

UAE Corporate Tax (CT) regime

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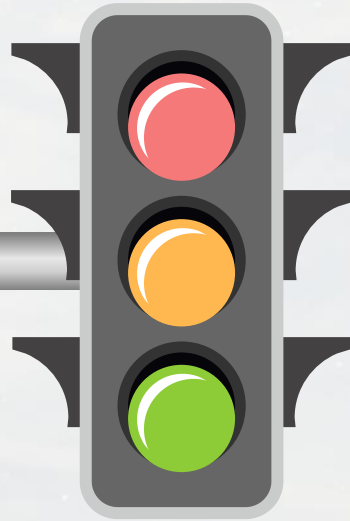
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01

Basic Introduction of CT - Back ground



1st July 2023



The UAE's Ministry of Finance (MoF) published a public consultation document on the proposed **Corporate Tax (CT)** regime on April 28, 2022. It has requested comments from all parties by May 19, 2022.

Objective: To incorporate **internationally known and accepted principles** and to ensure that UAE CT regime is readily understood rather than introducing new concepts

Background and rationale

- The OECD and G20 inclusive framework on BEPS has been developing to address BEPS challenges and tax evasion as well as to guarantee the consistency of international tax regulations.
- BEPS 2.0 is divided in 2 pillars – Pillar One is focused on reallocation of consolidated profit of multinational groups, and Pillar Two introduces a **global minimum effective tax rate**
- In support of BEPS 2.0 project, the MoF is introducing a **Federal CT** for financial years **starting on or after 1 June 2023**
- Key principles followed by MoF in development of UAE CT

Certainty and simplicity

Flexibility and alignment with modern business practices

Neutrality and equity

Transparency

Immediate action needed for FZ persons with FY beginning from 1 July 2023



Jan 31, 2022

MoF announced introduction of federal CT

Jan 31, 2022

UAE Federal Tax Authority (FTA) issued FAQs

UAE Federal Tax Authority (FTA) issued FAQs

April 28, 2022

MoF issued consultation paper

Contains info on proposed CT regime, and invites inputs by May 19

Introduction of detailed provisions of CT law (including administrative rules and regulations)

June 1, 2023

UAE CT regime will become effective for first financial year starting **on or after this date**



Multi National Groups



A higher CT is expected to be prescribed for large MNCs that meets specific criteria set with reference to Pillar 2

Above Threshold



Taxable Income above AED 375,000

Below Threshold



Taxable Income up to AED 375,000

02

Transfer Pricing (TP)

- TP regulation in line with internationally recognized Arm's Length Principle
- Transactions between 'related parties' and 'connected persons'
 - Requirement to maintain a Master and Local file, if value of related party transaction exceeds monetary threshold
- Arm's Length Price (ALP) determined using internationally recognized TP methods
- Excessive payment to owner / its connected person, not deductible

Related Party

- Individuals related to the fourth degree of **kinship**
- Individual holding directly or indirectly **50% or more share / control in the legal entity** (alone or with a related party)
- Legal entities, where one legal entity (alone or with a related party) holds directly / indirectly 50% or more share / control in another legal entity
- Legal entities, **where their 50% or more share / control is owned by a common person** (whether alone or with a related party)
- **Branch** or PE
- **Partners** of same unincorporated partnership
- Exempt and non-exempt activities of the same

VS

Connected Person

- An individual directly / indirectly **having control or ownership** of taxable person
- **Director or officer** of taxable person
- An **individual related to owner, director or officer** to the fourth degree of **kinship**
- **Partner** in an unincorporated partnership
- **Any other related party to the above**

Transfer Pricing Methods



03

Taxation of Free Zones Persons (FZP)

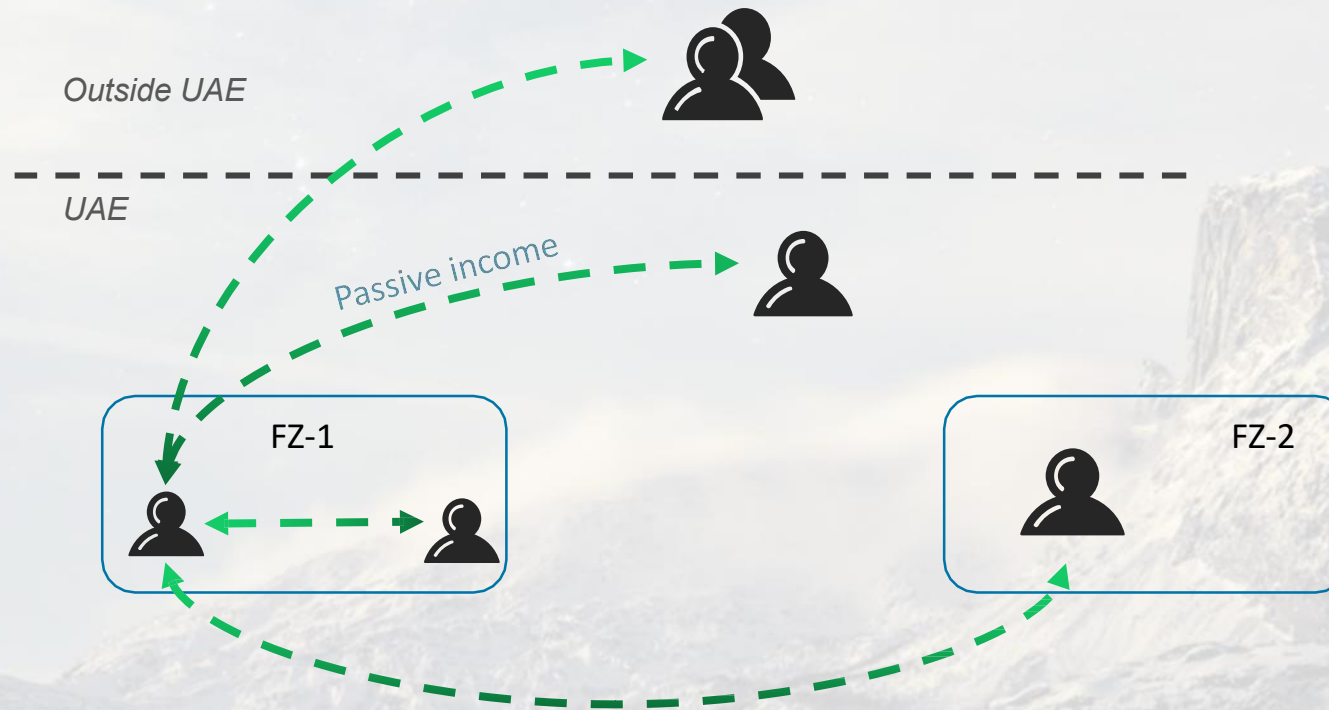
Free Zone Persons (FZPs) CAN BE TAXED!!

Free Zone Persons (FZPs) CAN BE TAXED!!

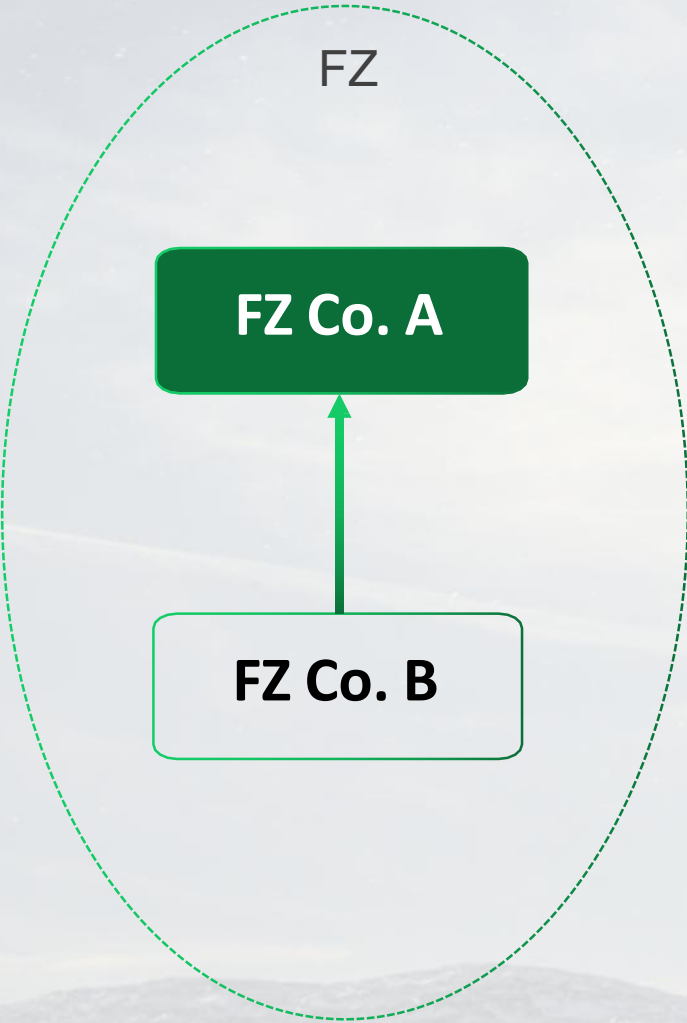
- No Blanket Exemption from CT
- 0% CT on companies / branches registered in FZ, in respect of **specified incomes**
- Certain income of FZPs to be subjected to CT (discussed in next slides)**
- FZPs will be required to file their tax return**
- Irrevocable option to move to regular CT regime
- A FZP can even be DISQUALIFIED from 0% CT rate – In such a case, its ENTIRE income will be subjected to CT**

Taxation - Free Zones Persons (FZP)

Passive incomes, such as interest, royalties, dividend and capital gains from sale of shares in mainland LLC

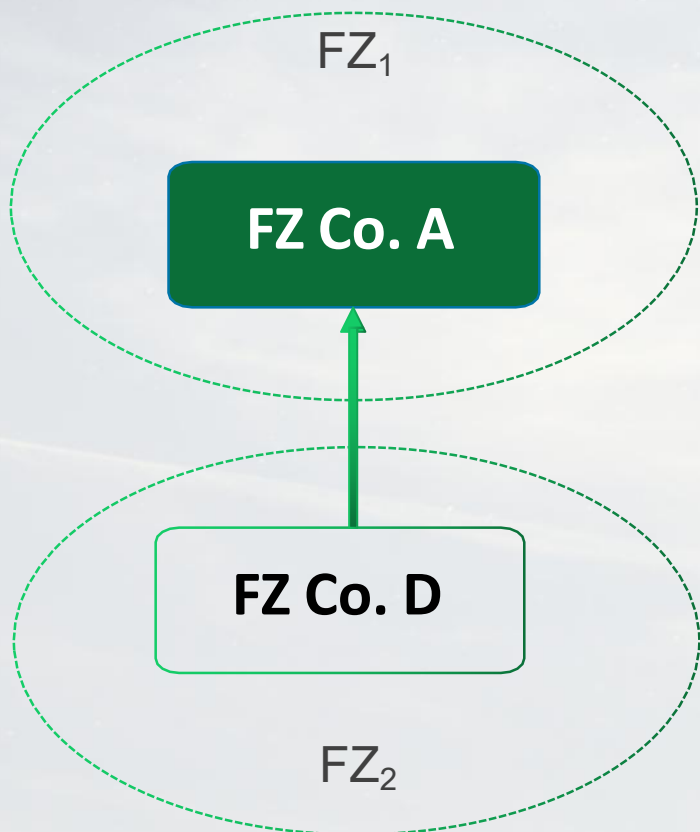


Scenario 1



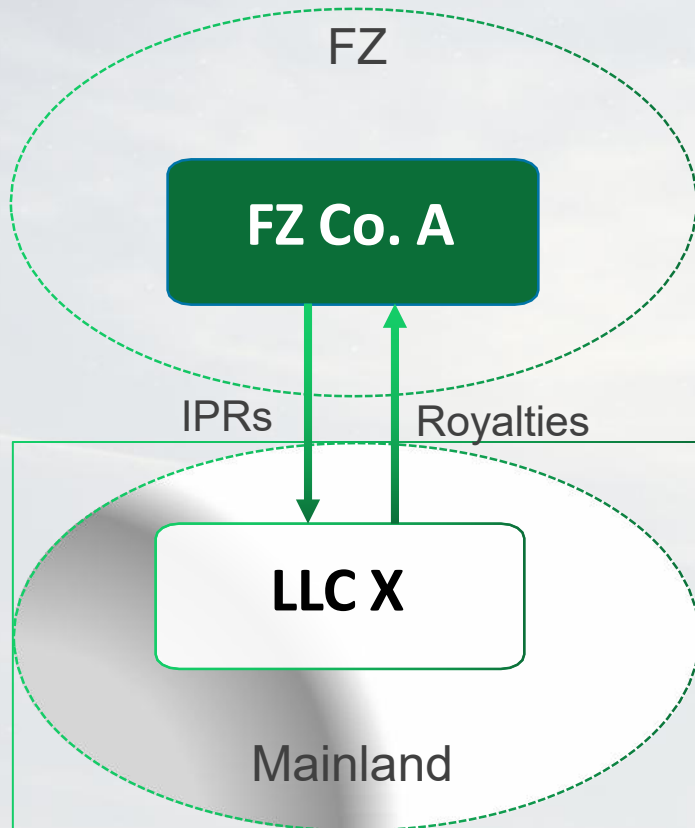
Income from transaction with a person in **same FZ**

Particulars	Accounting Income	Taxable income
1) Revenue from Co. B	400,000	0



Income from transaction with a person in **another FZ**

Particulars	Accounting Income	Taxable income
1) Revenue from Co. B	400,000	0
2) Revenue from Co. D	450,000	0

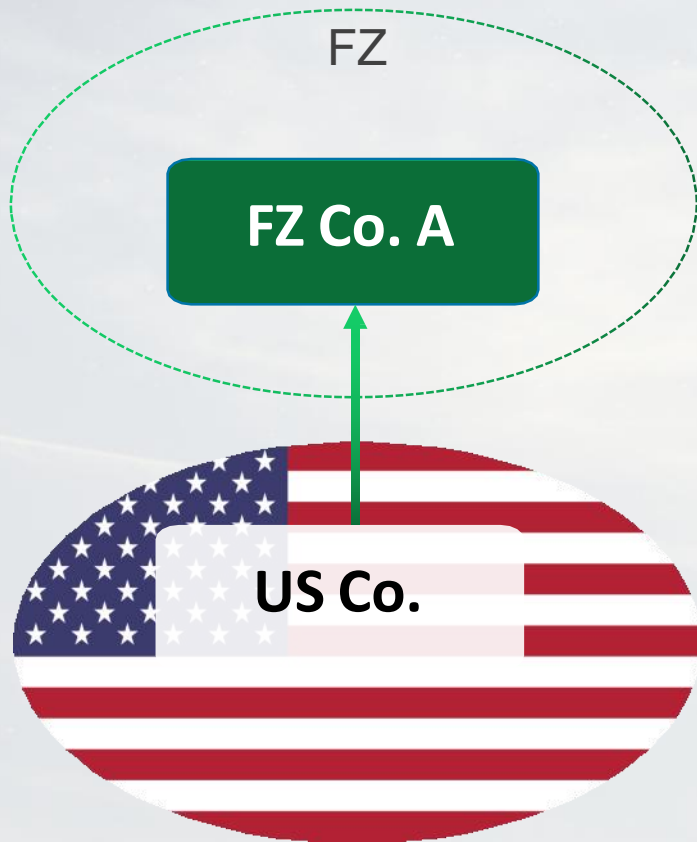


Passive income* from a Mainland entity

Particulars	Accounting Income	Taxable income
1) Revenue from Co. B	400,000	0
2) Revenue from Co. D	450,000	0
3) Royalties from LLC X	500,000	0

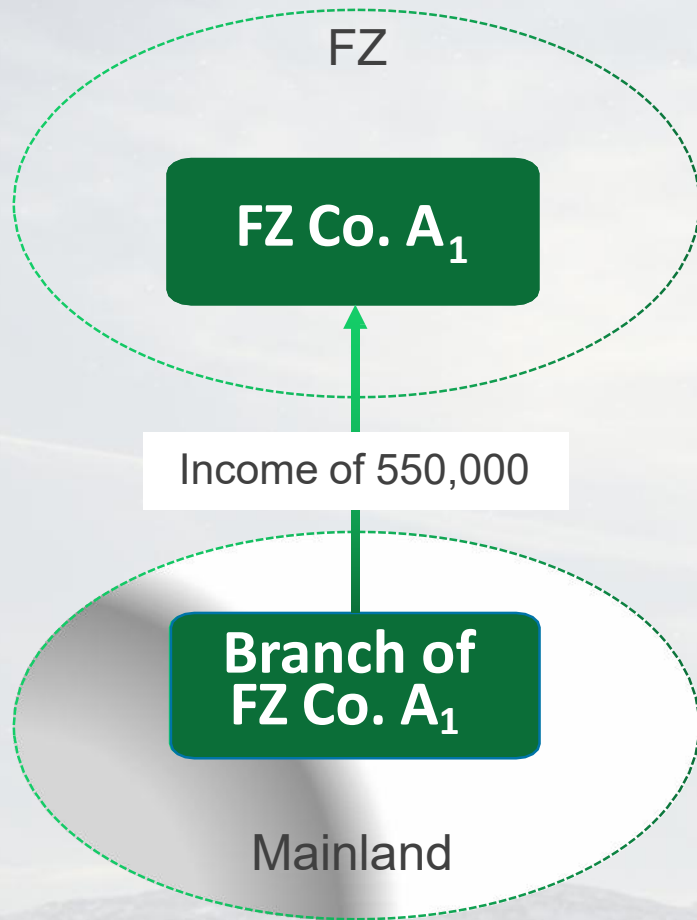
* Income such as interest, royalties, dividend, capital gains from transfer of shares in a Mainland entity

Scenario 4



Income from transaction with an entity outside UAE

Particulars	Accounting Income	Taxable income
1) Revenue from Co. B	400,000	0
2) Revenue from Co. D	450,000	0
3) Royalties from LLC X	500,000	0
4) Income from US Co.	600,000	0

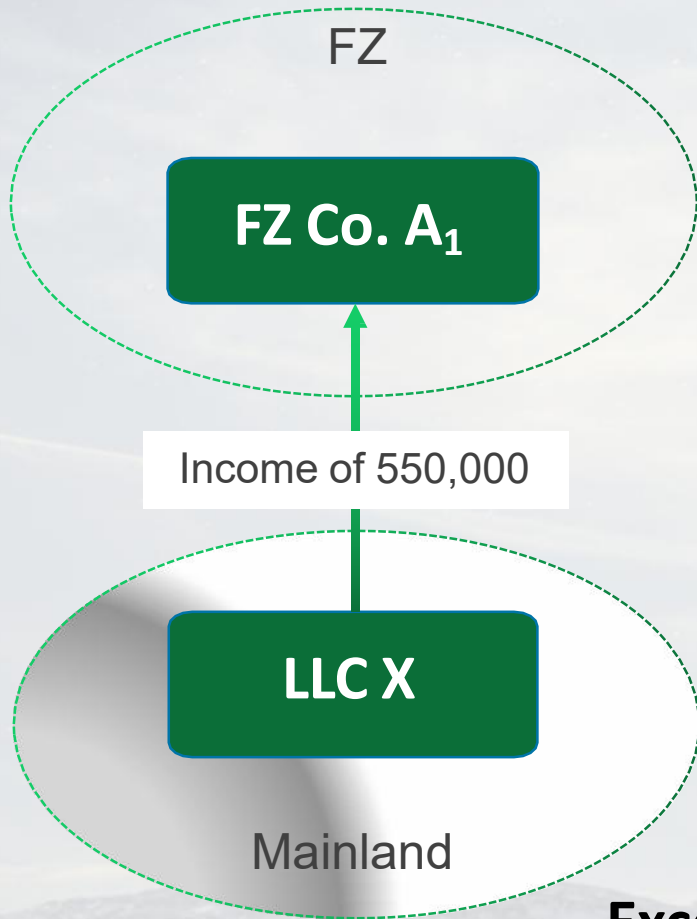


FZP’s income from transaction with its mainland branch

Particulars	Accounting Income	Taxable income
Revenues from Co. B, Co. D, LLC X and US Co.	1,950,000	0
5) Income from Branch office	575,000	575,000
Tax on taxable income upto AED 375,000	0%	0
Tax on taxable income > AED 375,000	9%	18,000

*Scenario 5B: Where the Branch’s net profits are **negative**, can they be accumulated, and carried forward – for an offset in future against any taxable income of the FZ Co.?*

Scenario 6

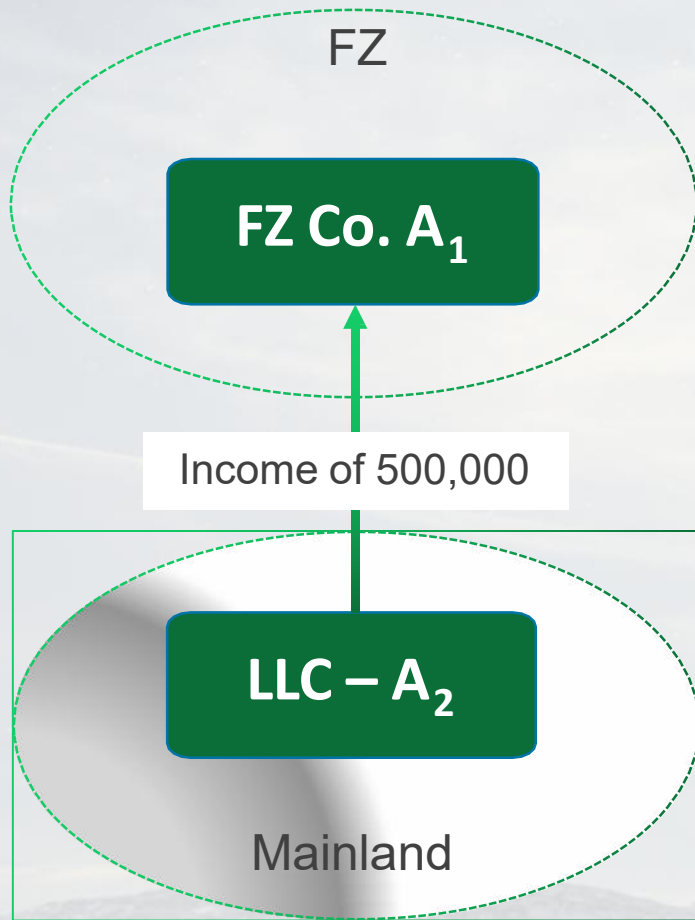


FZP's income (not passive) from an **unrelated** mainland entity. Say, a **service income** (potentially, a management cost allocation)

Particulars	Accounting Income	Taxable income
Revenues from Co. B, Co. D, LLC X and US Co.	1,950,000	
Income (other than passive income) from unrelated mainland entity	25,000	1,975,000
Tax on taxable income upto AED 375,000	0%	0
Tax on taxable income > AED 375,000	9%	144,000

Exception: Scenario 9

Scenario 7



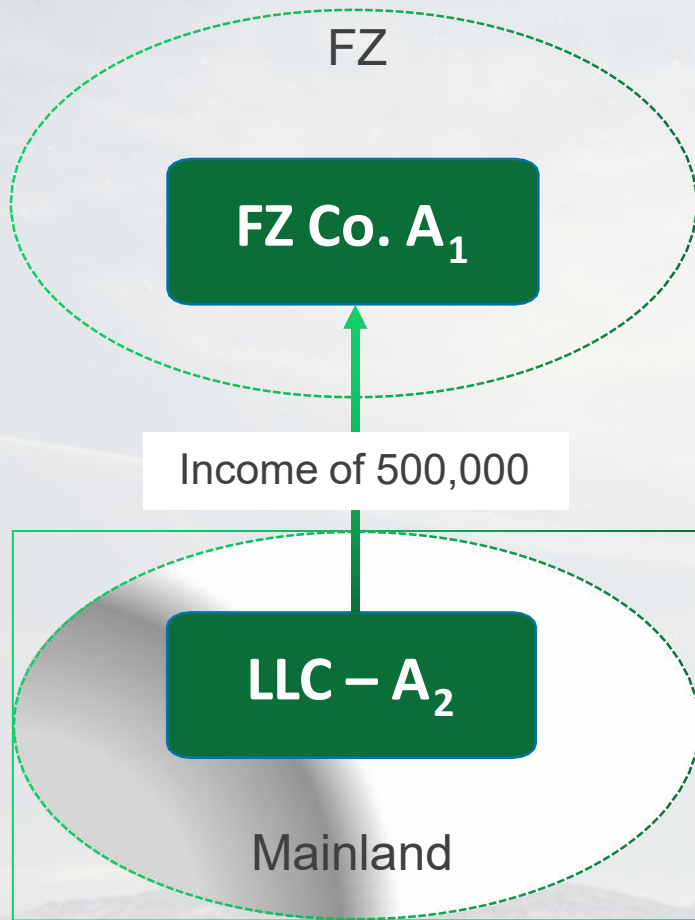
FZP's income from transaction with its mainland **Group** Co.

Particulars	Accounting Profits	Taxable income
Tax impact of income of AED 500,000	500,000	0

Mainland Co.'s income from transaction with Group Co. in FZ

Particulars	Accounting Profits	Taxable income
Tax impact of expenditure of AED 500,000	1,000,000	1,500,000

Scenario 8



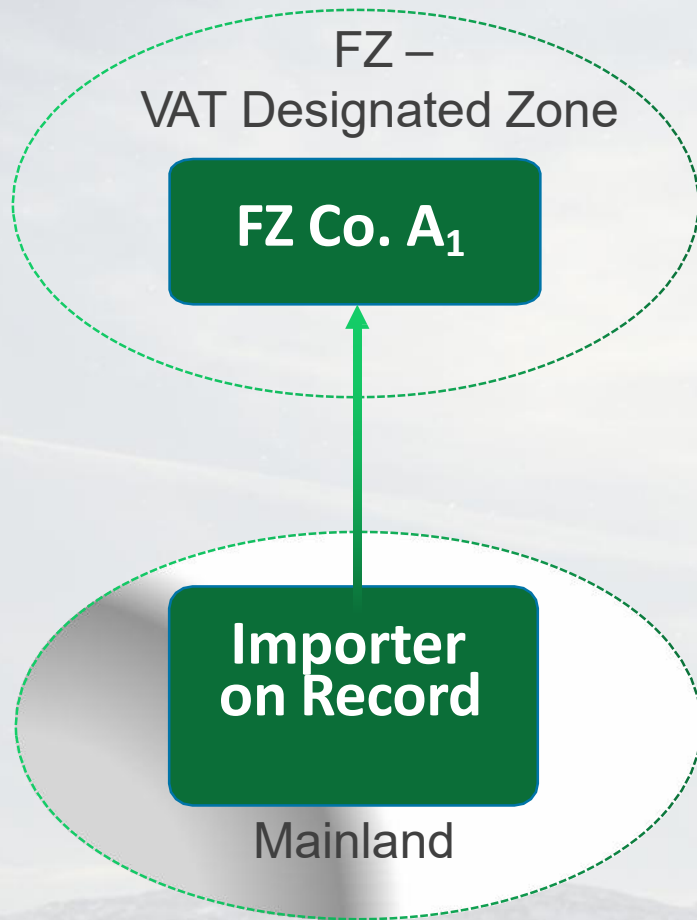
FZP's income from transaction with its mainland **Group** Co.

Particulars	Accounting Profits	Taxable income
Tax impact of income of AED 500,000 if FZ Co. opts to move to regular CT regime	500,000	125,000

Mainland Co.'s income from transaction with Group Co. in FZ

Particulars	Accounting Profits	Taxable income
Tax impact of expenditure of AED 500,000	1,000,000	1,000,000

Scenario 9



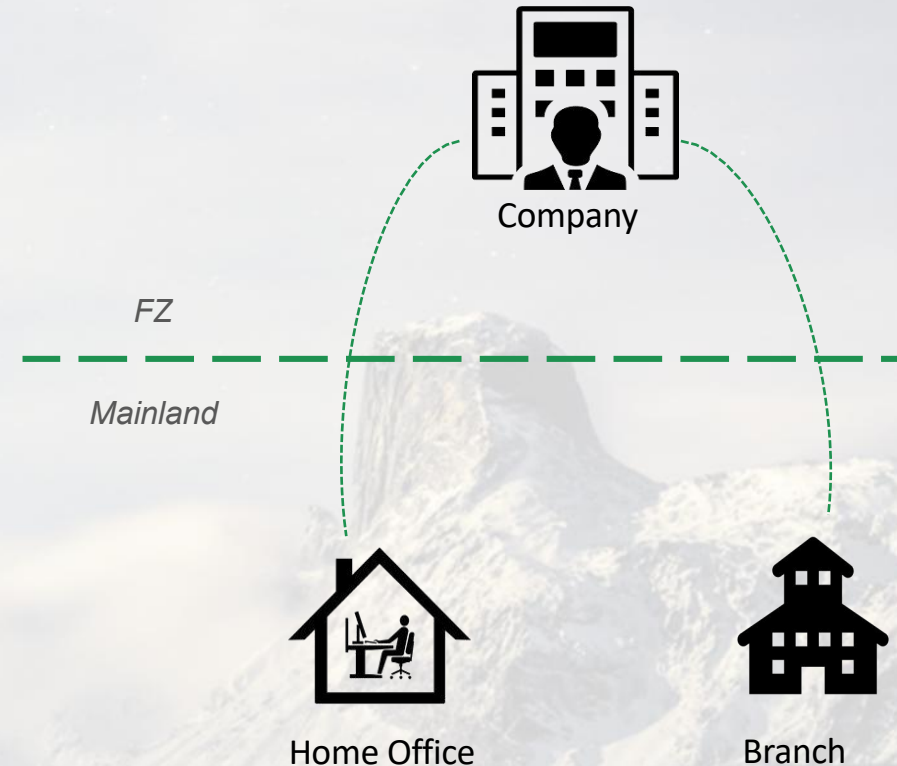
- All **VAT designated zones (Gated zones)** are FZ (but not *vice versa*)
- Sale to a 3rd party in Mainland – B2B
- Buyer needs to be an **‘Importer on Record’ (IOR)** – Needs to hold an **Import License**
- C&F agent can also be an IOR – Not compulsory for IOR to be the ultimate buyer / owner
- CT rate for income from such sale – **0%**

04

Permanent Establishment

Permanent Establishment - Concept

- ✓ A place of business through which a **foreign entity carries on its business in a host country (Mainland UAE)**
- ✓ Determination of PE is designed on the basis of **OECD Model Tax Convention**
- ✓ The **activity threshold** that will trigger a PE will be determined by certain detailed tests



Permanent Establishment - Concept



- A **fixed place** of business through which business of an enterprise is **wholly or partly carried on in other country**
- Includes, a place of management, branch, employee's home office, factory, workshop, real property, building site, etc.
- No PE if activity carried out are **preparatory** or **auxiliary** in nature

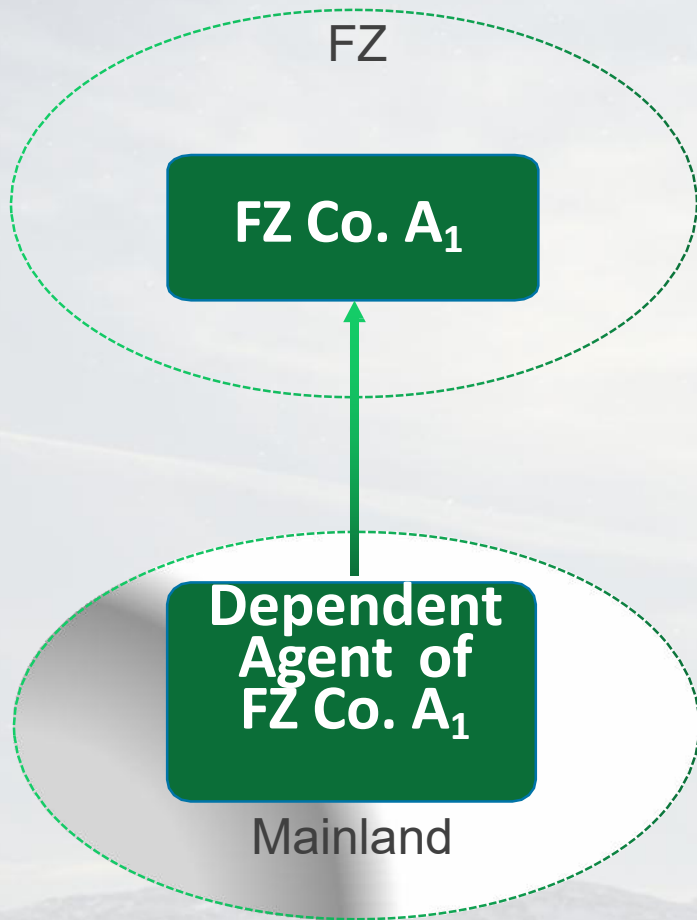
Fixed Place PE

Agency PE

- An agent who is legally, economically **dependent** on the foreign entity (i.e. its Principal)
- It **habitually** exercises authority to **conclude contracts** in the name of the foreign entity or **negotiates** or concludes contracts in UAE on behalf of the foreign entity
- Exclusion for **Independent agent** carrying on activities in the ordinary course of his own business



Scenario 10



- A FZP can create a Permanent Establishment ('PE') in mainland (clause 4.20 of the PCD)
- Such PE status of FZP will be determined using principles similar to the ones applicable in case of foreign entities doing business in UAE
- **OECD Model Convention** on PE – Fixed Place PE, Agency PE
- **Exclusive** dealers / distributors who sell on behalf of FZ Co.
- Subjectivity of '**attribution**'

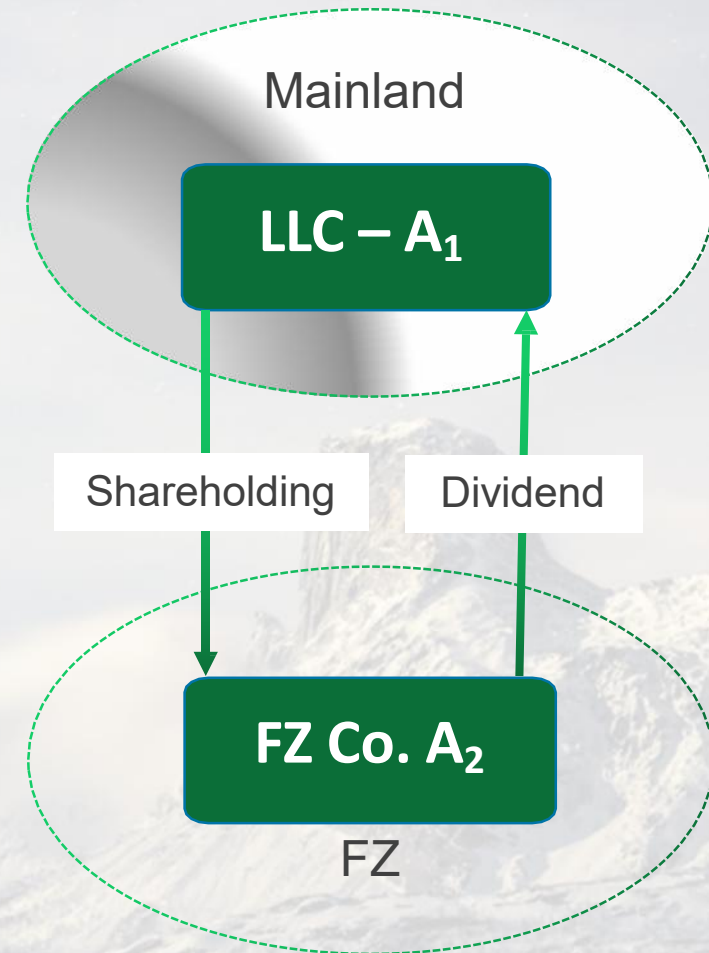
05

Participation Exemption and FZP

Participation Exemption and FZP

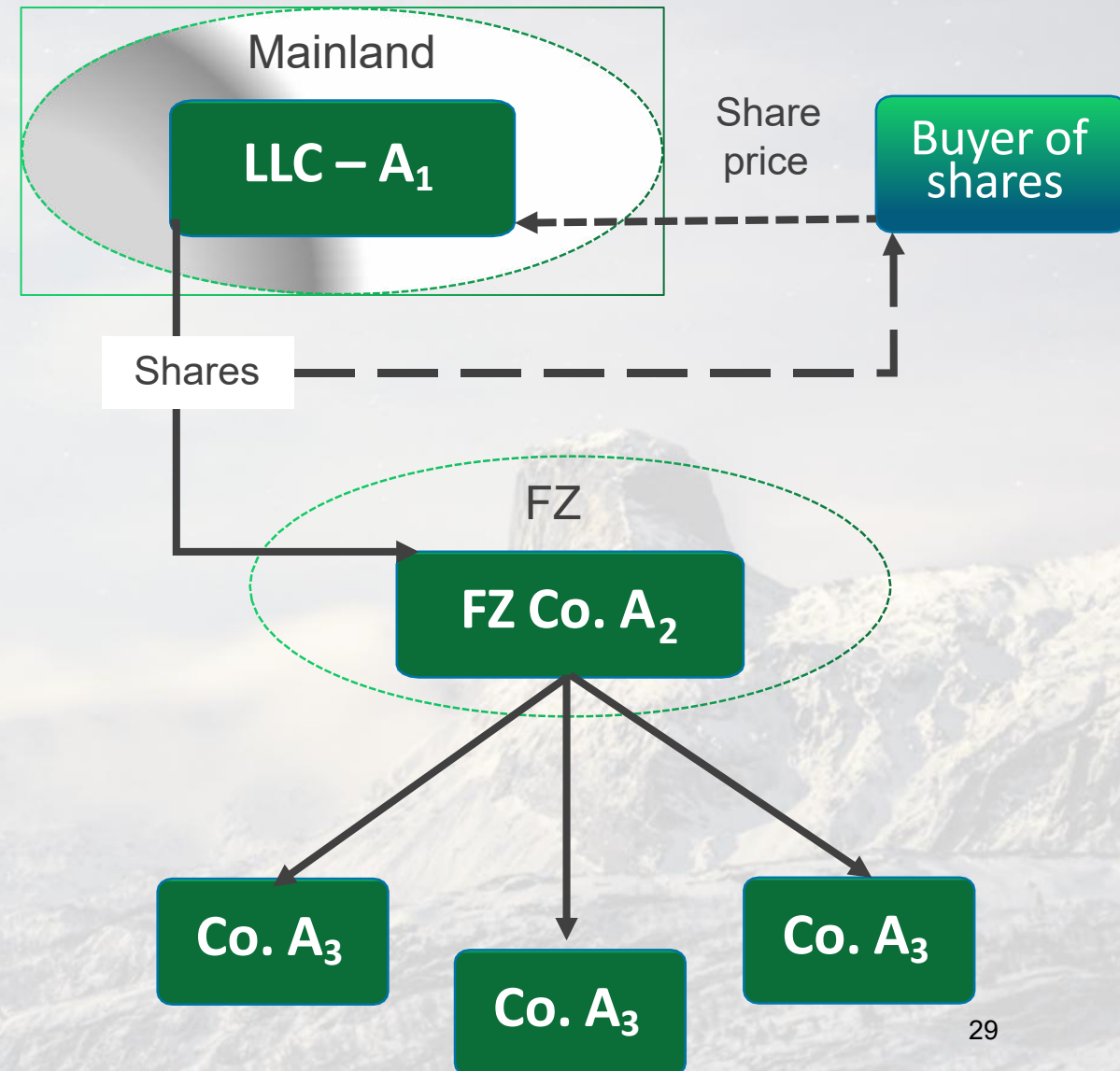
- **Participation Exemption:** Dividend, and Capital Gains from sale of shares in a subsidiary – to be exempt from CT, provided:
 - UAE shareholder owns minimum 5% shares in the company
 - In case of foreign company, it should be subject to a minimum of 9% tax

- Dividend received by UAE corporate shareholder **from FZP** (taxed @ 0%) also eligible for exemption



Participation Exemption and FZP

- **Participation Exemption:** Dividend, and Capital Gains from sale of shares in a subsidiary – to be exempt from CT, provided:
 - UAE shareholder owns minimum 5% shares in the company
 - In case of foreign company, it should be subject to a minimum of 9% tax
- **CG on sale of shares in FZP** also exempt, if:
 - **FZP is holding company** and
 - Substantially all its income is derived from **subsidiaries that meet participation exemption test**



06

How to compute CT payable

How to compute CT payable

Identify taxable person
(and its Residential
status)

Identify the incomes
that are taxable

Computation of taxable
income – Starting from
the Accounting Profit



Making adjustment for
exemptions, disallowances
(Example: Capping of Interest
expense)

Offset tax
losses (if any)
of earlier years

Other important
provisions (such as,
transfer pricing,
group relief, etc.)

Computing tax liability after
reducing tax credit available

Worldwide Taxation

- ✓ Legal person, **incorporated** in UAE
- ✓ Foreign entity with **PoEM** in UAE

Territorial Taxation

- ✓ Natural person: **Only** income from business activity carried out in UAE, is taxable under CT

- ✓ Income from Permanent **Establishment** in UAE

- ✓ UAE **sourced** income



Calculation Mechanism - Taxable income

<u>Particulars</u>	<u>Amount</u>
Accounting Net Profit / (Loss) as per financial statement	XXX
<u>Adjustments</u>	
Add: Unrealized loss pertaining to a capital item, if recorded in the financial statement (in case of unrealized gain , the same is to be reduced)	XXX
Add: Net interest expense in excess of 30% of EBITDA – Thin Capitalization <ul style="list-style-type: none"> • Safe-harbor protection and group ratio rules to be allowed • Valid commercial reasons in case of Intra-group borrowing 	XXX
Add: 50% of entertainment expenses on customers, shareholders, suppliers, etc.	XXX
Add: Administrative penalties , recoverable VAT, donation paid to unapproved charity	XXX
Less: Exempted income (discussed ahead)	(XXX)
Taxable income	XXX

Calculation Mechanism - CT Payable

Particulars	Amount
Taxable Income	XXX
Corporate tax	
Tax on taxable income upto AED 375,000 (A)	0% CT
Tax on income above AED 375,000 (B)	9% CT
CT liability (A+B)	XXX
Less: Foreign Tax Credit (FTC)*, if any	(XXX)
Final CT Payable	XXX

* FTC allowable to be lower of the following:

- Tax paid in foreign country
- UAE CT payable on **such doubly taxed income**

Any **unutilized FTC** will not be allowed to be carried forward / refund

Accounting and Audit

- ✓ Basis for Computation of **Tax Base**
 - IFRS / alternative accounting standards to form the '**Starting Point**'
 - Tax base computation and IFRS – Fundamental gaps. Experience with EU's CCCTB
 - Increased **relevance of accounting and audit** functions
- ✓ Need for **allocation of expenses**, say, between FZP and its branches
- ✓ Accurate **characterization** of expenses. Eg. Entertainment expenses
- ✓ Accurate distinction between **Revenue items** and **Capital items**
- ✓ Need for separate accounting by **Branches** of Foreign entities (also, to determine FTC available)
- ✓ Group **consolidation**
- ✓ **Transfer Pricing** and Related Party **disclosures in financial statements**

07

Compliances under CT

Compliances under CT

Compliances under CT

Withholding Tax

0% withholding tax is proposed for all domestic and international payments

Registration

Businesses to obtain Tax Registration number within a prescribed time

Payment

Tax to be paid within 9 months from the end of relevant tax period
(No requirement to pay Advance tax)

Return of Income

Tax Return to be filed within 9 months from the end of relevant tax period

Assessment

FTA may review CT return, and may issue an assessment within prescribed time

Certain other questions

- ❖ Can FZPs that are enjoying 0% CT regime **accumulate their tax losses**?
- ❖ Can FZPs be included for the purpose of CT Group **consolidation**?
- ❖ Can a FZP **transfer its tax losses to its group company** (with > 75% common shareholding)?
- ❖ What if a FZP is a part of a **VAT group**?

Assessment of Financial Statements
– for high level impact assessment of CT proposals

Study of existing corporate and business structure, and mapping of business activities (undertaken in Mainland, Free Zones, or Outside UAE)

Detailed report on impact of CT proposals, and suggesting re-alignment / re-structuring

Workshops / training for various stakeholders

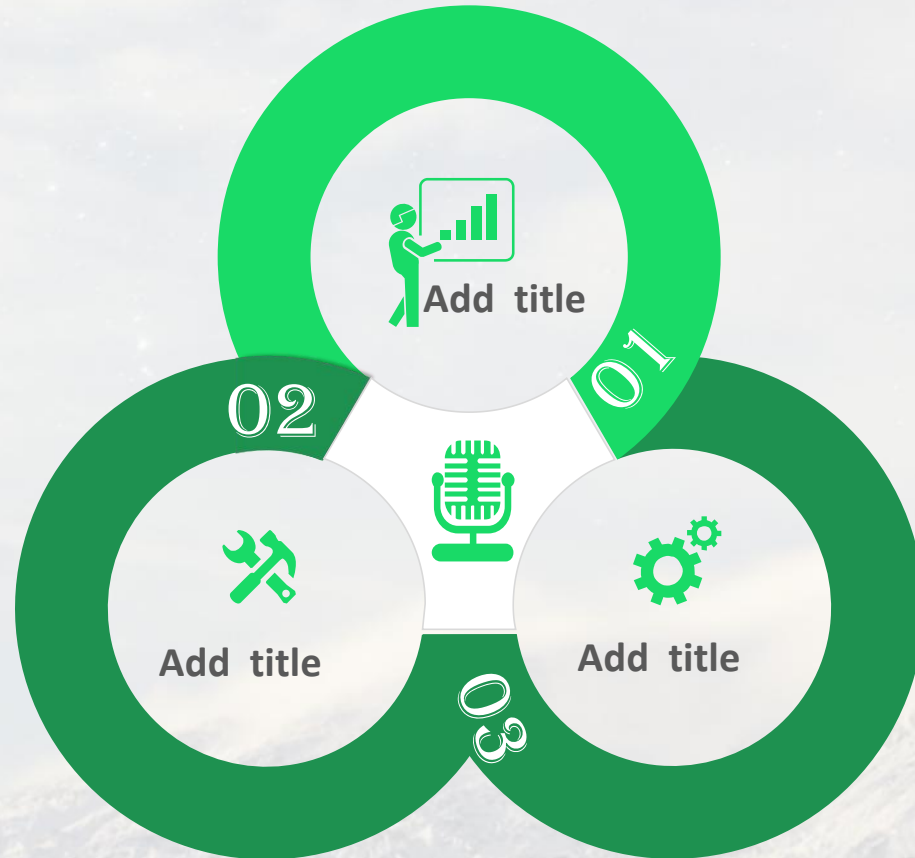
Developing implementation roadmap, outlining project timelines and steps

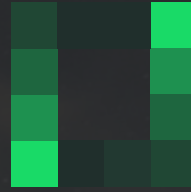


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THANK YOU