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1. Charities guidance - Overview

1.1. Overview

1.1.1. Short brief

VAT has been introduced with effect from 1 January 2018 in the UAE. As a general consumption tax on the supply of goods and services, its effects must be understood by charities in the UAE in two contexts:

- its application to the activities of all charities; and
 - the approach that should be taken by charities in the UAE when determining the amount of VAT on costs (i.e. input tax) which they are eligible to reclaim, specifically where they are engaged in both business and non-business activities (for example, such as where they provide goods or services without charging for these). In particular, certain charities in the UAE will be treated as designated charities. Where designated in that manner, designated charities will be entitled to recovery of VAT under a special regime.
- #### 1.1.2. Purpose of this document

This document contains guidance about the characteristics of a charity which must be present in order for it to qualify as a designated charity for VAT purposes. In addition, this document provides guidance for charities seeking to understand which of the services they provide are business activities and which are non-business activities, and in turn, the extent to which VAT recovery on costs is possible.

1.1.3. Who should read this document?

This document should be read by key stakeholders in charities who are responsible for tax matters. It is intended to be read in conjunction with the Taxable Person Guide for Value Added Tax.

1.1.4. Status of the document

In this guide, Federal Decree-Law No. 8 of 2017 on Value Added Tax is referred to as "Decree-Law" and Cabinet Decision No. 52 of 2017 on the Executive Regulations of the Federal Decree-Law No. 8 of 2017 on Value Added Tax is referred to as "Executive Regulations". This guidance is not legally binding on the FTA but is intended to provide assistance in understanding and applying the VAT legislation as it applies to charities. This guide is issued in accordance with Article 73 of the Executive Regulations and provides general guidance concerning the application of the Decree-Law and Executive Regulations in respect of charities in the United Arab Emirates.

This guide does not deal with all the legal detail associated with VAT and is not intended for legal reference. For details in respect of the general operation of VAT, refer to the Taxable

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Person Guide – Value Added Tax which is available on the Federal Tax Authority (FTA) website (www.tax.gov.ae).

The Federal Law No 7 of 2017 on Tax Procedures and Cabinet Decision No 36 of 2017 on the Executive Regulation of Federal Law No 7 of 2017 on Tax Procedures (collectively referred to as TP Law) regulates the administration of all Federal tax laws in the UAE. This law applies to tax procedures related to the administration, collection and enforcement of tax by the FTA.

The VAT Decree-Law and Executive Regulations must therefore be read together with the provisions of the TP Law (for example both the TP Law and VAT Decree-Law contain requirements in respect of record keeping which must be complied with). This guide must therefore be read in the context of the TP Law and any Cabinet Decisions and other official publications issued in connection with any general tax procedure matter.

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2. Charities

2.1. Charities and their activities

2.1.1. VAT treatment of charities

VAT is a general consumption tax imposed on most supplies of goods and services in the UAE. In that respect it will, by default, be chargeable on goods and services supplied by charities in the UAE where the charity is registered for VAT. Charities will therefore be subject to the usual rules of VAT regarding the making of supplies. For further details on the general VAT rules, please refer to the Taxable Person Guide for Value Added Tax. 2.1.2. Business activities for VAT purposes

Charities will typically make a mixture of supplies of goods and services with differing VAT liabilities. Where such goods and services are supplied for a charge, this is a business activity which may result in the making of a taxable supply for VAT purposes and VAT will have to be charged where the charity is considered to be a taxable person. The charity will be able to recover VAT on costs which directly relate to onward activities which are liable to VAT, subject to the normal VAT recovery rules applicable to all businesses. 2.1.3.

Donated goods and services

In the normal course of their operation, charities often receive donations of goods and services and may then use these as part of their onward provision of charitable activities. Where these activities are undertaken, and a charge is made, this is also a business activity for VAT purposes and VAT may be required to be charged. Since the relevant goods or services would be received by a charity free of charge, the charity will not have incurred any costs in relation to these and accordingly, there will be no VAT on costs to recover in such circumstances. All charities must comply with the Decree-Law No. 20 of 2018 and its Implementing Regulation Cabinet Decision No. 10 of 2019 as well as any Guidelines issued by the UAE Central bank on Anti-Money laundering and combating the Financing of Terrorism and Illegal organizations. 2.1.4.

Non-business activities for VAT purposes

Where an activity is performed by a charity that is acting in its charitable capacity ("relevant charitable activity"), and it makes no charge for the supply of goods or services concerned, the activity would ordinarily not be treated as being liable to UAE VAT as there is no charge, unless the supply is treated as a deemed supply (please see below). 4

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2.1.4. Non-business activities for VAT purposes

Where an activity is performed by a charity that is acting in its charitable capacity ("relevant charitable activity"), and it makes no charge for the supply of goods or services concerned, the activity would ordinarily not be treated as being liable to UAE VAT as there is no charge, unless the supply is treated as a deemed supply (please see below).

It is worth noting that in some cases the relevant charitable activity will be subsidised by grants or donations. Provided the grantor is not entitled to any benefit in return for the grant or donation (beyond a simple acknowledgement), no VAT would be chargeable as this is not a supply for consideration.

Ordinarily, no VAT on direct costs incurred to receive such free provision of goods and services would be recoverable by the charity in such circumstances. However, certain designated charities will be entitled to recover VAT relating to their relevant charitable activities where they make such free provision of services and goods under a special VAT refund scheme.

In some instances, it might be required for a taxable person to account for output tax even though no supply of goods or services was actually made for consideration by that person. In this regard, the Decree-Law and Executive Regulations specifically make provision for certain supplies to be deemed to be made by the taxable person. Such deemed supplies are generally subject to VAT at the standard rate but can also be subject to VAT at the zero rate, depending on the circumstances.

Since activities of the charities often require goods and services to be given away or used for non-business purposes, charities have to consider whether the deemed supply provisions could apply. 1 The following common situations may trigger deemed supplies:

- Where there is a supply of goods or services for which input tax was recovered

(in full or partially) but the goods or services were used, in part or whole, for non-business purposes; and

- Where there is a supply of goods or services for no consideration, where those

goods or services formed whole or part of assets of a taxable person but are no longer considered to be as such, for example if there was a change in use of the asset.

For purposes of the above, the FTA considers a broad interpretation of the term 'business' for VAT purposes which may include a charity using goods and services within the terms of its charitable activity. Therefore, where goods or services are used for such charitable purposes – e.g. property made available for free for events or kitchen appliances used in providing free meals – then this is not a deemed supply for VAT purposes if the relevant goods and services remain part of the assets of the charity.

If the charity claims VAT in respect of the acquisition of goods and then gives the goods away for free, the supply will be treated as a deemed supply for VAT purposes if the charity recovered input tax in respect thereof. For example, where a charity has purchased food and then donated it to the poor, the charity should account for the

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Article 11 of the Decree-Law. 5

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output tax on the deemed supply of the food if the charity recovered input tax when the goods were acquired. The deeming provision will, however, not apply if:

- Input tax was not recovered on the relevant goods or services;
- The supply is exempt from VAT;
- The refunded input tax on the goods and services is amended according to the

Capital Assets Scheme;

- The value of the supply of goods used as samples or commercial gifts does not

exceed AED 500 per recipient within a 12-month period; and

- The total of output tax payable on all deemed supplies made by the charity is less

than AED 2,000 over a 12-month period. 2.2. Designated charities

It is important to distinguish between designated charities and other charities as designated charities benefit from special VAT recovery rules which are discussed in more detail in Chapter 3 of this guide. A charity needs to meet the following criteria⁴ to be recognised as a designated charity for VAT purposes:

1. The charity must be

a. approved by the Ministry of Community Development to carry out a charitable

activity in the UAE as a designated charity, or

b. established as a charity under Federal or Emirate Decree, or

c. otherwise licenced to operate as a designated charity by an agency of the

Federal or Emirate Governments authorised to grant such licences, with its objectives including for instance, advancing health, education, public welfare, religion, culture, science, and similar activities;

2. The charity must operate within the terms of any approval, licence or other

authorisation which has been granted by the aforementioned bodies in respect of its charitable activities;

3. The charity must operate on a not-for-profit basis;

4. The charity must be funded primarily by means of grants or donations.

With reference to the above criteria for designated charities under criteria 1(a) and (c), the following will be considered by the Ministry of Community Development or other relevant government entity (Federal or Emirate level) in deciding whether to approve the charity as a 'designated charity':

- The charity only performs the charitable activity it has been licensed to perform

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Article 5 of the Executive Regulations.

3

See Article 46 of the Decree-Law for a list of supplies that are exempt from VAT.

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Charities in the UAE include societies and associations of public welfare, cultural awareness and similar.

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4. The charity must be funded primarily by means of grants or donations. With reference to the above criteria for designated charities under criteria 1(a) and (c), the following will be considered by the Ministry of Community Development or other relevant government entity (Federal or Emirate level) in deciding whether to approve the charity as a 'designated charity':

- The charity only performs the charitable activity it has been licensed to perform

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Article 5 of the Executive Regulations. 3

See Article 46 of the Decree-Law for a list of supplies that are exempt from VAT. 4

Charities in the UAE include societies and associations of public welfare, cultural awareness and similar. 6

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- The charity is not involved in undertaking trading activities. Trading activities that

are undertaken in the course of carrying out the licensed activities (sales) are disregarded provided such activities do not derive any profit or profit derived is applied for the purposes of the charitable activity; and

- The charity must be managed by 'fit and proper persons'.

The 'fit and proper test' is aimed at trustees of charities (including directors of corporate trustees⁵), directors of corporate charities, any employees of a charity and volunteers who act on behalf of a charity. Examples of factors that may lead to considering a person as not being a fit and proper person are involvement in tax fraud or other fraudulent behaviour including misrepresentation and/or identity theft, involvement in attacks against, or abuse of, tax repayment systems and where the person was previously removed from acting as a charity trustee by a charity regulator or disqualified from acting as a charity trustee or company director. Important: unless the Cabinet decides otherwise, only where a charity meets all the above tests can it be treated as a designated charity. The Cabinet Decision only applies to the entity named and any trading subsidiary set up by a charity will not be included. It should be noted that, in order to benefit from the special recovery rules⁶, designated charities need to apply and register for VAT. Such VAT registration also means that the designated charities will have to charge VAT on all taxable supplies they make. 2.3.

VAT registration of charities

Any charity carrying on a business activity in the UAE and making taxable supplies in excess of the mandatory VAT registration threshold must apply to be registered for VAT purposes. In addition, any charity carrying on a business activity and making taxable supplies or incurring expenses subject to VAT in excess of the voluntary VAT registration threshold may apply to register for VAT purposes. For further details on VAT registration, please refer to the Taxable Person Guide for Value Added Tax on the FTA website. Designated charities need to apply and register for VAT in order to benefit from recovery of input tax, disregarding whether they meet the threshold or not. 5 If the trustee is a corporate entity, the directors of that entity must meet the 'fit and proper person'

test. 6

Article 57 of the Decree-Law. 7

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excess of the mandatory VAT registration threshold must apply to be registered for VAT purposes.

In addition, any charity carrying on a business activity and making taxable supplies or incurring expenses subject to VAT in excess of the voluntary VAT registration threshold may apply to register for VAT purposes.

For further details on VAT registration, please refer to the Taxable Person Guide for Value Added Tax on the FTA website.

Designated charities need to apply and register for VAT in order to benefit from recovery of input tax, disregarding whether they meet the threshold or not.

5 If the trustee is a corporate entity, the directors of that entity must meet the 'fit and proper person'

test.

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Article 57 of the Decree-Law.

Furthermore, charities may register with other entities as a tax group. However, it is important to note that a designated charity may only form or join a tax group comprising of other designated charities.⁷

2.4.1. VAT treatment of sales or leases of new buildings to charities

The first supply of a new building or part of a building will be subject to VAT at the zero rate where the following conditions are met:

- It must be the first supply of that building. Subsequent supplies are taxable at

the standard rate (if it is not residential);

- The building, or part thereof, must be specifically designed to be used by the

charity solely for its relevant charitable purpose: this means the building must have been designed specifically with the charity as the tenant in mind and for its own use (for example it cannot simply be an office building built speculatively that a charity then chose to occupy);

o an activity other than for the purpose of profit or benefit to any proprietor,

member, or shareholder of the charity; and

o one which is undertaken by the charity in the course or furtherance of its

charitable purpose or objectives to carry out a charitable activity in the UAE as approved by the Ministry of Community Development, or under the conditions of its establishment as a charity under Federal or Emirate Decree, or as otherwise licensed to operate as a charity by an agency of the Federal or Emirate Governments authorised to grant such licenses.

Such charitable purposes and objectives include but are not limited to: advancing health, education, public welfare, religion, culture, science and similar activities.

Where the conditions for zero-rating outlined above are not met, the first supply of a new building or part thereof will be liable to VAT at the standard rate unless it qualifies as a residential building, in which case the special rules applicable to residential buildings would apply.

Subsequent supplies of buildings or parts thereof to be used for relevant charitable

purposes will also be subject to their normal VAT rate.

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Article 10(5)(e) and (6) of the Executive Regulations.

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Article 10(5)(e) and (6) of the Executive Regulations.

It is therefore possible that the first rent instalment for a building may be zero-rated
while subsequent periods are exempt from VAT in the case of a residential building.⁸
Since designated charities can recover VAT under the special refund rules, the relief
acts largely as a cash-flow benefit in preventing a large amount of VAT being charged
to the charity on the purchase of a building.

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It is therefore possible that the first rent instalment for a building may be zero-rated while subsequent periods are exempt from VAT in the case of a residential building.⁸ Since designated charities can recover VAT under the special refund rules, the relief acts largely as a cash-flow benefit in preventing a large amount of VAT being charged to the charity on the purchase of a building.

Please refer to the Real Estate VAT Guide (VATGRE1) for more information in this regard.

8 Article 26 of the Executive Regulations, read with Article 38 of the Executive Regulations.

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3. VAT recovery rules for charities

3.1. Overview

A charity may be making taxable supplies and also undertake non-taxable activities. The VAT incurred in respect of taxable supplies will generally be recoverable under the normal rules. Input tax will therefore not be recoverable where recovery is explicitly blocked in accordance with Article 53 of the Executive Regulation or where the goods or services were used to make exempt supplies.⁹ The remaining VAT may be recovered by designated charities under the special refund rules applicable to such charities. Consequently, a charity needs to apportion VAT incurred when making both taxable and exempt/non-business supplies (mixed-use costs) so that only the appropriate portion of the VAT can be recovered (see sections 3.2 and 3.3). Important: in all cases, VAT which is specifically blocked from recovery under the VAT Law cannot be reclaimed, regardless of whether the body concerned is a Designated Charity or otherwise. 3.2. VAT recovery by charities which are not designated charities

Charities that are not designated charities are subject to the normal VAT recovery rules.

What this means is that VAT is generally only recoverable to the extent it relates to taxable supplies. Therefore, where a charity which is not a designated charity incurs VAT in respect of activities which do not generate taxable supplies, the related VAT will not be recoverable. Likewise, where a charity incurs VAT which relates to exempt supplies this VAT is also not recoverable. Charities will therefore be required to allocate and apportion VAT incurred between taxable activities (recoverable) and non-taxable activities / exempt activities (non-recoverable). The following standard input-based apportionment method¹⁰ must be applied where a non-designated charity makes both taxable and non-taxable supplies:

3.2.1 Step 1: Direct attribution

In all cases, in each tax period, all input tax which can be wholly attributed to any particular supply must be attributed to that supply and either recovered or blocked from

9 Article 57 of the Decree-Law. 10 Article 55 of the Executive Regulations. 10

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recovery depending on whether the supply is wholly taxable or wholly exempt or does not relate to the making of taxable supplies. This is referred to as direct attribution. For example, a non-designated charity may incur

- legal fees in respect of setting up a new facility from which to provide free services

to its beneficiaries.

The input tax would be non-recoverable as it relates to free services ('non-taxable' activities). • VAT on goods that it purchases to sell on, in order to raise charitable funds. The

VAT is recoverable since VAT will be due on the sales of the goods (taxable activities). • legal fees associated with the sale of bare land, where the related VAT cannot be

recovered, as it relates to the making of exempt supplies. (The supply of bare land is exempt from VAT)¹¹

- annual audit fees which relates to all the activities of the charity and therefore only

a portion of the VAT may be recovered – refer to step 2 below. Any input tax which cannot be wholly attributed in this manner must be apportioned using an approved apportionment method in order to establish to what extent input tax may be recovered. A charity must use the standard input tax apportionment method to apportion input tax between exempt use and taxable use (see step 2 below), unless and until the charity submits a request for a special apportionment method and the FTA approved the method in writing. Refer to the Input Tax Apportionment: Special Methods VAT Guide (VATGIT1) for more information.

3.2.2 Step 2: Allocation of the residual input tax via the standard method

The charity is required to distinguish between taxable, exempt and non-taxable use during each tax period. All input tax that cannot be wholly attributed under step 1 ('residual input tax' or R) must be apportioned as follows:

1. Determine the recovery ratio as a percentage:

Input tax incurred in the tax period which is wholly attributable to the making of taxable supplies (T)
$$\frac{T}{T + \text{Input tax incurred in the tax period which is wholly attributable to the making of non-taxable supplies}}$$

2. The resulting figure is expressed as a percentage and rounded to the nearest

whole number. Apply the recovery ratio percentage to the residual input tax:

$$\text{Residual} \times \text{Recovery Ratio \%} = \text{Proportion of residual attributable to supplies for which input tax is recoverable (R2)}$$

3. Treat the proportion of the residual which is attributable to taxable supplies as

recoverable (and include in the tax return for the tax period in which the calculation was undertaken).

4. The total recoverable input tax = T + R2.

¹¹ Article 46(3) of the Decree-Law.

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red in the tax period which is wholly attributable to the making of taxable supplies (T)
T + Input tax incurred in the tax period which is wholly attributable to the making of non-taxable supplies

2. The resulting figure is expressed as a percentage and rounded to the nearest

whole number. Apply the recovery ratio percentage to the residual input tax:

Residual x Recovery Ratio % = Proportion of residual attributable to supplies for which input tax is recoverable (R2)

3. Treat the proportion of the residual which is attributable to taxable supplies as

recoverable (and include in the tax return for the tax period in which the calculation was undertaken).

4. The total recoverable input tax = T + R2. 11 Article 46(3) of the Decree-Law. 11

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Annual adjustment

In the first period following the end of the previous tax year, a calculation for the whole of the preceding tax year should be carried out, using the same principles as above. This is known as the 'annual adjustment' and may render an increase or a decrease in the amount of input tax previously treated as recoverable on a quarterly or monthly basis under (3). The required adjustment should be included in the return submitted for the first tax period following the end of the relevant tax year. Please refer to VATGIT1 for further details. The annual adjustment should not be used to correct errors as there is a specific

mechanism available to do so. Please refer to the Voluntary Disclosure User Guide for more information. 3.3.

VAT recovery by a designated charity

A designated charity may recover VAT on any expenses¹² incurred provided

- The expenses do not relate to exempt supplies made by the charity or
- The recovery of input tax related to those expenses are not specifically "blocked"

from recovery.¹³

Therefore, where a designated charity is not engaged in exempt activities, it may treat all VAT incurred on costs as fully recoverable unless the VAT is explicitly blocked from recovery. However, where the designated charity carries on activities which allow for VAT recovery and also exempt activities, it needs to apportion VAT incurred between those activities so as to accurately determine the recoverable amount of input tax. Similar to charities which are not designated charities, the first step is to do a direct attribution of input tax incurred in the tax period. • Input tax which is wholly attributable to supplies allowing VAT recovery (such

as taxable supplies) (T) may be recovered in full. • Input tax which is wholly attributable to exempt supplies (E) may not be

recovered.

- Input tax which is attributable to other non-taxable supplies / activities (C) may

be recovered in full due to the special VAT recovery scheme. Following the direct attribution, the designated charity would need to apportion input tax which cannot be directly attributed, i.e. residual VAT incurred on mixed expenses.

1. The remaining input tax is non-attributable, or "residual" (R). It is necessary to

calculate that which is partly attributable to activities which allow for VAT recovery

- 12 Article 57(2) of the Decree-Law.
- 13 Article 53 of the Executive Regulations.

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as taxable supplies) (T) may be recovered in full.

- Input tax which is wholly attributable to exempt supplies (E) may not be recovered.
- Input tax which is attributable to other non-taxable supplies / activities (C) may be recovered in full due to the special VAT recovery scheme.

Following the direct attribution, the designated charity would need to apportion input tax which cannot be directly attributed, i.e. residual VAT incurred on mixed expenses.

1. The remaining input tax is non-attributable, or “residual” (R). It is necessary to calculate that which is partly attributable to activities which allow for VAT recovery

12 Article 57(2) of the Decree-Law.

13 Article 53 of the Executive Regulations.

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and that which is attributable to exempt activities. The following calculation should be carried out for each tax period:

T+C

T+C+E

The resulting figure is expressed as a percentage and rounded to the nearest whole number. This percentage is applied to the total residual input tax (R) for that tax period to calculate the recoverable input tax (R2) for that tax period.

2. The total recoverable input tax = T + C + R2.

Annual adjustment

In the first period following the end of the previous tax year (this will vary depending on the charity's tax periods), a calculation for whole of the preceding tax year should be carried out, using the same principles as above. This is known as the 'annual adjustment' and may render an increase or a decrease in the amount of input tax previously treated as recoverable on a quarterly or monthly basis under (1). The required adjustment should be included in the return submitted for the first tax period following the end of the relevant tax year. Refer to the Input Tax Apportionment: Special Methods VAT Guide (VATGIT1) for more information.

The annual adjustment should not be used to correct errors as there is a specific mechanism available to do so. Please refer to the Voluntary Disclosure User Guide for more information.

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4. Cabinet Decisions - Designated charities

To date, there have been five Cabinet Decisions listing designated charities, namely:

- Cabinet Decision No. 55 of 2017 on Charities that May Recover Input Tax;
- Cabinet Decision No. 15 of 2018 on Amending the List of Charities Annexed to the Cabinet Decision No. 55 of 2017 on Charities That May Recover Input Tax.
- Cabinet Decision No. 46 of 2018 on Amending the List of Charities Annexed to the Cabinet Decision No 55 of 2017 on Charities That May Recover Input Tax (effective from 14 October 2018).
- Cabinet Decision No. 25 of 2019 on Amending the List of Charities Annexed to the Cabinet Decision No 55 of 2017 on Charities That May Recover Input Tax (effective from 1 April 2019).
- Cabinet Decision No. 13 of 2020 on Amending the List of Charities Annexed to the Cabinet Decision No 55 of 2017 on Charities That May Recover Input Tax (effective from 2 March 2020).

Please refer to the updated list of Designated Charities on www.tax.gov.ae.

5. Updates and amendments

Date of amendment: April 2020 | Amendments made: • Insert new Section 1.1.4 Status of guidance and Section 1.1.5 dealing with tax procedures.

- Rephrased Section 2.1.5 Deemed supplies.
- Added detail to Section 2.2 Designated charities to include criteria for applying to be recognized as designated charity.
- Rephrased Section 3.1 Overview.
- Rephrased Section 3.2 VAT recovery by charities which are not designated charities.
- Rephrased Section 3.3 VAT recovery by designated charities.
- Updated Section 4 to include latest Cabinet Decisions relating to designated charities.

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