

# The VAT Question

Tax reforms in the Middle East have led to some uncertainty throughout the emirates and KSA. We look at how Value Added Tax (VAT) could impact the education sector.

By Angitha Pradeep

According to a report published by HSBC, parents in the U.A.E. spend an average of \$99,378 on a child's education. This is the second highest in the world, with 80% of parents thinking that a post-graduate degree is necessary for their children to achieve their life goals. With such a significant investment, parents across the emirates and KSA are now for the first time considering the implications of Value Added Tax (VAT).

Following the introduction of VAT in the U.A.E., in accordance with the GCC VAT Framework, each member state of the council has agreed to adopt and implement their own national VAT legislation based on common principals. Accordingly, effective from January 1, 2018, the Kingdom of Saudi Arabia (KSA) and the U.A.E. implemented their respective VAT systems.

"To coincide with the Golden Jubilee of the U.A.E., the Vision 2021 earmarks education as a sector that will drive the government to be one of the best countries of the world in terms of a diversified and flexible knowledge-based economy," says Jeanine Daou, PwC Middle East's Indirect Tax Leader. She adds, "To achieve this, the government must create an enabling environment for stakeholders to operate in."

For the U.A.E. services are subject to zero-rate VAT—if the supply of the services provided by the institutions are according to the curriculum that is recognized by the federal or local government entity where the course is delivered. The zero-rate is usually considered

a very favorable VAT treatment, as there is no VAT amount applied on the fees charged to customers (i.e. a VAT at 0%) while the VAT incurred by the supplier on its expenses can still be reclaimed in full.

**Education services taxed and not-taxed**  
Educational institutions have evolved to provide more than just education to their students; they are now often involved in business activities such as the sale of goods from campus shops, restaurants, vending machines, admission to plays, concerts, dances and museums, etc. They may also provide short-term courses to non-students/the general public, all of which are likely to be subject to VAT.

In the U.A.E., education services provided by education institutions approved by the authorities and in line with a recognized curriculum (such as nurseries, preschools, schools (primary and secondary) are taxed at zero-rate (0%). The zero-rating is limited to tuition fees including books and other educational materials (which usually account for the majority of the total education costs).

Conversely, non-core activities, i.e. (extra-curriculum activities, uniforms, certain books and materials) are subject to VAT at the standard rate of 5%. Therefore, families may experience a slight impact on their school-related costs if the education institutions decide to apply the VAT on top of their existing fees for their non-core educational activities.

Meanwhile, similar to secondary education,



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zero-rating applies to "core education" supplies from higher-education institutions (i.e. tuition fees including books and other educational materials), to the extent that these institutions meet certain set conditions where they are owned by the local or federal government, or where they receive more than 50% of their annual funding directly from them.

Students who are not enrolled with qualifying higher-educational institutions, may indeed face an increase in their school fees, if these institutions apply VAT on top of their existing fees (they may choose to absorb such increases and maintain the level of fee as is).

**What this means for the future of the economy**  
Reports suggest that VAT is estimated to generate over \$3 billion in the first year, about 1.5-2% of GDP, while the revenues will shoot up to between \$4.9 billion and \$5.5 billion in the second year, according to the Federal National Council.

The decision to introduce VAT is part of efforts to secure new sources of income that boost the region's commitment to diversifying its economy and reducing reliance on hydrocarbons. The new revenues will be used to improve public services for citizens and expat residents alike, including hospitals, roads, public schools, parks, waste management and police services, according to officials.

"In the long term, the objective of the government is to ensure fiscal sustainability and VAT should contribute an important source of revenue for the government, which will benefit the economy as a whole," Daou says. It is also understood at this time that it is too early to assess the impact of the education sector on VAT revenues.

Consumers and business that have been long accustomed to relatively low taxation in the GCC are expected to make a big change in their spending and purchasing habits. Due to this, specialists are expecting a decline in purchases during the first quarter of 2018, opening the economy up to weakness. As the addition of VAT was announced in mid-2017, consumers have had enough time to make purchases in 2017 to avoid VAT.

"Individual families typically do not qualify as taxable persons; therefore, they are not entitled to recover the VAT incurred on their expenses. Families are at the end of the 'supply chain' and, as final consumers, bear the VAT cost," says Daou.

In addition to education services, determining the VAT treatment for ancillary services such as examination fees, the provision of course materials, research grants and donations are areas that will be considered as extensions to the education sector and maybe subject to the VAT treatment. Defining them early on during the beginning of the education year, will help clarify concerns that parents are bound to currently have. ①