



# Five Years of VAT in the UAE

Evolution, Challenges, Future

January 2023



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# | FOREWORD

The introduction of value added tax (“VAT”) with effect from 1 January 2018 was a revolutionary development for the United Arab Emirates (“UAE”). While VAT was not the first federal tax to be introduced in the UAE – this distinction goes to the Excise Tax, which came into effect a mere three months earlier – VAT was the first truly universal federal tax that directly impacted all segments of UAE population, business and government.

Now that we have passed the five-year mark since the introduction of VAT, it is fair to conclude that the tax has been a success and a true testament to the UAE’s ability to adapt to the new economic realities. This five-year anniversary is a good time to

look back at the progress of the UAE’s VAT regime, contemplate the lessons learned, and consider the path that VAT may take going forward.

In preparing this publication, we would like to thank the UAE business and tax leaders who have shared their experiences of the UAE’s VAT regime (refer to Part 7 of this publication). Their experiences give first-hand insights of how the introduction of VAT impacted businesses in practical terms and can serve as timely reminders for businesses that are currently contemplating the impending introduction of corporate income tax.



**Dinesh Kanabar**  
CEO





# | EXECUTIVE SUMMARY

**It is my pleasure to present the “Five Years of VAT in the UAE” report, which captures the journey of the VAT regime since its introduction on 1 January 2018.**

The introduction of VAT was a landmark step in the UAE as it was perhaps the largest Federal tax that resulted in organisations making a paradigm shift in the way business was being conducted.

The entire business community as well as government organisations were required to become rigorously compliant with the new VAT regulations, train their teams on managing taxes, re-configure ERPs to make them tax compliant, modify their HR policies and get ready to be penalised for any non-compliance. This was perhaps the first time this country had witnessed any regulatory change of such a magnitude.

**This report is our attempt to take the readers through a journey, captured in five parts:**



**Nimish Goel**

Partner



## Evolution of the VAT system

We talk about how the UAE initiated discussions for an introduction of VAT and the best global practices that were adopted in the drafting of the legislation. We also talk about founding the Federal Tax Authority.



## Journey until now

We discuss the amendments made in the VAT legislation and how they impact taxpayers.



## Industry specific issues

We pick up some key technical VAT issues for few of the prominent sectors in the UAE including real estate, retail, healthcare & hospitality.



## Our client's speak

Senior industry finance and tax leaders write about their experience of implementing and managing VAT in their organisations.



## Next five years

We share our perspective on where this country and the world in general is moving in the area of taxes. We discuss tax technology and the introduction of corporate tax and how such factors are going to impact businesses in the future.



# BACKGROUND TO INTRODUCTION OF VAT IN THE UAE



## SOCIOECONOMIC CONTEXT

Prior to the introduction of excise tax and VAT in October 2017 and January 2018 respectively, the UAE did not have taxes that would apply at the federal level in a consistent fashion across all Emirates. While different Emirates, municipalities and government organisations have been imposing their own duties and levies, these charges are not uniformly imposed throughout the country and are not collected or shared at the federal level.

At the same time, similar to the other Gulf Cooperation Council ("GCC") countries, the UAE's economy was heavily dependent on revenues from the oil and gas sector, with extractive industries accounting for approximately a third of the UAE's GDP throughout the 2010s. While this heavy reliance on the oil and gas industry was justified when the oil and gas prices were consistently on the rise, things became much more unpredictable with the 2008 global financial crisis – when the prices first fell by almost four times and then remained volatile throughout the next decade. This unpredictability convinced the UAE, along with the other GCC countries, to embark on the journey of revenue diversification – and the introduction of the VAT was an important step in that journey.



## WORK ON POLICIES AND LEGISLATION

Initial discussions between the GCC member states in respect of bringing VAT to the region began in 2008. Since nobody wanted to be left behind or find themselves at a competitive disadvantage relative to other member states by being the only country to introduce VAT, it was quickly decided that the introduction of the new tax was to be conditional on the agreement of all GCC member states. In 2016, after years of on-and-off discussions and negotiations, the GCC member states finally signed the Common VAT Agreement of the States of the Gulf Cooperation Council ("the GCC VAT Agreement"), which provided the common framework and principles that had to be adhered to by the GCC member states when implementing VAT within their own jurisdictions.

At the beginning of 2016 it was announced that VAT would be introduced in the UAE from 1 January 2018. In August 2017, the government issued the VAT Law, which provides the main VAT rules and principles. Lastly, in November 2017, the government released the VAT Executive Regulations, which are intended to supplement the VAT Law by providing additional details regarding the application of VAT rules. The VAT Law and VAT Executive Regulations form the backbone of UAE VAT legislation and are the primary source of reference for the tax officials, taxpayers, and courts in respect of the application of VAT.



## FOUNDING OF THE FTA

While introducing a new tax would generally be seen as challenging enough, the UAE had to initially deal with a unique additional complication of not having an existing federal tax authority.

In anticipation of the introduction of the excise tax and VAT, in 2016 the government established the Federal Tax Authority ("FTA") under the Federal Law by Decree No. 13 of 2016. The FTA was given jurisdiction over the administration, collection and enforcement of federal taxes, and therefore became the ultimate government department responsible for federal taxation in the UAE.

Since the FTA was established as a new organisation rather than being built upon an existing foundation of another department, an incredible amount of work had to be done to get it ready for the introduction of excise tax in October 2017 and VAT in January 2018. In less than a year since its establishment, the FTA had succeeded in becoming a fully functional authority with its own staff, resources and technological platform. It has been able to administer multiple tax regimes, collect different taxes and effectively communicate with taxpayers and other stakeholders.



# INITIAL CHOICES IN DESIGNING VAT

There are many ways to design a tax regime. Policy choices are often influenced by external factors such as the social and commercial environment in the country and the region.

In the UAE's case, it is important to remember that the VAT regime was not created in isolation – instead, the UAE is a signatory to the GCC VAT Agreement which provides common VAT principles to be followed by each of the GCC member states when introducing VAT. Therefore, as a starting point, UAE's VAT policies had to be aligned with the broader VAT framework as defined in the GCC VAT Agreement.

While the GCC VAT Agreement touched upon many of the fundamental design considerations for a VAT system, there was some scope for independent and creative policymaking. Being a high-level document, the GCC VAT Agreement is often silent on how the member states should go about implementing the prescribed rules; further, the Agreement expressly gives some discretion to the member states in respect of some policy decisions. This freedom gives discretion to policymakers to implement rules and principles that are specific to their member states, therefore allowing for diversity in the design and implementation of VAT among the GCC member states.

The initial implementation choices made in the UAE are indicative of the country's intention to establish a modern and efficient VAT regime that takes into account wider strategic goals and realities of the country. While analysing all aspects of the implemented tax environment would require a separate book, the remainder of this part of the report discusses the following key policy choices adopted in the UAE:

- Broad tax base with limited exceptions;
- Voluntary registration on the basis of expenses to allow early recovery of VAT;
- Special rules for Designated Zones as a mechanism to encourage trade and investment;
- Tourist Refund Scheme to encourage tourism; and
- Adoption of technology to assist in tax administration.

“

*Key to VAT's success appears to be in lessons learned from implementations in other jurisdictions and carving out a system that meets the UAE's unique ground realities.*

”

**Uzair Dawood, ENOC**







## BROAD TAX BASE

### Theoretical considerations

VAT is a transactional tax that aims to tax final consumption. The key feature of any VAT regime is the extent to which the tax is imposed on different goods and services. Imposing VAT on the broadest range of goods and services ensures the most comprehensive coverage of tax, resulting in increased tax revenues and a reduction of distortionary effects. On the other hand, a narrower tax base may allow governments to reduce the burden of the tax on certain sectors or consumers.

Historically, the longer-established VAT regimes around the globe have adopted the latter approach. Exceptions from taxation (usually by way of zero-rate, reduced rate, or exemption) have been commonly used as a tax policy mechanism to alleviate the burden of VAT on the necessities of life as well as to stimulate activities in specific sectors. It is therefore common to see VAT jurisdictions with multiple VAT rates and exemptions that apply on a broad range of goods and services (such as utilities, healthcare, tourism, entertainment, etc).

Evidence suggests, however, that VAT is not the most efficient way of achieving the wider economic and social goals of a country. Due to their higher spending on goods and services,

richer households tend to benefit more than the lower-income households from any exceptions to the imposition of VAT, thereby inhibiting initiatives to reduce inequality. Further, introducing multiple exemptions and special rates makes a VAT regime more complex for businesses to understand and comply with, which may somewhat mitigate the positive effects of these exceptions on businesses.

Instead, any wealth distribution and equality goals can be more efficiently achieved by non-tax means such as the use of subsidies to provide targeted support to affected households and businesses. As a consequence, the prevailing wisdom over the last few decades was to limit the use of VAT as a tool for achieving non-revenue goals. This was exemplified with the introduction of GST regimes in New Zealand (1985) and Singapore (1994), which adopted a broad-base, low-rate approach to VAT – where, to the extent feasible, VAT was uniformly applied at a low rate on most goods and services. The outcome of the broad base tax with minimum of exceptions is the reduction of costs associated with administering and complying with VAT, as well as a reduction of the risk that such exceptions may distort consumption and investment decisions.

### Scope of VAT

The VAT design choices adopted by the UAE are reflective of the intention to implement a broad-base regime, while taking into account the local realities. Thus, in comparison with many of the longer-established VAT regimes, UAE has significantly fewer exceptions to the application of the standard rate on local supplies of goods and services. Interestingly, while the GCC VAT Agreement gives discretion to the GCC member states to zero-rate certain foodstuffs (which is common in Europe), the UAE decided not to do so – undoubtedly, it was influenced by the frequent and well-publicised disputes concerning taxation of food in other jurisdictions.



*The introduction of VAT at the rate of 5%, being comparatively lower than other comparable economies, was well received by the business community.*



**Surender Kapoor, Merex Investment Group**



## Noteworthy exceptions to the standard rate of VAT that were introduced by the UAE include the following:



### 1. Zero-rating of healthcare and education

Due to the importance of healthcare and education to the wellbeing of general population, UAE VAT is not applicable on healthcare and education services (and related goods).

Although in theory, it may have been possible for the government to reduce the financial burden of VAT on consumers of healthcare and education by some other means (e.g. via targeted subsidies), zero-rating supplies in these sectors provides a fairly straightforward and ringfenced way of reducing their costs on households. Considering that these sectors and services do not have a close substitute and cannot be easily replaced, there is also less risk that these exceptions would impact competition or consumer behaviour.



### 2. Zero-rating of crude oil and natural gas

Crude oil and natural gas are products that are generally traded on business-to-business (“B2B”) basis, with the majority being exported to outside the UAE.

The decision to zero-rate all supplies of crude oil and natural gas ensures that VAT does not become an unnecessary cash flow concern in the oil and gas trade. It should be noted that this VAT treatment of crude oil and natural gas does not mean that the UAE has lost significant amounts of VAT revenues – since exports of oil and gas would have been eligible for zero-rating under the general rules for exports in any event, and any VAT charged on local B2B sales would have been recoverable by purchasers as input tax.



### 3. Limited exemption for financial services

Due to practical difficulties with identifying and measuring the value of financial services products, most VAT jurisdictions typically elect to exempt financial services from VAT. This way, governments still collect VAT revenues – however, the revenue comes from taxing the inputs, rather than the outputs, of suppliers of financial services.

This widespread approach of exempting supplies of financial services has its downsides. Importantly, it may encourage suppliers of financial services to pass on the cost of irrecoverable VAT to their customers, therefore increasing prices of financial services and potentially giving rise to tax cascading effect when these services are supplied to another VAT-registered business.

Against this background, the UAE has made a bold decision to limit VAT exemption to financial services that are not conducted in return for an explicit fee, discount, commission, rebate, or similar consideration. As such, where consideration payable for financial services is explicit and identifiable, supplies of such financial services are considered taxable at the standard rate. This means that depending on the nature of the supply and consideration chargeable, suppliers of financial services are able to recover a portion of their input tax, therefore reducing the negative impacts of irrecoverable VAT.

While this dual VAT treatment does somewhat complicate compliance in the financial services industry, it has been generally accepted as a necessary inconvenience in return for the benefits associated with the ability to recover input tax on expenses.



### 4. Exemption for local passenger transport services

The supply of local passenger transportation services is exempt from VAT. This treatment prevents the recovery of input tax by suppliers, which ensures that the FTA still indirectly receives tax revenues from the sector.

Interestingly, the treatment of local passenger transport services varies among GCC countries. While both the UAE and Oman chose to exempt such local passenger transport services, such services are standard-rated in the Kingdom of Saudi Arabia (“KSA”) and zero-rated in Bahrain – making it a prime example of the discretion provided by the GCC VAT Agreement to the member states to choose their own approach to taxing certain industries.





1.



**Healthcare  
and education**

2.



**Crude oil and  
natural gas**

### Noteworthy exceptions to the standard rate of VAT

3.



**Financial  
services**

4.



**Local passenger  
transport services**



### **VOLUNTARY REGISTRATION ON THE BASIS OF EXPENSES**

The ability of a business to register for VAT is typically linked to its turnover. The policy decision made by the GCC member states in the signed GCC VAT Agreement was to only allow businesses to register for VAT voluntarily if the voluntary registration threshold is exceeded (AED 187,500). This approach is different from many other global VAT jurisdictions, which do not have a threshold for voluntary registration. While the restriction on voluntary registration means that the GCC tax authorities have to deal with fewer taxpayers, it also means that unregistered businesses may be in disadvantage compared to VAT-registered businesses due to the incurring of irrecoverable VAT costs.

In a unique move aimed at mitigating the impact of the voluntary registration threshold, the GCC VAT Agreement gives discretion to the member states to allow businesses to voluntarily register for VAT solely on the basis of incurring taxable expenses (that is, the expenses that are subject to VAT) in excess of the threshold. This feature has been implemented by all of the GCC member states that have already introduced VAT.

The ability to register for VAT on the basis of taxable expenses is extremely useful for new and start-up businesses that may not otherwise exceed the registration threshold on the basis of taxable supplies. By registering for VAT on the basis of expenses, businesses with long lead-up times between starting operations and making first taxable supplies (for example, software developers and natural resource exploration companies) are able to start recovering input tax early in their operations on the basis of intentions to make future taxable supplies.

It will be interesting to see whether this feature will be adopted by any non-GCC countries that introduce VAT in the future.

## Conclusion

Although the above list of supplies that are exempt and zero-rated in the UAE is not exhaustive, it represents the more interesting departures from the pure broad-base approach to designing VAT. By keeping the exceptions to the standard-rated VAT treatment to the minimum, the UAE has departed from the design path historically adopted by many traditional VAT jurisdictions and chosen a more modern approach to its VAT regime.





## SPECIAL RULES FOR DESIGNATED ZONES

VAT is a tax on consumption. One of the overarching principles used in designing VAT – the so-called “destination principle” – is that taxation should take place in the jurisdiction in which goods and services are consumed. This principle is implemented in the UAE, which has only imposed VAT on goods and services where the place of supply is in the UAE.

One of the defining features of the UAE economic and commercial environment is the wide presence and use of free zones, which provide a simplified and convenient way to set up business and conduct commercial activities. Often, businesses established in free zones do not conduct any activities on the UAE mainland, but trade exclusively within free zones or overseas.

Due to the importance of free zones set ups to the UAE and foreign trade, special rules were introduced to treat certain customs-controlled free zones (“Designated Zones”) as being outside the UAE for VAT purposes. Consequently, in line with the destination principle, supplies of goods in such Designated Zones are treated as being outside the scope of VAT as long as it can be shown that the consumption of the goods will not occur in the UAE (with the legislation providing a number of the exceptions to the general rule).

The effect of this rule is that businesses that trade goods solely in Designated Zones and outside the UAE (i.e. avoiding the UAE mainland) may often benefit from not having to charge VAT on their supplies, and may avoid being required to register for VAT and comply with related compliance obligations. This is a welcome compliance cost-saving measure for many foreign-owned

businesses that may want to establish a UAE-registered entity for activities that do not involve trading with the UAE mainland.

It should be noted that the special rule applies to goods only and does not affect services that may be provided in or from a Designated Zone. Presumably, this distinction was implemented due to the practical difficulties with monitoring and controlling the place of the consumption of services, as opposed to tracking the movement and use of physical goods.



## TOURIST REFUND SCHEME

The UAE is a prime global tourism destination, famed for its beaches, entertainment, culture, architecture, and shopping. Since shopping is an inalienable part of most tourists’ experience, the additional cost of having to pay VAT can become an important consideration in travel and shopping decisions made by tourists.

To ensure that VAT does not act as a potential barrier to tourism and shopping, from 18 November 2018 tourists in the UAE have been able to refund VAT incurred on their purchases while they are in the UAE. This scheme, known as the “Tourist Refund Scheme” or “TRS”, utilises electronic refund kiosks located in departure areas to allow tourists to efficiently claim their refunds at the time of departure.

By all accounts, the TRS has been successful in uptake and in providing a seamless experience to tourists. According to the FTA<sup>1</sup>, in the first eight months of 2022, the number of TRS transactions amounted to 2.31 million, which marked a 104.15% increase from the previous year. The value of the tourist VAT refunds have also more than doubled from the first eight months of 2021 to the same period in 2022.

While the UAE’s TRS claim process had already been very effective, the FTA has taken it further. In September 2022, the FTA, in partnership with the TRS operator Planet Tax Free, announced the launch of the world’s first paperless tourist VAT refund process which would simplify the VAT refund claims even further. The FTA estimates

<sup>1</sup> Federal Tax Authority and Planet Tax Free announce world’s most innoVATive, 100% digital VAT-refund scheme for tourists, 14 September 2022.



that more than 3.5 million paper invoices will go digital, resulting in positive benefits to merchants, tourists, as well as to the UAE’s digital transformation strategy and natural environment.

Considering UAE’s already proven ability to attract international tourists in the current delicate global environment, it would have been easy for the UAE and the FTA not to put much further focus on the TRS – after all, there are many countries that have not introduced tourist refund schemes at all, and the UAE is losing tax revenues by offering tourist refunds and making it easy for tourists to receive them. Therefore, this ongoing investment into the TRS system is a strong indicator of UAE’s commitment to creating the best-in-class user experience for tourists in the belief that the long-term benefits to the economy from tourism will outweigh any immediate loss of tax revenues.





## FOCUS ON TECHNOLOGY IN TAX ADMINISTRATION

The digitalisation of tax compliance and tax-related processes is an important step in reducing the compliance costs of businesses and administration costs of tax authorities. Globally, many tax authorities have been slow in adopting technologies in their operations – often, this is due to having a well-established existing compliance process and the significant costs required in transforming their operations.

By building its tax regime from the ground up, the UAE had the unique advantage of not being restrained by existing processes and technologies. This allowed the FTA to implement an administration platform that largely operates electronically, including:

- Fully electronic / paperless processes for tax registrations, deregistration, tax return filings and refund applications
- Electronic mechanism for submitting clarifications, reconsideration applications, special refund applications, and administrative exceptions applications
- Automatic linking of VAT returns with customs databases to provide access to import data and documentation

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*Particularly, FTA has done a commendable job in implementing a robust VAT filing and payment mechanism, issuing public clarifications, and hassle-free corporate and tourist refunds.*

**Paul Gyles, Shamal Group**

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This focus on conducting tax administration with the use of modern technology continues to this day, with ongoing investments being made to update and improve the systems (including the recent implementation of “EmaraTax”). Knowing UAE’s penchant for adopting the most innovative and ground-breaking technologies, it will be fascinating to see what the future holds for tax administration in the UAE.





# JOURNEY SO FAR

A tax regime is a living breathing organism that constantly evolves to react to changing conditions and realities. The rules and policies that may have been fit for purpose at the time the tax was implemented may later become outdated, inadequate, or obsolete.

Consequently, it is usual to see different aspects of tax regimes undergo regular development and change. In this part, we discuss the evolution of the VAT regime from legislative and procedural perspectives during the past five years.

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*The efforts put in by the government and the FTA and the continuous evolution of the tax laws to make them simple and taxpayer-friendly is commendable.*

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**Siegert Slagman**





## EVOLUTION OF CORE VAT LEGISLATION



**Amendments in 2020:**  
Zero-rating of services



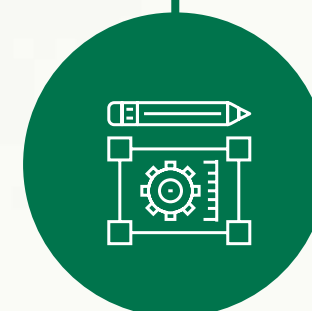
**Amendments in 2022:**  
Multiple changes to the  
VAT Law and Executive  
Regulations



## EVOLUTION OF PROCEDURES



**Administrative  
penalties for  
non-compliance**



**Statute of limitation  
and its extension**



**Voluntary disclosure  
requirements**



**Whistleblowing  
program**





## EVOLUTION OF CORE VAT LEGISLATION

Interestingly, compared to the developments in respect of the procedural aspects of tax administration (discussed later), the core VAT legislation has undergone relatively few changes over the last five years. The few changes that have been made mainly aim to clarify the tax rules.

While the UAE VAT legislation is already robust and comprehensive, there are still topics and issues that could be clarified further by legislative amendments. This is not unusual – even the longest-established VAT jurisdictions regularly make changes to their laws to deal with accumulated historical concerns and to proactively prepare for expected developments. Similarly, there are a number of VAT topics in the UAE that are commonly misunderstood or misinterpreted by businesses. While the FTA is doing extensive work in helping taxpayers to understand issues through public guidance and private clarifications, any inherent ambiguities are ultimately best dealt with through legislative amendments. As such, we would expect additional further changes to the VAT legislation being brought in the future to deal with ongoing issues and developments.

Below we summarise some of the main changes that were made to the core VAT Law and VAT Executive Regulations over the last five years.



## AMENDMENTS IN 2020: ZERO-RATING OF SERVICES

One of the most stirring and controversial amendments to the core VAT provisions involved a simple replacement of a single word.

Article 31 of the VAT Executive Regulations provides rules and conditions for zero-rating exported services. One such condition is that the supply should be made to a person who is outside the UAE at the time the services are performed. To ensure that incidental or minor presence in the UAE does not affect the application of zero-rating, Clause 2 of the Article, as originally introduced in 2018, specified that a person would still be considered as being outside the UAE if they are only present in the UAE for less than a month **or** if their presence is not effectively connected with the supply.

In 2020, Clause 2 was amended by replacing “or” with “and”. As a result, for a recipient to continue to be eligible for zero-rating, the recipient’s presence in the UAE now has to be **both** short-term and not effectively connected with the supply.

The amendment sent shock waves through the business community. In particular, it was not immediately clear whether the amendment would essentially prevent zero-rating when an overseas client had a UAE branch, even if that branch were not connected with the received services. This point was, however, quickly clarified by the FTA, which explained that a UAE branch can be effectively disregarded for the purposes of the application of the provision. Instead, the temporary presence of the staff of the recipient’s overseas establishment should be taken into account and assessed.

Nevertheless, the overall effect of this amendment was to narrow down the definition of “outside the UAE”. Now, any presence of the recipient in the UAE that relates to the supply may jeopardise zero-rating; similarly, any presence longer than a month would prevent zero-rating even if it is not related to the services (e.g. employees coming to the UAE on holidays). Since zero-rated treatment should only be applied when the supplier has determined that all conditions are met, this means that,



at least in theory, the supplier must be able to determine if the non-resident recipient has any presence in the UAE.

In practice, it is typically recommended that where a supplier is unable to ascertain whether or not the recipient has UAE presence, it should ask the recipient to confirm this in writing. Such recipient representation should normally be accepted by the FTA and will help the supplier to protect itself from the risk that zero-rated treatment will be challenged.



## AMENDMENTS IN 2022: MULTIPLE CHANGES TO THE VAT LAW AND EXECUTIVE REGULATIONS

In autumn 2022, the VAT Law and VAT Executive Regulations were amended within a few weeks of each other. While most changes are fairly cosmetic and do not affect the prevailing tax treatment, some of the changes did provide useful clarification on controversial issues such as the following:

- Place of supply for exports
- Reverse charge on hydrocarbons
- Timeline for issuing tax invoices and tax credit notes
- Director services

Let’s explore each of these on the next page. →



Amendments in 2022: multiple changes to the VAT Law and Executive Regulations



1. Place of supply for exports

An amendment to Article 27(3)(a)(4) of the VAT Law introduces a new place of supply rule for transactions involving imports or exports of goods. Specifically, it clarifies in respect of supplies that include periodic payments or consecutive invoices, stipulating that the place of supply will be in the UAE if the ownership of goods transfers in the UAE. The amendment ensures that UAE VAT is payable on the total value of the supply of goods in cases where the title of the goods transfers in the UAE, even if some invoices are issued or payments are received when the goods are outside the UAE.

The new provision is aligned with the FTA’s general approach that the place of the transfer of ownership is generally decisive for identifying the place of supply (with some notable exceptions, for example, where goods are supplied with installation or assembly). As such, businesses should pay attention to the place of transfer of the title (and not just to Incoterms or the date of invoice/payment) when considering where the supply takes place.



2. Reverse charge on hydrocarbons

Under Article 48(3) of the VAT Law, a supply of hydrocarbons between VAT-registered persons may be subject to the domestic reverse charge (“DRC”) mechanism if conditions are met. DRC shifts the obligation to account for VAT from the supplier to the recipient, therefore reducing the cash flow burden for the recipient.

Prior to the 2022 amendment, “hydrocarbon” was not defined. This had given rise to a number of ongoing disputes as to whether “hydrocarbons” could be interpreted widely to include any products made from hydrocarbons and additives.

The amendment has resolved this ambiguity by adding a definition of “pure hydrocarbons” which specifies that it only includes compounds consisting solely of hydrogen and carbon. Effectively, this change will remove from the definition any products that contain additives.

Since the amendments are effective from 1 January 2023, it remains to be seen whether a broader interpretation may still be applied to products supplied before the amendment comes into effect. If not, businesses that may have incorrectly relied on the DRC in respect of products that included both hydrocarbons and additives may potentially have to adjust their past VAT positions.



3. Timeline for issuing tax invoices and tax credit notes

The amendments introduced a timeline for issuing tax invoices (Article 67 of the VAT Law) for supplies that fall under Article 26 of the VAT Law and for tax credit notes tax (Article 62(2) of the Law). Prior to the amendment, there was no specific rule for issuing these documents.

The introduced timeline of 14 days aligns the requirements for issuing tax invoices and credit notes and brings certainty into this area.



4. Director services

A new clause in Article 3 of the Executive Regulations excludes director services provided by natural services from being considered a supply of services for VAT purposes.

This amendment changes the long-standing position that natural persons providing independent director services should register and charge VAT. This will significantly simplify compliance for many natural persons who sit on boards of companies going forward. Since the change is effective from 1 January 2023, directors still have to comply with their tax obligations for director services provided before that date.

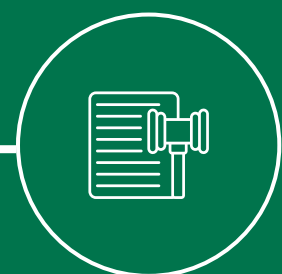




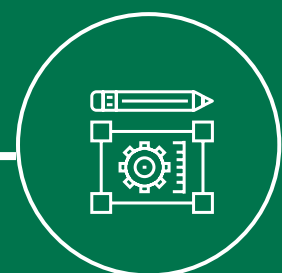


## EVOLUTION OF PROCEDURES

Compared to the relatively minor developments in core legislative provisions, procedural rules and regulations have undergone significant evolution since 2018. Developments in respect of penalties, audits, voluntary disclosure and whistleblowing rules have far-reaching impact on VAT compliance and administration, and will have long-term effects on the UAE tax environment.



**Administrative penalties for non-compliance**



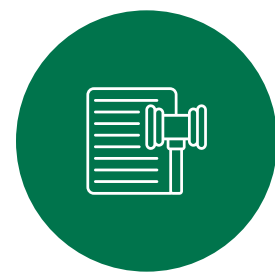
**Statute of limitation and its extension**



**Voluntary disclosure requirements**



**Whistleblowing program**



## ADMINISTRATIVE PENALTIES FOR NON-COMPLIANCE

VAT was the first modern tax introduced in the UAE that had widespread application and impact. Prior to the introduction of VAT, most UAE businesses – including their owners, directors and other staff – had never experienced operating in an environment that required knowledge, discipline and structure to comply with ongoing compliance obligations.



*In 2018, when UAE entered into a tax regime, it remarkably transformed businesses from no records to record-based business conduct in a short span of time.*

**Kalaiarasan Manoharan, Noon**

Owing to this lack of proven culture of tax compliance, it could have been expected that there would be a concern that the introduction of VAT would be met with widespread disregard and avoidance. To some extent, this concern is reflected in the penalties that were implemented at the time of introduction of VAT.

Specifically, one of the main characteristics of the original penalties regime was the ease with which it was possible to reach the penalty cap of 300%. This was due to the fact that the percentage-based late payment penalty, which was calculated daily on the amount of underpaid tax in a VAT return, was imposed retrospectively from the date when the incorrect VAT return was filed and the related shortfall of tax occurred. This meant that a person who disclosed an error in respect of a VAT return that had been filed a few months before, might have found themselves immediately facing the maximum amount of penalty – irrespective of whether the person was previously aware that the error was made.

While the original penalties regime also introduced different levels of penalties for errors committed in filed VAT returns – 5% if they were voluntarily disclosed and 50% if they were identified during a tax audit – this difference was negligible for a person who might have already been facing a late payment penalty of 300%. Due to such insignificant difference in the total amount of penalties irrespective of whether they were disclosed voluntarily or discovered during a course of a tax audit, businesses would often find themselves facing a dilemma of whether or not to voluntarily reveal their mistakes to the FTA.



*Reduction in penalties not only signifies a decrease in legal obligations and a boost to the working capital but also encourages the taxpayers to come forward and correct any reporting errors committed in the past period.*

**Sourav Chakraborty**

Against this background, the penalties regime underwent significant reformation in 2021. Following the reform, there is now a clear benefit for a taxpayer in voluntarily disclosing historical mistakes since doing this grants a grace period of 20 business days before the late payment penalty starts being calculated. Further, in case of a voluntary disclosure, the penalty for filing incorrect returns will range from 5% to 40% (depending on how promptly the error was identified and disclosed); while the same penalty when the error is discovered during a tax audit would start at 50% and increase by 4% for each passing month from the date when the additional payment was due until the date of the tax assessment by the FTA.

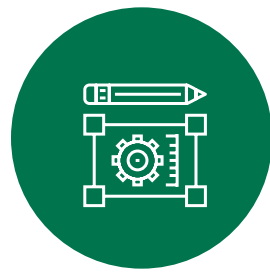
Following the penalties reform, hypothetical benefits from ignoring errors may often not be worth the risks if these errors are subsequently discovered by the FTA. To take full advantage of the new regime, businesses should be on the lookout for any incorrectly taken past tax positions and aim to correct them as soon as they are identified.



*The recent overhaul of the penalty system was a great relief for the taxpayers as the FTA consolidated major administrative penalties.*

**Kaushik Kothari, Sharjah Cooperative Society**





## STATUTE OF LIMITATION AND ITS EXTENSION

A “statute of limitation” is a prescribed time limit after an event beyond which a tax authority cannot amend a tax position adopted by a taxpayer – even if that tax position was not correct. As per the UAE Tax Procedures Law as it was originally introduced, the FTA was generally time-barred from making a tax assessment after the expiration of five years from the end of the relevant tax period.



*We firmly believe that preparation for an external audit is a continuous process and not a one-off task.*

**Anissa Jammousi, GEMS Education Group**



Considering that VAT was introduced effective from 1 January 2018, the five-year statute of limitation limit would start time-barring the first VAT tax periods from 2023. Whether coincidentally or not, the VAT Law was amended in late 2022 to potentially give the FTA more time to conduct tax audit and tax assessment activities. While the default tax period for conducting tax audits and making tax assessments remains five years, two new key main exceptions were introduced:

1. The FTA can issue a tax assessment after the expiration of the five-year period if the FTA has notified the taxpayer of a tax audit within the five-year period. If such tax audit notification has been issued, the FTA has four years from the date of the notification to complete its tax audit or issue a tax assessment.
2. If the taxpayer has submitted a voluntary disclosure in the fifth year from the end of a tax period, the FTA has one year (from the date of the submission of the voluntary disclosure) to conduct and complete the related tax audit and to issue a tax assessment.

In addition to the above exceptions, the introduced legislation also provides that a taxpayer cannot do a voluntary disclosure after the expiration of five years from the end of the relevant tax period.

The obvious impact of these new provisions is that by giving a notice of the tax audit, the auditor does not commit itself to conducting and completing the tax audit as soon as possible, but simply gives itself additional four years to do so. As a consequence, the new provisions may bring a new level of uncertainty to taxpayers:

- The audited taxpayer may not know for up to four years whether the tax positions adopted by it in the audited tax periods were correct.
- Since the taxpayer cannot do a voluntary disclosure after the expiration of a five-year period, the taxpayer would not be able to initiate an amendment of the incorrect tax position itself.
- Different levels of administrative penalties apply to errors depending on whether they were disclosures or identified before or after a notice of tax audit – with penalties being substantially higher if errors are discovered or disclosed after the FTA has issued a notice of a tax audit. Since the new statute of limitation rules give the FTA up to four years to complete a tax audit, any errors identified or disclosed during the period when the audit is open may be subject to the higher level of penalties.

The overall impact of, and the likely intention behind, the new statute of limitations is that it is now in taxpayers’ interests to ensure that they are not subject to a protractive and uncertain tax audit, but to deal with any mistakes quickly and transparently (by proactively disclosing errors in the fifth year after the tax period, the taxpayer ensures that the related tax assessment is issued within a year). In combination with lower penalties applicable to errors that are disclosed voluntarily, this

shorter extension period clearly encourages businesses to act proactively with respect to their historical tax compliance obligations.



*Businesses that do not engage with the FTA, and have yet to have a VAT audit, are sitting on a potential landmine of tax risk.*

**Edward Carter, NMC**



## VOLUNTARY DISCLOSURE REQUIREMENTS

In accordance with the Tax Procedures Law, a person is required to voluntarily disclose mistakes in tax returns that have resulted in an underpayment of tax. The Tax Procedures Executive Regulations supplement this general rule by specifying that a voluntary disclosure is not required where the amount of tax payable in a tax return is understated by not more than AED 10,000 – in such cases, the taxpayer can simply correct the error in the subsequent tax return.

Further, a voluntary disclosure is not required if the reported tax payable in a tax return is *more* than it should have been – since such errors do not negatively affect tax revenues, the taxpayer is only required to do a voluntary disclosure if it wishes to claim back the overpaid tax.





## WHISTLEBLOWING PROGRAMME

Recent amendments to the voluntary disclosure article in the Tax Procedures Law introduced a new category of errors that will require a voluntary disclosure – that is, an error or omission that has not resulted in a difference in the amount of tax payable. The most obvious types of mistakes that do not result in a difference in tax payable are failures to correctly report zero-rated and exempt supplies and expenses subject to the reverse charge mechanism (where the VAT paid under the reverse charge mechanism is simultaneously recoverable in the same tax period).

The question does remain, however, as to whether we should expect any changes to the AED 10,000 voluntary disclosure threshold in the Tax Procedures Executive Regulations. As it stands, the threshold has not yet been removed, which creates an interesting dynamic where there is a requirement to file a voluntary disclosure when an error results in nil difference in tax payable but no requirement to do a voluntary disclosure when an error results in underpayment of tax between AED 0.01 and AED 10,000. It remains to be seen whether this differing treatment will be retained or whether there will be subsequent changes made in Tax Procedures Executive Regulations to align the treatment.

April 2022, the FTA introduced a Whistle Blower Program for Tax Violations and Evasion. The Program is a new mechanism that allows the FTA to receive and process leads relating to tax non-compliance and to offer a monetary reward to informants for successful leads.

The Program is yet another tool in the FTA's toolbox (in addition to audits and penalties) to improve the environment of tax compliance in the UAE. Unlike the other tools, however, the Program uses society's yearning for law and order to encourage members of the public to report wrongful behaviour. Ultimately, since paying taxes benefits society, should not society take some responsibility in helping to collect taxes?

Of course, the Whistle Blower Program does not rely exclusively on social responsibility and incentivises participation by paying whistleblowers for successful leads. Indeed, this is a necessary reward considering the potential, albeit remote, financial risks that may be involved in participating in the Program.

Considering that the Program has only been recently introduced, there has been no update on its uptake. If the FTA decides to share the high-level information on the successes of the Program, it may go a long way to increasing the Program's popularity with potential informants.



# ONGOING CHALLENGES: SECTOR-SPECIFIC ISSUES

## A knowledgeable taxpayer is a compliant taxpayer

The goal of any tax regime is to ensure that it has as few uncertainties as possible, while remaining flexible to accommodate new scenarios and developments. Having clear tax rules increases tax compliance and reduces costs of administering VAT.

One of the most efficient methods of improving tax compliance is raising awareness among taxpayers. As part of constant efforts to maintain the effectiveness and accuracy of the tax system, the FTA has published several guides and clarifications concerning the application and interpretation of the tax rules and processes. Over the years, the FTA has issued 25+ decisions, 30+ public clarifications and 60+ guides about VAT, responding to concerns and inquiries from taxpayers. These documents help to simplify and explain specific topics to increase awareness, contribute to the development of the tax environment and promote compliance. More recently, the FTA has also been very active in organising seminars and workshops with taxpayers, including physical workshops across the UAE.

Nevertheless, there are still some gaps in the public's knowledge of the FTA's views on certain topics. While the FTA has provided hundreds of considered and valuable responses to private clarifications submitted by taxpayers, such responses are not in the public domain and are often not commonly known to other taxpayers. Further, while there have been numerous disputes between the FTA and taxpayers since 2018 which ended up in the Tax Disputes Resolutions Committee ("TDRC") and higher courts, the decisions issued by these judicial authorities have also not been published. Although the principles used by the FTA and TDRC/courts to reach their decisions are often informally shared among taxpayers and tax consultants, this is not an efficient method of disseminating information and is prone to misrepresentations and misunderstandings. In fact, five years after the VAT rules have been introduced, we regularly see businesses making mistakes in the application of VAT rules, simply due to the lack of easily accessible information regarding how they are meant to apply them.







*The Authority maintained a client-oriented service and accessibility, agile to publish much-needed Guides and Clarifications and resolve arising issues.*



**Mohamed Faycal Charfeddine,  
Aujan Coca Cola Beverages Company**

In these circumstances, it is of ongoing importance that the FTA continues fostering taxpayer education by issuing public guidance on general, procedural and industry-specific VAT topics and conducting training and workshops. Such initiatives would help businesses to forge a better understanding of the application of VAT principles – which should reduce risks of mistakes and tax evasion.

This overall improvement in tax compliance behaviour would have a positive impact on the efficiency of tax administration and on tax collections by the FTA. Tax audits are not the most efficient way of using a tax authority's resources to raise revenues, since often they may produce minimal result by either targeting compliant taxpayers or identifying insignificant additional unreported revenues. Further, due to the continuous growth of the UAE as a place of doing business, it will be difficult for the FTA to continue growing at the same speed to provide sufficient coverage for its compliance activities. By educating taxpayers and creating a culture of compliance, the FTA could save costs and use the freed resources to focus on activities that support taxpayers in meeting their compliance obligations.

Notwithstanding the above, taxpayers are ultimately responsible for ensuring that they correctly interpret and apply VAT rules to their businesses. In this part, we discuss some of the common issues that are often faced by UAE businesses. While the application of VAT to these issues is not always complicated from a technical tax perspective, it is important that businesses are first able to identify that these issues exist.



## ONGOING CHALLENGES: SECTOR-SPECIFIC ISSUES



**Real Estate**



**Retail and E-Commerce**



**Transport and Logistics**



**Oil and Gas**



**Energy**



**Financial Services**



**Education**



**Healthcare**



**Hospitality**



**Automobile**



**Media and Entertainment**



**Crypto markets**



**Holding Companies**





## REAL ESTATE

### Bare Land

Any land that is not covered by completed or partially completed buildings, or civil engineering works (i.e. does not have any construction above the ground level) qualifies as bare land. The supply of bare land in the UAE is VAT exempt, whereas non-bare land is subject to VAT at the standard rate.

In order to avail an exemption, it is relevant to analyse, among other things:

- Whether any temporary structures, such as movable offices, security cabins, or sheds for storage, may disqualify the land from being “bare”.
- Whether reclaimed land created by removing water from oceans, seas, riverbeds or lake beds should qualify as bare land.
- Whether a fence around a plot, or water, drainage or sewage pipes running below the plot would change the character of the land such that it could no longer be considered bare land.

### Stalled projects

When a real-estate company starts a construction project, there could be multiple reasons why the developer might pause the project. It is important to consider whether any input tax that had already been recovered on expenses needs to be reversed due to the project being stalled and no taxable supplies having been made by the developer.

### Transactions involving cancellation of the sale of property

Upon reserving a property, developers collect a token payment amount from customers. Such amounts are treated as advances for the sale of property and hence, reported as zero-rated supply. Often, following the reservation, customers may have second thoughts and may wish to reconsider the decision of buying the property. In this case it will be important to consider the tax treatment of the payment, which will depend on the future intentions of the parties. In particular, the following should be considered:

- Whether the amount, if forfeited upon cancellation, should be treated as a compensation-type payment and therefore out-of-scope of VAT.
- How the amounts should be taxed where the customer swaps properties, for example, by cancelling the original purchase and reserving another property instead.
- In case of an assignment of SPA by one customer to another, the property owner needs to determine whether there will be any tax impact.

### Input tax apportionment

A complex issue for real estate businesses is the computation of input tax apportionment. As per the input tax apportionment method, the appropriate special method for businesses engaged in real estate business is the floorspace method. However, there are several practical challenges in adopting the said method:

- In case of a master development project, the gross floor area (“GFA”) may change over the period on account of changes in the master plan
- Where businesses are engaged in multiple projects, the question arises as to whether a single GFA percentage should be used for all projects
- Implication on GFA where a project is developed in a phased manner
- Implications on account of changes in unsold units

### Recovery of expenses from the tenant

It is important to classify recovery of expenses as either a ‘reimbursement’ or ‘disbursement’, based on the principles outlined by the FTA. If an expense is incurred as a principal, it should qualify as ‘reimbursement’; whereas if the expense was on account of the tenant, it should qualify as ‘disbursement’. Typically, reimbursement is taxable, while a disbursement is outside the scope of VAT in the hand of the intermediary.

### Holdover lease

A common phenomenon in the real estate sector is the hold-over lease where the lease expires and is not renewed while the tenant continues to occupy the property (for example, while the rental amount is being negotiated). During such holdover lease periods, the landlord has to consider whether the obligation to account for VAT arises and whether the date of supply is triggered under Article 25 or Article 26 of the VAT Law.

### Residential accommodation or serviced accommodation

Where employers provide accommodation to their employees, it will be pertinent for employers to analyse whether they are providing serviced accommodation which is taxable at 5%, or residential accommodation which is considered zero-rated or exempt. Employers should identify the facilities provided along with the accommodation in order to determine the nature of the supply.

### Agency contracts

The functioning of real estate dealings is largely dependent on property managers. Property managers are agents who act as a bridge between the property owners and tenants/ customers. In lieu of their services, property managers earn a commission. The property manager can operate as a disclosed or undisclosed agent.

A common mistake made by property owners is not to charge VAT on their supplies in the mistaken belief that the VAT obligations are always the responsibility of the property managers. All agency contracts with the property managers must be carefully analysed to ascertain the type of agency and the type of supplies made by property owners and property agents to ensure correct reporting of VAT by all parties.







## RETAIL AND E-COMMERCE

### Consignment Stock

In the retail industry, it is a common practice for brand owners to supply their goods on a consignment basis to retailers across the globe. While on the face of it, cross-border consignment transactions look straightforward, things are a bit more complex than what meets the eye.

In the UAE, the place where the transfer of ownership happens plays a critical role in determining the taxability of the transaction. For example, if the transfer of ownership by the brand owner to the retailer is in the UAE, then the brand owner may be considered to be making a local supply and be required to register for VAT – unless a reverse charge applies and the responsibility for such VAT passes to the retailer. The date of the imposition of VAT may also be affected by the special date of supply rules applicable to situations when goods are delivered on a returnable basis.

Further VAT implications may arise if the goods are imported into the UAE by a party other than the owner of the goods at the time of import – for example, if the retailers are importing goods on behalf of the brand owners. Since only the owner of the goods at the time of import can recover import VAT, the eligibility to recover the input tax by retailers in such situations may be in question.

### Online advertising

In the digital age, online advertising is a key marketing activity and a good source of side income for e-commerce aggregators and retailers. Determining the tax implications of electronically supplied services is always challenging. The key is to identify where the service is being used and enjoyed by the customer. In the above example, if the customer is benefitting from the service in the UAE from the advertisements made

across the globe, the transaction could be taxable in the UAE.

### Barter

Barter involves exchanging goods or services for other goods or services. For example, Company A may provide advertising services to Company B in exchange for some goods. Since no money is involved, companies may think there is no transaction/supply. However, this is not the case in the UAE, as consideration received in other forms is also considered part of the consideration for the supply.

Companies need to be mindful (including when entering in transactions within their corporate group) that there will be VAT implications from entering into barter transactions.

### Loyalty programmes

A customer loyalty programme is a rewards programme to encourage frequent purchases by rewarding customers with discounts and special offers. Points are issued to the customers on every purchase they make from the retailer or a group of retailers under the same loyalty programme. Customers can redeem these points in the form of discounts.

However, do such reductions in the value of supply qualify as a discount and may there be further tax implications for the seller? The answer will depend on the exact structure of the loyalty programme, including whether it is an exclusive programme with the retailer, whether a loyalty programme operator is involved, and if there are additional services provided and payments made behind the scene. Therefore, it is important to evaluate the mechanics of the loyalty programme to determine the VAT treatment of supplies and loyalty points redemption.







## TRANSPORT AND LOGISTICS

### Local leg of international transportation

A supply of international transportation services in respect of goods can be zero-rated if conditions are met.

Often, to be able to provide transportation services, the contractual supplier of the international transport services may outsource a local UAE leg to a third-party freight forwarder. Historically, such third-party freight forwarders would commonly zero-rate their delivery charges on the understanding that the services are provided for the purposes of international transportation.

The FTA has been clear, however, that it considers that the local transport leg can only be zero-rated where the supplier is also providing the related international transportation. As a consequence, freight forwarders must carefully consider the arrangement holistically to determine which services can be zero-rated.

### Transport-related services

For VAT purposes, a transport-related service can be treated in the same manner as the international transportation services to which it relates (e.g. either zero-rated or outside the scope).

It is important to carefully assess on a case-by-case basis whether a particular service constitutes a “transport-related services”. The common requirement is that the service must be necessary to enable the conduct of a particular transportation service – therefore, the supplier may need to be able to prove it would be difficult or impossible to provide the transportation service without the additional transport-related service.

### Supply of storage services

Related to the above, a question often arises as to whether storage of the goods before or after their transportation can constitute a transport-related service. In this respect, the supplier of the storage services would need to be able to show that the storage is necessary to conduct the transportation services. Factors such as the duration and timing of the storage may affect the findings, and there have been several cases of the FTA disallowing zero-rating and imposing penalties.

### Qualifying means of transport

Goods and services supplied in respect of qualifying air, sea and land means of transport can be zero-rated if certain conditions are met.

One of the conditions for a qualifying air and sea means of transport is that it should have been designed or adapted for use for commercial transportation. Suppliers of goods and services for aircrafts and vessels must therefore carefully consider the nature and purpose of these means of transport to determine if they meet the conditions; goods and services supplied for air and sea means of transports that are not used for commercial transportation (for example, for private purposes) should not be zero-rated.

### Services supplied in relation of qualifying means of transport

Services can be zero-rated if they are supplied directly in connection with the qualifying means of transport for the purposes of operating, repairing, maintaining or converting such means of transport.

Service providers must be careful in assessing which services fall under the zero-rating. Importantly, the FTA has been adopting a narrow

interpretation of the term “operating”, which may prevent zero-rating from applying to services that relate to the means of transport only in the broad sense.

### Supply of goods to international aircraft or marine vessels through agents / distributors

Goods that are supplied for use or consumption, or sale by or on an aircraft or ship can be zero-rated if they are supplied in respect of the international transportation services.

Importantly, the benefit of zero-rating is not limited to a person who supplies goods or services directly to the international aircraft or marine vessel. Accordingly, the supply of goods through distributors could be treated as a zero-rated supply if the said goods are to be consumed by the aircraft or ship in the course of undertaking international transportation services. The supplier should retain the documentary proofs evidencing the use and consumption of the goods.

### Local passenger transport services

The supply of local passenger transport services in the UAE can be exempt unless the trip is undertaken for the principal objective of sightseeing, catering, pleasure, entertainment or similar.

Often there is a thin line between a trip that is purely for transportation and the one that is for pleasure or entertainment. Suppliers need to be able to correctly classify their services. Simply treating transport services as taxable rather than exempt in borderline cases is not an ideal solution since exempt treatment would have a follow-on effect on input tax recovery.







## OIL & GAS

### VAT treatment Pure Hydrocarbons – amendment effective from 1 January 2023

Pursuant to the amendment to the VAT Law effective from 1 January 2023, the applicability of the domestic reverse charge has been limited only to “pure hydrocarbons” instead of all hydrocarbons. Pure hydrocarbons have been defined as pure combinations of hydrogen and carbon.

Taxpayers must therefore conduct a technical study to determine whether the composition of the present supplies qualifies as a pure hydrocarbon and must ensure that their operations and tax functions are updated to identify such supplies and ensure the correct VAT treatment.

### Import of oil and gas through pipelines

When goods are imported into the UAE, import VAT must be paid in respect of the import; this would include the import of oil and gas. Typically, the import of goods is prepopulated in Box 6 of the VAT return upon clearance from the customs department. When oil or gas is imported through pipelines, however, they do not physically cross customs, and therefore no import declarations are available. The taxpayer may subsequently (on a periodic basis) declare the goods after the delivery, pursuant to which the customs department may issue the import declarations.

There could be a situation where the customs declarations are not provided by the customs department. In such a scenario, it is still the responsibility of the importer to account for VAT in their VAT return rather than rely on the return being prepopulated.

### Export of oil and gas through pipelines

A direct or indirect export of goods to outside the UAE is treated as a zero-rated supply if conditions are met. The supplier should retain the official and commercial evidence in order to zero-rate the supply and the goods should be exported within 90 days of the date of supply.

When oil and gas is supplied directly through a pipeline and the supplier is unable to obtain the necessary documents as official evidence of export, the supplier should file for an administrative exception with the FTA to be able to zero-rate their supplies.







## ENERGY

### Charges on behalf of other entities

Utility providers are commonly involved in the collection of levies, duties, taxes on behalf of government bodies. It is important to look at the terms of charging and collecting the payments in order to understand the utility provider's obligations and the associated VAT treatment.

Due to the different VAT implications, it is important to determine:

- whether the utility provider could be considered as an agent acting on behalf of the government body with the payments constituting disbursements; or
- whether the remittance of revenue from the utility provider should be considered a reimbursement or recharge.

It is also important to note that utility providers would not typically be considered as making a sovereign supply when recharging government fees and therefore they should carefully consider the nature of the recharge before treating it as outside the scope of VAT.

### Foreign suppliers: Engineering, procurement, and construction ("EPC") contracts and supplies of goods with installation

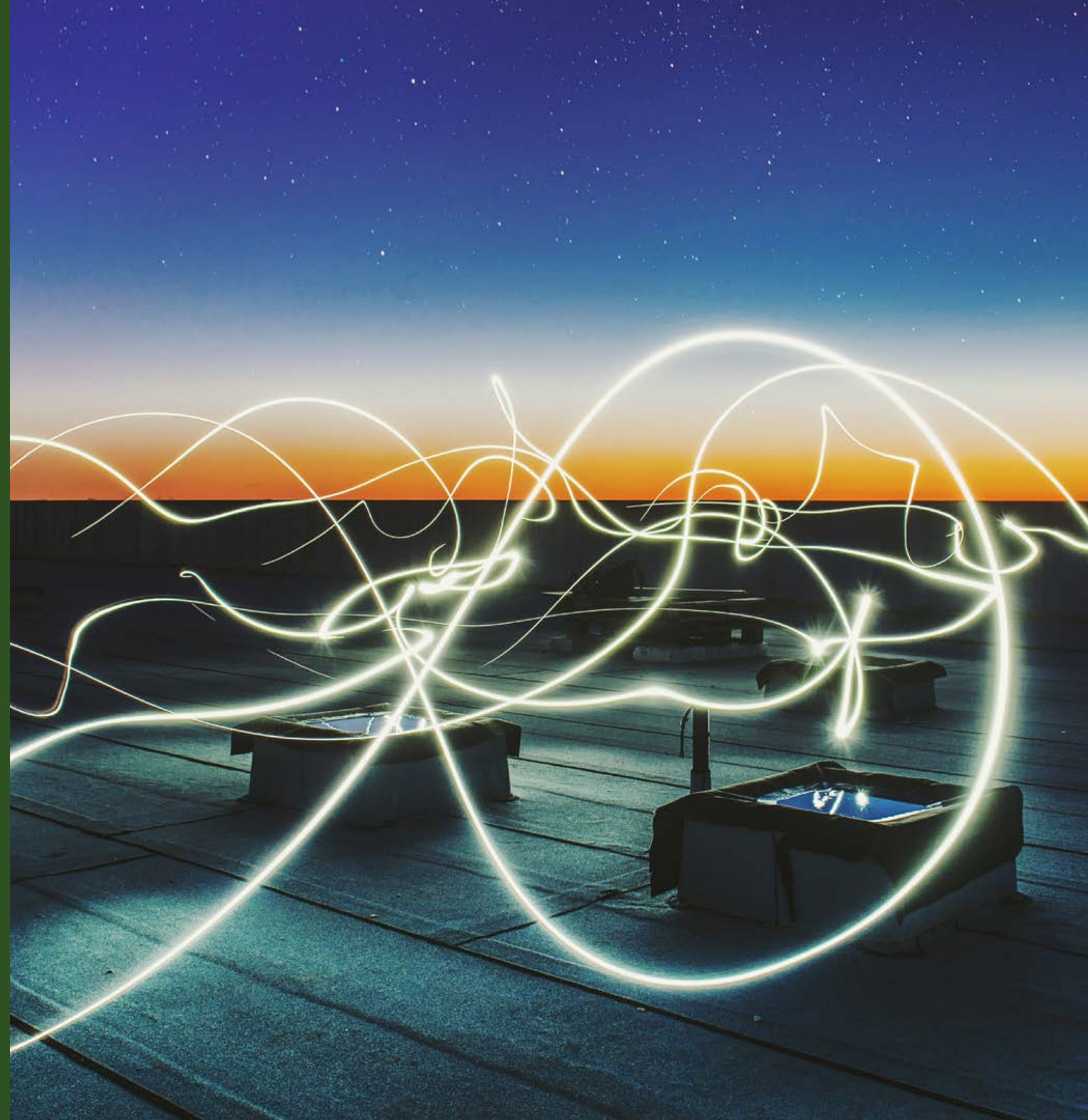
EPC contracts may involve, for example, a construction of a power plant and supply of materials, along with the procurement, installation, and commissioning of the power plant in UAE.

When a supplier is an overseas entity, such arrangements often give rise to numerous

complex matters, including:

- Whether VAT may be applicable on the supplied goods, services or both. The fact that the title of the goods passes to the customer outside the UAE does not necessarily prevent the application of UAE VAT if the goods are to be installed or assembled in the UAE.
- Whether VAT on a supply is the responsibility of the foreign supplier or of the UAE recipient under the reverse charge mechanism.
- The imposition of import VAT on the physical movement of the goods into the UAE. This VAT may be payable in addition to the "transactional VAT" chargeable on the actual supply of the same goods. While the responsibility for the payment of the import VAT is on the importer of record, only the owner of the goods may recover that import VAT as input tax.

Considering many potential pitfalls, it is important that contracts are reviewed and discussed from the VAT perspective in order to plan for any risks and liabilities.







## FINANCIAL SERVICES

### Interchange fees

The mechanism for charging interchange fees is complex. Interchange fees cover costs incurred for providing card services such as payment guarantees, uses of technology, CAPEX, software to track fraud, customer call centres, and so on. It could constitute consideration paid by the acquiring bank for the service provided by the issuing bank to the payment technology company, and hence be taxable. Alternatively, it may represent a money-related service between the issuing bank and the payment technology company, which may be an exempt financial service in terms of the UAE VAT Law. Finally, it could also be argued that the payment technology company is merely collecting and passing on the interchange fees that it has received from the acquiring bank and hence should be out of the scope of VAT.

Every service provider in the supply chain needs to carefully evaluate their specific arrangement, the flow of the transactions, and the way money changes hands amongst various parties in order to understand and apply appropriate VAT treatment.

### Remittance services

A remittance service involves the transfer of money from a person in one country to another person in another country, with two banks participating in the transaction. A bank or banks will charge a transfer fee or remittance fee for executing such a transfer. This fee could be borne either by the remitter or by the beneficiary in the receiving country.

It is relevant to analyse who the actual recipient of the service is: whether it is the person remitting the money or the person receiving the money. Depending on the nature of the arrangement and the recipient of services, the transaction could either be taxable at 5% or could be zero-rated under the UAE VAT Law.

### Valuation of sale of securities for reporting and apportionment

Sales of securities are generally exempt from VAT. Transactions of such nature would have implications from a reporting and apportionment perspective. It is imperative to identify the value that needs to be reported in the VAT return, which, in theory, could be either the actual sale value or the net value (such as the difference between the purchase price and sale price). The UAE VAT legislation is not clear on this aspect; in comparison, Bahrain VAT Law requires the reporting of the net value of the transaction.

Whether the transaction is reported at net value or full value will have a direct bearing on the input tax apportionment calculations for the year. While the FTA has clarified its stance on a number of securities products in private clarifications, there is still scope for interpretation and uncertainty.

### Late payment fees

Charges that are punitive or compensatory in nature are treated as outside the scope for VAT purposes. Late payment fees are peculiar to the financial services industry and depending on the nature of the fee, they could either be taxable, exempt, or out of scope. As an example, a charge for damage to or loss of a card could be out of scope from a VAT perspective. This can be contrasted with a charge for unpaid checks, which may be standard-rated. It is imperative that the nature of each charge be evaluated and appropriately taxed.

### Insurance and agency contracts

UAE VAT Law makes a clear distinction between a disclosed agent and an undisclosed agent. In the case of a disclosed agent, the insurance

company would be liable to pay VAT on the insurance premium charged to the insured, and the insurance broker would pay applicable VAT on its commission. In the case of an undisclosed agency, the insurance broker would first pay VAT on the insurance premium charged to the insured, and the insurance company would again charge VAT on the total amount charged to the broker (including his or her commission).

It is important to note that the rules have mandatory application and therefore it is critical that the correct party accounts for correct VAT liability. Therefore, parties in the transaction need to assess their respective VAT obligations holistically to ensure that they comply with the VAT requirements.

### Motor vehicle insurance

In principle, any settlement claims received by the insured from the insurance company with respect to an insurance claim are outside the scope of VAT. Similarly, any excess or deductible (an amount the insured bears in the event of a loss as a threshold before the insurance company will pay the settlement claim) is not a consideration for any supply by the insurance company, and as such, should be out of scope for VAT purposes.

In an insurance arrangement, it is important to identify which party is eligible to recover input VAT on expenses related to settlement claims. Depending on the arrangement, the insurance company may be eligible to recover input VAT on charges by the workshop and fees paid to surveyors, adjustors, investigators, and other specialists. However, this is not always the case and needs to be carefully assessed.







## EDUCATION

### Advance tuition fee

The supply of educational services and related goods and services is zero-rated. Accordingly, the advance tuition fee collected should be treated as a zero-rated supply.

On some occasions, an educational institution may charge an advance tuition fee from prospective students who do not end up enrolled with the educational institution. Since no goods or services are supplied by the educational institution to persons not enrolled with the educational institution, the fees should not be zero-rated. Instead, the fee should be subject to VAT at the rate of 5%.

Subsequently, if the student does end up enrolling in the course, the educational institute may issue a tax credit note to reverse the VAT charged.

### Field trips

As per the VAT Executive Regulations, field trips shall not be zero-rated unless they are related to the curriculum of an educational institute and are not predominantly recreational. Educational institutes should correctly identify whether the trips conducted are related to the curriculum or recreational in nature and accordingly VAT should be accounted at the correct rate.

### Medical fees charged to students

A healthcare service is defined as any service supplied that is generally accepted in the medical profession for the treatment of the recipient of the supply including preventive treatment. Healthcare services shall be zero-rated on the condition that the supply shall be:

- made by a healthcare body, doctor, nurse, technician, dentist, or pharmacy licensed by the Ministry of Health and Prevention (“MOHAP”) or by any other competent authority
- relate to the well-being of human beings

Accordingly, educational institutions that hold a MOHAP license under the classification ‘school clinic’ may zero-rate the medical fees, if the services provided fall within the meaning of “healthcare services”. However, if the medical fee is collected as a premium on a regular basis, irrespective of the fact that the student is not using the service or not, the premium charged by the school / educational institute will be subject to VAT at the rate of 5%.

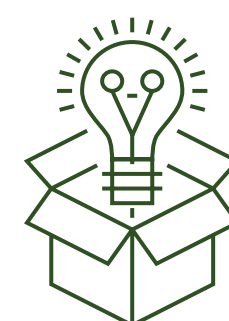
### Endowments / grants

VAT is a tax on supplies of goods and services. Hence, no VAT will be applicable unless there is an actual or deemed supply of goods or services.

Among other things, to determine whether an endowment or grant received by an education institute is within the scope of VAT, one has to consider whether any benefit is received by the person paying the endowment or grant. When there is no directly identifiable benefit provided in exchange for the payment, the amount would not constitute consideration and would fall outside the scope of VAT. However, if any identifiable and valuable benefit is provided to the payer, the amount may be considered as consideration for the taxable supply.

### Student accommodation

The supply of residential accommodation for students is generally included in the meaning of “residential building” and therefore, it is exempt from VAT. However, it excludes any serviced apartment for which services are provided in addition to the supply of accommodation from being regarded as a residential building.



Educational institutions should consider whether the additional services provided to students may impact the classification of accommodation as “residential”, which would result in tax being payable at 5%.







## HEALTHCARE

### Recipient of the healthcare services

Zero-rated treatment for healthcare services only applies when the underlying healthcare service is necessary “for the treatment” of the “recipient of the supply”.

In a normal situation, a patient visiting a hospital would be the recipient of healthcare services. However, it is a common practice in the healthcare industry to subcontract the provision of services – for example, a doctor may be supplying a service to the hospital, which subsequently supplies it to the patient. Similarly, different hospitals and clinics may enter into outsourcing arrangements for the provision of healthcare services.

It is crucial to assess different scenarios on a case-by-case basis in order to identify the actual recipient of the healthcare services. Where the service is not directed at the person who is being treated, it may not qualify for zero-rated treatment but may be taxable at 5%.

### Overseas doctors

Hospitals often engage specialists who are not residents in the UAE. These specialists are hired for specific treatment and visit the UAE for the purpose of that treatment only.

Since the doctor physically enters the UAE and performs the activity while not being a resident of the UAE, it should be considered whether the presence of the doctor in the UAE gives rise to a fixed establishment. Further, it is important to determine whether this transaction is subject to VAT under the reverse charge mechanism or if the specialist doctor is required to register for VAT.

### Technology-driven healthcare services

The UAE’s technology-driven market is set to grow swiftly in the coming years. In the case of mobile apps, it is important to note how the transactions are structured between the app operator, doctors, and the customers, and whether any transactions between them do not qualify as healthcare services.

The app operator and the doctors need to be clear on structuring the transactions in a way that adequately reflects the correct intention of the parties, including the way invoicing happens between them.

### Medical spas

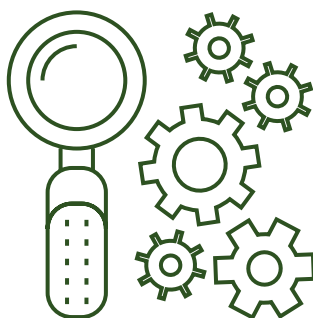
Medical spas, or medi-spas as they are usually called, are a unique blend of medicine and aesthetics providing cosmetic treatments that are medically recommended and supervised. Typically, facial and skin treatments such as anti-wrinkle treatment, acne therapy, hair removal, and laser procedures are conducted there.

Though the medi-spa centres are managed and supervised by well-trained doctors along with beauty aestheticians, VAT on their services should apply at the standard rate of VAT if the procedures are elective and cosmetic in nature.

### Composite and mixed supplies

The VAT treatment of the provision of two or more goods or services that are bundled together for a single price can be complex – as it can either be a single composite supply or multiple supplies. In the healthcare sector, identifying the right supply becomes important since different supplies may be either zero-rated or standard-rated – for example,

basic healthcare services can be zero-rated while additional elective treatments may be standard-rated. Large hospitals may even offer health packages for a single price that include rooms, healthcare treatment, medicines for patients, and bed and breakfast facilities for guests.



It is imperative to carefully analyse such transactions to determine whether they give rise to multiple supplies or a single composite supply, and the appropriate VAT treatment that should be applied.







## HOSPITALITY

### Food provided to employees

Hotels often provide food to their employees to facilitate continuous and uninterrupted operations. From a VAT perspective, input tax is not recoverable on goods or services purchased in cases where they are provided to employees free of charge and their personal benefit. As an exception, input tax will not be blocked in cases where it is a legal obligation on the part of the employer or it is a contractual obligation or documented policy to provide such services or goods so that employees may perform their role, and it can be proven to be normal business practice in the course of employing such people.

Arguably, hoteliers may rationalise that providing free food to employees is a contractual obligation or documented policy. However, they should likewise be able to establish that such provision of meals is necessary to enable the employees to perform their role and that it is a standard business practice. Factual analysis of every hotel business is crucial in determining the eligibility for input VAT recovery on these expenses.

### Determining the value of supply

Equally critical to applying the appropriate VAT treatment is determining the correct value of the supply on which VAT should be applied. Hoteliers in the UAE are billing customers various fees such as hotel booking fees, service charges, and municipality taxes. However, the value of supply subject to VAT will not always include all these fees; often there may be disputes with the FTA regarding the VAT treatment of the fees.

As observed in the hotel businesses, municipality taxes collected by the hotels from the guests are often treated as outside the scope of UAE VAT. This view can still be refuted if the fees are considered payments that form part of the consideration for the supply of accommodation charged by hotels. Therefore, hotels must ensure that the value of supply is carefully assessed and determined and is justifiable to avoid any risk of VAT underpayment.

### Local transportation services

Providing transport services is not uncommon for hotel operators. Usually, guests may take advantage of hotel transport services, for example, for pick-up and drop-off from the airport to the hotel and vice versa. Further, hotels may provide car services to guests, as well as local trips aimed at sightseeing and entertainment.

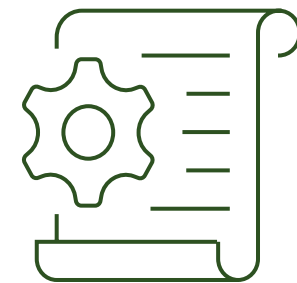
Hotels must consider their specific arrangements to determine:

- Whether the services are provided by the hotel or whether the hotel simply arranges such services.
- If the services involve the provision of passenger transportation (which may be exempt or standard-rated, depending on the purpose) or the provision of an actual car (standard-rated).
- Whether the services may constitute a single composite supply with any other services supplied by the hotel.

VAT implications may be different depending on the exact nature of the services provided.

### Complimentary stays given to guests

One of the hotel industry's most common and popular marketing activities is offering guests complimentary stays. The UAE VAT Law stipulates that goods or services provided for free may still be subject to VAT as deemed supplies unless an exception applies. However, some hotels fail to account for VAT on complimentary stays, which may potentially result in penalties for unpaid VAT.



Therefore, hotel owners must ensure that free supplies are strictly monitored and that VAT due is accounted for and paid for.







## AUTOMOBILE

### Use by personnel

It is a general practice for automotive dealers to import cars from outside the UAE for the purpose of reselling these in the UAE market. There may be cases when the car is later used by personnel of the dealer for personal purposes. As per the UAE VAT legislation, the dealer is not eligible to recover input tax on the purchase of such cars. Given that at the time of import, import VAT would have been recovered in respect of the cars based on the assumption that they are intended for resale, automotive dealers are required to reverse the input tax on cars given to employees.

### Manufacturer warranty

Generally, car manufacturers provide warranties to their customers. Manufacturers are often located outside the UAE and have tie-ups with dealers and workshops to provide warranty-related services in the UAE to local customers. The car is serviced, and spare parts are supplied, by the dealers or workshops free of charge to the local customers. The manufacturer, in turn, reimburses the warranty claim to the dealers or workshops. Some dealers or workshops have treated, and still treat, these reimbursements as zero-rated based on the location of the manufacturer.

However, since the services are supplied in respect of a motor vehicle in the UAE, the supply cannot be zero-rated and is taxable at 5% VAT. This position has been recently clarified by the FTA in the Automobile Guide.

### Car loans to employees

Automobile companies may provide financing for cars (usually at subsidised rates) to their employees. The loan amount and the interest are deducted from the employees' salaries. A common mistake is that many companies do not take such employee deductions into consideration for the purpose of disclosing supplies in VAT returns. However, interest deducted by companies is considered to be income and must be disclosed as exempt income. Companies should also consider the impact of input tax apportionment on recoverable input tax.

### Profit Margin Scheme

The UAE has an extensive second-hand car market. Since second-hand car dealers often purchase cars from individuals who are not registered for VAT, these dealers may opt for the profit margin scheme on the subsequent sale of the used cars.

If the original purchase of the car was done before the implementation of VAT, the car would not be eligible for the profit margin scheme and VAT would need to be disclosed on the full selling price. Further, when purchasing cars from unregistered sellers, car dealers should ensure that they issue an invoice showing the details of the purchase as provided in the VAT legislation – otherwise, they may not be able to apply the profit margin scheme.







## MEDIA AND ENTERTAINMENT

### Provision of accommodation to employees and clients

A UAE production company may be engaged in the production of films, documentaries, and television content in the UAE. In many cases, UAE production companies provide accommodation and meals for their employees or representatives of their clients.

The VAT incurred on goods and services that are provided to employees, clients, and similar persons free of charge is not recoverable unless specific conditions are met. As such, it will be necessary for the production company to consider all aspects of the transaction to determine VAT treatment, including:

- Whether the supply is actually free or whether charges are made for it (e.g. as part of the consideration payable by the client for the production services).
- Whether the provision of accommodation and meals to employees is a contractual obligation or documented policy that allows them to perform their roles.

### Provision of production services in the UAE

A UAE company may provide a range of production services to non-resident studios, including provision of crew and equipment, rental of studios and props, management and administrative services, post-production services, and similar.

While supplies of services to non-resident customers may often be zero-rated, this is subject to a number of conditions – including that the services are not directly in connection with any real estate or goods in the UAE and that the customer is outside the UAE when the services are performed. Production

companies should therefore consider the nature of and the circumstances surrounding the services that are being provided, and whether or not they may qualify for zero-rating. Where it cannot be ascertained that services meet conditions for zero-rating, VAT should be charged at 5%.

### Non-residents participating in events in the UAE

A non-resident may participate in an event in the UAE – for example, in a sporting event or a concert. In return for this participation, the participant will charge a fee to the local organiser.

The place of supply for any sporting, cultural or similar services that take place in the UAE is in the UAE. As a consequence, non-resident participants may be required to register for VAT and account for VAT in the UAE at 5%, unless the local event organiser is responsible for accounting for such VAT under the reverse charge mechanism.







## CRYPTO MARKETS

Cryptocurrency or ‘cryptos’ are digital or virtual currencies. Hence, unlike money, they do not physically exist. Cryptos allow for payments to be sent directly from one party to another without the involvement of an intermediary financial institution. Nowadays, cryptos have gained wide acceptance by the public and their usage goes beyond money transfers; they are increasingly bought as investments and used to make payments.

The FTA has not yet published any guidance on the VAT treatment of transactions involving cryptocurrencies. As cryptos are becoming more prominent and the quantity of transactions is on the increase, a lot of questions arise from a VAT perspective (a few examples are mentioned below). A common tax framework and consensus among different jurisdictions could help ease some of the issues involved in crypto transactions. It also becomes more important to have a proper framework in the UAE, since there is one more tax to worry about with the introduction of the corporate income tax.

### Classification of cryptos

Cryptocurrency (when in the nature of payment tokens) has been classified differently in various countries for VAT purposes. The majority of countries classify it akin to a fiat currency instead of regarding it as an asset, as its purpose is to provide a means of exchange. It is yet unclear how cryptocurrency will be classified in the UAE; that decision will have direct impact of the tax treatment of transactions with cryptocurrencies.



*With over 250 blockchain and crypto entities registered in the DMCC alone, one wonders if a crypto tax framework will align the Governments crypto expansion plans through certainty and simplicity.*



**John O’leary**

### Taxation of crypto activities

#### Mining

Since crypto miners work voluntarily, there is no client-service provider relationship between them and the people whose transactions they validate. Thus, would mining be considered a taxable supply in the absence of any nexus? If so, the question arises as to whom the service is provided.

#### Disposal

When cryptos are disposed of either through trading or as a payment for goods and services, the question arises as to whether it be treated as outside the scope of VAT considering that it is a means of exchange. Alternatively, it may be treated as a taxable supply if cryptocurrency is considered an asset for VAT purposes (which would result in a barter transaction).

### Valuation of cryptos

The cost of cryptos is volatile and is constantly changing – consequently, there might be challenges with valuations of supplies involving cryptos.







## HOLDING COMPANIES

Generally, a holding company earns income through investments and the provision of loans – including from gains from the sale of shares, dividends, interest income, and similar. Further, holding companies often incur expenses on behalf of their subsidiaries such as start-up expenses and salary costs.

From a VAT perspective, most activities of a holding company are typically exempt or outside the scope of VAT. This introduces complexity when it comes to assessing whether input tax on expenses incurred can be recovered.

### Expense recharges

There may be instances where a holding company incurs expenses on behalf of its group entities, with contracts and tax invoices that are under the holding company's name. Often, when the holding company recharges such expenses to its group entities, no VAT implication is considered. It is imperative that holding companies do consider such matters, as depending on circumstances a holding company may either be unable to deduct its input tax on incurred expenses or should account for output tax on the recharges.

### Salary recharges

Salary recharges are a common practice across industries in the UAE. Often due to certain regulatory restrictions, labour contracts and visas are issued to employees by a holding company, while these employees may actually work for other group entities. As the entities are part of the same corporate group (but not within the same VAT group), the entities often tend to ignore the possible VAT implications of such arrangements. Typically, however, the arrangement may be regarded as a supply of manpower services by the holding company to its group entities.

### Sale of shares

Holding shares and subsequently selling them are key activities of a holding company, and subsequently selling these shares. Generally, the sale of shares is considered an exempt financial service for VAT purposes; however, if supplied to a recipient outside the UAE (which may not be easy to determine, especially in cases where the sale is through a stock exchange), such sale may be treated as a zero-rated supply. Such transactions may affect the input tax recovery for holding companies and should be closely considered.

### Input tax recoverability

In relation to the above points, it is important to remember that input tax on expenses is normally only recoverable if the acquired goods or services are used or intended to be used for making taxable supplies. Considering that a major part of a holding company's revenue comes from exempt/out-of-scope activities, there is a possibility that the input tax incurred will become an irrecoverable cost for a holding company.

Holding companies should consider the steps they can take to improve their input tax recovery. For instance, they could ensure that the supplies they make are taxable – if such an arrangement is commercially appropriate and viable.





07

# FROM THEORY TO PRACTICE: BUSINESS EXPERIENCE





# Askhay Nanda

CFO, Jumbo Electronics Co. Ltd (LLC)

**We first saw taxes in the year of 2018 in what was then a tax free world. Despite all challenges encountered due to lack of awareness and readiness, we pressed on and emerged better poised to take on what the next chapter has in store for tax in the UAE. We anticipate the tax laws to get even more challenging and equally responsive initiatives from the tax authorities, which have been ample thus far.**



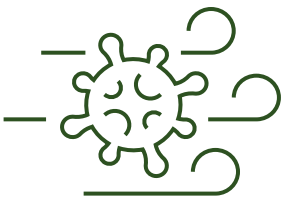
The newness of tax in the UAE called for much adjustment, especially as to manpower and internal infrastructure. It was difficult in the beginning to recruit tax-experienced personnel and have high level of acumen within the establishment to navigate our way through tax obligations. Thankfully, the authorities have published a good number of Public Clarifications and Guides which made the acclimation manageable. We await more industry-specific clarifications from the Authority, especially one for the retail sector. This and retail-tailored tax benefits would also be envisaged to propel industry growth for one of the main business drivers in the UAE.

Additionally, overhaul of the ERP system was required to integrate tax-specific functions. More than ever, the coalescence of business and technology has proven to be crucial for growth and continuity. There is an emerging necessity for tax professionals to obtain tax technology certifications and familiarize themselves with tax-specific ERP software, as well as the latest developments in digitization and automation. This comes especially important as the FTA continuously demonstrates efforts to keep pace with technology, with the recent rollout of the upgraded tax platform—Emaratax.

# Anissa Jammousi

Vice President, GEMS Education Group

The introduction of VAT in 2018 was a landmark change in the otherwise non-tax economy of the UAE. Implementing VAT was a challenge for us at GEMS Education, requiring us to customise our accounting systems, change some business strategies, revisit ongoing contracts, and educate stakeholders. GEMS also invested in hiring people with specialist educational backgrounds along with domain-specific experience to achieve technical efficiency and ensure compliance with the VAT law. The timely clarifications and guidance issued by the FTA helped us reduce ambiguity and tax exposure on critical transactions along the way.



The subsequent arrival of COVID-19 necessitated a shift in priorities for finance and tax teams with increased emphasis on remote working and risk management. As one of the world’s top private education providers, we have always invested in technology initiatives to fix the fundamentals, strengthen the building blocks, and accelerate disruption and incremental value creation. New modules and reports were customised to extract detailed financial data and enhance analysis along with technology training to improve efficiency in our reporting.



With the focus on e-invoicing in other countries of the region like KSA and Egypt and given the high likelihood of a similar shift in the UAE, it is crucial for GEMS to assess its accounting systems to successfully deliver their integration with the FTA system. This automation will allow the taxpayer’s data to be available on a real-time basis to the tax authorities, businesses, and other stakeholders. Automation should not only reduce the lead time but also invite increased scrutiny from the tax authorities, i.e. frequent audits or inquiries. We firmly believe that preparation for an external audit is a continuous process and not a one-off task. It covers the ongoing assessment of all operational transactions to anticipate errors, to VAT enabling and compliance of all IT systems, to ensuring up-to-date financial records.

After VAT, we are now seeing the introduction of corporate tax, which will be effective after June 2023. Since the new tax regime will have a direct impact on business profits, it will require significant business process overhaul and tax planning. Our agile team at GEMS is looking forward to implementing this new tax successfully too.



# Edward Carter

Head of Tax, NMC

### The UAE VAT journey: an in-house perspective

This year marks the fifth anniversary of the UAE’s VAT regime, and as with every significant milestone, it is an opportunity to reflect, celebrate, and resolve to improve.

This article provides an in-house perspective of some of the important takeaways of the VAT journey to date.

### The importance of tax technology

Every large organisation should have a tax technology roadmap, and this should form a key part of the overall tax strategy. Given the global trend of tax authorities toward digital audits and electronic invoicing, this is particularly crucial.

Due to the short lead time for the VAT go-live date, many VAT implementation projects were rushed. This commonly resulted in IT systems with:

- Flawed tax determination (inadequate system rules to determine the tax applicability);
- Lack of data validation and system controls, such as real-time auditing and reconciliations; and
- Lack of data granularity (i.e., the inability to ‘drill down’ to relevant data), which makes it difficult for tax functions to analyse data meaningfully.

These challenges meant tax functions were often rushing to manually extract, validate, and consolidate data to meet filing deadlines. The time and resource spent on these manual tasks detracted from other activities where an in-house tax function can add value, like tax advisory and governance activities.

Numerous third-party vendors offer excellent tax technology solutions. But without the proper integration between these technology solutions and business IT landscapes/key tax processes, they can become glorified tax invoicing systems that should not be relied upon for preparing tax returns.

In some cases, a reimplementation may be necessary. However, most cases often require a ‘crawl, walk, run’ approach, by first alleviating major pain points, tweaking the ERP and other upstream/downstream source systems, and standardising the existing process to make it as efficient as possible. Third-party software that can be successfully integrated with the business should then be considered.

### Business partnering

There are various tax strategies employed by businesses, the most common being financial-based (such as improving VAT cash flow, reducing irrecoverable VAT, minimising VAT-related compliance costs, etc.) and compliance-based (minimising FTA penalties, ensuring VAT returns are filed by the due date, improving the efficiency of the return process, automation, clarifications with the FTA, closing out FTA enquiries and audits, etc).

These strategies are understandable given the efforts of many in-house tax functions are focused on putting out the fires arising from the rushed implementation and uncertainty of many aspects of the VAT regulations.

But one strategy that is often overlooked is transforming the tax function into an effective business partner. This strategy focuses on improving business engagement and driving more business value.

Business partnering requires the tax function to be proactive, rather than reactive, and is an area where tax teams often have the biggest opportunity to make a difference. Reactive tax functions are the ambulance at the bottom of the cliff instead of helping build the fence at the top. The goal of the tax function should be to get involved as early as possible in any business planning and put plans in place to mitigate VAT risk before it crystalises.

It is not just a pre-requisite for tax functions to have in-depth knowledge of the VAT regulations and policy, but also to have a good understanding of the business. This often requires spending time at the coal face to learn the business model, the commercial value drivers, the supply chain, and the commercial pressures.

Tax advice given in isolation is typically meaningless. It must be given in the business context and be practical and relevant. Ultimately, the tax function is an enablement cost centre where its costs (likely with a markup) are allocated to the business. Accordingly, tax teams should justify these costs and be able to demonstrate the value they are providing.

### Engage with the FTA

The UAE’s VAT policy is deliberately broad, but it will never cover every transaction (past or future) that the policy intends to address. Consequently, there are areas of the VAT law and regulations that are ambiguous and result in uncertainty.

Often, this uncertainty may result in scenarios where the tax function must make certain judgements and assumptions relating to a tax position. It’s important to be transparent with the FTA with these judgements; transparency is paramount to building trust and credibility with the FTA.

There are various ways to engage with the FTA, either through formal channels, such as clarifications, voluntary disclosures, refund requests or tax audits, or by proactively requesting a meeting (this can either be as a business, or through an industry association). Regular FTA engagement can be hugely beneficial. As we’ve seen with the recent changes to the VAT penalty regime, there are substantial penalties for VAT errors discovered post-audit notification.



Businesses that do not engage with the FTA, and have yet to have a VAT audit, are sitting on a potential landmine of tax risk. While VAT audits can be painful, cause business disruption, and have a potential material financial impact, they have the benefits of providing certainty for historic tax periods, preventing unknown VAT risks from continuing, and providing the business an opportunity to demonstrate to the FTA their (hopefully) robust tax governance procedures.

### Revisit tax positions and the tax control framework

Employee changes within a business are inevitable. When enquiring about the reasoning behind historical VAT positions or processes, it’s not uncommon to hear “because that’s the way it’s always been done”. This is generally not a compelling argument to make to the FTA during an audit or review.

To avoid these scenarios, it is critical to document the business’s key tax positions and present the facts and basis for the VAT treatment.

The tax control framework should also be documented. This should outline the key aspects of the businesses VAT governance, such as the process for any change of events (e.g., a new product, a new IT system, change of tax codes, change of VAT regulations etc.), key VAT controls, VAT policies and should clarify ownership, which could be outlined in a responsibility assignment matrix (RACI). In addition, the framework should include the VAT determination rules for each system and tax processes (including any inter-department agreements).

Often, the facts surrounding a complex transaction can become murky over time, or the tax policy or precedent may have since changed. Therefore, these tax positions should be periodically revisited to determine whether the conclusion is still reasonable.

It’s also important to evaluate the key VAT controls. Controls should be added where there are clear weaknesses. However, any existing control or process that consumes resources but adds limited value should be removed if those resources can be better deployed elsewhere. Tax departments are being asked to do more with less, and any opportunity to make the VAT compliance process more efficient should be taken advantage of.



# Jignesh Sanghvi

CFO, DMCC

Our experience of the VAT introduction has overall been a positive one, in large part owing to the proactivity of the UAE Federal Tax Authority in ensuring a smooth transition and continuous awareness sessions to clear teething issues faced by the taxpayers during its introduction. We encountered some initial challenges in managing the transition effectively with both internal and external stakeholders and mitigated these by not only adopting a hands-on approach to the new Tax's application and interpretation, but also setting up a robust technology platform to ensure correct and timely compliance. Most of our processes are automated, and we continue to explore ways to maximise efficiencies and leverage the benefits of technology.



'Nothing is constant except change' and this phrase can be rightfully applied to VAT. We have observed a number of changes in the VAT law over these years, namely, the reduction of penalties, penalty waivers and instalment plans, and audit timelines. We at DMCC keep up with the changes by having continuous discussions on the interpretation and application of the Tax Law. As an entity focused on promoting trade through Dubai, DMCC remains highly invested in helping shape new, progressive, and robust regulations affecting, in particular the physical trade of various commodities.

While, the FTA has been proactive in issuing clarifications, guides, etc., we have listed below a few areas which could help in further enhancing the ease of doing business in the UAE –

- Creation of a dedicated helpdesk to help collate and manage the issues faced by an industry
- Expediting the disposals of the procedural applications such as change / amendment in the VAT registration, tax clarification requests
- Remain aligned with international best practices and alert to emerging market conditions to attract FDI



2023 will witness the introduction of the new corporate tax regime and the introduction would also pave way for adoption and implementation of the OECD BEPS 2.0 measures to address tax challenges arising from the digitisation of the global economy and the introduction of a global minimum tax rate for large multinationals. We look forward to implementing the same at our organisation.

# John O'Leary

ex-Tax Director, BitOasis

In recent months we have seen Sheikh Hamdan launch the Dubai Metaverse which aims to add 40,000 virtual jobs and add USD 4bn to Dubai's economy in 5 years. We have also seen the creation of the Dubai Virtual Assets Regulatory Authority (Vara), where State minister Omar Bin Sultan Al Olama stated the UAE needed a positive, yet robust, regulatory steer to prosper. With over 250 blockchain and crypto entities registered in the DMCC alone, one wonders if a crypto tax framework will align the Governments crypto expansion plans through certainty and simplicity.

As we approach the five-year anniversary from the implementation of VAT in the UAE and patiently await the UAE CIT to come into effect, the UAE crypto industry looks to the future for both market improvements and guidance from the FTA on the taxing of 'virtual currencies'.

With the FTA still not having provided any public stance on the taxation of crypto currencies, the OECD's 2020 paper 'taxing virtual currencies', would still appear to be one of most relevant papers available to tax professionals in the region.

Around 70% of the 43 OECD countries currently have certain tax guidance available on the classification of crypto assets. With more stringent regulation expected to follow globally in the aftermath of the last number of weeks market turbulences, it will be interesting to see if the FTA follow suit with tax classification on the subject matter following the likes of the UK and USA.

With the UAE becoming known for its ambition to become a crypto hub, the industry awaits official tax guidance to mirror the commercial aspirations of the government.







# Kalaiarasan Manoharan

Global Tax and Compliance Lead, Noon

In 2018, when UAE entered into a tax regime, it remarkably transformed businesses from no records to record-based business conduct in a short span of time. The greatest success of VAT in UAE shall be accredited to the vision of the UAE’s leadership, Ministry of Finance and FTA to keep it simple, transparent, and efficient with minimal to no business impact during the transformation.



Typically, countries look to design taxes as revenue streams with a focus on “Taxes” on Businesses, while the UAE is a classic example of “Businesses” with Tax, and this focus automatically contributed to a paradigm shift in its revenue growth. With the launch of the new platform “EmaraTax”, UAE looks to have the best system that can be agile, and dynamic to the waves of regulatory changes in recent times.

# Kaushik Kothari

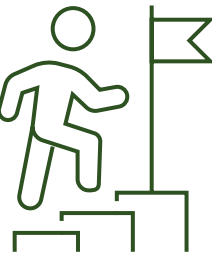
Taxation Division Manager, Sharjah Cooperative Society

As the world celebrated the end of 2022, VAT, United Arab Emirates’ most historic tax reform, also completed 5 years of its journey. VAT has seen its share of peaks and valleys in the past 5 years as it passed through a phase of uncertainty in compliances and tax application and entered the stage of clarity amongst businesses as they eased into the law. The UAE Government and the Federal Tax Authority (FTA) must be lauded achieving the humungous feat of drawing the country’s indirect tax horizon and their continuous efforts to iron out the ambiguities and inefficiencies in VAT.



Introduction of a new law bring with itself inevitable challenges both for the administration and taxpayers more so for a country which has never been exposed to a taxation system before. Incorporating changes in the ever-evolving modules of the ERP system and making them tax compliant has been the most challenging task. Despite best efforts from businesses, the ERP systems could not be updated completely leading to innocent errors and omissions while undertaking tax compliances. When the error was corrected by the taxpayer, the auto application of the long host of administrative penalties resulted in piling up of substantial penalties as high as 200%-300% of the tax amount. The recent overhaul of the penalty system was a great relief for the taxpayers as the FTA consolidated major administrative penalties.

With the onset of the audit phase, businesses need to be proactive in identifying past data errors to ensure a smoother closure of the task with minimal tax and penal liabilities, if any. While major focus of all the stakeholders in the first 5 years has been on a complete implementation of the tax law, the focus is likely to shift on matters of interpretation of law, identifying tax irregularities and inefficiencies and easing compliance procedures. Effective implementation of the Electronic Service System throughout the GCC for hassle free movement of goods and provision of services tops the wish list of all the stakeholders. This will bring maturity in the tax provisions and clarity and stability in their application resulting in a win-win situation for all parties involved, Governments in GCC countries, taxpayers, and the tax administration.



**It’s the beginning with the long road ahead wherein every stakeholder has a critical role in cementing VAT stronger in the region.**



# Mohamed Faycal Charfeddine

Group Head of Tax, Aujan Coca Cola Beverages Company

Five years after its implementation, the journey of Value Added Tax in the UAE has been an interesting one so far. Although the concept of tax in the UAE was prefaced by the introduction of excise tax, the effects of VAT were more palpable: the consumption tax revolutionized the business and tax landscape in the country, requiring a correspondingly significant change in mindset for the businesses. Everyone from business owners, professionals, employees, consumers, and especially those who have stayed in the country for decades, were now to understand this added cost to every transaction, its purpose, the mechanisms and processes of collection and remittance, and translating it to the value it is intended to add to the economy; VAT would permeate almost every facet of life in the UAE.


The implementation came with its own challenges. In terms of understanding the law, clarifications were found to be necessary, for although the provisions may seem straightforward, it was eventually seen that much room was left for interpretation when everyone took varying positions in determining the taxability of transactions. In our business, although the typical transactions are straightforward, much dialogue was warranted among our customers and suppliers in determining the correct VAT treatments to be adopted, which more often than not concluded in taking a conservative position for the lack of a certain answer.

The taxpayers were not alone in their predicament with the then-confounding VAT, however. We have found that the FTA, despite the gargantuan task at hand, commendably executed the project. For us, the Authority maintained a client-oriented service and accessibility, agile to publish much-needed Guides and Clarifications and resolve arising issues. One salient move that was immensely integral in the taxpayers navigating through VAT compliance was the reduction of penalties. Further, the facilities available as well as the procedures in place were also reasonable, particularly on the duration of processing refund requests from experience.

Technology has also played a key role in the implementation of VAT. This proved truer than ever during the COVID-19 pandemic. Amidst the lockdown, our business group's finance and tax functions were preserved since meetings could be held over online platforms, documents were available or could be converted into digital format, and tax return filing and payments could all be accomplished online. All these aided greatly in the continuance of business which was critical for us in the FMCG industry.

Yet with what it has overcome and achieved so far, VAT in the country is still in its nascent stages. Recently, several legal amendments to the laws and regulations were made. Among these was the extension of the statute of limitation for tax audits. But having witnessed how the FTA has handled changes in the past, I count on the continued support perhaps in the form of more specific examples in the Tax Guides, and comparative versions of publications revised, to better assist taxpayers in identifying any incorrect tax positions adopted and making the necessary corrections. On our part, we are continuously assessing our processes and positions to ensure that we are fully compliant; we are regularly conversing with our experts and consultants, as well as conducting VAT health checks to cover all bases, and I would recommend the same proactive exercise for all taxpayers.

We can all definitely expect more in the future as tax continues to evolve in the UAE. And being in a country that has always been at the forefront of innovation, it would do us well to keep ourselves updated with the latest trends in technology and explore ways to use these as modern solutions to modern problems. The omnipresent tech talks about Artificial Intelligence or AI, for example, can prompt the idea of collaborating with this modern technology to ease VAT compliance burdens. This comes with greater emphasis for tax professionals as well who are the primary go-tos of taxpayers for any tax dilemma.



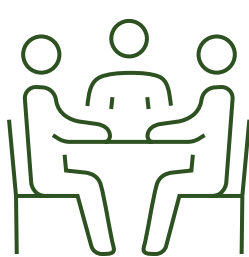
In sum, from a non-tax to a tax environment, it was fascinating to witness how the law, the environment, the organizations, and the people within those organizations have transformed and progressed throughout the VAT journey. As 2023 approaches ushering in Corporate Tax, we are anticipating a riveting sequel to VAT as we will soon see how the two taxes interplay with each other, the challenges that may arise, and how we tackle such challenges with what we have learned from the eventful past five years—the journey continues.

# Paul Gyles

Chief Financial Officer, Shamal Group

It's hard to believe that it's been 5 years since VAT was introduced, and the time has gone very quickly. It was a significant project for the UAE which took a huge amount of effort from the FTA and all companies, but it was implemented very smoothly.

Upon VAT implementation, the development of tax technology/ ERP solutions has been one of our core focus areas. Initially, there was quite a bit of effort to configure our Oracle ERP system to ensure this was fully compliant to successfully meet the VAT requirements. In 2021, we migrated to Microsoft Dynamics 365, and having a market-leading ERP system makes things much easier, especially for VAT accounting. In fact, as ERP plays a significant role in VAT, I believe tax professionals could upskill themselves with a detailed understanding of ERPs and business practices which will help them to assist us more efficiently. They should look forward to the full integration of ERPs with the tax requirements.



The Tax Authority continues to develop its systems to facilitate and expedite its services. The website is very user-friendly and has all the guides and reference documentation online for easy access. Particularly, it has done a commendable job in implementing a robust VAT filing and payment mechanism, issuing public clarifications, and hassle-free corporate and tourist refunds. The VAT return submission processes through the portal have been very straightforward, and we have always found the Tax Authority very supportive.

The Tax Authority has always, since the introduction of VAT, ensured simplification in the understanding of the VAT legislation including its implications on any transactions. To facilitate businesses and encourage taxpayers to achieve compliance, it ensures making development in the VAT legislation –changes in penalties rules in 2021 are one of them. We especially, highly appreciate the detailed responses provided by the Tax Authority promptly. One such

issue specific to the real estate industry was clarification on whether the land would be regarded as bare land or serviced land, particularly reclaimed land. Although, one such recent amendment that would have a significant impact on businesses is in relation to the introduction of the statute of limitations (FTA audit, VD filing, etc.).

Although we haven't yet been audited, because of continuous support from the Tax Authority, we are confident that with a finance team consisting of qualified finance professionals, supported by our expert tax agent, as well as a market-leading ERP system and record management process, that we are in a strong position to facilitate a smooth tax audit when required.



The major legislative change required for a positive boost and acceleration of growth for the real estate industry would be to include the real estate development/ construction sector under the zero-rate benefit instead of being standard rated as in most cases, tax collected is refunded, or alternatively, reverse charge mechanism to apply in this case so that business cash flows are not negatively impacted. Another significant change to further strengthen the VAT regime would be to introduce e-invoicing which would be directly linked to the FTA system. Also, face-to-face interaction with the Tax Authority officials with an opportunity to explain and discuss clarification matters would add to the ease for the taxpayers.

The Tax Authority in the UAE has now introduced the corporate tax effective June 1, 2023 – this is another major project. We will soon start working on a corporation tax impact assessment, and then the implementation project. With good planning and preparation, and support from the Tax Authority, I am confident that this will be another smooth implementation.



# Nitin Agarwal

## Head of Tax, Large Family Business Group

The implementation of Value Added Tax (VAT) in the United Arab Emirates and the Kingdom of Saudi Arabia in 2018 was a perfect example of how the cohesive/ disrupting interplay of digitalization, tax and business operations can make or break the balanced scorecard of a business. Implementation of transaction taxes meant the addition of a new yet significant stakeholder for every tax registered business – the tax administration. A new stakeholder meant the businesses had to manage newer and wider expectations. This in turn forced the new category of taxable businesses to revisit their strategy, structures, plans, resources, technology and processes to be prepared to meet the needs of these “new” stakeholders and the revised expectations of the existing ones.

Having said that, tax is not the only transformation challenge that businesses in the region and elsewhere have been dealing with, in the recent decades. Business, as we knew it a few decades ago, has completely transformed, riding on the wave of technological advancement. We have witnessed massive strides in all fields impacted by technology, especially information technology. The question that we ask today: Has tax kept up with business in this evolution and transformation journey?

To me, the answer is - a Yes & No. The tax digitalization journey has been passive, at best. Digitalization of tax has far and wide implications on various stakeholders. The roadmap to digitalization involves typical approaches synonymous with other business functions. This is especially relevant in jurisdictions implementing taxes for the first time.

The implementation of VAT in 2018 was in a way a strategic and redefining moment for many businesses in the way they operate. Tax is now the new and significant business impacting function and is here to stay. This creates the need of a strategy for the tax function that is aligned to the overall strategy of the business and the expectations of all stakeholders and what they want to achieve.

To consistently achieve this, it is imperative that you identify the right stakeholders, note their expectations, align your operational (e.g. tax digitalization) strategy to those expectations. You do not need a space shuttle for inter-city travel and you cannot drive a bus to the moon! Deciding on your tax digitalization approach is somewhat similar, in very simplified terms. The global focus is a gradual transition towards compliance by design with Tax happening “naturally” – Ref: Tax Administration 3.0 (OECD).

The right choice of technology can be a key enabler for tax digitalization. There is a huge array of offerings that support your determination and compliance goals. What you select depends on your needs - your size, complexity, number of jurisdictions, maturity of teams, existing IT infrastructure and the budget. Digitization initiatives may require significant investment into physical IT resources based on its IT-design considerations. Choices like whether the business wants to enhance its existing systems’ capabilities to determine tax or buy a new bolt-on software, whether it chooses to design an on-premise solution or cloud solution, can mean significantly different approaches and requirement of IT assets.

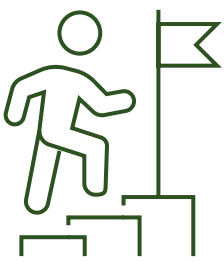
While technology does play a key role, the state of your data determines the efficiency of the technology employed. If not enough is done on the data front, even the best in class technology cannot do any magic for your determination and compliance needs. Having a robust master data governance framework is one of the most important ingredients for the success of any tax digitalization strategy.



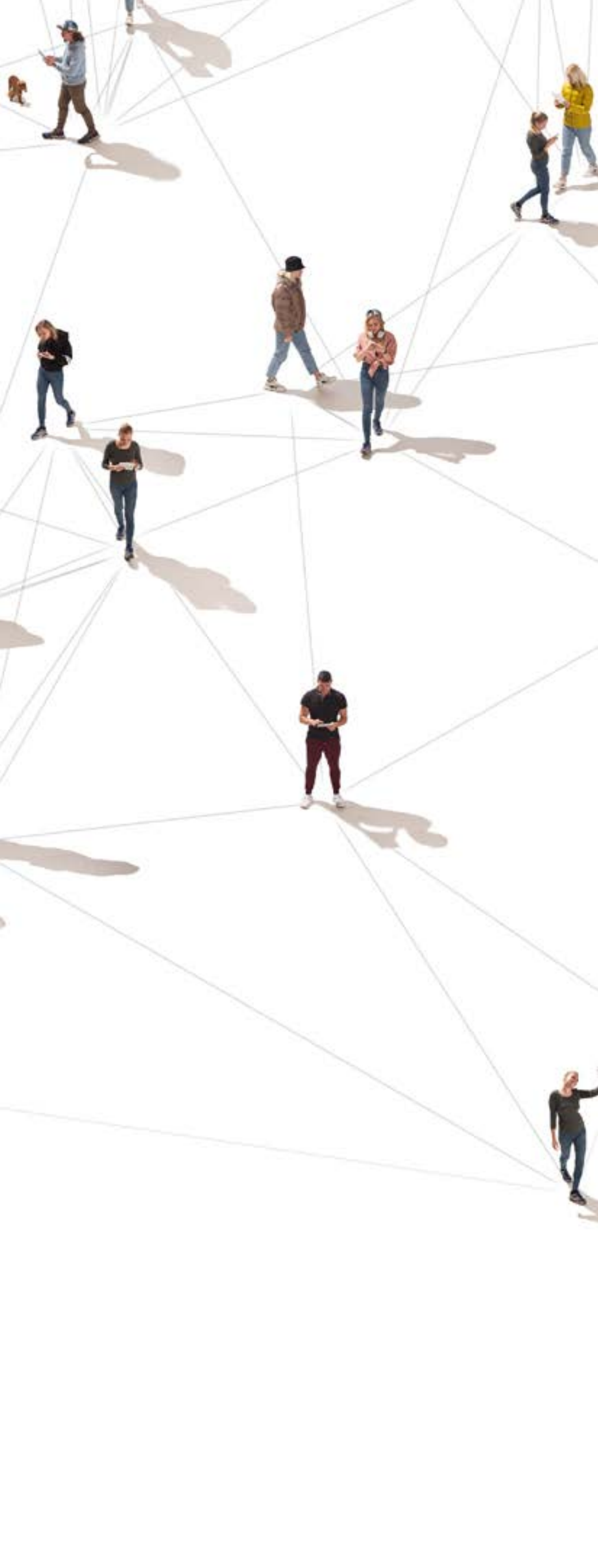
It is not an exaggeration to say that people are the center of all things great. Tax is not an exception. Tax digitization projects are not IT implementations but multi-functional and integrated in nature. These require heavy cross-functional engagement and commitment. Depending on the size, spread and complexity of the business, the tax function needs to be staffed with skilled employees with the right technical knowledge and relevant skills and experience. The factors include the expected scope in terms of diversity and size of business, number of applicable taxes, geographies of operation, complexity of operations, state of processes and technology etc. The right technical knowledge and experience is usually taken to be combination of relevant education and experience in similar taxes, among other things. You need a team that understands “What success looks like” and what classifies as “issues” and the ability to bridge that gap if you wish to have a meaningful digitalization roadmap. People who understand tax but not business and technology or vice versa, may struggle visualizing and

Last but not the least, you need to review and align your business processes in line with your strategy and resources to achieve the desired goals on the tax digitalization front. We come back to the reality that – Tax is not a function that operates in isolation. Rather the success of your compliance initiatives largely depends on the robustness yet agility of the processes around you.

A strategic and results driven digitalization of tax will have challenges, but the benefits of digital transformation of the tax function far outweigh these challenges. With effective digital tools at hand, tax teams can add more value to the business by proactive business partnering rather than trailing and problem solving. This can be one of most effective levers of optimization of cost of tax compliance for business based on multiple parameters and not only the Effective Tax Rate. Digitalization also has the potential to reduce the impact of “voluntary” in tax through tech-enabled uniformity and definitiveness. This can eventually help the entire ecosystem to evolve and enable the Autonomous Driving mode in tax compliance with an option to interrupt and intervene where and when there is a need.



**This is a journey of thousand miles. Most of us are still taking the first steps...**







# Siegert Slagman

Ex-Head of Tax, multinational  
in the Middle East

2018 marked a momentous landmark for UAE which had attracted businesses from around the world mainly due to its standing as a tax-free business hub. The UAE introduced VAT whilst incorporating the best practices globally with the objective to minimise compliance burden on businesses.

The efforts put in by the Government and the Federal Tax Authority (“FTA”) and the continuous evolution of the Tax Laws to make them simple and taxpayer-friendly is commendable. It is also worthwhile to mention that the dissemination of information and clarifications is much better in comparison to established jurisdictions that have implemented indirect taxes for several decades. There have been major hits like – digitisation of tax compliance, revamped tax portal, robust revenue collection, etc. but there have been some misses as well. In a trade, i.e. largely an import and export-oriented scenarios, the authorities could relax the documentation / procedural requirement to a certain extent making it comfortable for the businesses to seamlessly export / import goods. Faceless audits and assessments have proven effective, however, the limited response time provided to the taxpayers can be challenging. The FTA should also aim at performing an industry-wide risk profiling to determine and initiate reviews on businesses with a gap in risk management.



Corporate tax is also set to kick in from 2023 as the UAE further pushes to broaden the horizon of its economy away from the oil-based revenue. The impact of corporate tax will be completely different considering the greater emphasis on accounting and IFRS / GAAP concepts. The new introduction should also require a whole new set of skills not only for the Finance or Tax functions but also for the external advisors and the Tax authorities. Businesses must also foresee the significance of reconciliations amongst the numbers reported in the VAT returns and the Corporate tax returns vis-à-vis the financial statements.

# Sourav Chakraborty

Senior Manager Corporate Finance & Investments,  
large UAE-based conglomerate

VAT was introduced in the UAE with the objective to operate effectively and to streamline and strategically manage the end-to-end processes. However, many taxpayers faced difficulties due to a very short window between the publication of VAT Law / Regulations and the effective implementation date, and lack of clarity on the applicability of VAT on certain transactions. The FTA has been the driving force in easing out teething troubles and ensuring that guides and clarifications are available in the public domain to clarify any differing opinions.



Reduction in administrative penalties on various counts came forth as a welcome relief for the businesses. Reduction in penalties not only signifies a decrease in legal obligations and a boost to the working capital but also encourages the taxpayers to come forward and correct any reporting errors committed in the past period. Furthermore, the launch of penalty waivers and instalment schemes also helps the eligible taxpayers who are struggling due to the aftermath of Covid and the stressed economic condition.

There has been a significant uptick in the number of businesses that use their enterprise-wide financial systems to prepare the net VAT payables thereby replacing the spreadsheets and/or traditional tax technology solutions. We have also been upscaling our technological solutions and advanced into the online mode right from the introduction of VAT. The push for technological advancements helped in successfully navigating through the challenges during the Covid-19 lockdowns resulting in little impact from the pandemic.

In the global tax environment, businesses are expected to respond promptly and precisely to the increasing compliance and reporting mechanisms. That said, there are a few areas which could help in developing competencies in the ever-changing tax setup –

- Automated reconciliation of input and output supplies through the Emara Tax Portal;
- Facility to change the tax periods for the business to streamline the VAT return preparation processes; and
- Aligned tax positions with other GCC countries to avoid double taxation on the movement of goods and provision of services amongst the countries.



# Surender Kapoor

Vice President Finance, Merex Investment Group

UAE is recognised across the globe for its diversity, developed infrastructure, technological advancements and ease of doing business. It is considered an economic hub and a popular business destination in the Middle Eastern because of its strategic location. The introduction of VAT in the UAE was part of a GCC-wide effort to diversify the economy. The introduction of VAT at the rate of 5%, being comparatively lower than other comparable economies, was well received by the business community.



The FTA has effectively streamlined the VAT process and procedures over the course of these five years. Furthermore, the timely issuance of clarifications and guidance has elevated the business and stakeholder confidence. The tax authorities have been proactively engaging with the taxpayers in order to improve the VAT automation process and the tax portal's user interface. Various changes have been brought in with the launch of the new tax portal – Emara Tax viz. raising grievance / complaints through the user portal, procedure for payment, self-allocation of payments towards the tax dues, etc. Recent amendment in the UAE VAT Law to minimize the tax penalties for taxpayers willing to file voluntary disclosures for better transparency has had a positive impact on businesses.



With continuous growth in technology and digitisation of VAT processes, tax professionals have to acutely understand the business and transactions of the organisation and accordingly develop their skills in the interpretation and applicability of Tax. As a continuous improvement, they have to keep themselves updated on tax reforms happening in the country, region and wider world to be able to advise clients as a full-service practice.

Last but not the least, the introduction of corporate tax will have a direct impact on business net profits and would require significant business re-structuring and effective tax planning. The businesses could possibly restructure their existing business models and pricing strategies which will also have an impact from a VAT perspective.

# Uzair Dawood

Group External Reporting & Taxation, ENOC

## Where perception meets reality!

Taxes matter. Be it public sector development and social uplift schemes, tax revenues allow fiscal space to finance critical public projects and initiatives. Five years on, the introduction of VAT in the UAE can be surely called a successful implementation given the current state of evolution of both the authority and the regulation.

Key to this success appears to be in lessons learned from implementations in other jurisdictions and carving out a system that meets the UAE's unique ground realities.

Despite significant challenges in the preparatory work, the main building blocks of this success was the establishment of a federal level regulatory authority, supporting IT system and training procedures for staff, registrants and practitioners. The cherry on the cake was a broad-based and single rate of 5% and a limited number of exemptions and zero rating for financial, medical, and educational services.

When it comes to tax administration, an unfair and capricious tax practice is likely to bring disrepute to tax authority and undermines compliance of other taxes in the system due to perception. On the contrary, a simplified, just and transparent tax system, even with reduced rates, has the potential of generating more revenues as a result of preserved trust and compliance at large. This is practically evident in the UAE whereby VAT revenues crossed phycological threshold of AED 100 million in the first five years.



The collective perception of taxpayers warrants a closer attention in formulating tax policy. Like any factor affecting business environment externally, there is a risk that perception of taxes creates a different picture than the one tax policy-setters have in mind. Hence, when introducing, amending, clarifying or otherwise waiving applicability of taxes, the perception management is as critical as the macroeconomic substance underlying the tax policy. The recent clarifications and guides on varied issues by the Federal Tax Authority (FTA) should further strengthen the VAT framework by ironing out prevalent differences in application of VAT rules.

The same philosophy will go a long way in achieving an effective introduction of corporate income tax in the UAE and we hope to call the UAE a tax landscape where perception meets reality!



# Anil Rajanala

GSP Business Head, Cygnet Infotech Pvt Ltd

**VAT in the Middle East was a landmark tax reform impacting various aspects of business processes, starting from maintenance of records to reporting of the transactions, payment of tax liabilities, claiming of the input VAT and the need for automation to bridge the gaps between the process and the practices.**



A significant challenge faced by the companies after the introduction of VAT was about data management. We came across various reasons for this such as different source systems, nature of operations, different regions. The data required to prepare VAT returns was also completely different from the data found in the financial statements, and thus the businesses had its own set of challenges to extract the relevant VAT data from their accounting systems. The systems had to be modified to capture tax identification number of the vendors and the customers at source, as well as retrieval of data for the returns from various sources for compliance.

Coping with these complexities without technological intervention was no longer sustainable for the companies having widespread operations. For the companies using the industry standard ERP systems, a shock came with the realization that they were not equipped to manage the complexities out of the box and left the role of providing up-to-date changes related to tax legislation to either the customers or third-party solution providers.

Building an in-house automation system also did not diminish the challenge of keeping the multiple financial systems for ERP, procurement, etc. updated with the changes in the rules and rates. Rather, companies operating in GCC increasingly preferred a specialized solution to streamline their VAT compliance processes across the region by relying on tax-tech service providers to adjust quickly to changes in tax legislation.

Besides the assessment of the capabilities of the existing IT systems and reconfigurations necessary to be compliant with the VAT regime, the companies in the Middle East did remarkably well in coping up with the initial challenges with regard to the day-to-day compliance, interpretation of the clarifications provided by the tax authority and adjusting to the new normal. We are proud to have partnered with some of the large players in the region to help them navigate this change. On the anvil are even more opportunities for the companies to digitalise their tax processes as we move towards real-time reporting through e-invoicing. To comply with this mandate, the taxpayers having multiple source systems and ERP across the business lines will have to streamline their processes to integrate it with a compliance platform for real-time e-invoice generation. Once the e-invoice has been generated, its response in the form of unique reference number would have to be fetched back to the ERP and stored for compliance purpose.



The tax authorities are constantly finding new ways to efficiently gather accurate tax data and use it to optimise tax collections. When we imagine the future of e-invoicing, we see the tax authorities taking control of the e-invoicing process to plug revenue leakages and improve VAT returns. Given this fundamental shift in the reporting, the VAT returns may be replaced by auto-populated returns. In the long run, the VAT returns, reclaims and refund applications may even become completely redundant as tax authorities analyse, validate, and reconcile tax at a transactional level in real time by consolidating data from a variety of sources. Besides, we believe the tax authorities in future will evolve the audit and compliance check methodologies with the rich set of transactional data available at their disposal. With the use of advanced data analytics, the routine and periodic in-person audits and inspections by the tax authorities will likely become a thing of past. The trend will continue to accelerate, it is just the start of the digital journey for the businesses.





**ROAD AHEAD:  
THE NEXT  
FIVE YEARS**





While the journey of the last five years has been astonishing, it is just the beginning for VAT in the UAE. In this part we consider developments which may take place over the next few years as well as where businesses should focus their attention.



**LEGISLATIVE  
DEVELOPMENTS**



**FUTURE OF INDIRECT-TAX  
AUTOMATION**



**INTRODUCTION OF  
CORPORATE TAX IN UAE**





## LEGISLATIVE DEVELOPMENTS

As the UAE’s VAT regime continues to develop, we can expect further changes to VAT and procedural legislation.

Leaving aside changes aimed at dealing with any emerging uncertainties in the legislation, below we discuss some of the more interesting developments that may take place.

### VAT rate increase

The 5% standard VAT rate currently in force in the UAE is currently aligned with the rate prescribed in the GCC VAT Agreement. This is a low rate by international standards, with the unweighted OECD average standard VAT rate being 19.2% in 2022.<sup>2</sup> Further, while KSA and Bahrain’s standard VAT rate was initially also set at 5%, both countries have since increased the rate to 10% and 15% respectively.

Considering the growing tendency in countries around the globe to use VAT as a convenient and efficient way to raise additional tax revenues, it would not be surprising if the UAE decided to increase its standard VAT rate as well. The low 5% standard rate was appropriate in the environment where taxes were previously non-existent and therefore there was no absolute certainty regarding whether the new tax could be successfully implemented; now that it is evident that VAT has been accepted by taxpayers and it has become an integral part of doing business in the UAE, increasing the tax rate would be a natural next step.

If the VAT rate were to increase, it would be unlikely to exceed 15%, which is the standard rate currently in force in the KSA. This would ensure that the UAE remains a competitive destination for doing business compared with the other GCC countries.

### Taxation of digital economy

Digital commerce has been on the increase. Partially with the help of COVID-19, online shopping has become a new normal. Most goods and services can be purchased online either directly from suppliers or through electronic marketplaces.

Such shopping is not limited by geographical location, and a UAE resident can buy goods and services from an overseas supplier as easily as he or she can buy from a UAE vendor.

The topic of the taxation of digital economy has been on the global agenda in the recent years. Over the last decade, a number of jurisdictions, including a few European countries, Australia, and New Zealand, have introduced special VAT/GST rules for taxing digital products. The OECD has also provided intellectual support to policymakers by publishing a number of research papers that discuss, and provide suggestions on, the taxation of the digital economy.

While the UAE VAT rules capture most local sales, their application to goods and services supplied by overseas vendors is not without its problems:

- Import VAT might not be correctly charged on importations of goods
- There have been known cases of VAT-registered persons facilitating importations of goods on behalf of unregistered UAE residents, and incorrectly recovering import VAT charged on the border
- While overseas suppliers of B2C services may have an obligation to register and pay VAT for supplies made in the UAE, it is practically impossible for the FTA to track and enforce the majority of such cases

In light of the global trends for special VAT rules for the taxation of the digital economy, similar targeted rules may also be considered for the introduction of VAT in the UAE. In introducing such rules, policymakers would need to consider, among other things, whether:

- the rules should apply to goods, services, or both
- the obligation for tax should be the responsibility of individual vendors or electronic marketplaces
- simplified VAT registration for non-resident vendors is required

Introducing comprehensive rules for the taxation of digital economy would help to ensure taxation of supplies made by non-residents and put them on equal footing with the local UAE vendors. It will also prepare the UAE VAT regime to deal with the ever-expanding size and reach of the digital economy in the modern world.

### Increased use of domestic reverse charge

A reverse charge mechanism (“RCM”) is a mechanism that shifts the obligation to account for VAT from a supplier to the recipient of the supply.

In inbound cross-border transactions, the RCM is commonly used to free non-resident suppliers from the obligation to register and to charge VAT – this improves the ability of tax authorities to monitor and enforce the payment of tax from local recipients of supplies. In domestic transactions, the RCM is also often used to lessen the impact of VAT on customers’ cash flows.

Currently, the UAE legislation only allows the domestic reverse charge (“DRC”) to be used by VAT-registered parties for domestic supplies of oil, gas, and hydrocarbons and of gold and diamonds. However, an amendment to the VAT Law introduced in 2022 now gives a broad discretion to the Cabinet to issue a decision specifying any other goods or services that are subject to the DRC.

The new mandate provides a strong signal that we should expect the DRC to be implemented in the UAE more broadly over the next few years. While the DRC may be used in a wide range of scenarios, it is most likely to apply to high-value supplies and supplies in sectors where customers are generally able to recover VAT in full. Presumably, some of the potential transactions that may be considered for the DRC may include supplies of real estate and supplies in the construction industry, supplies of high-value assets above a certain threshold, supplies to government entities and government-owned enterprises, and similar.

### GCC: path to harmonisation

The GCC VAT Agreement provides a framework for local VAT legislation to be introduced by the GCC member states.

One of the aspects of GCC VAT framework is that it establishes a set of common rules that would only be applicable to goods and services traded within the GCC. Such rules include, among other things:

- special place of supply rules for goods and services
- special rules for taxation of imports, including on

assigning the right to tax imports

- a special transfer mechanism between member states that would allow one member state to collect VAT on behalf of another member state (where the consumption will occur) and then directly transfer that revenue to the latter
- a common electronic system for exchanging information related to intra-GCC taxation

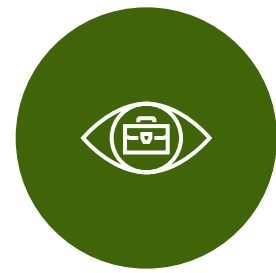
Currently, none of the above rules are yet in force in any of the GCC countries that have already introduced VAT. At least initially, the reasons for this would likely be that each member state wanted to test the operation of the VAT regime in a ‘simplified’ mode, before adding the additional layer of intra-GCC complexity. Five years after the introduction of VAT, however, we can see more, rather than fewer, differences between the member states which means that even more work would be required to harmonise the GCC VAT regimes before the common GCC rules come into force.

One of the main examples of the lack of harmonisation in the GCC is the standard VAT rate – which is 5% in the UAE and Oman, 10% in Bahrain, and 15% in KSA. Since the GCC VAT Agreement contemplates that member states may need to be collecting VAT on each other’s behalf, the differing VAT rates introduce a new nuance factor to consider, which was not predicted when the original GCC VAT Agreement was signed.

**Due to the absence of public announcements, it is currently unclear what the short-term plans for a common GCC VAT regime are. It is certain, however, that if the member states are still serious about implementing a common harmonised GCC VAT regime, further work would have to be conducted by the states to agree how to deal with developing differences in their local GCC VAT jurisdictions. It remains to be seen in the next few years whether this topic will remain on their agenda, or if the GCC states are content with the status quo.**

<sup>2</sup> OECD, Consumption Tax Trends 2022.





## FUTURE OF INDIRECT-TAX AUTOMATION

Technology changes the way businesses operate, both externally and internally. Considering the almost certain introduction of e-invoicing in the UAE over the next couple of years, technology will become an even more relevant and pressing issue for UAE businesses.

Tax operations across organisations are transforming from being a compliance function to influencing the business structure and decisions. Emerging technologies have the potential to improve operational efficiency and uncover insights that can drive fact-based decision-making and change the value tax brings to the company's bottom line. For the tax authorities, the scope of data acquisition has expanded to collections of non-tax data, which if linked appropriately with tax data, enables a broader understanding of the business operations of taxpayers and facilitates the audit and analysis of tax data.

On the other side, technology is helping tax teams to cope with increased demands for data and transparency from regulators. Historically, taxpayers had been reactive to the changes brought by the tax administration, but now, aided by the technologies, tax teams have started taking a more proactive approach to use data for predictive and prescriptive analysis, tax modelling, and decision making to optimise tax across the breadth of their operations and speed up planning, reporting and compliance processes.

### From push to pull: the fundamental shift

The overlap between business processes and tax reporting is steadily increasing with tax authorities demanding more transparency and real-time access to information. In many countries, companies are not only increasingly obliged to report transactional data digitally, but they must also now do it in 'real time' with an e-invoicing mandate.

Around the world, countries are at different stages of implementing e-invoicing and live reporting obligations. While the requirement to issue an e-invoice to customers is generally limited to domestic transactions, tax authorities are also

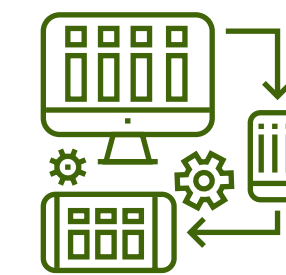
introducing a parallel e-reporting requirement for invoice data for cross-border transactions, both for invoices issued and received. This mandate requires companies to integrate various source systems with the compliance platform so e-invoices can be generated in real-time and so companies can receive and store the response in the form of unique reference number in their ERP systems.

Multinational operations just add to these data complexities due to varying country-by-country reporting rules and the collation of data spread across the countries. Coping with these complexities without technological intervention is no longer sustainable for companies with widespread operations. Adopting the right technology and deploying sustainable e-invoicing and tax-reporting systems will enable businesses to reduce risks of unnecessary audits and help ensure tax and e-invoicing compliance.

Going ahead, as real-time reporting becomes a new normal, many of the related tax processes will become more suitable for digitalisation. For instance, the availability of real-time transaction data can help tax authorities and governments in multiple ways. Tax authorities may want to use the data to scrutinise taxpayers' activities to secure its share of tax and provide auto-populated VAT returns to taxpayers. As more and more taxpayers come within the ambit of real-time reporting via e-invoicing, as a natural progression towards digitalisation, the process of tax reclaims may also be automated and we may even see VAT returns becoming redundant in the long run. The data collected for indirect tax purposes may also be used to establish correlations with direct tax reporting and financial statements. The data could also provide insights to the government about the level of economic activities and help them in taking economic and commercial policy decisions.

### Digitalisation – the only way ahead

To overcome these risks and challenges, organisations have started using automated emerging technologies that will help them to aggregate, validate, and report for compliance purposes, while using the analytics on the data gathered to help identify irregularities and mitigate risk. These emerging technologies have the potential to improve operating efficiency and uncover insights that can drive fact-based decision making and change the value tax brings to organisations' bottom lines. It is only a matter of time before we see these emerging technologies starting to support tax functions in their strategic decisions.



It is essential that companies look at the digitalisation journey not as a compliance burden but recognise the fact that it can bring direct benefits to the business and that it can minimise the company's exposure to in-depth scrutiny and penal actions by the tax authorities.



*Choice of technology can be a game changer, using the appropriate financial system has been key to the positive outcomes.*

**Ankur Khanna**







## INTRODUCTION OF CORPORATE TAX IN UAE – WHAT DOES THE FUTURE HOLD?

One of the significant developments in the UAE tax landscape has been the introduction of Corporate Tax (“CT”) for businesses. The announcement of the CT regime was imminent considering the OECD development of introducing a global minimum tax of 15% and UAE’s aim to diversify itself from an economy dependent on oil and tourism. Economic Substance Regulations and the introduction of country-by-country reporting with effect from 2019 were the first steps towards the introduction of CT.

The UAE proposed the introduction of CT in January 2022 with the release of FAQs giving a high-level overview of the CT regime to be effective from financial years starting on or after 1 June 2023.

This was followed by the issuance of a Public Consultation Document (“PCD”) in April 2022, which laid down the broad contours of the proposed UAE CT Law. Following the international best practices, the regulator invited comments from the stakeholders on the PCD.

The English translation of the CT Law was released on 9 December 2022.

A tax rate of 9% (the lowest amongst the GCC countries with CT) makes the UAE one of the most competitive countries to have introduced a CT law in the world.

### Overview of the CT Law

The CT Law is drafted based on internationally accepted taxation principles and aims to keep the compliance and complexities at a minimal level. The aim is to keep small taxpayers out of the CT net and adequate provisions regarding the basic exemption limit of AED 375,000 and relief to small businesses with revenue below a specified threshold have been incorporated to ensure the same.

The UAE CT Law is simple and comprehensive. Simplified compliances (including 0% withholding tax, no advance tax, an option for tax grouping) and the clarifications on various concepts through more than 150 FAQs make it easy to understand. An appropriate blend of various international tax concepts, such as permanent establishment, transfer pricing (“TP”), tax groups, interest

capping rules which are prone to varied interpretations provide room for stakeholders and tax practitioners for different interpretations.

To ensure that the UAE continues to be an attractive business destination, a host of tax measures have been provided. The UAE has many free zones that provide tax holidays for periods of 15 to 50 years. Free zone entities have been provided with a beneficial 0% CT rate on qualifying income. Exemption to capital gains on sales of shares meeting the participation exemption conditions ensures that the UAE continues to be an attractive holding company jurisdiction. Individuals earning personal income are out of the CT net. While there are benefits, anti-abuse provisions are inserted to make sure that benefits are given in genuine cases backed by economic substance. Taxpayers will have to consider their existing business operations and proposed arrangements and restructuring from an anti-abuse perspective.

As expected, transfer pricing provisions are in line with the OECD TP guidelines. Certain transfer pricing provisions are forward looking and taxpayer friendly, and provide flexibility to allow taxpayers to adopt methods other than the five widely accepted and internationally recognised methods for determining arm’s length price.

### Way forward

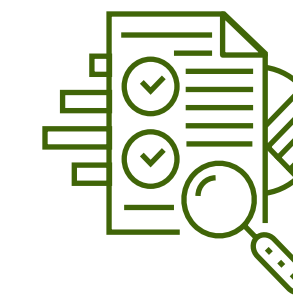
Businesses will have to evaluate their readiness for CT implementation. Businesses will have to ensure that internationally accepted methods of accounting are followed for the preparation of financial statements. Reconciliation of data reported in the financial statements vis-à-vis CT returns and VAT returns will have to be maintained. ERP systems might need an upgrade to ensure readiness for the collation and reporting of data. Transactions between related parties should be in line with the group’s transfer pricing policy, backed by appropriate documentation and at arm’s length.

Large multinational groups covered by Pillar Two rules would be subjected to tax at a likely rate of 15%. Multinational Corporations (MNCs) should evaluate the

impact of Pillar Two rules on their overall CT liability and options for group restructuring.

From a compliance standpoint, businesses will have nine months from the end of a tax period (i.e. financial year) to submit their tax declaration along with the transfer pricing disclosure form. Businesses following the calendar year will need to submit a tax return by September 2025.

It would also be interesting to see the FTA’s approach for conducting tax audits of the declarations filed. The FTA would have five years to conduct a tax audit and depending on when the notice is issued the declaration filed could remain open for a total period of nine years.



In conclusion, given its continuing ability to attract global businesses, investments and skilled workers and the dynamic changes on its tax and regulatory front, the UAE is one of the brightest spots in the world economy.

Businesses and tax practitioners in the UAE have plenty on hand to achieve an effective implementation.



# The FTA: going from strength to strength

As discussed at the beginning of this publication, the FTA was only established in 2016 and is a very young organisation by international standards. Nevertheless, a few years after since its establishment, the FTA is administering two full-fledged federal taxes, with a third tax on the way.

The core administration activities of the FTA require significant and well-qualified human resources; these resourcing requirements naturally grow over time with increases in the number of taxpayers. Due to the disruption to the natural order of things caused by the introduction of the corporate tax, these resourcing requirements will grow exponentially over the next few years.

It is expected that the FTA will continue to invest heavily in hiring new people to be able to deal with the additional work created by the corporate tax. Since new employees would require knowledge of corporate taxes, which have historically been absent from the UAE, a significant portion of new employees may come from the overseas market, rather than from the UAE's local market.

In parallel with its recruiting activities, the FTA is expected to continue focusing its resources on technology. EmaraTax has been recently introduced and further changes and updates are expected to the FTA's internal- and external-facing systems. E-invoicing is expected to be announced in 2023 – it will give the FTA more control over the information that it can access, while generating more challenges and opportunities to taxpayers.

Over the last five years, the FTA has showed that it is a modern and sophisticated organisation that can successfully deal with the responsibilities that were given to it. Going forward, the FTA will need to show that it can successfully grow and evolve with new challenges without compromising what has made it successful in the first place.

“  
*The FTA continuously demonstrates efforts to keep pace with technology.*  
”  
**Akshay Nanda, Jumbo Electronics**







## More open interaction between the FTA and public

Open and transparent interactions between tax authorities and taxpayers are important on a number of levels.

From the tax authority's perspective, regular interactions with taxpayers and taxpayer groups will allow it to better gauge the current business environment and to predict and prepare for any incoming market trends and developments. Such frequent and open interactions will help the tax authority to be proactive, rather than reactive, with respect of tax policies and ensure that the legislation and decisions are based on a comprehensive and pragmatic understanding of the real-world environment and are fit for purpose.

From the taxpayer perspective, the ability to have an open and informal discussion with the tax authority would give it a better understanding of the authority's views on things and increase the chance that taxpayers will buy into decisions and policies of the authority.

While, to date, there has been limited scope for taxpayers to interact or share their views with the FTA, there are indications that this may change in the future:

- The introduction of the corporate tax has been accompanied by the gathering of the public's opinions through consultations.

It would be useful to see this trend continue in respect of the more significant tax decisions, including those related to VAT.

- Where a taxpayer wishes to understand the FTA's view, the existing process is fairly formalised and inflexible. The main avenues for communication available to taxpayers typically require them either to enter into a clarification request process or arise during a tax audit by the FTA. Where a taxpayer disagrees with a decision of the FTA or wishes to discuss a decision further, there is often no informal mechanism for doing so.

The ability to informally discuss a viewpoint with the FTA would go a long way in improving compliance without the

fear that it may result in an official decision or immediate negative outcome to the business.

“ *Creation of a dedicated helpdesk to help collate and manage the issues faced by an industry.* ”

**Jignesh Sanghvi, DMCC**

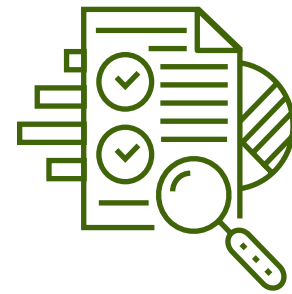


The past five years have shown that the FTA is willing to make changes to processes and practices in ways that benefit the overall UAE tax environment and make it easier for taxpayers to comply with their tax obligations. As the UAE tax environment continues to evolve and become more complex, improving the quality of taxpayer interaction should be the next goal for the FTA.



# CONCLUSION

The past five years have been a rollercoaster ride for VAT in the UAE. From the moment of its introduction in the barren no-tax landscape, there has been no single aspect of private or business life in the UAE that has not been impacted. The FTA was established from the ground up to become a modern and sophisticated tax authority; businesses had to change the ways they conducted their activities by implementing new policies, processes and technologies; and a whole new industry – that of tax experts/consultants – was created out of nowhere.



While the FTA and taxpayers spent the first two years following the introduction of VAT coming to terms with the new tax, the last few years have seen further evolution of the tax and associated procedures. The clear common theme of these changes is to encourage voluntary self-compliance in order to reduce the FTA's engagement in basic compliance activities.

Although the introduction of the corporate income tax may give impression that VAT is destined to becoming less relevant in the overall UAE tax landscape, it would be dangerous for businesses to take away their focus from the VAT now. VAT will continue being the main revenue-generating tax for the UAE for the next few years and the recent changes to the rules concerning the powers of the FTA to conduct audits indicate that the tax is still at the centre of the FTA's attention. The likely implementation of e-invoicing (which will give the FTA more immediate information about businesses and their activities) and the increase in the VAT rate will further reinforce the need for businesses to ensure that their VAT affairs are in order.

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**Happy fifth birthday and many happy (VAT) returns!**

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