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Value Added Tax - Update

Amendments to the UAE VAT Executive Regulation

Contact Us

+971 4 243 5666
info@ae.Andersen.com

UAE Office Locations

402 Arenco Tower, Dubai Media City, Dubai
103 Sama Tower, Electra Street, Madinat Zayed, Abu Dhabi

Amendments to the UAE Value Added Tax (VAT) Executive Regulation

Via Cabinet Decision 100 of 2024
Effective from 15th November 2024

Brief

On October 2, 2024, the Federal Tax Authority (FTA) announced Cabinet Decision No. (100) of 2024, updating the Executive Regulation of Federal Decree-Law No. (8) of 2017 on Value Added Tax (VAT). This regulation will take effect on November 15, 2024, addressing the evolving business landscape in the UAE. It includes amendments to over 30 articles impacting various industries. Below are the key updates and changes to note.

Financial Services

The amendment in Article 42 of the VAT Executive Regulations introduced a welcome change regarding the scope of Financial Services, covering Virtual Assets, i.e., cryptocurrencies and NFTs, which are defined as "Digital representations of value that can be digitally traded or converted and can be used for investment purposes, and does not include digital representations of fiat currencies or financial securities."

The scope of the exemption from VAT includes transfers, conversion, keeping, managing, and enabling control thereof Virtual Assets. Note that the scope of exemption must meet the criteria of the definition set forth for Virtual Assets—in cases where activities related to digital fiat currency (e.g., conversion of Bitcoin to USD) and financial securities, the transaction may not fall within the definition, and the VAT treatment must be assessed independently.

Further, Article 42 of the VAT Executive Regulations was amended to include the services relating to management of investment funds under the scope of the 'Financial Services' definition, thereby allowing the exemption from VAT for any such services.

It is imperative that the companies engaging in such activities keep a note of the implications of input tax due to the new scope of exempted financial services, as any input tax may only be claimed to the extent that is directly related to taxable supplies made by the company.

Article 42(3) exempts activities in 42(2) not conducted for an explicit fee, including fund management and services from paragraphs (k) and (l), with effect retrospectively from 1 January 2018.

Businesses in the UAE used to be involved in selling NFTs (Non-Fungible Tokens). NFT is a unique digital asset that represents ownership of a specific item or piece of content, like art, music, videos, or virtual real estate, on a blockchain.

Lack of clear guidance in the earlier versions of regulations, businesses experienced an ambiguity in VAT treatment, where some of the businesses, following a conservative approach, treated such sales as sales of intangible assets, constituting them as a taxable supply and subject to 5%.

However, with the recent amendments, such transactions shall be benefitted by exemption from VAT.

Andersen's Take

Cryptocurrency has emerged as a global phenomenon, experiencing exponential growth over the past decade. The UAE has witnessed remarkable growth in crypto transactions and activities. However, the absence of appropriate legislation for cryptocurrencies has underscored the need for clarity regarding their tax treatment. Businesses used to face issues in claiming the input tax credits with respect to services received in relation to cryptocurrency. To address this, positions were established based on guidance from foreign jurisdictions and private clarifications.

The recent amendment concerning virtual assets is essential, as the use of cryptocurrencies and NFTs has surged without clear VAT guidelines. Previously, companies operating in this sector faced uncertainties due to a lack of concrete regulations, resulting in inconsistent VAT treatment.

This amendment provides much-needed clarity, thereby reducing the risk of incorrect VAT application. The ITC apportionment after the amendment between taxable and exempt supplies will need to be closely monitored by the businesses to ensure necessary compliance with the provisions of the law.

Moreover, the ancillary services such as commission, brokerage, account handling fee, management fee, and like will still be under the purview of VAT at the standard rate, as these are services against which explicit fees will be charged by the supplier.

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Zero-rating the export of goods

Article 30(1) and (2) of the ER now outlines the official and commercial evidence exporters must retain to meet the conditions of zero-rating Direct and Indirect Exports. Exporters should maintain either of the following:

1. A customs declaration and commercial evidence of export.
2. A shipping certificate and official evidence of export.
3. A customs declaration proving a customs suspension arrangement for goods under suspension.

Clause 4 of Article 30 clarifies definitions:

- **Official Evidence**: An export certificate from customs or a clearance document verifying the goods' departure.

- **Commercial Evidence**: Documents from transport companies proving the transfer of goods, including air waybills, sea waybills, or land waybills.

- **Shipping Certificate**: A certificate from transport companies as a substitute for commercial evidence when unavailable.

The change introduced by the amended Article 30(1) provides beneficial clarity through specification of the documentation required to be maintained by exporters for adhering to the conditions for zero-rating.

Andersen's Take

Practical challenges often arise with customs authorities regarding the procurement of exit certificates, which used to create uncertainty in proving that goods have indeed left the UAE and thus entitling them for a zero-rating benefit of export of goods. The expanded definition of official evidence now allows taxpayers to consider alternative documentation to satisfy regulatory requirements, enhancing compliance and operational efficiency and reducing the potential for disputes with the FTA.

However, it is important to note that the FTA retains the right to deny or reject any submitted documents. Therefore, maintaining comprehensive documentation from both a commercial and export perspective is advisable.

From a customs law perspective, exit certificate requirements are still prevalent, and taking a conservative approach, businesses should still try to get exit certificates in most cases. The detailed clarification following the amendment is awaited from FTA.

Zero-rating the export of services

Article 31(1) has been amended to state that the export of services will be zero-rated if the services are not considered performed in the State or a Designated Zone, as defined in Clauses 3 to 8 of Article 30 and Article 31 of the Decree-Law.

Articles 30, paragraphs 3 to 8, and Article 31 of the Decree-Law outline special place of supply rules for services such as real estate-related services, electronic services, and telecommunications services. This amendment may potentially limit the application of the zero-rating for exports.

For instance, if a business is providing services of digital marketing supplied via electronic means to a customer who does not have a Place of Residence in the UAE and who is outside the State at the time the Services are performed, but the target audience and enjoyment of service are taking place in the UAE. In this case, these services shall be subject to the VAT at the standard rate of 5% as applicable by the special place of supply rules under Article 31 of the Decree Law, where the place of supply is determined by the extent of use and actual enjoyment of such service in the UAE.

Andersen's Take

This change is a welcome development, as it aligns with the principle that the export of services should not be subject to zero rating when the actual consumption, use, and benefit of those services occurs within the UAE. This update significantly reduces the ambiguity surrounding tax positions for service export transactions that many multinational companies in the UAE have faced.

Input Tax Recoverability

Article 53(1) of the ER brought upon a positive change, wherein the input tax related to health insurance and enhanced health insurance provided to dependants of the employees is now recoverable, to the extent of one spouse and up to three children under eighteen.

Andersen's Take

This update offers substantial benefits for businesses providing comprehensive health benefits. Previously, VAT on dependent insurance was non-recoverable, placing a tax burden on companies. The companies faced difficulties in their refund application from back in 2018, where FTA rejected the refunds of tax relevant to health insurance claims of the employee and their dependents, and companies had to file for VD in order to rectify their error. This change by the FTA is particularly advantageous for organizations with large employee bases. We have noted considerable litigation regarding input tax claims on dependent medical insurance in Dubai. The new regulations establish a revised tax position, which could have implications for ongoing retrospective litigation cases.

Government Entities

Article 69(3) concerning tax refund claims by Foreign Governments now requires submission within "36 months from the date the tax was incurred" or another specified period under international agreements. A new Article 3(bis) introduces Exceptions to Supplies for the first time in the VAT Law, stating that the following are not considered supplies:

1. The grant or transfer of ownership or disposal of government buildings and real estate from one Government Entity to another.
2. The transfer of rights to use government buildings and assets, effective January 1, 2023.

For Clause 1, government buildings and assets include:

- Government premises
- Capital projects
- Infrastructure projects
- Real estate used by Government Entities
- Assets serving public utilities
- Developed government land

The scope of these assets will be defined by a decision from the Minister. These changes aim to streamline operations within government entities and address public sector transaction needs in the UAE.

Andersen's Take

These amendments provide much-needed relief to government entities, allowing them to operate more efficiently by eliminating the need to consider VAT for intra-government transfers. Previously, these transactions were VAT applicable, creating unnecessary complexities. The new rules provide a streamlined approach to taxability for such activities.

Zero-rating the international transportation services

Article 33(1) states that the supply of international transportation services and transport-related services will be zero-rated when transporting goods within the State, provided the services are supplied by the same supplier as part of the international transport. In the scenario where a company is exporting goods from the UAE to a location outside the UAE and two logistics companies are involved in the transportation process, where logistics company A is appointed to transport goods from its warehouse in Dubai to another warehouse in Abu Dhabi and logistics company B subsequently assists with exporting the goods from Abu Dhabi to an international destination, the VAT treatment for these services, according to the recent amendments, shall be such that the supply of transportation services provided by logistics company A will be subject to VAT at the standard rate.

This is because the entire leg of the transportation was not provided by the same supplier; thus, it does not qualify for zero-rated export status under UAE VAT law.

Andersen’s Take

Earlier, businesses that provided service for local transportation of goods used to claim the benefit of zero-rating the international transportation services, assuming that the final leg of such a logistical arrangement would have been an export.

Profit Margin Scheme

Article 29(5) of the ER on Accounting for Tax on the Profit Margin states that the "purchase price" in Clause 4 includes not just the price of the good but also any costs and fees incurred in the purchase.

Andersen’s Take

This clause provides clear guidelines for taxable persons using the profit margin scheme on what to include in the purchase price. Businesses used to have an asymmetric view of whether to include the associated cost under the purchase price or not. Businesses will need to revisit how they calculate the purchase price of goods, including all associated costs—such as shipping, handling, and transaction fees—which could increase the purchase price and result in a lower taxable profit margin. This may result in lower taxes owed when selling goods under profit margin schemes.

Apportionment of Input Tax

The newly added clause 4 of Article 55 on tax periods states the tax year ends in the following cases:

a. When a Taxable Person applies for deregistration, it ends on their last day as a Taxable Person.

b. For a member joining a Tax Group, it ends the day before joining.

c. For a member leaving a Tax Group, it ends on their last day as a member.

Clause 11 of Article 55 states that if the difference between the calculated Recoverable Tax and the actual usage of Goods and Services exceeds AED 250,000, the Taxable Person must adjust the Input Tax in the specified Tax Period.

Additionally, a new Clause 12 of Article 55 specifies that if a tax year is less than 12 months, the amount referenced in Clause 11 of Article 55 must be adjusted proportionately.

For instance, a company applies for tax deregistration on 30th June 2024. As per the amendment, the tax year of such a company shall end on the last day of it being a taxable person, i.e., 30th June 2024.

For such a company, if the difference between the calculated Recoverable Tax and the actual usage of Goods and Services exceeds AED 123,972.60 (AED 250,000/365*181), the Taxable Person must adjust the Input Tax in the specified Tax Period.

Andersen's Take

When companies are applying for tax deregistration or are joining/leaving a tax group, they need to assess the pro-rata calculations for the actual use adjustment of input tax, taking into account the amended tax period on a case-by-case basis. The companies need to proportionately adjust the AED 250,000 difference to such a tax period as is applicable. This amendment signifies that businesses shall have the benefit of AED 250,000.00 only to the extent they are righteous for.

Tax Credit Notes

The amended Article 60(1) regulations have specified that in case more than one Tax Credit Note is issued in relation to the same Tax Invoice, the value of the supply shown on the Tax Invoice in the subsequent Tax Credit Note shall be the adjusted value based on the previous Tax Credit Note.

For example: A supplier of goods issued a tax invoice worth AED 50,000 to the customer. Later, the goods worth AED 10,000 were returned by the customer due to some reason, and the supplier issued a tax credit note worth AED 10,000.

Subsequently, the customer happened to return the remaining goods worth AED 40,000 to the supplier due to non-conformity with the quality of the goods.

In this case, the supplier should adjust the value of the original invoice based on the previous Tax Credit Note, i.e., the original invoice shall now be valued at AED 40,000 and not AED 50,000.

Andersen's Take

As a conservative approach, the supplier's subsequent tax credit note should include the reference to the original tax invoice as well as the first tax credit note issued. This change shall have some implications in the format of the tax credit note, along with some system changes to accommodate this amendment.

Exceptions related to Deemed Supply

The Deemed Supply Exception provision has been streamlined and expanded, permitting up to AED 250,000 for each supplier that qualifies as a government entity or charitable organization, provided the recipient is also a government entity or charitable organization, within a twelve-month timeframe.

Andersen's Take

This extension alleviates the VAT burden for charitable organizations and government entities, allowing them to pursue their activities more freely.

Tax on supplies of more than one component

Article 46(1) of the ER has been amended to state that if a single composite supply lacks a principal component, tax treatment will be based on the nature of the supply as a whole.

Andersen's Take

Retailers often create bundled offers to attract customers. With the new tax treatment, they will need to analyse whether their bundles will be taxed more favourably or unfavourably, potentially leading to a re-evaluation of marketing strategies.

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This amendment has led to several significant changes that will impact taxpayers in various ways. Below, we outline key steps companies may consider when planning their next steps:

System Changes

- VAT accounting systems to accommodate both exempt and taxable transactions related to virtual assets, including changes in VAT rates and tax invoice and credit note formats.

Documentation

- Ensure proper documentation for transactions to comply with the new definitions and requirements.

Public Clarification

- Wait for further guidance from the FTA, which will provide a public clarification guide to assist taxpayers in adapting to these changes.

VAT Returns

- Review upcoming VAT returns to determine if any adjustments or voluntary disclosures (VDs) are necessary for transactions affected by the amendments.

Cross-border Tax Considerations

- Businesses engaged in cross-border transactions should prepare for potential adjustments in future returns to comply with the new regulations.

Impact on Ongoing Litigation

- Evaluate any pending VAT litigation related to transactions affected by these amendments, such as those involving medical insurance or export of goods, as this amendment may retroactively resolve such disputes.

Our Team

Contact Us

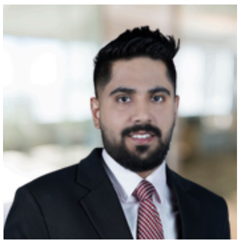
Anurag Chaturvedi
Chief Executive Officer
anurag.chaturvedi@ae.andersen.com

Kanika Duseja
Partner, Leader M&A Tax
kanika.duseja@ae.andersen.com

Krishnan Narayanan
Abu Dhabi Partner
krishnan.narayanan@ae.andersen.com

Prateem Sengupta
Director, Direct Tax Leader
prateem.sengupta@ae.andersen.com

Thomas Lassey
Partner, Indirect Tax
thomas.lassey@ae.andersen.com



Gaurav Chugani
Associate Director
gaurav.chugani@ae.andersen.com

Gurleen Sethi
Associate Director
gurleen.sethi@ae.andersen.com

UAE Office Locations: *Dubai*: 402 Arenco Tower, Dubai Media City | *Abu Dhabi*: 103 Sama Tower, Madinat Zayed.
Contact Us: +971 4 243 5666 | info@ae.andersen.com