UAE VAT Update

President His Highness Shaikh Khalifa Bin Zayed Al Nahyan has issued the long-awaited Federal Decree-Law No. 8 of 2017 for Value-Added Tax (the Law), providing some much-needed detail around how the new value added tax (VAT), to be introduced in the UAE on 1 January 2018, will work.

While many provisions of the Law are consistent with what business and advisors had anticipated, there are some differences, and some of the legislative drafting appears to create ambiguities, gaps and potential loopholes. The Law confirms our view that the introduction of VAT in the UAE will not be straightforward.

There had been some speculation that the UAE might introduce transitional rules for contracts pre-dating the introduction of VAT (or the date of the announcement of its introduction) that did not provide for the payment of VAT in addition.

Article 80(2) of the Law appears to provide that where an existing contract does not contain an "exclusive of VAT" clause, the consideration will be treated as inclusive of VAT; but Article 80(3) states that "special provisions" may be provided by Executive Regulation, which may have the effect of overriding or supplementing this rule in certain cases. If the Executive Regulation, which has not yet been published, does make "special provisions" in relation to existing contracts, they are unlikely to be straightforward.

If a contract ultimately ends up being governed by Article 80(2), the supplier under a long-term existing contract that does not provide an "exclusive of VAT" clause is likely to end up bearing the VAT cost, reducing the amount of consideration retained by nearly 5%.

Whatever the interaction between the Law and the Executive Regulation, areas of uncertainty will remain. What will be the case if the contract provides that each party will bear the cost of its own taxes, without explicitly referring to VAT? What if the contract provides for a gross-up and indemnity in respect of taxes, again without referring to VAT?

With only four months before the introduction of VAT in the UAE, businesses need to review their contracts that will or might extend into 2018, and consider how, as a matter of legal construction, those contracts provide for the allocation of the VAT cost between the parties.

Contracts currently being negotiated should be reviewed by a VAT expert to ensure that the VAT cost falls on the appropriate party, and to consider what steps can be taken to improve the overall tax efficiency of the transaction.

Please feel free to contact either of our co-heads of GCC VAT – Lindsay Fainé in Abu Dhabi and Jeremy Cape in London – or your usual firm contact if you would like us to review your contractual wording, or help you devise and implement your VAT strategy.

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