

## inBrief



### **UAE VAT Executive Regulation Update: Free Zone Guidance**

By Bashir Ahmed | 14 November 2017

The UAE Ministry of Finance has announced the Executive Regulation for the Federal Decree-Law No. (8) of 2017 on Value Added Tax (**UAE VAT Legislation**) at a Cabinet meeting on 7 November 2017, headed by His Highness Sheikh Mohammed bin Rashid Al Maktoum, Vice President and Prime Minister of the UAE, Ruler of Dubai.

It is expected that the Executive Regulation to UAE VAT Legislation will be released this week in draft form on both the UAE Ministry of Finance's website ([www.mof.gov.ae](http://www.mof.gov.ae)) and the Federal Tax Authority's website ([www.tax.gov.ae](http://www.tax.gov.ae)).

The Executive Regulation operates in conjunction with, and provides substantive details to many operative provisions within the UAE VAT Legislation. As such, the UAE VAT Legislation, Executive Regulation and relevant UAE Cabinet decisions are required to be read together for a practical application of UAE VAT law.

In this multi-part inBrief, we will disseminate the most significant provisions for which the release of the draft Executive Regulation has provided additional legislative and procedural detail for the application of VAT within the UAE.

Operative clarifications in a number of specific areas have now been provided in the Executive Regulation, amongst which the most important and anticipated is the intended application of UAE VAT regime with respect to Free Zone entities.

#### **Designated Zones**

The Executive Regulation does not specifically prescribe treatment to UAE Free Zone entities or references the term Free Zone, as not all Free Zones will attract the same treatment.

#### **The Author**



**Bashir Ahmed**  
Managing Partner  
[bahmed@afриди-angell.com](mailto:bahmed@afриди-angell.com)  
Tel: +971 4 330 3900

Bashir is the managing partner of Afridi & Angell. He joined the firm in 1988 and became a partner in 1993. He advises clients on cross-border, general corporate and commercial, private equity, banking, licensing and maritime matters. Bashir is a member of the New York State Bar, the Lahore High Court Bar Association, and the International Bar Association. He holds an LLM from Punjab University Law College and a BA from Oxford University.

Rather the Executive Regulation introduces a new term, Designated Zone, which is defined by the Executive Regulation as:

*Any area specified by a decision of the Cabinet upon the recommendation of the Minister, as a Designated Zone for the purpose of the Decree-Law.*

Therefore, as a Designated Zone will be specified by a decision of the UAE Cabinet and such decision has not been published in the UAE Federal Gazette the situation remains that there is no comprehensive guidance on whether a specific Free Zone entity would fall under the Designated Zone VAT provisions, or if they would be treated as a regular onshore entity for UAE VAT purposes.

The operative provisions of the Executive Regulations pertaining to Designated Zone entities however do allow us to provide some certainty to a large number of Free Zone entities.

### **A Question of Physical Segregation**

A Designated Zone specified within a future UAE Cabinet decision will be treated as being outside of the UAE and of the GCC for VAT purposes subject to three conditions.<sup>1</sup>

The Designated Zone is required to be a specific fenced area with security measures and Customs controls in place to monitor entry and exit of individuals and the movement of goods to and from the area. A Designated Zone will also have internal procedures regarding the method of keeping, storing and processing of the goods within the Designated Zone, and the operator of the Designated Zone shall comply with the procedures set by the Federal Tax Authority (FTA). These specific procedures are at this time unknown.

If a Designated Zone fails to maintain the required conditions above, it will cease to be treated for UAE VAT purposes as being outside of the UAE/GCC.

It is apparent that the UAE has chosen to align the concept of a Designated Zone with existing bonded customs procedures both as a concession to compliance (as entities currently trading within such bonded Free Zones would be familiar with the imposition of Customs Duties) and also as a simplification measure (as such areas already have the physical and procedural infrastructure in place to control the flow of goods within a fenced geographic area).

From the required Designated Zone conditions above, a large number of forty five<sup>2</sup> Free Zones within the UAE will not satisfy the physical segregation requirements in order to qualify as a Designated Zone, and thus entities incorporated within these Free Zones will be subject to the same VAT operative provisions as all other onshore entities within the UAE.

### **Bonded Free Zones**

Free Zones such as Dubai Airport Free Zone, Jebel Ali Free Zone, Sharjah Airport International Free Zone, Hamriya Free Zone, Ras Al Khaimah Free Trade Zone, and Fujairah Free Zone<sup>3</sup> currently have geographic segregation, security and customs controls in place and hence have the ability to be scheduled as a Designated Zone in a future UAE Cabinet decision.

Imports of goods from outside the UAE into Designated Zones will not be treated as imported into the UAE<sup>4</sup> and thus will not be liable for UAE VAT until such a time when a supply of goods is made from within the Designated Zone to another person to be used by them,<sup>5</sup> or consumed by the owner within the Designated Zone.<sup>6</sup>

---

<sup>1</sup> Article (51) (1) a, b, c.

<sup>2</sup> As at August 2017.

<sup>3</sup> Non inclusive.

<sup>4</sup> Article (47)(1) b.

<sup>5</sup> Article (51) (5).

<sup>6</sup> Article (51) (8).

Acquisition of goods within a Designated Zone for incorporation into another unconsumed good located within the same Designated Zone will not be subject to UAE VAT.<sup>7</sup>

Goods may also be transferred between Designated Zones without being subject to tax if the goods are not used or altered during the transfer process, and the transfer is undertaken in accordance with the rules for customs suspension per GCC Common Customs Law.<sup>8</sup> The FTA may require a guarantee equivalent to the tax liability of the goods to be transferred in case the conditions for the transfer of goods between Designated Zones are not met.<sup>9</sup>

The movement or supply of goods into a Designated Zone from within the UAE will not be considered an export of such goods from the UAE,<sup>10</sup> and as such will not receive zero-rating which an export outside of the GCC would receive.

### **Service Entities**

A large number of entities operating in bonded Free Zones that may qualify to be Designated Zones would provide services as their primary taxable supplies. The Executive Regulation provides that the place of supply of services is considered to be within the UAE if the place of supply is within the Designated Zone<sup>11</sup> and in effect, aligns the VAT treatment of service entities operating within Designated Zones to similar onshore entities within the UAE.

### **Conclusion**

The draft of the Executive Regulation to the UAE VAT Legislation in respect of Free Zone entities confirmed our view of the expected UAE VAT treatment of Free Zone entities insofar that it would be harmonious to all other onshore UAE entities. Although a number of Cabinet decisions are still to be released pertaining to the implementation of the UAE VAT regime, most Free Zone entities now have reasonable certainty to their UAE VAT outlook. Free Zone entities that have delayed planning or registration for the implementation of UAE VAT on 1 January 2018 have a highly compressed timeline in which to make important internal procedural and operational changes.

The general alignment of UAE VAT and Customs Duty in regard to the definition, operation and compliance of Designated Zones provides some familiarity in changing times to Free Zone entities already operating within the bonded goods warehouse regime, which will reduce administrative compliance overhead to importers and exporters of physical goods.

Please stay tuned for our next installment of this multi-part inBrief as we further disseminate the most significant provisions for which the release of the draft Executive Regulation has provided additional legislative and procedural detail for the application of VAT within the UAE. ■

---

<sup>7</sup> Article (51) (5).

<sup>8</sup> Article (51) (3) a, b.

<sup>9</sup> Article (51) (4).

<sup>10</sup> Article (30) (3).

<sup>11</sup> Article (50) (6).

### **Afridi & Angell**

Founded in 1975, Afridi & Angell is a full-service UAE law firm in its fifth decade at the forefront of the legal community. From the beginning, our hallmarks have been a commitment to quality, unsurpassed knowledge of the law and the legal environment, and crafting of innovative business solutions. Licensed in the three largest Emirates of Abu Dhabi, Dubai and Sharjah as well as the Dubai International Financial Centre, our practice areas include banking and finance; corporate and commercial law; arbitration and litigation; construction; real estate; infrastructure projects; energy; project finance; maritime (wet and dry); and employment. We advise local, regional and global clients ranging in size and sophistication from start-ups, sole proprietorships, family-owned businesses, entrepreneurs and investors to some of the world's largest public and private companies, governments and quasi-government institutions. We attract and retain clients with our dedication to practical guidance focused on their business needs supported by decades of experience here in our home jurisdiction, the UAE.

Afridi & Angell is the exclusive member firm in the UAE of top legal networks and associations, most notably Lex Mundi, the world's leading network of independent law firms, and World Services Group.

[www.afridi-angell.com](http://www.afridi-angell.com)