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WHITEPAPER

VAT

Preparing for the Future – A success playbook

VAT – Principles & GCC

There exist many forms of Indirect taxes viz General Sales Tax, Turnover tax, Customs Duty, Stamp duty, Entertainment tax, Luxury tax, border tax, Value added tax and Goods & Services tax. More than 150 countries have adopted indirect taxation. Indirect taxes are levied on the production and consumption of goods and services. It influences the retail price, and hence affects patterns of trade and consumption. Indirect taxes are ultimately paid by the end consumer. In contrast with direct taxes, indirect taxes are often not progressive.

Indirect Taxes are a major source of additional revenue for the exchequer. In some of the major economies Indirect Tax contribution to GDP can be as high as 10.5%, which gives a phenomenal boost to the country's expenditure budgets. Here's a look at current state of affairs in GCC countries with respect to tax as a % of GDP:

The word "open" is vital for both the main drivers of API development in financial services: the rise of financial technology companies & fin-tech start-ups and regulatory initiatives taken up in certain geographies to open up the market for further innovation and competition. Open banking has the power to completely change and revolutionise the way Banks offer products & services to the customer and the way a customer interacts with the bank.

Country	Tax as a % of GDPsaas
UAE	1.40%
Kuwait	1.50%
Oman	2.00%
Qatar	2.20%
Bahrain	4.80%
Saudi Arabia	5.30%
India	17.70%
European Union	35.70%
Belgium	47.90%
Sweden	49.80%

Includes direct & indirect tax collections

VAT is mostly based on destination principle. It is anticipated that GCC will move towards unified VAT regime sooner or later and will adopt destination principle in VAT. The destination principle states that consumption of all goods in one destination should be subject to the same tax, irrespective of the origin of their production. This principle removes tax distortions on competition between goods on the consuming country's market. The goods compete on equal tax conditions and this principle does not interfere with the location of production. It is widely accepted in international trade relations even though it requires the existence of fiscal frontiers among countries.

VAT – Preparedness

Regulator Preparedness: Regulatory body's preparedness is the most essential in the implementation of VAT. Policy document needs to state clearly the objective, methodology, mechanism and framework. The two countries that recently implemented VAT in the GCC adopted simplified VAT framework and laid down laws regulating the collection and claim mechanism. The focus was on collection of taxes. Since the draft law came out, there have been few key modifications to the law which include GCC implementing states not getting any special tax treatment and being treated like any other export or import. Computation of liability, adjustment of input credits and filing of returns is clearly laid out and lays out the path for high level of automation / digitization.

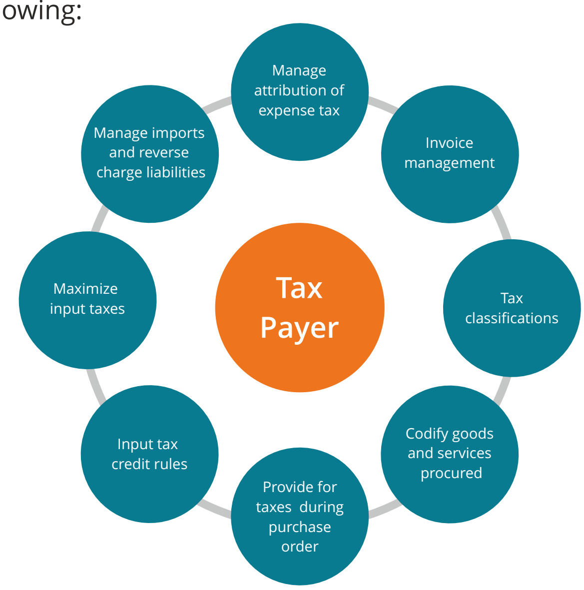
Industry Preparedness: Majority of the tax collectors are going to the industry players. Whether it is retail chains, manufacturers, financial institutions or small and medium enterprises, they are going to collect and pay taxes. Their preparedness is quite an essential part of overall VAT implementation. Preparedness ranges from knowledge preparations, software upgradations, accounting changes, customer communications, registrations, auditing, return filing etc.

Tax Payer Preparedness: Tax payers are consumers, they need to prepare in terms of understanding how VAT will impact them either as an additional expenditure or as some adjustments to the expense taxes. Accounting for taxes is a major change in business house books in GCC, so adapting to proper accounting and moving to organized trade is a key step towards VAT adoption.

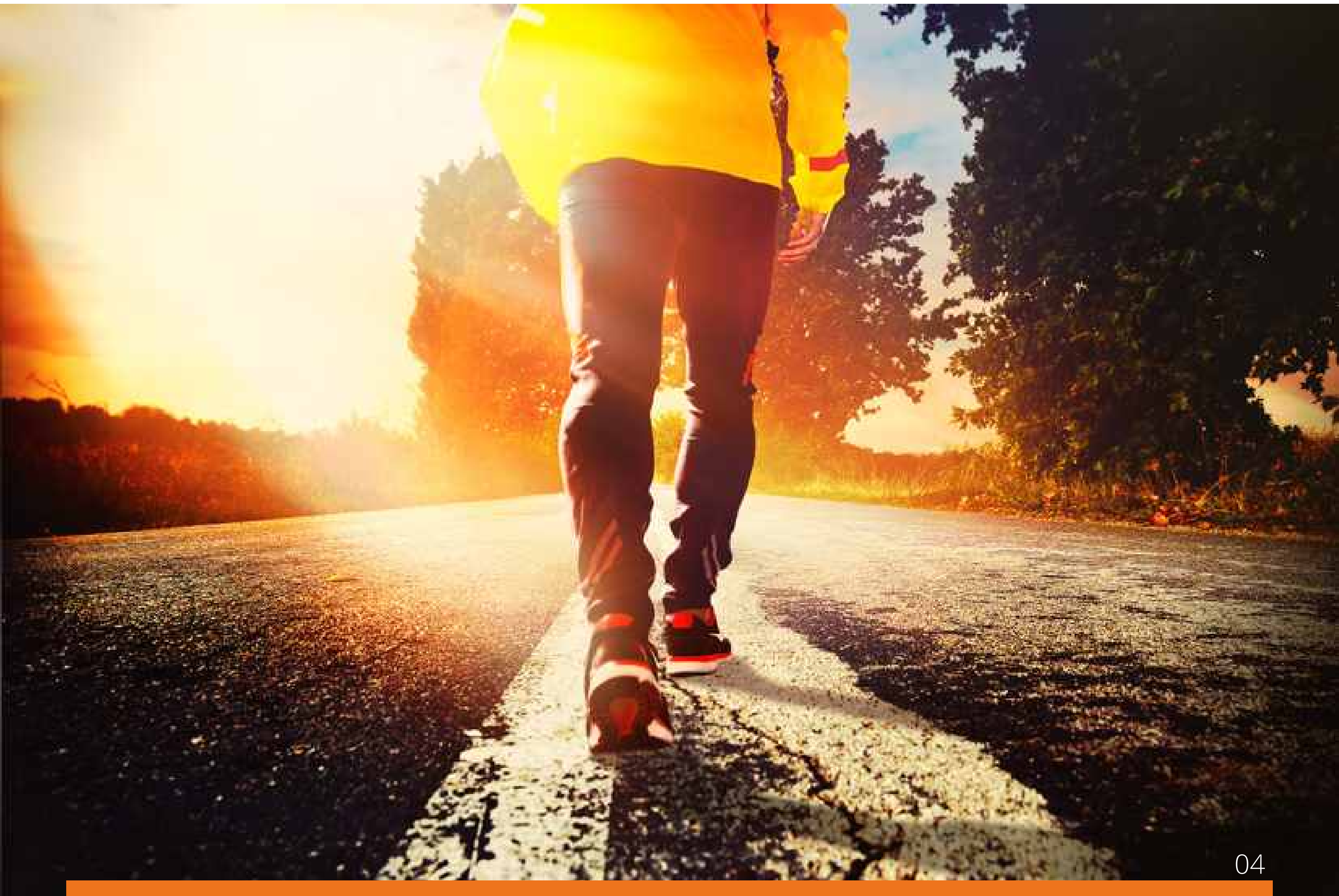
VAT – Journey

Tax Collectors need to carefully plan steps to achieve VAT compliance. A strong software partner could help in flawless implementation as the guidelines are quite set in UAE & KSA. It is important for tax collectors to do the following:

Tax Payers also need careful planning to maximise benefits in an additional expenditure situation. Again, a strong software partner to implement best practices on attribution will help the tax payer make most of the expense. It is important for the tax payer to do the following:



The above preparation will ensure a proper tax return can be generated and filed. An end to end indirect tax software application will help the tax payer to effectively account for taxes, claim inputs and file returns in the most digital way.



GST Journey

The GST introduced in India is not greatly relevant to GCC as the complexities are quite different. India is used to indirect taxes and, for long, has practised VAT [for goods] & Service charges [for services] and host of other indirect taxes. However, the challenges a market such as India throws to both software and compliance teams is immense and useful for implementing tax regulations in newly adopting countries. India's GST went live on 1st July 2017, and marked the unification of 17 indirect taxes into one common tax called GST. Though India continues to have VAT on few products, rest of the goods and services have been migrated to GST. India records INR 100,000 Crore in GST collection every month, which contributes to approximately 10.5% to the GDP of the nation.

The challenges

The Goods & Services Tax in India is a comprehensive, multi-stage, destination-based tax that is levied on every value addition. It replaced many indirect taxes in India previously set and levied by individual states by centralising them. Institutions, specifically Financial institutions are not used to Federal and State tax structures as service tax was a federal tax and there was no large concept of input tax credit.

The entire GST law – the federal and state law- had to be interpreted well and businesses had to register based on maximisation of credit based on output generated. There was tremendous challenge in accounting books, due to movement of all indirect income to cash based income, as the GST Tax was on accrual of services. There was a techtonic shift in the country and most of the business houses had to create a proper book and get into organized trade of issuing and receiving invoices for goods and services.

Lessons learned

- A flexible solution is crucial as governments tend to change the legislation frequently and its implementation both before and after it officially enters into force.
- Businesses need a centralized platform to achieve compliance, tax segregation, accounting, invoicing and manage exemptions.
- Compliance and implementation of GST/VAT is challenging for all businesses but turning to modern digital solutions will undoubtedly benefit customers and enterprises alike.

VAT in United Arab Emirates & Kingdom of Saudi Arabia

The challenges

VAT as a concept is quite new to the region and, like many countries, the impact assessment took more time leaving little time to software application changes. Though the Unified Agreement for Value-Added Tax provides the framework for the operation of VAT across the GCC, it was deferred for implementation. This deferment made each GCC member country formulate their own strategy for VAT.

Financial service organizations in specific faced tremendous challenges as many business systems were procured and each of these systems was providing services for which indirect income was being made. A uniting software application was seldom seen and an over the top Tax engine was well adopted.

Lessons learned

- **Rules of registration** – Individual and Group registration. Group registration as a concept is quite unique to the region as group companies share input and output taxes.
- **Tax codification** - Tax determination, though appeared simple, had multiple dimensions such as VAT implemented countries, Minimum retail price for fee, Tax inclusive of charges etc. These make the implementation quite challenging. A flexible software application that will be a rule configurator was the need of the hour.
- Managing Cross-border transactions and segregation of intra and inter GCC country transactions require a granular view of data in order to adapt easily to different legislations, specific trade zones and specific supplies.
- Ability to analyse and locate specific data while quarantining a specific portion is invaluable for businesses to have close control over their operations.
- Reporting of VAT needs to be as flexible as possible, and data needs to be managed very closely, as it is frequently subject to change.
- As the VAT regulation will have a negative impact on the revenues and profitability, banks have a challenge ahead of them in terms of bridging these gaps. For this, they have to adapt to new innovative products and offers to compensate for the additional expenses. Product offers and services must be analysed to identify the impact of the service and to ensure minimal rework for the bank.
- A quick adaptation of the new billing of goods and services is also crucial to make the impact and the proportion of VAT understandable.
- To ensure business continuity and avoid unnecessary delays, organizations should work with a middle layer solution to collate all VAT-related transactions instead of overhauling their core systems to be VAT compliant.

Taking the first steps of your VAT journey

What you need to start doing now – the MADE principle:

More detailed steps:

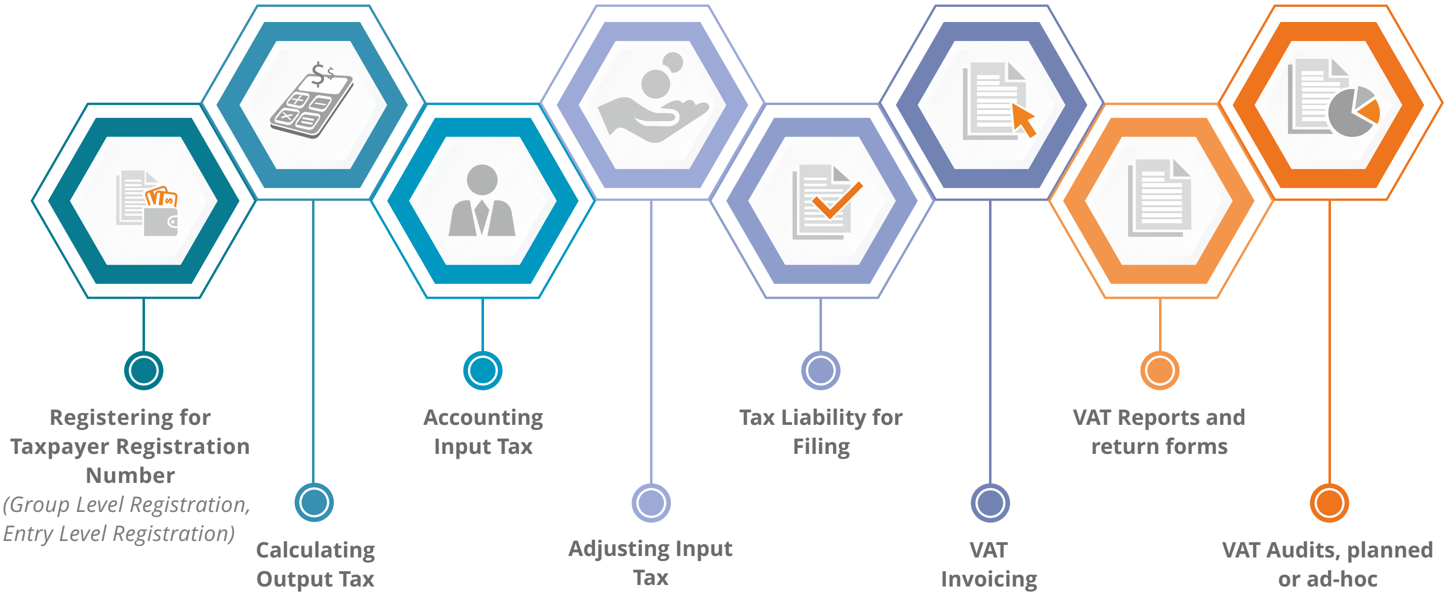
- Early engagement with tax consultants to analyse the impact of VAT on the organization, to finalize the business requirement, and to determine the impact area
- Advance resource planning and allocation of a dedicated team to execute the VAT compliance : Tax officer, Business, Operations, and IT
- Decision on in-house or off-the-shelf product from proven vendor
- Financial institutions and other organizations need to realign their processes, while considering the impact of VAT
- Define a roadmap for the solutions impacted, to cover analysis of upgrades or changes
- Cover the price of compliance by having complete visibility of the cost and allocation of sufficient budgets
- Identify a flexible and proven vendor with domain expertise who can be a strategic partner with the organization
- Regularly interact with Ministry of Tax to obtain and understand the legislations being introduced and obtain clarifications around VAT
- Educate employees, vendors and customers well in advance and make them aware of their role and responsibilities. This step is crucial to make sure everyone understands how much VAT will impact goods and services. It needs to be explicitly clear throughout the organization and be made clear to customers as well.

Meet your checkpoints

Each GCC country will implement individual national legislation outlining all the necessary requirements for VAT compliance.

Organizations need to know what they are expected to do and how VAT will affect them. These checkpoints will help them understand what they need to factor in their budget and organizational processes.

What to prepare for:



But businesses should also factor in:

- International Trade considerations
- Numerous import and export regulations
- Other government related requirements
- Intra and inter-GCC transactions

These extra factors should not be neglected. In the UAE, on the 28th December 2017, only three days before the VAT compliance deadline, the Central Bank published a mandate to all Financial Institutions, asking them not to charge extra for VAT as it had to be inclusive in the current price list of their products and services. This example shows why banks need a centralized tax engine with the flexibility and agility to adapt to new regulatory demands quickly.

The data obstacles you will encounter on the road to compliance

All organizations will face challenges while implementing VAT and should be aware of them before planning for compliance.

Why data management is crucial to solve VAT issues:
In order to be compliant to the VAT regime on time, avoid reputational risks and monetary losses due to penalties. Businesses need to have the right data management tools that will allow them to be compliant in the time allotted by local governments.

VAT can be prone to bring in quick and unpredictable changes that require data to be changed overnight to comply with new laws. Businesses should have flexible systems that can cope with the inevitable multiple evolutions of VAT. Data must be managed efficiently so that customers can be accurately informed of the variations in the prices of goods and services at any time.

With the right tools, efficient data management can turn VAT into an opportunity. It can help businesses take advantage of tax adjustments to improve cash flow, gain a better vision of customer data, and have better transparency through getting a complete view of their data.

Asset deployment challenge:
With components being hard-coded as well as quite dated on some occasions, compliance is a risk from a time and commercial perspective that might cause businesses to stop functioning and incur considerable revenue loss. To meet compliance requirements, businesses need to deploy assets to solve the compliance challenge, which could mean a slowdown in affairs and expenses.

These assets could be an overhaul of core IT systems, bringing on new processes, on-boarding new staff and customers, or sending new marketing assets to inform the customers of the changes. The range of these assets is broad and depends on the needs of the organization. The assets also need to be deployed in the time allotted by each government in order to avoid fines and penalties. This is a strenuous challenge for anyone in charge of operations.

Resource and competence challenge:
VAT might require vast resources not immediately available to some companies and this might put crucial projects on hold. It will also be a challenge to find people with the right skill sets to combine the knowledge of VAT issues with technical nous.

As an important strategic decision, organizations facing these challenges should assess whether they want to address VAT compliance in house or outsource it.

Two Ways to Comply: Buy or Build?

VAT compliance is a data issue. Both insourcing and outsourcing VAT compliance have merits. The choice depends on businesses' timely accessing resources, changing management processes and having the appropriate technology to comply in time.

Insourcing: the tactical path through building your own solution

- Cut down on on-boarding time, and avoid spending time coaching suppliers about the businesses' objectives and challenges in terms of VAT, or company culture
- Have complete control over data internally, instead of passing it on to a supplier. However, employees may have to spend time and resources on non-core business activities like building new IT processes, testing, on-boarding new team members to fill in the skills gap.
- Reputational benefits: Customers enjoy knowing a company has in-house capabilities to tackle the data challenge and be self-sufficient
- Without a flexible and parameter driven VAT solution, bank will increase dependency on the IT team for any new changes and compliance related requirements. Centralized tax engine delivered in a productized approach will cater to immediate and future needs of the banks to comply the regulation.
- Any changes done to core processing systems will be tactical in nature and will not support long term strategic needs of the bank. As changes are introduced to the GCC VAT, this becomes a continuous development cycle for the bank
- Best option for companies which have a lack of expert knowledge on VAT intricacies from an implementation perspective and which can allocate vast amounts of resources to VAT compliance .

Outsourcing: the strategic path through a centralized tax engine

- Most financial institutions are using multiple specialized solutions for their daily operations and the introduction of VAT will call for changes in all of these systems. With a purpose-built, off-the-shelf centralized tax engine, the impact to these systems will be reduced, as well as limiting the expenses allocated for the development and change requests
- Changes made in multiple systems will increase multiple vendor dependencies in getting resource or competencies. This could delay VAT compliance. A platform-agnostic centralized tax engine can reduce this risk significantly. Centralizing tax rules reduces duplication and helps VAT compliance validations to be maintained at multiple systems of the bank and thus enables quick turnaround time
- With a centralized VAT engine, bank can decouple rich and complex functionality of VAT from core processors. This will ensure banks are not impacted by degraded performance of core banking transaction solution and run their day to day operations smoothly
- A centralized tax engine will act as a single source of truth, helping banks to provide complete transparency and traceability of VAT transactions
- A local VAT specialist can be hard to find in GCC countries and hiring one from abroad might be costly and time-consuming. Outsourcing can save businesses from the HR headaches of such difficult hires
- Have dedicated specialists for VAT and taxation issues looking at your problem 24/7 and maximize return on core competencies.
- The fastest road to deployment is by handing over the compliance process to experts, who already have field-tested and time-tested processes in place. This is much faster that building them from the ground up.
- Best option if you lack internal resources and if you want a long term compliance plan

Conclusion

VAT compliance is a major challenge to organizations, not only in India and GCC but globally. Firms need to be aware of the regulations specific to their country and examine the implications of implementing VAT. While adhering to such formalities is critical, it is only the tip of the iceberg. It is in the long-term interest of the organizations involved to deploy the correct technology and tweak their IT framework to account for VAT. It can help businesses take advantage of any impending tax regulatory changes and enable them to improve revenue and gain an analytical view of consumer transactions and data. To be prepared, companies need to be proactive to the changes in regulatory law and practices, and simultaneously adapt their knowledge and internal processes. This will ultimately help them do away with out-of-the-blue huge investments of time, effort and resources, while simultaneously decreasing the chances of manual error. The ones prepared for the future will be the ones primed and ready to ensure greater efficiency and transparency in transaction tax compliance.

Acknowledgments:

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About SunTec

At SunTec Business Solutions, we help our clients increase the lifetime value of their customer relationships through effective revenue management and real-time customer experience orchestration. We are the leading provider of experience orchestration solutions not only to financial services but also digital and communications services industries. With a legacy of deployments in 45+ countries, SunTec is a trusted partner of the world's leading banks and digital and communication service providers. Headquartered in India, we have our offices in USA, UK, Germany, UAE and Singapore.

With a team of highly skilled folks and our highly innovative product development models, we help our clients to always remain at the cutting edge of technology. A stable, mature and flexible product suite, Xelerate® is benchmarked regularly for optimum performance. Coupled with insights from our industry experts and a robust future-ready roadmap, Xelerate® continues to develop along with the market. Able to seamlessly integrate with any ecosystem, it is one of the fastest products to implement.

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