UAE Customs Alert
Free zones' customs audits

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In brief

The Dubai Customs Authority ("Dubai Customs") is currently auditing entities established in Dubai free zones (whether fenced or unfenced free zones) to control their compliance with the applicable customs laws and regulations. In particular, Dubai Customs is focusing on the import and export balances of potential high-risk free zone entities. A free zone entity may be considered as a high-risk entity if its customs records show material discrepancies in terms of weight, quantity or customs value according to the Dubai Customs database. In case of insufficient documented evidence or justification, the free zone entity may face severe customs fines and penalties.

In detail

In recent years, Dubai Customs has invested heavily in its customs systems and capabilities including advanced risk engines and procedures to investigate the compliance of importers and exporters with its laws and regulations.

Although not expressly stated in the Gulf Cooperation Council ("GCC") Common Customs Law, which governs the UAE and the other GCC States, Dubai Customs requires free zone entities to be able to trace the whereabouts of their goods at any time while being in the free zone. In addition, most UAE free zones have set out in their regulations that an entity must obtain a fully computerised, thoroughly auditable and accountable inventory system to trace the whereabouts of its imported goods until the entity exports or disposes the goods out or within the free zone.

The inability to provide evidence of the destination of the goods may lead Dubai Customs, pursuant to Article 143 of the GCC Common Customs Law, to the assumption that the entity is introducing its goods into the local market without following adequate customs formalities or it is manipulating the quantities, weights or values of its imported and exported goods into and out of the free zone.

How does it work?

When an entity is identified as a high-risk entity, Dubai Customs may request the entity to provide its inventory count for the audit period in scope. Based on this information, Dubai Customs will compare the entity's inventory count with the import and export customs declarations that the entity processed under its customs code for the same period. If the comparison results in material discrepancies whether in quantities, weights or values, Dubai Customs will request the entity to provide a customs reconciliation, accompanied by supporting documentation, to justify such discrepancies. Failure to provide valid justification of the discrepancies may be viewed by Dubai Customs, as a 'smuggling' act that could lead to severe penalties and fines in addition to the payment of the applicable customs duty on those goods.

Dubai Customs also expects free zone entities to export goods out of the free zone using a value that exceeds the goods' import value, based on the assumption that a free zone entity should generate profit from its transactions within the free zone. Therefore, where the goods' export value is equal to or less than the goods' import value, Dubai Customs may question such a pattern and levy fines and penalties if the free zone entity fails to provide proper justification of this divergence. In practice, we have seen this mainly with entities involved in service activities, such as, oil and gas service providers and entities that are involved in maintenance services which export (for example) depreciated equipment out of the free zone.

Unfenced free zones

Dubai has over 30 free zones, each with different industries and business offerings. The Dubai free zones are either fenced (such as Jebel Ali Free Zone and Dubai Airport Free zone) or unfenced (such as Dubai Multi Commodities Centre and Dubai International Financial Centre) free zones.

Entities located in unfenced free zones are also required to comply with the customs laws and regulations, as well as any specific customs related rules set out by the free zone authority they are registered under.

An entity importing goods (such as furniture, laptops) into the free zone under its customs code for its own use should also be able to trace the whereabouts of those goods. The requirement to trace goods is also applicable to entities located in unfenced free zones, unless in some instances the entity pays customs duty upon the import of goods into the free zone. In such cases, the customs audit risk should not be, in principle, applicable to the entity.

In practice, a large number of unfenced free zone licensees assume that being established in an unfenced free zone should not expose them to any customs risks. However, this is not the case and entities are highly recommended to assess their position in relation to their import transactions to confirm whether or not they are in compliance with Dubai Customs' laws and regulations, in anticipation of any potential customs audit.

Statute of Limitation

According to Article 176 of the GCC Common Customs Law, prescription period for the Customs Administration, if not prosecuted, shall be 15 years for acts of smuggling and the like, and 5 years for other cases (such as customs duty that has not been collected by the customs authorities due to a mistake made by them, etc.).

The GCC Common Customs Law does not set out different statute of limitation for free zone entities and thus, the statute of limitation should not differ between free zones and onshore entities. However, based on our experience, Dubai Customs may take the view that there should be no statute of limitation in a free zone due to the assumption that a prescription period should only begin from the date of declaring the goods out of the free zone. If goods are not declared out from the free zone, the goods therefore should be available at the entity's premises.

In practice, we have seen Dubai Customs auditing entities and going back to the date of their establishment in the free zone.

Risk and customs duty exposure

As mentioned above, the inability to trace an entity's goods within the free zone may be attributed by Dubai Customs as a smuggling act. However, subject to the discussions with the customs officials during the audit process and the justification provided by the entity audited, Dubai Customs may take a more lenient approach and impose, for example, non-compliance fines instead. The penalties imposed by the customs authority vary depending on the final decision of the customs audit.

The takeaway

Free zone entities should be aware that operating in a UAE free zone (especially in Dubai) does not mean that the entity is outside the radar of the customs authorities. Entities should adhere to the rules and regulations set out in the GCC Common Customs Law and ensure that they are compliant with any specific customs and regulatory requirements issued by the local customs administrations they operate under, to avoid any potential customs exposure. Entities are advised to maintain a fully computerised inventory system to trace the whereabouts of their imports and exports in terms of weights, quantities and values.

We recommend entities to assess their import and export transactions within the free zones and seek consultation to ensure compliance with the applicable customs laws, regulations and current practices.

Let's talk

For any questions or clarifications on how this topic may affect your business, please do not hesitate to contact us.

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