

Bahrain VAT - Reimbursement or disbursement?

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Background

As per the Bahrain VAT Executive Regulations, where a taxable person incurs an expense in his name and subsequently recharges the expense to another person, such recharge will be taxable. However, where the expense is incurred directly in the name of the other person, recovery of such expense by the taxable person from the other person will be outside the scope of VAT. Many businesses incur expenses on behalf of their customers as well as related parties. Therefore, it is critical to examine the following:

1. Do you know the VAT treatment of billing those costs to your customer/related party?
2. Should the cost be treated as a disbursement (outside the scope of VAT) or a taxable recharge?
3. If it is a taxable recharge what is the applicable VAT rate?

Taxable reimbursements

Where an expense is incurred directly by a business in the course of making supplies to its customer, the expense should, generally, be treated as a reimbursement subject to VAT. Examples include:

- ✓ ABC Consultants WLL incurs flight and hotel costs in the course of conducting a client engagement and recharges these to its client.
- ✓ ABC Consultants WLL engages a law firm to provide input on a legal point which forms part of the advice it delivers to its client and recharges the lawyers' fees to its client.
- ✓ Parent Company WLL incurs rental costs for the premises occupied by it and its subsidiaries and then recharges the relevant portion to its subsidiaries.

Non-taxable disbursements

Where third-party supplies directly to a customer but a business pays the amount to the third party on the customer's behalf - both the payment to the third party and the repayment by the customer are disbursements and therefore, outside the scope of VAT. Examples include:

- ✓ A customer engages a law firm directly but requests ABC Consultants WLL to pay the legal fees on its behalf.
- ✓ ABC Consultants WLL pays government fees on behalf of its client in relation to a regulatory filing and recharges this government fees to its client.

NBR guidance

As per the guidelines issued by the NBR, in order to determine whether a transaction is a taxable reimbursement or a non-taxable disbursement, a taxable person should consider the following questions:

- ✓ Does the taxable person contract with the supplier in his own name or the contract is between the supplier and the other person?
- ✓ Is the taxable person considered as receiving the goods or services from the supplier?
- ✓ Who is legally liable to pay the supplier, i.e., in default of payment, who does the supplier sue?
- ✓ Who is the "bill to" person on the invoice issued by the supplier? Is the invoice issued in "care of" the taxable person?
- ✓ Does the taxable person record the payment to the supplier as an expense and the refund from the customer as income in his profit and loss account, or does he simply record a receivable in his balance sheet which is credited when the refund is received?

Conclusion

Whilst the above examples and guidance may seem straightforward, in practice not all cases are clear-cut (see above the difference between the two scenarios where a law firm is being engaged) and questions often arise as to whether VAT should be charged at the standard rate, zero rate or should the supply be treated as an exempt supply (see above the example of the Parent Company recharging rental costs).

This document is for general information only and is not intended to address the circumstances of any particular scenario. Please seek professional advice in relation to your particular circumstances.

If you are unclear about how to treat a recharge or disbursement reach out to one of the KPMG Bahrain VAT specialists.

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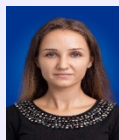
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