THE POWER OF BEING UNDERSTOOD

AUDIT | TAX | CONSULTING

VAT AND RIGHT OF DEDUCTION

RSM

VAT INSIGHTS

VAT and right of deduction

VAT must not be a cost for businesses carrying out taxable activities. To reach this goal of neutrality the right to deduct the input VAT is granted to tax Persons. Several steps must be followed.

The first question is to know for each purchase if the cost is among transactions not entitled to deduction. Even though there are similar, each country has its own list.

In both KSA and UAE are excluded all kind of entertainment or hospitality, goods and services used for a private or non-business purpose, costs linked to cars available for personal use and cost linked to goods or services were purchased to be used by employees for no charge if it is not a legal or contractual obligation.

This consequence must be mitigated in UAE because the VAT borne on provision of accommodation, food and drinks, which are provided in a normal course of a meeting, remains deductible.

The second question is to identify for each purchase if the cost is allocable to a taxable or zero-rated operations. The best way to do this is to follow the branches of the decision tree below.

However, KSA and UAE give a VAT deduction right to Public Bodies or Charities for exempt supplies.

On top of that, unlike KSA, UAE gives a higher deduction right to public entities.

For instance Government entities are allowed to deduct input VAT on a broader range for entertainment services and some others Government entities or Charities are allowed to deduct almost all the input VAT they paid.

Supplies provided without compensation are not actual supplies, and are therefore located out of the scope of VAT and therefore do not give rise to input VAT deduction.

Article 15 of the KSA VAT regulations puts the following limits: samples/gifts would not attract VAT, if the value is below 200 riyals per person per year, or below 50,000 total value of all gifts/samples per year.

Similarly, article 5 of the UAE VAT regulations put the following limits: 500 AED per person per year, and the total output VAT that would have been levied on the value of the gifts/samples does not exceed 2,000 AED per year. That is to say that there is a value exclusive of tax of 40,000 AED.

The third question is to know how much to deduct for mixed supply on the right of the tree decision. The calculation of the deduction ratio is quite different in KSA and UAE.

KSA ratio

$$\text{Deduction Ratio} = \frac{\text{Total Taxable Supplies}}{\text{Total Taxable and Exempt Supplies}}$$

UAE ratio

$$\text{Deduction Ratio} = \frac{\text{Total Input VAT (related to taxable supplies)}}{\text{Total Input VAT (related to taxable \& exempt supplies)}}$$

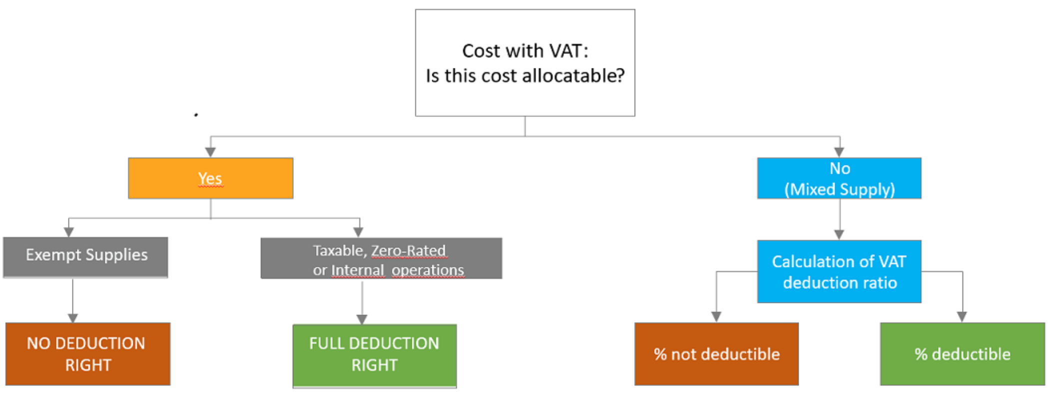
In both countries, if the standard ratio leads to a non-balanced input VAT deduction a specific calculation of the ratio can be proposed to the Tax Administration for approval.

The fourth question is to know when to deduct the input VAT. The right to make a deduction arises when a deductible tax is due by the supplier to the government. For exercising the right of deduction, the tax Person must hold the tax invoice or the custom import document. The input VAT on reverse charge mechanism is deductible only if the output VAT has been declared.

On top of that, some adjustments would have to be made in some circumstances.

In order to avoid bearing illegitimate costs the businesses have to make an accurate VAT implementation in the IT systems and in their processes.

VAT DECISION TREE



Contact
Jean-Paul Ouaksel
Partner - Tax Services
RSM KUWAIT
E: jeanpaul.ouaksel@rsm.com.kw
Arraya Tower 2, Floors 41 & 42 , Abdulaziz Hamad Alsaqar St.,
Sharq, P.O. Box 2115, Safat 13022, State Of Kuwait
T: +965 22961000 | F: +965 22412761 | M: +965 66334467