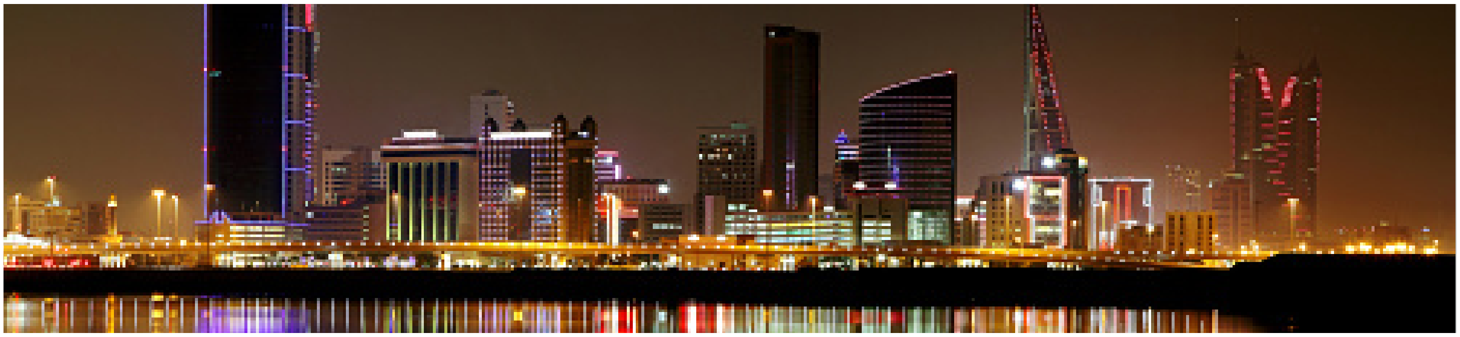
Deloitte.

Value Added Tax
March 2017



The introduction of VAT in Bahrain

1. VAT Implementation

The representatives of the Member States of the Gulf Cooperation Council (GCC) confirmed the introduction of a formal VAT system across all six Member States through the signing of a VAT Framework Treaty. The Treaty acts as the basis for the domestic VAT legislation in each Member State by stipulating certain principles, which must be followed by all members, while allowing the countries to opt for different VAT treatments in relation to some supplies.

3. Timing

Following the signing of the VAT Framework Treaty, all GCC members show signs of aiming to implement local VAT systems from 1 January 2018 or at the least the first quarter of 2018. We expect that the first draft local laws may be released in the first quarter of 2017.

5. Zero-rated or exempt?

VAT Framework Treaty provides that VAT on the supply of goods or services within the scope of VAT will generally be charged at a standard rate of 5%, unless the goods or services are exempt or zero-rated. The Member States have been granted the flexibility to choose whether the supply of specific goods or services are considered treated as zero-rate or exempt. While being required to either exempt or zero-rate other specific supplies.
The distinction between zero-rating and exemption is an important one; in both cases **VAT must not be accounted on the supply**, however, a supplier making exempt supplies is generally not allowed to recover input VAT in relation to such supplies. **Recovery of input VAT incurred in relation to zero-rated supplies is generally allowable.**

Must zero-rate:

- Medicine and medical equipment
- Cross-border good and passenger transportation services
- Goods exported outside GCC territory are zero rated
- Certain cross-border supplies of services

May zero-rate:

- Certain food items
- Supply of transportation for commercial purposes
- Oil, oil derivatives and gas sector

Can zero rate or exempt:

- Education sector
- Healthcare sector
- Real estate sector
- Local transport sector

Must exempt:

- Financial services (with some flexibility to tax)
- Importation, if the goods are exempted or exempted from VAT in the respective member state

2. Impact

VAT will impact most industries, but in particular:

- Consumer and industrial products
- Technology, media and telecommunications
- Financial services
- Real estate

4. Standard rate

The VAT rate will be 5% in all six GCC countries. This is significantly lower than the OECD average VAT rate of approximately 19%.

6. Prepare early – what to think about now

Uncertainty around implementation dates is no reason to delay thinking about readiness steps your business should take.
Preparation is key because VAT liabilities are generally self-assessed, with errors often subject to severe penalties and time consuming interactions with local tax authorities, or worse, causing a business disruption.
Finance and operational teams in the business need to identify and claim necessary resources early. VAT implementation projects take around a year.

7. Common pre-implementation actions

There are a number of actions businesses can take long before VAT is implemented to determine their systems, processes and contractual arrangements are 'ready to go'. Immediate actions include:

- Assess VAT readiness with **GCC VAT Review Smart** (VRS), Deloitte's online assessment tool, which considers everything from the financial impact of VAT, through to staffing and accounting processes
- Develop **roadmaps** through to 1 January 2018 or at the least the first quarter of 2018 and develop a **resourcing plan** to identify the work necessary to be ready to submit VAT returns in 2018.
- Business and industry groups often begin lobbying authorities long before draft legislation is released
- Mapping your transaction footprint to determine all future VAT liabilities and compliance obligations are easily overlaid
- Reviewing and updating contractual arrangements with vendors and customers to determine each party is aware of its responsibilities for paying and accounting for VAT
- Include appropriate clauses in contracts and implement changes to contractual terms, where necessary, e.g. to manage VAT costs in Vendor contracts or future pricing/revenue in customer contracts
- Business and industry groups often begin lobbying authorities long before draft legislation is released

8. The risks of getting it wrong are potentially enormous

Reputational
- Legal and moral requirement to pay the right amount of tax at the right time. The ability to pay the right amount of tax depends if an organization is fully versed in its tax obligations and understands how to meet them
- Failure to meet these obligations can lead to ongoing public perception challenges and a difficult relationship with authorities

Operational
- The operational imperative is to maintain the status quo over the course of a tax implementation
- Disruption of procure to pay and sell to receive processes will give rise to major operational difficulties with logistics unable to import goods, sales unable to raise invoices etc

Financial
- The business-as-usual under VAT can, depending on the level of preparation undertaken, create substantial cash-flow and absolute tax costs
- Moreover the inability to sell goods and services due to a failure to implement the necessary changes in time can lead to major revenue shortfalls
- Financial penalties for errors levied by tax authorities can be enormous

VAT and the impact areas in the implementation cycle

VAT system requirements

Sales and Marketing
- Effect on demand
- Pricing strategies
- Impact on current pipeline and inventory
- Treatment of exports

Legal
- VAT impact on contracts
  – Current contracts
  – Future contracts

Strategy
- VAT impact on corporate plans e.g. restructuring, new projects and transactions
- Clarification of issues and treatment with tax authorities
- Interaction with your Supply Chain

Internal / Human Capital
- Education and communication
- Training

Information System
- Systems review and changes for VAT compliance

Suppliers
- End of current business tariffs and charges
- Preference for VAT registered Vendors to maximise ITCs
- Use of self-billing/other billing best practices to maximise credits
- Imports of capital goods and raw materials

Customers
- Communication changes in business practices
- Structure of offers/financing
- Support mechanisms and incentives

Finance and Administration
- Impact on cash flow
- Identification of transactions and VAT liability
- Maximisation of VAT input tax credit on purchases
- Registration & compliance
- Need to be more involved

Middle East VAT Services

Specialized VAT knowledge, coupled with a local team that have been involved in the GCC VAT proposals, allows us to provide you with specific insight relevant to the GCC VAT implementation.

Contacts

Justin Whitehouse
Indirect Tax Leader
jmwhitehouse@deloitte.com

Jesus Ricart
Senior Manager, Indirect Tax
jricart@deloitte.com

Gaurav Patney
Manager, Indirect Tax
gpatney@deloitte.com

Mubeen Khadir
Director, International Tax
mkhadir@deloitte.com

Nik Faiziman
Manager, International Tax
nfaiziman@deloitte.com

Omar Hisham
Assistant Manager, Indirect Tax
ohisham@deloitte.com