VAT brief | Retail

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We have entered a new tax era. Saudi Arabia and the UAE implemented VAT on 1 January 2018. Bahrain implemented - for businesses with taxable turnovers above BD5m - on 1 January 2019 - with other businesses going live on 1 July 2019 or 1 January 2020. Other GCC countries are expected to follow. Key decision makers in the UAE, Saudi Arabia and Bahrain need to ensure their processes and systems are - and remain - VAT-compliant, while their peers in other GCC states need to start preparing now for VAT's implementation.

What is VAT?

- The GCC countries have agreed a standard VAT rate of five percent.
- Supplies of goods and services can be exempt, zero-rated or standard-rated (five percent), or out of scope.
- The mandatory registration threshold (MRT) is the equivalent of US$100,000. The voluntary registration threshold is the equivalent of US$50,000. Bahrain has staggered VAT's introduction.
- Registered businesses account for VAT - a consumption tax - on the price charged for the goods or services they supply and regularly pay the VAT to the tax authority.
- Where registered businesses make supplies that are standard- or zero-rated or out of scope with recovery, they should be able to recover the VAT they have incurred in making those supplies.
- Registered businesses making supplies that are exempt from VAT cannot recover the VAT they have incurred in the course of making those supplies.
- Registered businesses may be unable to recover VAT incurred on purchases that are deemed to have a private element.
- Registered businesses making 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 does VAT affect businesses in the retail sector?

- Supplies of most goods and services are standard-rated (5%). Generally, prices are required to be displayed inclusive of VAT to ensure that consumers are not left to work out for themselves the final price they have to pay.
- Saudi Arabia, the UAE and Bahrain have zero-rated certain medicines and medical equipment, as in many other VAT jurisdictions.
- While the GCC treaty allows each state to zero-rate basic food items, they are standard-rated (5%) in both the UAE and Saudi Arabia.
- Bahrain has zero-rated the supply of certain food items (a prescribed list).
- Other GCC states may choose to provide direct subsidies to citizens in lower socio-economic groups.
- The UAE and Bahrain have implemented tourist refund schemes, with Saudi Arabia soon to follow. GCC residents are not eligible for VAT refunds.
- The GCC VAT rules require businesses to self-account for VAT when they provide goods or services for free. However, there are exceptions if no input VAT is claimed on the initial acquisition or if the total value of free goods or services falls below a minimum threshold. This is likely to impact promotional schemes such as loyalty and reward schemes.
- Special rules apply to the cross-border supplies of goods and services between businesses within the GCC. In essence, a reverse charge applies.

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- For sales to other GCC countries, retailers may be required to register and account for VAT in the other jurisdiction. For example, goods sold by a retailer in Saudi Arabia to a non-registered customer in Bahrain before 1 January 2019 were zero-rated for Saudi VAT (since Bahrain had not implemented VAT). However, once the electronic services system (ESS - a system designed to track the movement of goods within the GCC) is in place, the Saudi retailer must charge Saudi VAT - or register in Bahrain and account for Bahraini VAT if the Bahraini VAT registration threshold is exceeded.
- Exports from the GCC are zero-rated, provided evidence of removal is obtained.
- VAT is generally accounted for at the earlier of the goods being supplied, the invoice date and the consideration being received. Since retailers tend to receive payment up-front, they are generally in a cash-flow positive position.
- Retailers who provide finance or instalment plans should consider the impact of VAT on their cash-flow as they may need to account for VAT before they receive payment. Interest charged on financing arrangements is an exempt supply, impacting VAT recovery on costs incurred in making those supplies.
- Retailers should evaluate pricing strategies, either passing on VAT by increasing prices by the VAT amount, maintaining prices (absorbing the VAT impact), or something in between. Any pricing decision has to balance profit margins, sales volumes and market share.
- Saudi retailers may issue simplified tax invoices for supplies less than SR1,000 (US$265). In the UAE, the limit is AED10,000 (US$2,650). Bahrain allows simplified invoices for supplies not exceeding BHD 500 (US$1,300) or to non-VAT registered customers.
- The VAT treatment of business promotions offered by retailers, support schemes offered by distributor or manufacturer and the redemption of vouchers and loyalty points is complex and must be carefully considered.

What should businesses in the retail sector be doing now?

- Examine all goods and services and assign the correct VAT treatment.
- Look at marketing strategies to minimise impact on profits during the lead-up to and after VAT is in place.
- In the UAE, Bahrain and Saudi Arabia, purchases of high-value goods accelerated in the lead up to VAT implementation. Retailers in other GCC countries should consider stock levels in the months leading up to their implementation of VAT. A corresponding drop in sales of non-essential items following implementation is also likely.
- Consider the impact of VAT on pricing – should the cost of VAT be passed on to consumers?
- Review business promotions and agreements with customers and suppliers, particularly in relation to volume discounts, incentive payments, loyalty schemes and other adjustments.
- Examine any long-term contracts spanning the date of implementation and decide whether VAT can - or should - be charged to customers.