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VAT on Telecommunications

About Telecom

Telecommunications is one of the most dynamic sectors and also act's as backbone of innovation, infrastructure and development in a country.

Generally, the Telecommunication domain is segregated into two primary segments i.e. Consumer (B2C) and Business (B2B). The multiple revenue streams from end consumers include pre-paid and post-paid services, internet services, fixed line, broadcasting, sale of devices etc. The telecommunication companies also offer infrastructure solutions, turnkey projects and carrier & wholesale services to various enterprise customers.

Generally, every country has a Telecommunications Regulatory Authority (TRA) to regulate and govern the various operational aspects of Telco's to protect and cater the interest of the subscribers. However, now with introduction of Value Added Tax ('VAT') by Gulf Cooperation Council ('GCC'), the VAT authorities have also become a stakeholder and therefore, it is vital to understand how VAT will impact the Telecommunication sector.

VAT in the GCC

With the implementation of VAT in the UAE and KSA, most goods and services except for a limited number of transactions (which may be exempt or zero rated), supplied by companies are taxable at a Standard Rate of 5%.

On procurement side, VAT registered businesses will also be able to claim any VAT paid on their business expenses subject to specified conditions. Where one is unable to claim VAT credit, such VAT credit will be considered as cost to the Company.

VAT on Telecommunication services

What is telecommunication?

Telecommunication services means delivering, broadcasting, converting or receiving any of the services specified below by using any communications equipment or devices that transmit, broadcast, convert, or receive such service by electrical, magnetic, electromagnetic, electrochemical or electromechanical means or other means of communication, including, but not limited to:

- Wired and wireless communications.
- Voice, music and other audio material.
- Viewable images.
- Signals used for transmission with the exception of public broadcasts.
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- Services of an equivalent type which have a similar purpose and function.

Based on the above, it appears that most of the supplies affected by a Telecom company gets covered in the above definition. However, one cannot rule out the possibility that there may be additional services which may or may not get covered under the above definition.

Place of supply rules (use and enjoyment)

VAT being a consumption based levy, it is imperative to determine the location of consumption of service. For telecommunications, the place of supply is specified where the services are actually **used and enjoyed** by the recipient, regardless of contractual payment teams.

In practice, this means generally that VAT will be applicable based on consumption of telecommunication services and not upfront on sale. Also, where the services are consumed outside UAE, no VAT should be due, even if the supplier is established within the state.

It is important to highlight that in some countries, VAT is applicable on point of sale and not on use and enjoyment, i.e. VAT is collected as soon as the initial top up voucher is sold to the customer instead of taxing it on subsequent use and enjoyment of the services.

Taxability of various supplies by Telco's

Generally, most Telecommunication supplies are standard rated. However, given the wide gamut of services offered by Teleco's, some may be subject to different tax treatments.

Considering the complexities, it is imperative that correct VAT treatment is accorded to each transaction and corresponding tax determination logic is defined in IT systems.

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Input credit

Considering the size and complexity of operations, Telco will incur huge capital and operating expenditures for construction and operation of towers, repair and maintenance expenditures, laying network across the countries etc. Under GCC VAT regime, all such expenditure (if procured locally) will be subject to VAT at standard rate (5%).

UAE VAT Laws have prescribed that credit of any input VAT should be admissible on all such expenses subject to fulfilment of prescribed conditions.

Additionally, there is specified scheme for Capital Assets, whereby input VAT credit recovered on capital assets used for long term use is subject to constant monitoring (till the prescribed time period) depending on the nature and use of such asset for respective activities (taxable or exempt).

Information systems

Most of the companies only have an ERP system for managing the operations of the Company. With Telecom specifically one may observe that there are multiple information system's billing which sync to provide multiple types of information, reports and data. Therefore, from a VAT implementation perspective a huge exercise is required to align/update all such information systems for a Telecom company to be compliant with law and also furnish correct records per the requirement of each authorities (Regulatory or Tax authorities).

Invoicing

Invoicing under VAT holds importance, as businesses are required to issue valid Tax invoices especially for B2B transactions, where the recipient may claim input tax paid on procuring such services. Further, to simplify the requirement the GCC VAT law also provides an option for issuing simplified invoices for customers where the value of supplies are less than a specific value.

This is a challenging exercise for Telecom companies considering the base/size and nature of customers they service.

Records and Documents

With introduction of VAT, emphasis is always place on the manner and duration of keeping records for all supplies (sales and purchases). The UAE VAT Law also requires businesses to maintain and retain documents (such as tax invoices, records of adjustments or corrections made to tax invoices,) related to all supplies for a prescribed period of 5 years (for Real Estate such requirement is for 15 years). Specifying the period in the VAT Law, enables the VAT authorities to seek such details for conducting audits.

In Telecom, considering the number of transactions run in million's a day, it is important for Telco's to plan in advance the manner for keeping such records and making available such records in a timely basis.

Transitional considerations

Transition entails change from current practice to complying with new rules and regulations. There is always a push back/dichotomy considering various seen and unseen challenges, which makes the transition period turbulent from VAT implementation standpoint.

As the UAE and other GCC countries rolled over to the VAT era, this period observed various activities such as amendments for future contracts, negotiations for ongoing contracts, Pricing based on Tax inclusive or exclusive, communications to customers, establishing new teams, framing new policies and procedures, cut-off procedures etc.

Considering the varied nature of business activities it is important for companies to factor various commercial (such as pricing, increase in cost, compliance with other commercial laws) as well as non-commercial (consumer experience, consumer handholding) considerations to steer through this period. This entails detailed planning and guidance to all such telecom companies.

Penalties

Under the self-governed tax regime, the VAT authorities entrust that the businesses be responsible and compliant with the law of the land. However, for exceptional cases the Authority has clearly laid down the nature of offenses and corresponding penalties levied on each scenario. Such penalties may range up to five times or in worst case scenario the authorised person may have to serve time at jail.

From draft of the law what appears is that VAT authorities may take a no tolerance approach for any non-compliances. Thus, Companies should take every effort in the book to be compliant and avoid any penal consequences.

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