

E-commerce VAT rules in the GCC: a missed opportunity at perfect harmonization with the EU?

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Few events in the last decade have contributed as much to the growth of the digital economy as Covid-19. The pandemic forced entire populations to go into lockdown, working from home became the norm and outdoor activities were limited to a bare minimum out of fear of infection. All these factors have contributed to a change in consumer behavior as a result of an increase in screen time, which has in turn significantly increased our exposure to digital advertisements. To no one's surprise, electronic platforms and digital marketplaces have reported an enormous surge in online engagement due to people massively ordering goods and services via the internet. At a time where large numbers of bricks-and-mortar stores are experiencing a serious economic slowdown, the e-commerce sector in the GCC is set to reach a value of over \$24 billion by the end of 2020, a figure which is \$3 billion higher than the projected value of \$21 billion (of which more than \$2 billion is reportedly due to Covid-19)^[1]. It is against the background of a thriving e-commerce sector that we will have a closer look at the applicable VAT rules for electronic services in the GCC^[2]. This article does not consider supplies of goods, which are subject to an even more complicated regime in the GCC.

VAT status in the GCC

In 2016, all six GCC countries signed a multilateral treaty titled the 'Common VAT Agreement of the States of the Gulf Cooperation Council' (GCC VAT Agreement), in which all Member States agreed to implement VAT in their respective jurisdictions.

Although initially all six GCC countries were expected to implement VAT over the course of 2018 and 2019, only the Kingdom of Saudi Arabia (KSA) and the United Arab Emirates (UAE) did so on 1 January 2018, followed one year later by Bahrain on 1 January 2019. Oman is expected to introduce VAT in April 2021, thereby becoming the fourth GCC country to implement VAT.

The GCC VAT Agreement forms the basis of the legal VAT framework in the GCC. Conceptually, the GCC VAT system is heavily inspired by the EU VAT system. Nevertheless, it would be unfair to state that the GCC VAT system is a mere reproduction of the EU VAT directive. For better or for worse, for each similarity there are also a significant amount of differences between these two VAT systems. It is not always clear whether these differences are the result of conscious policy decisions or whether they are simply inevitable byproducts of performing a legal transplant with GCC legislators looking at the same concepts through different eyes.

In this article, we will compare the e-commerce VAT rules for services in the GCC and highlight some remarkable similarities and differences. Where relevant, we will draw parallels with the applicable VAT rules in the EU.

Definition of electronic services

In the EU, 'electronically supplied services' are defined as services which are (1) delivered over the Internet or an electronic network, (2) are essentially automated, (3) involve minimal human intervention, and (4) are impossible to ensure in the absence of information technology^[3]. In addition, the EU VAT Implementing Regulation contains an indicative list of services which are considered to qualify as electronic services^[4]. The EU has very extensive guidance, which multiple jurisdictions have adopted as their own internal guidance.

By contrast, the GCC VAT Agreement does not include a definition of the term 'electronic services'. In this respect, it should be noted that contrary to Bahrain and the UAE, KSA considers the GCC VAT Agreement to be an integral part of its domestic VAT legislation. This approach is a bit different from the position which has been taken by the two former countries. In general terms the difference in the positions adopted by these three countries can be summarized very concisely as follows: where Bahrain and the UAE have effectively transposed the GCC VAT Agreement into their own domestic VAT legislation, KSA has chosen to use its domestic VAT legislation to build further on the GCC VAT Agreement and supplement it where required. Given this background, it is perhaps a bit surprising that KSA has not taken the opportunity to include a broad-based definition of electronic services in its domestic legislation. KSA has instead limited itself to including an indicative list of electronic services, based on the EU list of services^[5]. An approach which was also taken by Bahrain^[6].

Only the UAE has defined electronic services as follows: "services which are automatically delivered over the internet, or an electronic network, or an electronic marketplace"^[7]. In this definition, the UAE has also included a non-exhaustive list of electronic services. It should be noted that this definition does not include any reference to the criterion of human intervention.

In its administrative guidance, the Federal Tax Authority (UAE) has clarified that the meaning of the term 'automatically delivered' implies that there should be minimal or no human intervention (although a small degree of human intervention is acceptable to enable or complete a supply)^[8]. The National Bureau for Revenue (Bahrain), on the other hand, has stated in its guidance that "Electronic services are services provided over the internet or any electronic platform, and which operate in an automated manner with limited human intervention and which are impossible to complete without the use of information technology". Although not completely based on the law, both Bahrain and the UAE have incorporated a definition which comes very close to the concept of electronically supplied services in the EU, in the sense that a joint reading of the law and administrative guidance will generally lead to the same outcome in the both the EU and these two GCC countries.

From a policy perspective, it is the author's opinion that the approach taken by Bahrain and the UAE seems to be more preferable as compared to KSA, which has not implemented the concept of minimal human intervention. Especially foreseeability internationally for businesses supplying electronic services is important. The different positions unfortunately also open the door to diverging outcomes between different GCC countries in terms of the qualification of certain services.

Given the ever-evolving and constantly changing nature of the digital economy and in particular, electronically supplied services, it is seemingly more convenient for taxpayers to be able to rely on a broad-based definition, based on general criteria such as the requirement that the services is essentially automated and requires minimal human intervention, rather than having to make an assessment to see whether a particular service fits the indicative list of electronic services or not. In other words, it could be argued that a broad-based definition would generally lead to more legal certainty in terms of the qualification of services as electronic services.

Place of supply of electronically supplied services

Under the EU VAT legislation, the place of supply of electronically supplied services supplied to non-taxable persons shall be the place where that person is established, has his permanent address or usually resides^[9].

According to the GCC VAT Agreement, the place of supply of electronically supplied services supplied to non-taxable persons shall be the place of actual use of or enjoyment of these services^[10].

Although both place of supply rules are different, this is a clear example of how the GCC VAT system re-uses concepts of EU VAT law, but implements them in a (slightly) different way. Readers who are familiar with EU VAT will have undoubtedly picked up on the reference to the so-called 'effective use and enjoyment' rules^[11].

In short, EU Member States may decide to shift the place of supply of services, which are either inside or outside the EU to inside or outside their territory, when according to the effective use and enjoyment of the service this differs from the place of supply as determined on the basis of the normal place of supply rules^[12].

It is worth noting, however, that whereas under the EU VAT system, use and enjoyment rules function as a correction mechanism in regard to the place of supply rules to prevent double taxation, non-taxation or distortion of competition, under the GCC VAT system, the use and enjoyment rules surprisingly simply function as a regular place of supply rule.

They are the criterion to determine where the services are actually used or enjoyed for VAT purposes by a private individual. In other words, where there is a potential two-step approach to determine the actual place of supply of electronic services under the EU VAT rules (firstly on the basis of the normal place of supply rules and secondly on the basis of the applicable use and enjoyment rules, which may lead to a correction of the outcome determined under the first step), there is only a single step when determining the place of supply under the GCC VAT rules.

To determine where the use and enjoyment of electronic services effectively takes place, the GCC VAT legislator has once again drawn inspiration from the EU VAT system, whilst at the same time providing its own interpretation of the rules in question. The conflating of the concepts can be traced back to the implementation in the UK of the place of supply rules for electronically supplied services which substantially deviates from the Recast EU VAT directive 2006/112/EC. Although the end result may come down to the same, the place of supply rules in the EU are **not** use and enjoyment rules, since they do **not** correct another place of supply rule. While UK VAT practitioners use the term loosely, it leaves other European practitioners scratching their heads. In turn, it makes the GCC laws conceptually less clear.

Broadly speaking, the EU VAT system has a tiered system to determine the location of a non-registered customer. In the first instance, the EU VAT Implementing Regulation provides a number of presumptions for specific situations, such as the provision of services at a physical location, through a land line or mobile network^[13]. Secondly, in situations where the aforementioned presumptions are not applicable, the supplier must capture and retain two pieces of non-contradictory information as evidence of the location of the customer^[14] ^[15], such as the billing address, IP address or country code of the SIM of the customer^[16]. Finally, if the supplier has reason to doubt the location given from the presumed list then they must provide three pieces of non-contradictory information as evidence for their rebuttal^[17].

Although slightly different, the rules to determine the location of the customer in the GCC are clearly inspired by these rules. In the UAE and KSA, the VAT law differentiates between electronic services provided in a specific location and electronic services not provided in a specific location (e.g. on a portable device):

- The first category refers to the situation where electronic services are provided at a telephone box, a telephone kiosk, a Wi-Fi hot spot, an internet café, a restaurant or a hotel lobby or other cases where the physical presence of the customer at a particular location is needed for those services to be provided. In such a case, the customer is considered to have actually used and enjoyed in that location.
- For the second category, the place of use and enjoyment is determined on the basis of the customers (usual place of residence (see Bahrain and KSA) or location at the time the services are supplied (see UAE)). For the purpose of determining the location of the recipient the supplier may use the following indicators:
 - the internet protocol ("IP") address of the device;
 - the country code stored on the SIM card;

- the place of residence of the recipient;
- the billing address of the recipient; and / or
- the bank account details of the recipient.

This non-exhaustive list is based on the list of evidence used to determine where the customer is established under the EU VAT system. Note, however, that there is no requirement to collect two non-contradicting pieces of evidence^[19].

Another point worth noting is that in Bahrain, the application of these indicators is limited to the supply of electronic services to taxable customers only^[20], whereas such a limitation does not apply in the UAE and KSA. Since the decision to restrict the application of these indicators to registered customers does not appear to be motivated by a specific policy reason, it is the author's view that this restriction is the result of an oversight by the Bahraini legislator.

In the UAE, these rules were implemented through administrative guidance, rather than by force of law^[21], whereas KSA and Bahrain have effectively implemented the principles outlined above in their VAT legislation, followed by the publication of administrative guidance by the respective tax authorities which confirmed these principles^[22] [23].

Conclusion

Electronically supplied services are highly mobile services. In order to ensure compliance from the tax authority perspective, they require harmonization and standardisation. This should translate into a common legislative framework with no or little differences between jurisdictions, an easy sign up, easy reporting and paying. While this article only covered the first aspect, there are substantial issues with the differences in the legislative framework and their interpretation, as well as with the other aspects. Non-compliance with VAT rules around electronically supplied services is extremely hard to police and enforce because in almost all cases the tax authority deals with a foreign supplier. The EU has led the way in making compliance easy, and it is perhaps a missed chance that the GCC has not gone the same way so far.

^[1] Source: Kearney analysis GCC e-commerce sector, <https://www.consultancy-me.com/news/3092/gccs-e-commerce-sector-surging-ahead-amid-covid-19>.

^[2] The term GCC refers to the Cooperation Council for the Arab States of the Gulf, originally known as the Gulf Cooperation Council. The Member States are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates

^[3] Art. 7, paragraph 1 of the Council Implementing Regulation (EU) No 282/2011 of 15 March 2011 laying down implementing measures for Directive 2006/112/EC on the common system of value added tax (EU VAT Implementing Regulation)

^[4] See Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (the "Recast EU VAT Directive"), Annex II (indicative list of electronically supplied services). See also Art. 7, paragraph 2 of the EU VAT Implementing Regulation. See also EU VAT Implementing Regulation, Annex I.

^[5] Art. 24 (1) of the KSA VAT Implementing Regulations

^[6] Art. 18, A of the Bahrain Executive Regulations of the Value Added Tax Law

^[7] Art. 23 (2) of the UAE VAT Executive Regulations

^[8] FTA, E-Commerce VAT Guide, VATGEC1 (August 2020), <https://www.tax.gov.ae/-/media/Files/EN/PDF/Guides/E-Commerce--VAT-Guide--EN--09-08-2020.pdf>, p. 20.

^[9] Art. 58 (1) (c) of the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax

^[10] Art. 20 of the GCC VAT Agreement

^[11] In KSA referred to as the consumption and enjoyment of services (see Art. 24 (2) and (3) of the KSA VAT Implementing Regulations)

^[12] The implementation of use and enjoyment rules is optional for EU Member States. See Article 59a of the Recast EU VAT Directive

^[13] Art. 24a, paragraph 1 and 2, Art. 24b paragraph 1, (a) – (c) of the EU VAT Implementing Regulation

^[14] Art. 24b, paragraph 1, (d) of the EU VAT Implementing Regulation

^[15] It should be noted that only one item of evidence is required for so-called micro-businesses.

^[16] Art. 24f of the EU VAT Implementing Regulation

^[17] Art. 24d, paragraph 1 of the EU VAT Implementing Regulation

^[18] In the UAE, the FTA has stated, however, that the supplier should give priority to the factors which give the most precise information regarding the actual place where the electronic services will be used and enjoyed.

^[19] Art. 18, B – C of the Bahrain Executive Regulations of the Value Added Tax Law

^[20] For UAE, see FTA, E-Commerce VAT Guide, VATGEC1 (August 2020), <https://www.tax.gov.ae/-/media/Files/EN/PDF/Guides/E-Commerce--VAT-Guide--EN--09-08-2020.pdf>

^[21] For KSA, see GAZT, Digital Economy Guide, Version 1, <https://gazt.gov.sa/en/HelpCenter/guidelines/Documents/Digital%20Economy.pdf>

^[22] For Bahrain, see NBR, VAT Digital Economy Guide, version 1.0 (March 2019), <https://s3-eu-west-1.amazonaws.com/nbrproduserdata/media/hOLhKSh8QwUx0uUAcn90vhcv9H9L3SHfrNb4YW.pdf>.