VAT brief | Automotive

May 2018 | Kingdom of Bahrain

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Saudi Arabia and the UAE implemented VAT on 1 January 2018, with the other GCC countries expected to follow in the next 12 months. Business leaders should now be more aware than ever that we are entering into a new tax era. Key decision makers in the UAE and Saudi Arabia need to ensure their processes and systems are - and remain - VAT-compliant, while their counterparts in the other GCC states need to start preparing now for the implementation of VAT.

What is VAT?

- VAT is a tax on consumption, not income or profits.
- The GCC countries have agreed a standard VAT rate of five percent.
- The supply of goods and services can be exempt, zero-rated or standard-rated (five percent), or out of scope.
- Registered businesses account for VAT on the price charged for the goods or services they supply and pay it to the tax authority on a regular basis.
- Registered businesses should (where the supplies they make are either standard- or zero-rated or out of scope with recovery) be able to recover the VAT they have incurred in the course of making those supplies.
- Registered businesses that make supplies that are exempt from VAT cannot recover the VAT they have incurred in the course of making those supplies.
- Registered businesses may not be able to recover the VAT they have incurred on certain purchases that are deemed to have a private element.
- Registered businesses that make supplies that are predominantly zero-rated are likely to be in a VAT refund position.
- Businesses that make both exempt and taxable supplies can only recover a proportion of their input VAT.

How will VAT affect the automotive sector?

- Supplies made by auto dealers – such as the sale of cars, parts and repair services – are standard-rated.
- However, auto dealers also make other supplies. Certain financial services in relation to auto loans and credit are likely to be exempt from VAT.
- When providing finance, the appropriate VAT treatment will need to be considered:
  - Is there an operating or finance lease?
  - Is the dealer acting as an intermediary or directly providing financing?
- Auto dealers leasing cars generally need to account for VAT on the principal element of lease payments. However, they need to consider the impact of the imposition of VAT on customers and when to account for VAT, as specific time of supply rules apply.
- Supplies made under contracts that span the VAT implementation date (such as in lease-to-own or instalment payments) may be subject to special rules which determine when VAT is applied.
- Special rules may apply for second-hand cars, where VAT is only charged on the profit margin. The UAE - unlike Saudi Arabia - has a second-hand margin scheme.
- The VAT treatment of demonstrator, employee and courtesy cars must be carefully considered as any element of private use will rule out the recovery of VAT incurred when bought.

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- Dealers may sell more cars and parts in the run-up to the introduction of VAT, requiring them to increase stock levels in the months immediately beforehand.
- Cars sold prior to the introduction of VAT but delivered to customers after VAT may still attract VAT.

What should the automotive sector be doing now?

- Consider pricing and its impact on demand.
- Evaluate stock levels to deal with fluctuations before and after VAT implementation.
- Examine sales and accounting processes to ensure the correct VAT treatment is being - or will be - applied.
- Evaluate the impact of time of supply rules on deposits, warranties and service contracts.
- Review leasing contracts to confirm whether VAT can be charged following implementation - or whether transitional provisions apply.
- Examine any long-term contracts spanning the date of implementation and decide whether VAT can - or should - be charged to customers.

Important note

These briefs are based on a translation of the GCC VAT Treaty, UAE and Saudi Arabia's VAT legislation, the relevant regulations and general VAT principles and are provided for information purposes only.

Saudi Arabia and the UAE implemented VAT on 1 January 2018 and the other GCC countries continue – as of the date of release of this brief – to work towards implementation in 2019.

This brief is not a substitute for professional advice. You should seek appropriate professional advice from a tax advisor before making any decision relating to your particular circumstances.