



VAT Public Clarification – Labour Accommodation

Introduction

The Federal Tax Authority (FTA) has recently issued a Public Clarification (VATP003) on VAT treatment on Labour Accommodation, pursuant to the Clarification User Guide issued by FTA in April 2018. In this clarification, FTA has specified the mechanism to determine whether the accommodation provided is supply of residential building and hence not subject to VAT (the first supply is zero-rated, and subsequent supplies is exempt) or the accommodation provided is a supply of service accommodation and hence subject to VAT @ 5%.

Important aspects clarified by FTA are as below:

When would supply of labour accommodation be treated as supply of residential building?

If labour accommodation is provided in a residential building, which is defined to mean:

- the building or lodging
- the building that is fixed to the ground and which cannot be moved without being damaged
- the building has been constructed or converted with lawful authority
- it is not a building that is similar to a hotel, motel, bed & breakfast establishment, or serviced apartment for which services in addition to the supply of accommodation are provided

then it would be treated as supply of residential building.



If certain additional services are provided along with labour accommodation in a residential building, then would the supply be regarded as supply of residential building?

If additional services are incidental to the main supply of accommodation and is not provided for an additional fee, then the same should be regarded as supply of residential accommodation. Such incidental services may include, but are not limited to, the following:

- cleaning of common areas
- maintenance services required for the general upkeep of the property
- pest control
- garbage collection
- security
- utilities e.g. electricity, water, etc

It may be noted that the above list is indicative and not exhaustive.

These specified services would be regarded as incidental to the principal supply and taxability would be determined on the basis of principal supply, i.e. supply of residential building. However, if the services are provided for an additional fee that is charged to the customer, it would be regarded as separate supply and VAT @ 5% would be leviable.

In our view, the test that needs to be fulfilled to ascertain if the supply is of residential building is that the additional services provided should be incidental or ancillary to the principal supply and this should be necessary for provision of principal supply or better means of enjoyment of principal supply.

When would supply of labour accommodation be treated as supply of service accommodation/ service apartment?

A supply of labour accommodation would be treated as supply of service accommodation/service apartment in the following situations:

- Any place that is not a building fixed to the ground and can be moved without being damaged.
- Any building that is used as a hotel, motel, bed and breakfast establishment, or hospital or the like.
- A serviced apartment for which services in addition to the supply of accommodation are provided.
- Any building constructed or converted without lawful authority.



Which additional services provided along with accommodation would lead to supply of service apartment?

If following services are provided along with accommodation for a single value (i.e. composite supply), then the supply would be regarded as supply of service apartment:

- telephone and internet access
- cleaning of the rooms, other than common areas of the property;
- laundry services, including the regular changing of bed linen
- catering
- maintenance services other than those required for the general upkeep of the property.

It may be noted that the above list is indicative and not exhaustive.

Accordingly, if any of these services are provided along with accommodation, it would lead to supply of service apartment and VAT @ 5% would be leviable.

In our view, if any of these services are provided along with supply of residential building, then the value of each supply should be identified separately, and VAT treatment should be determined based on each supply.

For supply of residential building, if different charges are charged then would the supply would be regarded as single composite supply or mixed supply?

If different charges are charged separately to the customer, the supply may not be regarded as a single composite supply and the supply would be regarded as a mixed supply. Taxability would be determined based on each supply and the value of each supply must be mentioned separately on the tax invoice.

If a composite supply of residential building/service apartment is made, then which factors should be considered for the purpose of determination?

The following factors are to be considered:

- Supply is of the following:
 - a principal component
 - a component or components that are either necessary or essential to the making of the supply, including incidental elements that normally accompany the supply but are not of a significant part of it; or do not constitute an aim in itself, but are instead a better means of enjoying the principal supply
- Supply has two or more elements that are so closely linked as to form a single supply, which it would be impossible or unnatural to split
- The price of the different components of the supply is not separately identified or charged by the supplier
- All components of the supply are supplied by a single supplier



Supply shall be prevented from being treated as single composite supply, if various components are supplied by different suppliers or where the prices of each component are separately listed out.

Accordingly, if the supplier has used services from different suppliers for the provision of services to the customers, then the supply would be regarded as a mixed supply unless the services used from different suppliers are incidental to the main/principal supply (provided by the supplier). It is further clarified that charging a single price does not necessarily mean that it is a composite supply, i.e. there is no principal component in the supply.

Comments

Businesses should assess the impact of this clarification for their similar transactions and appropriate actions should be undertaken if there is a requirement to change the tax position, i.e. supply treated as residential building is regarded as supply of service apartment or vice versa. Also, businesses should evaluate whether there is a requirement to change the contractual terms including pricing considering the principles specified for classifying the supply as composite supply or mixed supply.



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