
Late payment of tax due	14% per annum	Ensure payment of tax due within legal timeframe
Voluntary Disclosure (before audit notice)	1% per month only	Early detection through a VAT Health Check

Submitting a Voluntary Disclosure before the FTA issues an audit notice results in a significantly lower penalty 1% per month only. Once the FTA notifies you of an audit, the penalty rises to 15% fixed plus 1% per month. Early detection through a VAT Health Check is always the lower-cost path.

3. What Does a VAT Health Check Cover?

A well-structured VAT Health Check examines twelve key compliance areas. Each represents a common source of audit findings in the UAE:

1. Date of Supply

VAT is triggered at the earliest of: the invoice date, the date payment is due, or the date payment is received. Many businesses incorrectly recognize VAT on a cash basis, creating timing mismatches that are easily flagged during an FTA audit.

2. Revenue Reconciliation

Trial balance figures must align with VAT returns for every filing period. Unexplained variances between accounting records and VAT returns are a primary audit trigger.

3. All Revenue Streams

Every income stream must be correctly classified for VAT. Incidental income such as late payment penalties, management fees, disposal of assets, or recharge costs is frequently omitted or misclassified.

4. Transitional Contracts

Retentions and milestone payments under contracts that span the VAT introduction date (1 January 2018) carry specific transitional rules. Incorrect treatment of these continues to surface in audits years later.

5. Cross-Border Supplies

Zero-rated exports must be supported by valid proof of export. Without documentation such as customs declarations, shipping records, or proof of physical departure zero-rating cannot be substantiated.

6. Input Tax Recovery

Only eligible input VAT may be recovered. Blocked categories under Article 53 of the Executive Regulation include entertainment, personal expenses, and motor vehicles used for personal purposes.

7. Tax Invoice & Credit Note Compliance

All tax invoices must contain the mandatory fields prescribed by Articles 59 and 60 of the Executive Regulation. Non-compliant invoices are not only a penalty exposure; they may invalidate input tax recovery for your customers.

8. Voluntary Disclosures

Known errors or omissions must be corrected proactively. Unaddressed errors discovered during an FTA audit attract significantly higher penalties than self-corrected disclosures.

9. Reverse Charge Mechanism (RCM)

Imports of goods and services from overseas suppliers must be self-assessed and declared. Under-reporting of RCM is a common finding, particularly for businesses receiving IT, professional, or marketing services from abroad.

10. VAT Classification

Supplies must be correctly classified as standard-rated (5%), zero-rated, exempt, or out of scope. Misclassification particularly treating taxable supplies as exempt or out of scope is one of the most financially significant errors identified in health checks.

11. Bad Debt Adjustments

Input VAT may be recovered on bad debts in defined circumstances under Article 64. Many businesses either miss this relief entirely or claim it without satisfying the required conditions.

12. Record Retention & Audit Trail

All VAT-related records must be retained for the statutory period with a clear, traceable audit trail. Incomplete or disorganized records alone can result in penalties during an audit.

4. Know Your Customer (KYC) and Know Your Vendor: VAT Compliance Considerations

One area frequently overlooked in VAT compliance reviews is the quality and completeness of customer and vendor master data. Under the UAE VAT Law and its Executive Regulations, businesses must ensure that tax invoices are issued accurately and that information recorded for both customers and suppliers is verified and up to date. Failure in this area can have direct VAT consequences from invalid input tax recovery to non-compliant tax invoices that do not meet the FTA's prescribed requirements.

From a customer (KYC) perspective, businesses must verify whether their customers are VAT-registered, as this in certain cases determines the invoicing treatment, the place of supply rules applicable to the transaction. Issuing a tax invoice with an incorrect or unverified Tax Registration Number (TRN) without cross-checking against the FTA's public TRN verification portal can result in invoices that are technically non-compliant, exposing the supplier to penalties under the Tax Procedures Law.

From a vendor perspective, the integrity of supplier data is equally critical. Input tax credit can only be claimed where the business holds a valid tax invoice from a VAT-registered supplier. If a vendor's TRN is incorrect, expired, or unverifiable, any input tax claim associated with that vendor becomes vulnerable to disallowance during an FTA audit. Businesses that have not periodically validated their vendor master data against the FTA's TRN verification portal may be unknowingly carrying invalid input tax claims across multiple tax periods.

What a VAT Health Check addresses in this area:

A VAT Health Check provides the opportunity to systematically review both customer and vendor master data, verifying TRN accuracy, identifying gaps in invoice documentation, confirming that the correct VAT treatment is applied based on the customer's registration status, and ensuring that the business's records are audit-ready before the FTA makes contact.

5. E-Invoicing Implementation: Why a VAT Health Check Is the Right Starting Point

The UAE's e-invoicing framework is being progressively rolled out, with businesses expected to transition to a structured digital invoicing environment across phased implementation waves. While much of the early conversation around e-invoicing has focused on technology and system integration, the underlying VAT compliance requirements are equally, if not more, critical to address before go-live.

At the core of e-invoicing is tax code mapping: the process of assigning the correct VAT treatment to each transaction type, line item, and supply category within a business's ERP or invoicing system. This mapping determines whether a supply is tagged as standard-rated (5%), zero-rated, exempt, or out of scope, and that classification feeds directly into the structured data transmitted to the FTA under the e-invoicing regime.

The critical exposure:

Errors that previously existed only in manually prepared VAT returns will, under e-invoicing, be embedded and transmitted in real time. A misclassification that may have gone undetected in a return will now be systematically replicated across every invoice issued and will be immediately visible to the FTA upon transmission. Businesses that approach e-invoicing as a purely technical exercise, without first ensuring their underlying VAT positions are correct, may end up automating non-compliance at scale.

A VAT Health Check conducted ahead of e-invoicing implementation is therefore not just a compliance exercise; it is a foundational step in ensuring a smooth, accurate, and fully compliant transition. Specifically, a pre-implementation review allows businesses to:

- ▶ Verify their current VAT positions across all supply types and ensure these are correctly understood before being hardcoded into the e-invoicing system.
- ▶ Review tax code mapping logic to confirm that the VAT treatment applied in the ERP aligns with the requirements of the UAE VAT Law and Executive Regulations.
- ▶ Identify and correct historical misclassifications before they are carried forward into the e-invoicing environment, avoiding the compounding of existing errors at scale.
- ▶ Assess customer and vendor data readiness ensuring that TRNs, entity names, and invoice data fields meet the structured format requirements of the e-invoicing schema.
- ▶ Ensure contract and pricing structures reflect the correct VAT treatment, particularly where long-term agreements may not have been revisited since the original VAT implementation in 2018.

Businesses that invest in a VAT Health Check now before e-invoicing implementation will be significantly better positioned to transition seamlessly, avoid costly corrections post-go-live, and demonstrate a proactive compliance posture to the FTA.

6. Real-World Examples: What Health Checks Uncover

The following scenarios are illustrative of findings commonly identified across UAE industries during structured VAT Health Checks.

Case Study: Real Estate Developer

Scenario: A large developer in Dubai had been issuing tax invoices to buyers at the time of handover rather than at the earlier of payment due date or receipt of payment.

What we found: Systematic date of supply errors across hundreds of transactions, resulting in VAT being declared in the wrong tax period. Exposure to underpayment penalties spanning multiple years.

Key takeaway: Date of supply rules for real estate are strict. VAT is triggered at the earliest event, not at handover. Proactive correction through Voluntary Disclosure before an audit notice significantly reduced the penalty exposure.

Case Study: Logistics & Freight Company

Scenario: An international freight company operating across several UAE free zones was zero-rating cross-border transport services. Documentation was incomplete; many shipments lacked bill of lading or proof of physical export.

What we found: Without valid export evidence, the zero-rating applied to a significant proportion of supplies could not be substantiated. The company faced a potential reclassification to standard-rated, with VAT, and penalties payable.

Key takeaway: Zero-rating is not automatic. Every zero-rated supply requires documented evidence retained for 5 years. A documentation gap is the most common and most avoidable finding in cross-border supply reviews.

Case Study: Financial Services Institution

Scenario: A UAE bank was using the standard inputs-based apportionment method to recover residual input tax. A health check was conducted ahead of a planned FTA audit.

What we found: The standard method was yielding a recovery rate significantly higher than what the outputs-based special method, which was more appropriate for the bank's business model would produce. The FTA subsequently required the bank to apply for the approved special method.

Key takeaway: Financial institutions making both taxable and exempt supplies should assess whether the standard apportionment method reflects their actual use of inputs. An incorrect method, even if applied consistently, may be challenged during audit.

Case Study: Retail Business (Multi-Brand)

Scenario: A multi-brand retailer with operations in both the UAE mainland and a Designated Zone had been treating intercompany stock transfers as out-of-scope supplies.

What we found: Depending on the nature of the goods and the point at which title transferred, certain transfers were taxable supplies, not out-of-scope movements. The business had both under-declared output VAT and over-claimed input VAT on the same transactions.

Key takeaway: Designated Zone rules are nuanced and frequently misapplied. Intercompany transactions between related entities deserve close attention; the substance of the transaction, not just the documentation, determines the VAT treatment.

7. Businesses/transactions which are frequently audited or reviewed by FTA

While any VAT-registered business can benefit from a health check, the following categories carry the highest exposure based on FTA audit trends:

High-Priority Businesses	Also Recommended For
Companies with multiple revenue streams or subsidiaries	Designated Zone and Free Zone entities
Exporters with input VAT refund claims	Groups with cross-border or related-party transactions
Construction, real estate, and infrastructure businesses	Finance teams with recent turnover or ERP system changes
Businesses that have never had an external VAT review	Any entity that has received an FTA audit notification
Companies with high volumes of intercompany transactions	Businesses with complex supply classifications (exempt + taxable)

8. What Does a Health Check Deliver?

A structured VAT Health Check typically results in:

- ▶ A priority-ranked issue log with corrective steps and prioritized recommendations
- ▶ A revenue-to-return reconciliation report identifying unexplained variances
- ▶ Input VAT recovery validation and optimization recommendations
- ▶ Tax invoice and TRN compliance review across a sample of transactions
- ▶ Voluntary Disclosure recommendations with penalty quantification
- ▶ Record-keeping and audit trail assessment
- ▶ A management briefing and, where required, finance team training on identified gaps

The outcome is not a list of problems; it is a practical, commercially grounded action plan that a business can implement to strengthen its compliance position ahead of any FTA engagement.

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