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# Applying VAT to electronic services in the UAE

Your guide to managing VAT in an increasingly digital economy





The digital economy is an important part of global trade and it is a sector that continues to grow. However, it can be a complex sector for VAT, particularly where services are supplied internationally. In such cases, it can be difficult to establish where the service is delivered – and thus where it should be taxed.

To deal with this complexity, the UAE VAT law includes some special rules for supplies which it classifies as ‘electronic services’. In this whitepaper, we address these rules and provide some guidance on the two main questions that cause difficulties for taxpayers – namely:



**1.** Which supplies are covered by the term ‘electronic services’?



**2.** How do taxpayers decide where the service is supplied?

We also provide guidance on how companies can ensure that they have the appropriate expertise, knowledge and systems in place to meet increasingly complex VAT compliance obligations.

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## What are electronic services?

Article 23 of The Cabinet Decision No. 52 of 2017 on the Executive Regulations of the Decree Law ('the Executive Regulations'), outlines what constitutes an electronic service. According to this Article, they are:

**'services automatically delivered over the internet, or an electronic network, or an electronic marketplace..'**

This definition clarifies the key characteristics of an electronic service.

To begin with, the Article states that the service must be 'automatically' delivered. This implies that delivery should be made from an automated system, with minimal or no human intervention. Therefore, this means that a system that relies on human operators answering requests might not qualify as an electronic service, even if this is accessed over the internet.

The next important word in the in the definition is 'delivered'. This suggests that a service will not automatically qualify as an electronic service just because it is bought online; it must also be received online. For example, online or in-app purchases or bookings of tickets to events, hotel rooms, car-hire, restaurant services and taxi booking systems are not electronic services. They may be booked by electronic means, but that does not change the nature of the principal supply. As a result, the VAT treatment of a concert ticket purchased online is the same as that of a concert ticket purchased over the counter.

The next phrase to consider from the definition is that the service must be delivered 'over the internet, or an electronic network or an electronic marketplace'.

Article 23 defines an 'electronic marketplace' as follows:

'a distribution service which is operated by electronic means, including by a website, internet portal, gateway, store, or distribution platform, and meets the following conditions:

- a.** Which allows suppliers to make supplies of electronic services to customers.
- b.** The supplies made by the marketplace must be made by electronic means..'

This is a reasonably clear – and broad – definition which covers all of the normal means by which purchases are made online.

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## APPLYING VAT TO ELECTRONIC SERVICES IN THE UAE

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To further assist the taxpayer, Article 23 provides some examples of services that can be seen as supplied electronically:

- a. The supply and updating of software
- b. The supply of images, text, and information provided electronically such as photos, screensavers,
- c. The supply of music, films and games on demand
- d. The supply of online magazines
- e. The supply of advertising space on a website and any rights associated with such advertising;
- f. The supply of political, cultural, artistic, sporting, scientific, educational or entertainment broadcasts,
- g. Live streaming via the internet
- h. The supply of distance learning
- i. Services of an equivalent type which have a similar purpose and function

This is a helpful and relatively comprehensive list. Anything similar to these services should qualify. However, it is possible to be misled by the list; and it is always important to remember that these services will only be treated as electronic services where they meet the basic conditions – that they are delivered automatically and that this delivery takes place online. For example, whilst the supply of software is listed as an electronic service, it will only be treated as such where it is delivered automatically, online – such as a download from an online seller. If software is bought on a physical medium such as a disk or flash drive, it is not treated under the rules for electronic services.

Taking all of the above into account, there is a series of questions that the taxpayer can ask to decide whether it is supplying electronic services:

- Is it a service listed in Article 23, or a service similar to any service in the list?
- Is it delivered online?
- Is it delivered automatically?

If the answers to those questions are all positive, it is safe to assume the service is an electronic service for the purposes of the VAT law.

# Should the service be taxed in the UAE?

The VAT law uses the concept of 'place of supply' to establish whether a supply will be taxed in the UAE.

For electronic (and telecommunication) services, there are special place of supply rules set out in Article 31 of The Federal Decree-Law No.8 of 2017 on Value Added Tax ('the Decree Law'). This Article states that:

1. The place of supply shall be:
  - a. In the State, to the extent of the use and enjoyment of the supply in the State.
  - b. Outside the State, to the extent of the use and enjoyment of the supply outside the State.
2. The actual use and enjoyment of all ..... electronic Services shall be where these Services were used regardless of the place of contract or payment'

The principle here is quite straightforward and easy to understand. Essentially, the taxpayer needs to establish where the service is used.

In practice, of course, this may be far from simple because by their very nature, electronic services can be received in multiple locations at the same time and can cross borders almost without restriction. For example, someone could subscribe to a streaming service in UAE but will then be able to access their account across the world. Clearly, it would be impossible for a supplier to predict the use of a service of this type when the sale is made, in order to only charge VAT when it is used in the UAE.

The taxpayer therefore has to find a practical way to determine where the service will be used – or at least a reasonable way to make an assumption of where the service will be used at the time the sale is made.

In due course, the Federal Tax Authority will probably provide some guidance on how this might be done. In the meantime, taxpayers need to consider the options for themselves.

The most obvious reference point is the location of the customer. In many cases, this might be accepted as an appropriate test to establish where the service will be used. However, this cannot be taken for granted and it is important bear in mind the final part of Article 31 of the Decree Law which states that 'use' is the determining factor 'regardless

of contract or payment'. What this means is that the supplier always needs to consider whether a purchase made from one location will actually be used somewhere else; and whether the service will be used by a different party to the one that contracts or pays for the purchase. This is especially relevant with corporate buyers – where, for example, a head office company might purchase software that will be used by group companies in multiple locations.

The principle applies in all cases; and the supplier needs to think about the type of service they are providing and the type of customers they are supplying to in order to decide whether the location of the customer is sufficient evidence of use or whether additional data should be gathered and assessed. For example, in some other jurisdictions which have a VAT system similar to the UAE's, factors such as IP addresses and bank accounts are used to support or contradict an assumption based on the customer's location.

Ultimately, it is the supplier's responsibility to establish why a particular supply has been treated as subject to UAE or VAT or not. Taxpayers therefore need to assess the risks based on the nature of their services and the markets in which they operate. They then need to consider what data they are required to collect, as well as which safeguards or controls they can build into their system. Very importantly, they also need to make sure everything is properly recorded and documented, so that it is readily available for FTA audits.

## Could electronic services be zero-rated?

The Executive Regulations, Article 31 provides zero-rating for 'exported services'. This allows services that have a place of supply in the UAE to be treated as zero-rated rather than subject to VAT at 5%.

The rules are complex. In brief, however, services (provided they do not relate to real estate or goods in the UAE) can be zero-rated when supplied to a person who does not have a place of residence in the UAE and who is outside the UAE at the time the services are performed.

In principle, it appears these rules could apply to electronic services. For example, a non-UAE resident could download software while outside the UAE, which will be used during a short stay in the UAE. In these circumstances, the supply would be seen as taking place in the UAE, as the services will be used and enjoyed in the UAE. However, they should qualify for zero-rating because the customer is established outside the UAE and the purchase was made outside the UAE.

To date, there has been no guidance from the FTA on how the place of supply rules for electronic services and zero-rating should interact. This area should therefore be approached with extreme caution and it is possible that the intention is that electronic services should be excluded from Article 31. In any case, it seems unlikely that opportunities for zero-rating will arise frequently.

## Meeting increasing compliance demands

With the challenges of a relatively new tax regime in UAE and the additional burden of navigating the nuances around applying VAT to electronic services, it is important for taxpayers to feel confident that they have access to reliable tax advice, as well as the latest updates and guidance from the Federal Tax Authorities.

Companies' IT systems cannot be ignored, either. As discussed, VAT regulations can be complex for organizations to analyze and apply to their business models. Companies should therefore view technology as an enabler of faster, more accurate compliance rather than a cost center.

Organizations should also not allow outdated systems hinder their ability to cope with change. In our fast-evolving technological age, legacy software or poor IT architecture cannot be used as an excuse for non-compliance. Whether or not the UAE will, at some point in the future, change the taxability of electronic supply services should not matter from a system point of view.

Companies should have the flexibility to adapt their systems as legislation evolves without needing a total revamp of their configurations. Leveraging tools available today, systems can be adapted to manage a change in taxability of a good or service, without the need for IT intervention.

Obviously, this requires the right tax technology setup in the first place, as well as the right amount of detail at a master data level in business systems, to allow for such an automated process. Having smartly designed VAT technology in place dramatically reduces human touch points, increases accuracy and accelerates the speed at which a VAT return can be produced and filed.

### In closing

Electronic services and their taxability have been an ongoing debate in the VAT world. Through this whitepaper, we have shown how complex these regulations can be. Any new development on this matter should be carefully analyzed – as the margin for error is narrow in this environment.

Going forward, it will be essential for taxpayers in the UAE to prepare for the fact that the region's tax regime is constantly developing. They also need to be aware that tax administrations around the world are moving towards a more digitally enabled tax environment.

In this environment, as businesses face pressure to meet increasingly complex regulatory demands, they need to be confident that they have access to the professional support, intelligence and technology required to meet ongoing challenges with efficiency, clarity and confidence.

If you want to automate VAT within your company, Thomson Reuters can help. Contact us at [onesource.mena@thomsonreuters.com](mailto:onesource.mena@thomsonreuters.com) today.

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