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الجهاز الوطني للإيرادات

National Bureau for Revenue

Preface

This guide sets out general principles relating to the concept of an economic activity for VAT purposes.

This guide is intended to provide general information only, and contains the current views of the National Bureau for Revenue (NBR) on its subject matter. This Guide is not a legally binding document, and does not commit the NBR or any other person, including a VAT payer, in respect of any transaction. This document should be used as a guideline only and is not a substitute for obtaining competent legal advice from a qualified professional.

The main principles of the VAT system in the Kingdom of Bahrain are set out in the VAT General Guide issued by the NBR which is available on the NBR's website, www.nbr.gov.bh. This document should be read in conjunction with the VAT General Guide.

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1. Introduction

If a person is carrying out an economic activity in Bahrain, he may be required to register and account for VAT. The purpose of this Guide is to help a person determine whether or not he is conducting an economic activity for VAT purposes.

Generally, one may think of conducting an economic activity as conducting a business, and in many cases, it will be apparent whether a person is conducting an economic activity. However, the VAT Law and Regulations set out specific additional features that will need to be considered to establish the existence of an economic activity.

VATable persons in Bahrain are required to charge VAT on their supplies of goods and services. A VATable person is a Person carrying out an economic activity independently for the purposes of generating income, and who is registered or obliged to register for VAT purposes in accordance with the provisions of the law.

The VAT Law defines “economic activity” as:

“An activity conducted in an ongoing and regular manner for the purpose of generating income, and includes commercial, industrial, agricultural, or professional activities or services or any use of tangible or intangible assets, and any other similar activity.”

The purpose of this Guide is to explain the concept of an economic activity with particular focus on:

- What activities will typically be regarded as comprising an economic activity;
- When an activity is conducted independently;
- When an activity is conducted in an ongoing and regular manner; and
- When an activity will be regarded as being carried out for the purposes of generating income.

This Guide will also discuss when an economic activity starts and ends, and will deal with specific cases where an economic activity is or is not carried out.

Where a person is carrying on an economic activity, he may be required to register for VAT and to comply with other requirements in the VAT Law and its Executive Regulations. The VAT General Guide and the VAT Registration Manual both set out the circumstances when a person (individual or corporate) who is carrying out an economic activity independently for the purposes of generating income is obliged to register for VAT.

2. Indicators of an Economic Activity

As a general introduction and overview, the following indicators may also help to determine whether a person is conducting an economic activity. These indicators are not exhaustive, and should be considered collectively with all relevant facts and in the context of the guidance in this document.

- Profit motive

An activity does not need to be profitable for it to be considered an economic activity. However, the intention to make a profit when conducting an activity may indicate that an economic activity is being undertaken.

- Regular transactions

A one-off, isolated transaction does not usually indicate that an economic activity is being undertaken (although each transaction will need to be considered separately). However regular transactions of the same kind, or character, or conducted in the same way may indicate that an economic activity is being undertaken.

- Quantity of purchases

The quantity or volume of goods purchased may indicate whether a person is carrying out an economic activity. For example, the purchase of goods in quantities which are in excess of those needed for non-business or personal use and have no intrinsic investment value may suggest the existence of an economic activity.

- Financing

The method of financing the activity / transaction may also indicate whether an economic activity is being undertaken. For example, where a loan has been taken to purchase the goods, and can only be repaid by selling the goods, this may suggest the presence of an economic activity.

- Time and effort

Where a person expends considerable time and effort into the sale of goods, including the establishment of a structure to facilitate the sale (e.g. website / advertising), this is likely to be indicative of an economic activity, particularly where the sale of goods is the sole source of income.

- Advertising and promotion

Where a person actively advertises and promotes (e.g. by website) the sale of goods, this may indicate the promotion of an economic activity. However, this would not include the sale of a number of personal items on the internet (e.g. the sale of a table, chairs and TV

cabinet), but would include the ongoing sale of items via an internet sales platform (e.g. eBay / Amazon).

- Transactions relate to an established activity

The person engages in transactions which are related to him or his business' main activity i.e. connections can be drawn between the person and the type of sales/purchases made. An example is a cybersecurity firm purchasing computer monitors.

- Nature of the asset(s)

The nature of the asset(s) acquired may provide an indication of the intent to undertake an economic activity. For example, if assets are acquired for investment purposes, or for personal use and enjoyment, it is less likely that an economic activity is being undertaken. However, where the value of an asset can only be realized by way of a sale / transfer, this is more likely to indicate an economic activity.

3. Types of economic activity

3.1. Types of economic activity in the VAT Law

It is clear from the definition of “economic activity” in the VAT Law that the term should be interpreted widely. The Law includes the following activities as specifically falling within the definition:

- Commercial activities;
- Industrial activities;
- Agricultural activities;
- Professional activities;
- Services or any use of tangible or intangible assets; and
- Any other similar activity.

The above list is indicative and not exhaustive.

3.2. Impact of legal or regulatory requirements

It is not necessary for a person to have certain qualifications or licenses in order to be regarded as carrying on an economic activity. For example, the provision of legal services by a person who is not formally qualified as a lawyer will not prevent this activity from being an economic activity.

An economic activity can still exist where the person carrying out the activity does not have the required legal or regulatory permissions or licenses. For example, if a person manufactures and sells goods without the required commercial registration from the Ministry of Industry, Commerce and Tourism, he will still be regarded as conducting an economic activity.

3.3. Hobbies and private activities

Engaging in hobbies will not normally be regarded as carrying on an economic activity. This will be the case, even where they are conducted in a manner similar to a business as no VATable supplies will be made for consideration.

In some cases, a hobby may involve selling goods to others. Examples include a stamp collector may sell stamps to another collector or a stamp dealer or a collector of classic cars occasionally selling a vehicle to another person. Where there is no organized business of selling the goods and the volume of transactions is not high, it would not be expected that an economic activity is being carried on. However, where sales are made on a regular and frequent basis, the activity could be seen as an economic activity. An activity that starts out as

a hobby could become an economic activity. Ultimately, each situation will need to be looked at on a case-by-case basis, but the following will be relevant:

- Is the activity carried on purely as a hobby and for personal enjoyment, or does the person intend to carry it on as a regular and ongoing activity? If the latter, there is a likelihood that there is an economic activity.
- What is the number and value of transactions carried out? If more than a few transactions take place and their total value exceeds the mandatory registration threshold, it is more likely that an economic activity is being carried out.
- Is the activity carried on in a way that is similar to the way in which other businesses carry it on? If so, it is likely that there is an economic activity.

Example

Khalid collects classic cars as a hobby and usually buys one or two a year. He occasionally sells one of his collection to enable him to buy another car. Khalid should not be regarded as carrying on an economic activity as the number of transactions is low and he does not have any business apparatus to support the activity.

Over a period of time, Khalid begins to buy and sell more cars. As the number of cars bought and sold increases, it becomes more likely that he will be regarded as carrying on an economic activity, rather than a hobby.

After a few years as a collector, Khalid is widely regarded as an expert in classic cars and receives requests to source cars for third parties. He sources them as requested, imports them to Bahrain and sells them. This activity will be regarded as an economic activity as Khalid has clearly moved from carrying on a hobby to carrying on a business.

Supplies made in a private capacity will not be regarded as taking place in the context of an economic activity.

Example

Aisha decides to sell her diamond ring to a jewelry store for BHD 50,000. Given that the sale of the ring takes place as private (non-business) transaction, and selling jewelry is not a regular and ongoing activity carried out by Aisha, the sale of the ring will not be an economic activity for VAT purposes.

4. Requirements for an economic activity to exist

4.1. Activity is conducted independently

An economic activity must be carried out in an independent manner. A person is considered as conducting an economic activity independently when he is free from any outside control and he is not subject to another person's authority.

The requirement that an economic activity is carried out in an independent manner mainly excludes employees and directors who are natural persons from being VATable persons and thus being required to register for VAT. The position in relation to employees and directors is discussed in Sections 6.1 and 6.2 of this Guide.

Persons who will be regarded as carrying on an activity in an independent manner include:

- Sole traders (whether or not they have a commercial registration or another applicable license or permit governing their activities);
- Separate legal entities such as joint stock companies or Bahrain Shareholding Companies (B.S.C.), With Limited Liability Companies (W.L.L.) and Single Person Companies (S.P.C);
- Partnerships, whether these are formed under Bahrain law or not; and
- Unincorporated joint ventures (as discussed in Section 6.6.3 of this Guide).

The supply of goods or services by a partner to a partnership (other than services provided to the partnership which he is required to provide as a partner, i.e. services similar to those of an employee) will be regarded as being made by the partner in an independent capacity. The partner will be treated as acting in his own name and on his own behalf, even where he is the manager of the partnership. The same will apply to supplies of goods or services by a shareholder to a company (other than core functions of a director where the shareholder is a director, as discussed at Section 6.2.2 of this Guide).

4.2. Activity is conducted in an ongoing and regular manner

The activity must be carried out in an ongoing and regular manner. Where supplies are made on an one-off or infrequent basis, the activity will typically not be regarded as being conducted in an ongoing and regular manner.

What will be regarded as ongoing and regular will depend on a number of factors including the type of business and the type of supplies being made. The number of supplies and the time during which such supplies are made will be relevant as well as whether the person has promoted his products or services in the market. In terms of number of transactions, there is no threshold that must be exceeded for the activity to be regarded as being carried out in an ongoing and regular manner; it will be necessary to consider the facts and circumstances of each case.

Example

A dealer in rare antiques sells four high-value items over the course of one year. He will be regarded as carrying on his activity in an ongoing and regular manner as selling a few rare pieces in one year is the usual practice for his business.

A break in activity in line with normal practice in the relevant business sector will not mean that this condition is not satisfied. For example, where it is normal to close a business for a particular season, the status of that business as an economic activity will not be affected.

Example

A water park closes for the winter season from October to March. This is in line with its normal business practice and the tourist industry generally. The closure will not affect the fact that the water park's activity is being conducted in an ongoing and regular manner. The water park will be regarded as having carried on an economic activity during the time it was closed for the winter.

A temporary cessation of activities should not normally impact the activity being an economic activity.

Example

A restaurant in Manama closes for two months to be refurbished. After refurbishment, it reopens and carries on business as normal. The restaurant owner will be regarded as having carried on the restaurant activity in an ongoing and regular manner despite the closure, and will be treated as having carried on an economic activity during the period of closure.

Irregular or one-off supplies will generally not normally result in an activity meeting the requirement to be carried out in an ongoing and regular manner. However, the circumstances of such supplies need to be considered in full. For example, irregular supplies by a speculative builder could meet the threshold to be ongoing and regular.

4.3. Activity is conducted for the purposes of generating income

In order to be an economic activity, it must be carried out to generate income, even where the activity will result in an ongoing loss. If there is no intention to derive income from the activity, it cannot be an economic activity. Further, the income generated must be in return for goods or services provided as part of the economic activity.

If goods or services are provided for free on an ongoing basis and there is no intention ever to charge for them, there will be no economic activity.

It is not necessary for an activity to be conducted with an objective of realizing a profit in order for that activity to meet this test and be an economic activity.

The mere fact that an activity results in the earning of income does not mean it is automatically an economic activity. The other requirements of the definition as explained in this Guide must also be present.

Example

A newly established electronics company began trading on 1 April. The company purchased 50 new laptops at a price of BHD 100 each, plus VAT. The company intends to sell each of them at BHD 150, but, over the course of six months, the company is only able to sell two laptops. The company reduces the price of the remaining laptops to BHD 80 each and sells them. As a result, it has made an overall loss of BHD 860 on the sale of the laptops.

Although it incurred a loss on its laptop business, the electronics company will be considered as carrying on an economic activity even though it has made a loss on the sale of the laptops. The fact that it generated income for making supplies is sufficient for the purposes of the activity to be an economic activity.

5. The start and end of an economic activity

5.1. Start of an economic activity

An economic activity can start before the person carrying out the activity generates any income from his activities. Preparatory acts can indicate that the economic activity has started. Such acts include:

- Acquiring a business premises and preparation of that business premises for the activity (e.g. furnishing, refurbishing the premises);
- Hiring staff;
- Purchasing inventory;
- Purchasing and installing equipment and machinery needed to make supplies; and
- Incurring advisory fees relating to the future business such as fees for marketing consultants, legal counsel, business advisory services etc.

In order for NBR to regard an economic activity as having started before supplies of goods or services have been made, there must be objective evidence that preparatory acts have been carried out. An economic activity will not be regarded as having started where a person simply has the intention to carry out the economic activity without actually incurring costs.

There is technically no maximum period of time between commencing preparatory acts and actually making supplies in order for the preparatory acts be regarded as starting the economic activity. This will depend on the type of business concerned. For example, in the oil and gas sector, significant initial investment (surveying, test drilling, installation of equipment etc) will normally be required over a long period of time before any supplies are made. However, the time between preparatory acts and making supplies in a service business (e.g. law firm) would be expected to be quite short.

Example

A new Bahraini company is established with a view to engaging in specialist manufacturing activities. The company acquires land and, over a two year period, constructs its specialist manufacturing facility. It then engages in a six month testing phase of the manufacturing process before acquiring raw material, beginning manufacturing and making sales. The company will be regarded as conducting an economic activity from the time it first incurred expenditure, i.e. acquiring the land. Once it incurred expenditure exceeding the voluntary registration threshold, the company could register for VAT and recover input VAT on expenditure incurred.

5.2. End of an economic activity

An economic activity is considered to have ceased when no further supplies of goods or services are made, or, if later, when all necessary actions required to shut down operations have been taken.

Input VAT on costs required to wind down and close the economic activity of a VATable person is recoverable, subject to the normal input VAT recovery rules. Such costs, while not directly attributable to making VATable supplies, will be general business overheads incurred for the purpose of the VATable activity.

Example

A production facility ceases its operations and makes no further acquisitions of inventory and does not make any further supplies. However, due to the nature of the business which was carried on, it is legally required to decontaminate its premises and surrounding land as part of closing down. The economic activity will be treated as ending once the decontamination work has been completed, even though the facility does not make supplies during the period when this work is being done. Input VAT incurred in relation to the decontamination costs will be deductible.

6. Specific cases

6.1. Employees and contract staff

6.1.1. Employees

In return for carrying out their duties to their employers, employees will receive a salary or wage in return, usually in the form of cash. Employees providing services to their employers under an employment contract, also known as a “contract of service”, are not seen as conducting an economic activity independent from their employers. Therefore, an employee is not required to register for VAT in respect of services provided to his employer under his employment contract.

6.1.2. Contract staff

Businesses may hire individuals “on contract” to perform certain tasks. Such individuals are usually regarded as “contractors” and are not bound to the employer by way of an employment contract. The contractor operates under a “contract for service” arrangement with the employer.

A contractor who is not operating under an employment contract is regarded as conducting an economic activity. If a contractor’s annual supplies exceed the mandatory registration threshold, he will be required to register for VAT. He may choose to voluntarily register for VAT where his annual supplies exceed the voluntary registration threshold.

Where a contractor is registered for VAT, he is required to account for VAT on the amount charged for the services he renders. The standard 5% VAT rate will normally apply, unless the supply meets the conditions for zero-rating. VAT should be applied on the gross consideration charged by the contractor (including any GOSI and LMRA fees which form part of the amount charged).

Example

Fatima is a natural person in Bahrain who has entered into a contract with a manufacturing company in Bahrain to provide consultancy services. Fatima is considered as a contractor and receives BHD 3,500 monthly in return for her consultancy services. Given that Fatima’s activity is carried out independently and in an ongoing and regular manner, that activity is an economic activity for VAT purposes and Fatima will need to consider whether she is required to register for VAT or whether she wishes to voluntarily register for VAT.

6.2. Board members

6.2.1. Introduction

This section sets out the NBR's position on the VAT liability of fees earned by board members or directors in carrying out their duties as board members of a company, governmental organization, institution or similar body.

6.2.2. Core functions of board members

Board members and directors are considered to be instruments of the entity they represent when carrying out their core duties in their capacity as board members or directors. On this basis, they are not considered to be independent from the entities concerned. Hence, a board member is not regarded as carrying on an economic activity in relation to that activity, and remuneration for services as a board member is outside the scope of VAT.

Core duties are those that are required to be carried out under the Commercial Companies Law (Decree Law No. (21) for the year 2001 and its amendments in Decree No. (50) for the year 2014, Decree No. (27) for the year 2015, Decree No. (1) for the year 2018), as may be amended from time to time.

6.2.3. Other functions

Other functions, which are not core duties, exercised by persons in an independent way on behalf of an entity of which they are a board member are considered to be an economic activity and may trigger an obligation for these persons to register and account for VAT on the services provided. One example includes the provision of consultancy services for an additional fee. In such a case, the person may be required to register for VAT if the amount of his annual supplies exceeds the mandatory registration threshold. See the "Mandatory VAT registration" section of the VAT General Guide for more information.

6.2.4. Professional directorship services

A third party who, as part of its business and in consideration for a fee or similar payment, offers a service whereby it acts or arranges for another person to act as a board member will be considered to be acting independently. Such a third party may be a trust or company service provider, a law firm or accounting firm. Where the third party provides this service, it is considered to be engaged in an economic activity and may be required to register (if not already registered) and to account for VAT on the services provided.

Where a legal person appoints a board member to an entity by virtue of that legal person having a right to appoint a director (e.g. exercising shareholder rights under articles of association or having a right to do so under a shareholders' agreement), this will not be regarded as that legal person providing a professional directorship service. This will be the case even if the legal person or the individual appointed receives a fee. In such cases, the legal person will be seen as exercising its shareholder rights to appoint a board member,

rather than acting in an independent manner. Hence, any fees paid by the entity to the legal person or the board member will not be within the scope of VAT.

Example 1

Khalil holds board membership in several organizations across Bahrain. In return for his board membership, Khalil earns BHD 42,000 annually. Khalil does not provide any non-core services such as research or consulting on behalf of the organizations of which he is a board member. Although Khalil's income from his activities as a board member exceeds the mandatory registration threshold, the services he provides as a board member are not an economic activity. The consideration Khalil earns as part of his board memberships will therefore be considered as outside the scope of VAT.

Example 2

XYZ Services WLL (XYZ) is a Bahraini based company that provides a range of services including company formation, providing registered offices and office space for companies, and arranging for other persons to act as directors of clients. Fees charged for arranging other person to act as directors of Bahraini entities will be regarded as part of the economic activity of XYZ and will be subject to VAT at the standard rate.

Example 3

Bahrain Trading Group B.S.C. is a family owned company that holds shareholdings in a number of trading companies. By virtue of its shareholdings, it is entitled to appoint directors to the trading companies. It appoints family members and third parties as board members of these companies. In some cases, the companies pay Bahrain Trading Group B.S.C. a fee for providing the directors and, in others, fees are paid directly by the companies to the directors. The activities of Bahrain Trading Group B.S.C. in appointing the directors and the activities of the directors themselves will not be regarded as an economic activity and neither Bahrain Trading Group B.S.C. nor the individuals will be required to account for VAT on fees received from the companies.

6.3. Charities, Not-for-Profit and similar organizations

A charity, not-for-profit or similar organization may be seen as conducting an economic activity even if its aim is not to make any profit. If it engages in commercial transactions and receives income as a result, this could be an economic activity.

Where a charity, not for profit or similar organization receives donations and/or funding, where no supply is provided in return, the receipt of donations/funding will be outside the scope of VAT. As no supply is being made by the organization, there is no economic activity being conducted by the organization in relation to the funds received.

Charities, not-for-profit or similar organizations which conduct activities that are commercial in nature (e.g., collecting used clothes and goods in order to sell them in charity shops) will be considered as carrying out an economic activity and may be VATable persons. The fact that these activities are not conducted with the aim of making any profit or to raise money for the main purpose of the charity, not for profit or similar organization is not relevant.

Example 1

Smiles is a charity registered in Bahrain that helps children with learning disabilities. As part of its fundraising, the charity organizes an annual 10km run. The charity charges each participant BHD 15. The sale of tickets to participants is a supply conducted within the scope of the charity's economic activity and should be included when determining whether the charity is required to register for VAT.

Example 2

A homeowners' association is responsible for the upkeep and repair of the common areas of an apartment development. Each apartment owner, which is a member of the association, contributes a fee to the association each year which is used to fund the association's expenses and running costs. The association engages third parties to carry out necessary works (e.g. management company, landscapers, plumbers, painters etc) who charge the association VAT on services provided.

The association is set up specifically as a non-profit organization and any excess income received over expenses incurred is regarded as a surplus for carry forward. The association cannot distribute any surplus to a third party. The association will not be regarded as conducting an economic activity as it merely exists to manage the pooled funds of the homeowners to procure services which are the collective responsibility of the homeowners to ensure the ongoing maintenance of the development.

If the association was engaged to provide services to another development which is not owned by its members, those services would be regarded as being provided in the course of an economic activity if the association received payment for providing the services.

6.4. Holding companies

6.4.1. Introduction

A holding company is a company that typically holds shares in other companies. The holding company may hold controlling interests in these other companies (in which case they will be subsidiaries) or minority interests in them. A holding company may be a passive holding company or an active holding company.

6.4.2. Passive holding companies

A passive holding company typically holds shares in its subsidiaries and receives dividends (as a passive investment). It may also introduce long-term non-interest bearing loan capital to subsidiaries, without carrying on any other activity other than merely holding shares in its subsidiaries. A passive holding company is not regarded as carrying out an economic activity.

6.4.3. Active holding companies

In addition to holding shares in subsidiaries and receiving dividends from them, holding companies may also be engaged in actively managing their subsidiaries in consideration for a fee or similar remuneration. The active management of subsidiaries is an economic activity for VAT purposes and a holding company engaged in this activity may be required to register

for VAT, subject to the normal rules, and may recover input VAT incurred on purchases subject to the normal input VAT recovery rules.

The following are indicators that a holding company may be an active holding company, i.e. one which is carrying on an economic activity and which may be required to register for VAT:

- It provides services to subsidiaries (e.g. management services);
- It incurs costs other than those needed for it to retain its legal or regulatory status (i.e. costs other than individual company registration fees, individual company audit fees etc) and recharges these costs to its subsidiaries;
- The company has employees which are engaged in the management of the company's subsidiaries;
- The company provides interest bearing loan finance to subsidiaries;
- The company licenses intellectual property rights to its subsidiaries;
- It owns real property and movable property and makes this available for use by its subsidiaries for consideration.

A holding company will need to assess, based on all relevant information (including referring to the indicators above) whether it is an active holding company carrying on an economic activity.

Example 1

HoldCo W.L.L., incorporated and resident in Bahrain, holds a majority interest in five subsidiaries. HoldCo W.L.L. does not have any employees, holds no assets other than the shares in its subsidiaries and does not provide any services to its subsidiaries or others. Its costs mainly comprise those relating to renewing its commercial registration and annual audit fees. Its only source of income is dividends from its subsidiaries.

HoldCo W.L.L. will be regarded as a passive holding company not carrying on an economic activity for VAT purposes. It will therefore not be required or eligible to register for VAT.

Example 2

GroupCo W.L.L., incorporated and resident in Bahrain, holds a majority interest in five subsidiaries. GroupCo W.L.L. has a number of employees and provides services for a fee on an ongoing basis to its subsidiaries, including overseeing and managing the annual group audit, accounting services and human resources services. The company also negotiates with banks for favorable lending terms on behalf of its subsidiaries.

GroupCo W.L.L. will be regarded as an active holding company carrying on an economic activity for VAT purposes. It will be required to register for VAT if fees received for its services exceed the mandatory registration threshold.

If GroupCo W.L.L. did not, in fact, charge any fees for the services provided, for VAT purposes, it would be required to determine the market value of the services provided to any subsidiary where that entity would not be entitled to recover input VAT in full on the services.¹ This market value would be taken into account when determining whether the mandatory registration threshold is exceeded and, if GroupCo W.L.L. is a VATable person, the amount on which it would be required to account for VAT.

¹ Article 22 of the Law

6.5. Dormant companies

A dormant company is a company that does not carry out any business activities and does not trade. From a VAT perspective, a dormant company does not carry out an economic activity and therefore will not be required or eligible to register for VAT.

6.6. Joint ventures

6.6.1. Introduction

A Joint Venture (“JV”) is as an association of persons who come together for the purposes of undertaking a particular economic activity / project with a view to mutual profit, with each participant usually contributing money, assets or skills.

6.6.2. Incorporated JVs

An incorporated JV takes the form of a legal entity (e.g. a company) that is distinct from the JV participants. The participants’ level of involvement in the JV is usually reflected in the percentage of interest/shares they each hold in that legal entity. This separate legal entity is deemed to carry out an economic activity separate from the participants and may be required or entitled to register for VAT in Bahrain accordingly.

6.6.3. Unincorporated JVs

An unincorporated JV takes the form of a contract (written or unwritten) between the participants whereby they agree on the terms of the activity to be undertaken collectively. The rights, duties and obligations of each participant are regulated by the contract that is entered into by them. This contract may or may not result in the creation of a formal partnership between the JV parties.

For VAT purposes, the unincorporated JV (i.e. all participants collectively) is considered to be carrying on any economic activity covered by the JV contract, as opposed to each participant carrying out an economic activity individually. As such, any VAT obligations (e.g. registration, filing VAT returns etc.) arising from the activities undertaken by the unincorporated JV rests with the JV itself, rather than its constituent members.

7. Government bodies and public sector entities

7.1. Introduction

Government bodies and public sector entities acting in a sovereign capacity are not considered to be carrying out an economic activity. As such, VAT is not charged on supplies which are sovereign or statutory in nature. Where, however, a government body conducts an economic activity in a non-sovereign manner in competition with the private sector, it may have VAT obligations.²

7.2. Sovereign activity

Government bodies and public sector entities are generally branches of the government who are funded by the State to carry out certain functions. Certain services supplied by government bodies are sovereign in nature (i.e. such services can only be supplied by the government body or public sector entity) and will therefore be outside the scope of VAT. Decision No. (43) for the year 2018 and Decision No. (13) for the year 2019 in relation to supplies made by government bodies includes the list of sovereign government supplies on which VAT is not charged.

Where a government body subcontracts a sovereign activity to a non-government third party, the nature of the supplies made by the third party will need to be considered. Such supplies may fall within the scope of the subcontractor's economic activity. The subcontractor may be required to charge VAT on such supplies, as applicable.

Example

A taxi company based in Bahrain wishes to renew its taxi operation license at the Land Transportation Regulation Directorate at the Ministry of Transportation and Telecommunication. Given that the renewal of taxi license is a sovereign activity only offered by the Ministry of Transportation and Telecommunication, the supply by the Ministry will be a sovereign activity and it will not be considered as undertaking an economic activity.

7.3. Non-sovereign activity

There may be cases where government bodies are making supplies that are considered to be economic activities for VAT purposes. Typically, such supplies are in competition with the private sector and not sovereign in nature. In such cases, the normal VAT rules in Bahrain will apply and any VAT collected by government bodies carrying out an economic activity should subsequently be paid to the NBR.

² Article 9 of the Law

Example

Fawaz owns a plot of residential land in Muharraq and would like to know the size of the plot of land. Fawaz contacts the Survey and Land Registration Bureau (SLRB) which supplies surveying services. Given that surveying services are not sovereign in nature, the SLRB is deemed to be carrying out an economic activity and must charge VAT at the standard rate, where applicable.

Further, where a company that is wholly owned by a government body makes supplies, it will be important to consider whether or not this is an economic activity for VAT purposes.

8. VAT incurred as part of an economic activity

As a general principle, VAT incurred on expenses by a VATable Person conducting an economic activity is recoverable, subject to specific rules relating to VAT recovery. VAT incurred on expenses incurred for the purposes of an economic activity can be recovered (in whole or in part) to the extent these expenses are used (in whole or in part) for making VATable supplies (i.e., supplies subject to VAT at 5% or 0%), and are not specifically disallowed.

VAT incurred on expenses used for the purposes of an activity that is not an economic activity for VAT purposes cannot be recovered. For example, if a person holds shares as a passive investment and incurs specific costs relating to this activity, VAT on these expenses may not be recovered.

If a person incurs VAT on expenses which relate to both his economic activity and non-economic activity, he is required to apportion these expenses between their use for the economic activity and the use for the non-economic activity. This should be done using an allocation that reflects their fair use. Only the VAT on the portion of the expenses allocated to the economic activity will be regarded as input VAT which can be included in his recovery computation.

