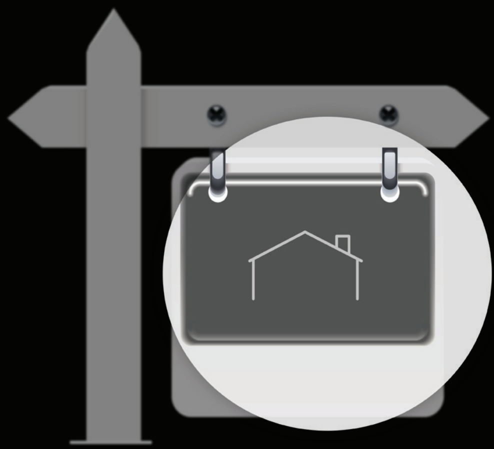

The Indirect Tax implications of COVID-19 in the GCC

The real estate industry

Impacts

The real estate sector has implemented various measures in response to the economic impact from COVID-19, from landlords offering rent exemptions to developers waiving off certain charges on the acquisition of property. We look at the Value Added Tax (VAT) impact of some of these below as well as how the sector can better manage VAT cash flow costs.

In recognition of temporary pay cuts, landlords are offering rent reductions through rent exemptions, discounts and rent free periods. Depending on the specifics of the arrangements, these initiatives may oblige the landlord to issue credit notes. However, since suppliers can only issue credit notes in limited circumstances, taxpayers should seek advice on the correct approach.

Property developers seem to have also introduced a number of measures to navigate this downturn. For example, in a bid to sell property, developers are increasingly enticing buyers with the provision of "free" goods and services e.g. savings on service charges, maintenance fees etc. Such savings could inadvertently result in VAT cost for the developer under the deemed supply provisions, and therefore we strongly recommend understanding the VAT impact of these initiatives and structuring sales contracts appropriately to reflect the substance of the transaction.

Additionally, as demand for residential properties fall, developers may be at risk of properties being vacant for more than 3 years following their completion, such that their first sale or lease would no longer qualify for the zero-rating and potentially jeopardizing the recovery of VAT on development costs. Developers should consider the strategies available to manage this risk. Similarly, in cases of cancelled property sales, developers should consider the VAT impact of retained and returned sums based on the terms of the cancellation.

Managing cash flow and reducing VAT costs

Property developers involved in making exempt and taxable supplies, i.e. bare land, letting residential property as well as selling property, could consider revisiting the input tax apportionment method used to calculate recoverable VAT on residual costs of the business. Where businesses have been overly conservative in their approach to recover VAT on costs previously, they can now reassess whether any additional VAT can be recovered to which the business is entitled based on the guidance provided by the Federal Tax Authority (FTA).

On the other hand, construction companies, often dealing with tight margins and high cash flow costs before the pandemic, will feel the crunch of the economic uncertainty, especially with projects being put on hold and extensions in payment terms. To manage VAT cash flow costs associated with delayed payments, the industry may wish to implement "pro-forma invoicing" or "demand for payment" arrangements which sees VAT invoices issued only once a customer makes a payment, relieving taxpayers of the burden of having to pay VAT to the tax authority before receiving it from customers.

Other ways of easing VAT cash flow costs, is to query whether suppliers are correctly charging VAT, for example on labour accommodation and supplies of bare land, both of which can be exempt from VAT depending on the fact pattern, as well as reviewing whether VAT is due on all outputs such as penalties under lease agreements and supplies of residential property, where reliefs can apply.

Overall, the VAT impact of strategies employed to manage the businesses cash flow situation during these times should be evaluated in order to avoid any compliance related risks moving forward. If you are a business in the real estate sector and would like to discuss any of the measures taken to support the cash flow position of your business, please do not hesitate to contact us.

Contacts

Mark Junkin
ME Indirect Tax Leader
Deloitte Middle East

Nurena Tarafder
Director, Indirect Tax
ME Indirect Tax Real Estate Industry Leader
Deloitte Middle East

Sabeka Arshad
Manager, Indirect Tax
ME Indirect Tax Real Estate Industry Manager
Deloitte Middle East

Suhail Joosub
Manager, Indirect Tax
Me Indirect Tax Real Estate Industry Manager
Deloitte Middle East