Chapter 5 – VAT technology

Technology considerations – using technology to automate VAT compliance
VAT is characteristically embedded throughout a business’s entire supply chain. The strength of a business’ VAT compliance function is highly dependent on the processes in place, the capacity of the technology system, and the knowledge of VAT within the finance and tax departments. The right approach to VAT will ensure control over compliance while reducing error, risk and cost.

With the formal announcement of VAT in the GCC, businesses need to focus on the practical implications of updating their systems to manage this tax. Deloitte’s VAT readiness in the GCC survey shows that 61% of organizations feel that they need more than six months to prepare for the introduction of VAT. As such, there is an immediate need for executive teams to work closely with their technology partners to agree and implement the right VAT technology architecture.

Further, nearly half of the surveyed organizations indicated that the top two stumbling blocks to a successful introduction are technology and a lack of knowledge regarding the VAT rules. This highlights an issue between the need to begin preparing now and a lack of certainty as to what businesses are preparing for.

In this chapter, we aim to reduce the uncertainty and highlight the key areas that organizations should focus on as they embark on their journey to VAT readiness.

**Revenue**

Businesses above a minimum taxable supply threshold (this is normally sales income – but for VAT purposes may include other activities) must register for VAT. Thus, before making any decisions in regards to change, it is crucial to check the applicability of VAT to your business in a particular jurisdiction.

**Nature of business**

The complexity of a specific VAT solution will depend on the nature of the business. The kind of purchases and sales a business makes could fall into three categories for VAT purposes:

1. Standard rate (predicted to be 5% in the GCC) – the majority of goods and services are expected to fall within this category for most retailers and law firms.
2. Zero rate (0% but still a taxable supply for VAT purposes) – this will apply to the export of goods, for example.
3. Exempt from VAT (i.e. no VAT charged but no VAT recovery on purchases) – this is typically applied to many services offered by banks and other financial institutions.

Furthermore, the location of the supply plays an important part in determining within which jurisdiction the VAT needs to be accounted for and by whom. Under normal rules the place of supply in a business-to-business supply of services transaction is where the customer is located.

For example, when a consultant in Dubai provides processional advice to a business customer in Oman, the place of supply is likely to be treated as Oman and as such the Dubai-based consultant would not...
charge VAT. Instead, the business in Oman would self-account for Oman VAT under the reverse-charge mechanism.

**Extent of integration of current business processes**

GCC organizations, especially the small- and medium-sized businesses, have often managed many of their wider financial processes such as employee expenses, inter-company invoices and petty cash transactions outside their core transactional finance system. The introduction of VAT is very likely to encompass these types of transaction and so you may have more than just your main accounting system to think about.

**Existing IT architecture**

The complexity of your existing IT architecture is going to have a large influence on how straightforward it is to update for the introduction of VAT. Below are typical scenarios:

- **Simple architecture** – One mainstream ERP (e.g. a recent implementation of Oracle/SAP with existing VAT capability from another jurisdiction) with minimum customization being used for all the processes impacted by VAT introduction. Updates will be focused on enabling or customizing the existing tax determination and reporting functionality.

- **Medium complexity architecture** – Two or three systems are being used for all the processes impacted by VAT introduction, or the VAT capability (calculation and reporting) of the existing systems is limited. More system configuration time and effort is required where there is more than one system in use. Care must also be taken to ensure that the VAT configuration of each existing system is consistent.

- **High Complexity architecture** – Multiple systems are being used, including older linked finance systems, and the systems have multiple interfaces with the financial management and accounting systems. Additionally, the VAT capability (calculation and reporting) is non-standard across the systems and may be limited. Older finance systems may not offer the automated VAT determination functionality required and therefore may need to be updated as part of a systems upgrade project. The use of many ERP systems multiplies the configuration and effort required when establishing the VAT system logic. Furthermore the work required around process flows and the points of data integration will be similarly increased.

**Ongoing or planned IT projects**

Any ongoing or planned IT projects that could potentially impact the VAT processes should be re-assessed in the context of the timing of the introduction of VAT, as implementation plans may need to be adjusted. There are different ways that VAT could be implemented in view of existing and planned projects with the most common scenarios being:

- **Pause and implement VAT** – The IT project interferes with the VAT implementation (e.g. updating a new billing system). In this case, a business may choose to pause the effort and resume only after VAT is implemented.

- **Complete and implement VAT** – The project is near completion and so it may be most efficient to complete the project and then subsequently implement the changes required to enable or build VAT capabilities.

- **Re-plan an ‘in flight’ implementation of VAT** – If the project is in a nascent phase, then the option of bringing VAT functionality into the project scope should be looked at by the management.

**IT knowledge**

The extent of knowledge of existing IT systems within the organization can make a big difference when implementing the functionality critical for VAT. Organizations which have highly customized finance solutions are often very dependent on the ‘in-house’ knowledge or long-term service partner relationships. Therefore, it is important to include the right stakeholders when planning to implement major VAT changes that will impact many business processes at the same time.

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**Automation of VAT processes**

It is important to determine the extent of VAT process automation that an organization wants to achieve immediately (at the beginning of the VAT mandate) and the level of automation desired over the long term. As an example, an organization may be focused on automating the majority of processes as part of an initial implementation but may defer automation of more complex transactions that...
The complexity of an organization may mean that some configuration of the finance system is required, but it is important to recognize that customization will increase the maintenance burden compared to a more standard approach.

**Options for technology enablement**

**Invest in existing systems**

The majority of current ERP systems offer automated VAT determination and reporting functionality and we expect that using this native functionality will be the most common approach for companies in the GCC to enable their finance systems to deal effectively with the new VAT system.

When enabling VAT functionality in existing systems, it is preferable to use the standard, ‘out of the box’ functionality where possible. The complexity of an organization may mean that some configuration of the finance system is required, but it is important to recognize that customization will increase the maintenance burden compared to a more standard approach.

Older finance systems may offer less inbuilt functionality for automated indirect tax determination and this should be factored into preparations for change.

**Take advantage of planned investment or upgrades in finance systems**

Where finance system projects are underway in the business, there is an opportunity to include tax in the work plan such that VAT is included alongside the other activities of the business. A project to implement a new financial system or additional system functionality can take advantage of the economies of scale provided when similar activities are taking place in other areas of the business.

**Balance automated and manual effort**

Successful VAT implementations will appropriately balance the automated and manual effort in end-to-end processes. When automating a process, businesses should weigh up the cost of automation against the perceived benefit. In many cases where there are one-off or complex transactions, manual processes may be more beneficial and cost effective than attempting to automate.

**Make use of tax specific third party solutions**

Third-party providers are preparing to offer ‘bolt-on’ solutions that integrate with native finance systems to support tax determination and calculation. Solutions are also available which assist with tax compliance and reporting obligations. These solutions can provide automation capability beyond that available within typical finance systems.

Third-party solutions offer an interesting alternative to investing in existing systems but careful consideration is recommended to determine whether a ‘bolt-on’ solution is suitable and necessary before implementing.

**Consider leveraging adviser relationships**

Outsource providers typically have standard methodologies and technologies for consolidation, processing and reporting of VAT information. Businesses can choose to leverage this approach as an alternative to investing internally in a compliance and reporting solution.
Businesses will still need to provide the source transactional data to an outsource provider and ensure that sensible tax decisions have been made, so it is still likely that GCC businesses will need to invest in existing systems.

Don’t underestimate the overall VAT reporting process, i.e. the time taken to consolidate, test and get comfortable with the figures extracted from finance systems that will be submitted to tax authorities.

Managing an effective VAT implementation

An effective implementation for VAT in the GCC relies on a number of factors. The relative importance of these will vary depending on how far the implementation has progressed but, in our experience, all consistently feature in a successful implementation.

Before implementation

− Ensure that you fully understand the requirements and these have been communicated to all relevant stakeholders.
− Understand whether the finance system will be customized in any way.
− Business should have a clear view on the processes needed to support the systems implementation.

During implementation

− It is important to ensure that the right skills and knowledge are available at all stages of implementation.
− Ownership of the various stages of an implementation should be agreed upfront (e.g. design, build, and testing).
− Communicate clearly and regularly with the process owners and any other stakeholders that will be impacted at different stages of the implementation.

After implementation

− Training and support has to be provided so this should be planned for in advance.
− Business should strive for continuous improvement of the system, whether through improved automation processes or better supporting processes.
− The ownership for system and data maintenance should be communicated and managed within tax, finance and IT departments.

It is important to ensure that the right skills and knowledge are available at all stages of implementation.
Businesses in the GCC should think about what success looks like for them before they proceed with any system implementation for VAT. There is likely to be a subtle distinction between the view of success immediately after a system goes live on day one of VAT being set up and the view of success after the new VAT processes have been embedded within the business and you’re looking for further efficiencies; both of these should be given weight when decisions regarding the implementation are taken. The development of strong processes and controls alongside a new finance system will help businesses in the region, ensuring both views of success are achieved.

Hallmarks of an effective implementation

- The right skills to consolidate and test data, submit returns, adapt systems and handle relationships with wider business, professional advisers and the local tax authorities.
- Strong technical and systems knowledge needs to be embedded into the business. Ongoing training is essential to keep teams’ knowledge current and this typically falls to the ‘tax team.’
- Clearly communicated process underpins the success of finance systems, if the systems are not utilized correctly, their full potential will not be realized.
- Technology solutions can provide greater efficiency and accuracy where automation of tax decision is enabled. Tax reporting and compliance solutions can provide further assistance.

Lessons learned from our experience

- Always consider the ‘end-to-end’ process and solution
- Don’t underestimate the timescales and skillsets required
- Balance of automation and end user flexibility
- Communication, training and change management are key

Conclusion

Businesses in the GCC should think about what success looks like for them before they proceed with any system implementation for VAT.