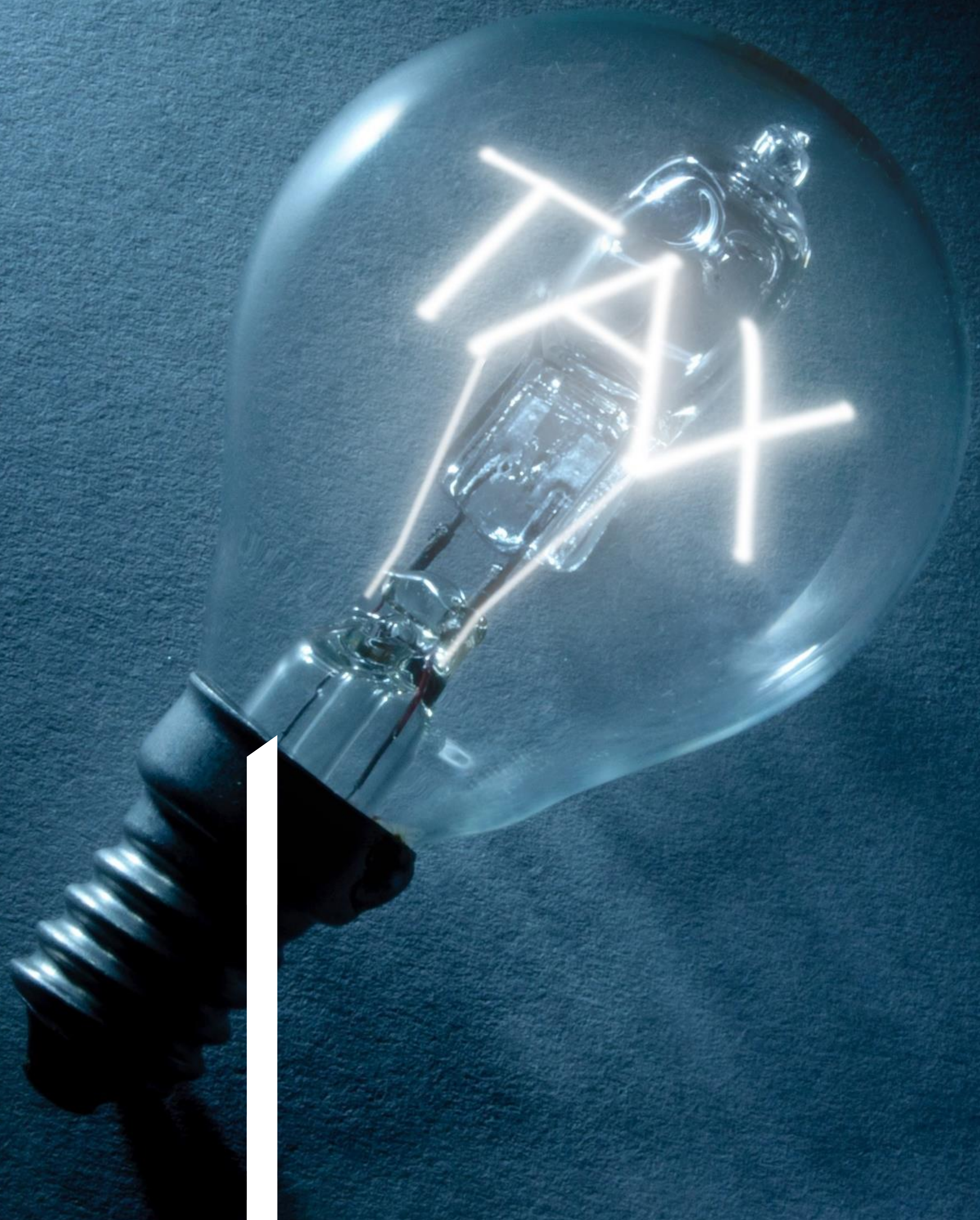
A PREFACE TO CORPORATE TAX IN THE UAE



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UAE INTRODUCES FEDERAL CORPORATE TAX

UAE's Ministry of Finance has announced that Federal Corporate Tax (CT) will be implemented in the UAE from the financial years starting on or after 01 June 2023.

Businesses and commercial activities will be subject to CT, except for the extraction of natural resources, which falls under the jurisdiction of individual Emirates.

In general, CT will be due on the profits of UAE-based businesses, as reported in the Financial Statements prepared according to internationally accepted accounting standards with minimal adjustments.

The Federal Tax Authority (FTA) has updated its website and published Frequently Asked Questions (FAQ) on CT.

RATE OF CT

CT rates will be 0% for taxable profits up to AED 375,000 and 9% for taxable profits above this threshold in support of small businesses and start-ups. SMEs, startups, and individuals earning net income (gross income less deductible expenses) of less than AED 375,000 will not have the additional burden of CT liability and compliance.

There will be a different rate for large multinationals that meet specific criteria set with reference to 'Pillar Two' of the OECD Base Erosion and Profit Shifting project. However, the rate applicable to larger multinationals has not yet been announced.

Large Multinationals for these purposes include multinational corporations with consolidated global revenues of more than EUR 750m (approx. AED 3.15 bn).

EFFECTIVE DATE

The UAE CT regime will become effective for financial years starting on or after 1 June 2023. Below is an illustrative list of financial years within and outside the purview of CT:

FY outside the purview of CT		FY within the purview of CT
01 June 2022- 31 May 2023	**CT Will be applicable from financial years starting on or after 01 June 2023**	01 June 2023- 31 May 2024
01 August 2022- 31 July 2023		01 August 2023- 31 July 2024
01 October 2022- 30 September 2023		01 October 2023- 30 September 2024
01 January 2023- 31 December 2023		01 January 2024- 31 December 2024
01 April 2023- 31 March 2024		01 April 2024- 1 March 2025

There is no clarification on longer or shorter financial periods, and similar treatment is expected to be followed in such cases.

SCOPE OF THE TAX AND EXCEPTIONS

CT will be applicable to all businesses in the UAE on tax profits after minimal adjustments to book profits reported in financial statements prepared in accordance with international accounting standards. A business is considered as a separate legal person requiring a license or permit to carry out the relevant commercial, industrial and/or professional activity in the UAE.

There are certain exceptions clarified in the FAQs. The inclusions and exclusions/ exemptions are summarised below:

Inclusions	Exclusions/ Exemptions
Business income earned by an individual under a commercial license will be within the scope of CT.	Individuals earning income from employment, real estate, investment in shares or other personal income not related to a UAE trade or business
Banking operations will be subject to CT. The position on current Emirate level Corporate taxes will be clarified in due course.	Dividends or capital gains earned by a UAE business from its qualifying shareholdings
Freelance professionals will be subject to CT if they earn income from activities carried out under a freelance license/permit.	Businesses engaged in the extraction of natural resources will remain subject to Emirate level corporate taxation and be outside the scope of UAE CT.
Foreign entities and individuals conducting a trade or business in the UAE in an ongoing or regular manner	Free Zones in the UAE can benefit from the CT incentives that are currently being offered to them, provided they adhere to all regulatory requirements. However, Free Zone companies will be required to register and file CT returns

Information on other UAE CT exemptions and exclusions will be provided in due course.

TAX GROUP AND TAX LOSSES

Businesses in the UAE can form a tax group and be treated as a single taxable person. As a result, tax groups can file a single return for the whole group and offset losses among members.

Tax losses can be carried forward and offset against taxable income in subsequent financial periods under the CT regime. The FAQs have not provided further information on the rules to carry-forward tax losses.
Qualifying intra-group transactions and reorganisations will not be subject to UAE CT provided the necessary conditions are met

Tax grouping can be a good option to take benefit of group losses. If all the entities of the group have taxable income above the threshold, tax grouping may not be preferable

OTHER RELATED TAX PROVISIONS

- There will be no withholding taxes on domestic and cross-border payments of any nature.
- Transfer pricing rules and documentation requirements will be applicable as per the OECD Transfer Pricing Guidelines to ensure that transactions between related parties are carried out on arm's length terms (i.e., as if the transaction was carried out between independent parties).

REGISTRATION AND COMPLIANCE REQUIREMENTS

Currently, no information is available on the registration process. However, we expect that FTA will issue guidance soon.

To ensure the compliance burden is kept to a minimum, only one CT return will be filed per financial period electronically. Therefore, there will not be any requirement for provisional or advance filings.

KEY TAKE AWAYS

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By implementing CT, the UAE has stated that it intends to address the challenges arising from the digitalization of the global economy and ensure the implementation of a global minimum tax.

The UAE CT will be one of the most competitive CT regimes in the world, with 9% as the statutory tax rate combined with exemptions and relief to small businesses.

Businesses will have plenty of time to prepare for the introduction of CT. While the fine print provided in law and regulations is awaited, the following areas could need immediate attention:

1. As CT liability is based on accounting profit [post making certain allowable adjustments], having audited financial statements could be a mandatory pre-requisite for filing CT returns.
2. Foreign businesses that have obtained non-resident VAT registration in the UAE, will need to consider whether the implementation of CT exposes them to the creation of a Permanent Establishment (PE) and, accordingly, being liable CT compliance in the UAE along with payment of CT liability. The Double Taxation Avoidance Agreements will be required to be assessed in such cases.
3. Salaries/compensation paid to shareholders/members may need to be revisited as typically, deduction on such accounts is restricted.
4. Maintaining asset-wise details to capture accurate depreciation as the standards as per CT law may differ and recording movement of assets in order to record differences.
5. Transactions with related parties within and outside of the UAE may need to be made with a mark-up approved by concepts driven by Transfer pricing standards. Accordingly, deductions of the expenses/costs from related parties may be questioned. All intra-group transactions should be assessed in line with the Transfer Pricing (TP) requirements from the OECD. A Transfer pricing policy may be required for such intra-group transactions.
6. As specified dividends and capital gains are exempted from certain qualifying shareholdings, deductions attributable to such expenses associated with earning this revenue may be restricted.
7. If the business is involved in taking or loans and providing loans, deductions attributable to interest expenses may be restricted.
8. Typically, there are special provisions around the deduction for the following expenses under Corporate Tax, which need to be assessed, once guidance has been received from the FTA:
    - Relief on bad debts.
    - Deduction on charitable contributions, Corporate Social Responsibilities (CSR), innovation spends and similar.
9. Commitments on CT exemptions provided by the Free Zone licensing authorities.
10. Evaluating the applicability of thin capitalization rule.
11. In the light of CT and Transfer pricing provisions, the requirement for Economic Substance Regulation and Country by Country reporting may undergo a change.

HOW CAN WE HELP?

- Evaluating the overall impact of CT on your businesses in the UAE along with highlighting procedural aspects associated with compliance and exemptions.
- Preparing numerical simulation of your CT obligations with reasonable assumptions, which could aide in commercial negotiations.
- Highlighting the need to undergo restructuring/remodeling to optimize CT impact.
- Highlighting numerical benefits of CT optimization options.
- Highlighting the eligibility of foreign tax credits which could be used to optimize CT impact, which otherwise may be considered a tax cost.
- Identifying the need to conduct TP studies at domestic and international levels.
- Highlighting the need to update contracts, agreements, policies/procedures and systems to factor CT implications.
- Highlighting the need to collect and maintain additional documentation as prescribed by the law.
- Conducting awareness sessions for your key stakeholders/business partners.
- Identifying the need to plan the resources/departments that will have the additional responsibility of managing CT obligations.
- During and post-implementation of CT, we will assist businesses with registrations, preparation of forms and returns, TP documentation and tax accounting.

FOR MORE INFORMATION, PLEASE CONTACT OUR TAX ADVISORY TEAM

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