



# IMPACT OF VAT ON THE RETAIL INDUSTRY

## Introduction

The Member States of the Gulf Cooperation Council (GCC) have signed a Unified Agreement on VAT containing the majority of the regulations for the operation of VAT. Each GCC Member State will complete the rules with their own VAT laws. As Bahrain has just approved the Decree Law on VAT, the content in this newsletter is based on guidelines given under the Decree Law, the Unified Agreement and/or common practices followed by other countries.

## VAT Simplified

- VAT is a consumption-based tax levied on every value addition made at each stage of the product cycle.
- The standard rate of VAT as per the Unified Agreement and Bahrain VAT Law is 5%.
- Apart from the standard-rated goods there are exceptions for zero-rated and exempt goods and services. Each State will issue the list of such zero-rated and exempt supplies in its VAT legislation.
- The role of businesses is to facilitate the collection and payment of VAT to the government.
- $\text{Net VAT payable} = \text{Output VAT (due to be paid on sales at a rate of 5\%)} - \text{Input VAT (paid on purchases)}$
- In cases where the outcome of this formula is negative, then such net VAT is refundable from the government or can be carried forward to adjust in the next VAT return.

## The Retail Industry in Bahrain

### Industry Overview<sup>1</sup>

Bahrain's economy is one of the smaller markets in the GCC, with a real GDP of BD 11.9bn (\$31.6bn) in 2016, according to the IMF, which grew by an estimated 3.5% in 2017. Retail and wholesale trade contributed 4.2% to GDP in the third quarter of 2017 and contributed BD 152.5 (\$404m) at current prices, up from BD 132.6 (\$351.6m) in the third quarter of 2016. With almost a quarter of visitors reporting shopping as their main purpose of visit to the Kingdom in the BTEA's 2017

survey<sup>2</sup>, the retail industry is one of the key pillars supporting the country's tourism sector. With significant improvements to its transport infrastructure, as well as investments in new hotels, restaurants and retail offerings set to come on stream in the next few years, Bahrain is rapidly improving the supply of tourist attractions. At the same time, the country is also making an effort to advertise itself in new markets to stimulate increase tourist demand.

### Specific Considerations for the Retail Industry

VAT is a consumption tax borne by the final consumer, thus retailers play a key role in the VAT collection cycle. Tax authorities may choose to pay closer attention to retailers since they are the biggest tax collectors for the government.

**Article 31-** This article of the GCC VAT agreement allows Member States to tax food items mentioned in the unified list of goods approved by the Financial and Economic Cooperation Committee at the zero-rate. KSA and UAE have chosen to tax all food items at the standard rate of 5%. Bahrain, however, has chosen to apply the zero-rate to basic food items and to tax all other food items at the standard rate. The complete list of basic food items will be available in the executive regulations due to be published.

**Display Prices-** Retailers must amend all display prices to be inclusive of VAT. This includes price tags, shelf tags, display boards, menus, etc. VAT registered retailers who are found to display prices exclusive of VAT will be considered in violation of the law and may face hefty fines and penalties.

**Promotions and Discounts-** VAT laws allow retailers to provide discounts and promotions on their products including loyalty rewards, special days, and vouchers. However, these must be carefully monitored as they may modify input and output VAT computations.

**Free Samples and Gifts-** VAT laws are strict on the treatment of free samples and gifts.

Although businesses are allowed to provide free samples and gifts to customers, the ability to claim input VAT on these is restricted as they are not considered to be economic activities. Each Member State will set its own criteria and threshold on how much input VAT can be claimed, if any. Any amount in excess of the threshold (or which does not meet the set criteria) will have to be repaid to the government by the business. This is done by entering an adjusting entry in the next VAT return.

**Archiving and Retention of Records-** All Data must be archived in a way that allows the business to access past records in a hassle-free manner. This is especially relevant in case of a tax audit which is performed by the tax authorities to verify the revenue filed in the VAT return of the business. Tax invoices, records and accounting documents shall be retained for a period of five years from the end of the tax year as per UAE laws, and six years as per KSA laws. Further guidance on the retention period for Bahrain shall be provided in the executive regulations.

**Cashiers-** The cashiers are the key to determining the VAT liability of a retailer. Data from all cashiers must be collated and entered in the respective sales and VAT accounting ledgers in an accurate and timely manner. This data may be used in a tax audit to verify the revenue filed in the VAT return of the business.

**Other Considerations-** Sales returns, inventory damage and stolen goods are examples of areas which may add complexity to the usual input and output VAT process. Justification for such events must be kept so as to avoid future VAT reassessment.

## General Considerations

**Human resources-** Where it is common practise to provide benefits such as gifts, memberships, and other perks to employees, the implication of VAT on such benefits will be a matter of concern to employers under VAT laws.

**Contracts-** Businesses should consider revisiting their existing contracts to update or include VAT related clauses.

## Why You Need To Start Preparing for VAT Today

A full-fledged, effective, robust and comprehensive VAT implementation takes ample time from planning to execution. Early preparation is recommended, as a short time span to implement VAT may result in an enormous burden on the company and its resources.

## Our Services

### VAT Implementation

RSM's VAT advisory services focus on understanding our client's activities and needs. This culture leads to developing a more strategic approach to VAT and creating opportunities to measure and improve efficiency our client's processes. Our methodology protects our clients from overstated tax liabilities, interest charges, and heavy penalties; and helps them, on a long term view, to control VAT liabilities. We advise our clients to proceed with a VAT assessment at the earliest to avoid a last minute panic.

### Post Implementation Support

We provide our clients with on-demand technical support in the frame of a pre-established budgetary framework.

### Customised Training

We design customised VAT training sessions focused on the client's business activities and on the day to day concerns of the internal VAT stakeholders.

### Complete VAT Audit

We propose a VAT audit to anticipate tax audit drawbacks and to evaluate the accuracy of the VAT implementation done by the business itself.

### VAT Record Keeping

The VAT record keeping process will become key for the VAT safety of businesses.

## Contact Us RSM Bahrain

3rd Floor, Falcon Tower, PO Box 11816, Diplomatic Area,  
Bahrain  
T +973 17537787  
F +973 17537757  
E [info@rsm.bh](mailto:info@rsm.bh)  
[www.rsm.bh](http://www.rsm.bh)



<sup>1</sup> Oxford Business Group Report 2018

<sup>2</sup> Bahrain Tourism and Exhibition Authority

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