

Public Consultation Document Corporate Tax in UAE



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INTRODUCTION

On 31 January 2022, the Ministry of Finance announced that the United Arab Emirates (UAE) will introduce a federal Corporate Tax (CT) on business profits effective for financial years starting on or after 1 June 2023. Ministry of Finance has published public consultation document & this document contains information on the proposed UAE CT regime to seeks views from interested parties on its main features and implementation.

The document does not reflect the final view of the UAE Government and is not intended to comprehensively address all possible aspects of the proposed UAE Corporate Tax regime. As such, this consultation document should not be used or relied upon to make individual or commercial decisions as it does not represent the final legislation. Further information on the technical details and other specifics of the UAE Corporate Tax regime will be made available in due course.



PARTNER'S MESSAGE



JAY KRISHNAN
PARTNER – TAXES,
HLB HAMT

The introduction of a federal CT regime is intended to help the UAE achieve its strategic ambitions and incentivise businesses to establish and expand their activities in the UAE. The certainty of a competitive regime, together with the UAE's extensive network of double tax treaties, will cement the UAE's position as a world leading destination for investment. By consulting with the business community and other interest parties as part of the implementation process, the UAE Government is demonstrating its commitment to implementing a CT regime that is compatible with the UAE's business environment. On behalf of the UAE Government, the Ministry of Finance welcomes comments on this consultation document by 19th May 2022. Responses should be submitted through <https://www.mof.gov.ae/en/resourcesAndBudget/Pages/Corporate-Tax-Submission-Public-Consultation.aspx>

The Ministry of Finance would appreciate clear and concise comments with, where possible, examples, data or other information to support views on the main features and implementation of the UAE CT regime. Interested parties are encouraged to focus their comments on aspects of the proposed CT regime that may help to reduce compliance cost and complexity, and improve certainty for both businesses and the tax administration. Interested parties can also provide comments on other areas, including areas that are otherwise not covered in this document. Any comments received after 19th May 2022 or that are submitted in any manner other than by using the prescribed online submission form will not be considered. Submissions will remain confidential and will not be published or shared with any other Government department.

I recommend you to follow the link mentioned above and share your valuable suggestions if any, so that the ministry will be able to compile such recommendations while the Corporate Tax regulations are going to publish.

DISCLAIMER

Views expressed in this document are based on the information published by the Ministry of Finance in the Public Consultation Document dated 28 April 2022 and certain generally accepted practices on corporate tax in other jurisdictions.

CORPORATE TAX APPLICABILITY

Residency is a key determinant of whether business profits will be subject to CT in the UAE.

RESIDENTS



LEGAL PERSON

An entity incorporated in the UAE or a foreign company that is effectively managed and controlled in the UAE.

UAE resident persons will be taxable in the UAE on their worldwide income, which for a natural person will be limited to the income earned from their business activity carried out in the UAE.



NATURAL PERSON

Natural person engaging in business either in their own name or through an unincorporated partnership will be treated as resident person.

NON RESIDENTS

Non-residents will be subject to UAE CT on taxable income from their PE in the UAE. The concept of a PE under the proposed UAE CT regime will be based on Article 5 of the OECD Model Tax Convention.

The activity threshold that will trigger a PE for a foreign company in the UAE will be determined by the following two main tests:

- Fixed place of business test.
- Dependent agent test.



FOREIGN COMPANY

Treated as a resident person if effectively managed & controlled in UAE. For determining whether an entity is effectively managed and controlled in the UAE is a question of fact.

Generally it intends, where the directors or other decision makers of the company make key management or commercial decisions.

INVESTMENT MANAGER EXEMPTION

The UAE CT regime will allow regulated UAE investment managers to provide discretionary investment management services to foreign customers without triggering a UAE PE for the foreign investor or the foreign investment fund. This exemption will be subject to conditions that are comparable to similar regimes in leading financial centres.

SCOPE OF CORPORATE TAX

TAXABILITY

Applicable to natural persons engaged in a business or commercial activity in UAE. This generally depends upon whether activity requires commercial or equivalent permit from competent authority.

OUT OF SCOPE

Salary income and other personal income by UAE or foreign individual such as dividend, interest, rental income from real estate etc.

Income from Real estate and other investments held through private or family trust on behalf of beneficiaries are natural person.

LEGAL PERSON

UAE CT is applicable to UAE companies and other legal person as well as foreign entities that have a PE. It includes:



Limited Liability Companies



Private Shareholding Companies



Public Joint Stock Companies



Other entities established under the laws of the UAE that have separate legal personality.

It also includes legal person incorporated in foreign jurisdiction managed and controlled by UAE.



EXEMPT PERSONS

- Federal and Emirate governments and their departments, authorities, and other public institutions.
- Wholly Government-owned UAE companies that carry out a sovereign or mandated activity, & that are listed in a Cabinet Decision.
- Businesses engaged in the extraction and exploitation of UAE natural resources that are subject to Emirate-level taxation.
- Charities & other public benefit organisations that are listed in a Cabinet Decision.
- Public and regulated private social security and retirement pension funds.
- Investment funds, subject to meeting the conditions referred to in section 3.7.



EXEMPT INCOME



DIVIDEND

Domestic dividends from UAE companies including dividends from Free Zone Persons are exempt from CT in the UAE. However, Dividend paid by a foreign company is exempt, provided certain conditions are met.



CAPITAL GAINS

Capital gain on sale of shares in UAE & foreign companies are exempt provided that the shareholding is at least 5% of share in subsidiary and the foreign subsidiary subject to CT (or similar tax) of at least 9%.

Capital gains on the disposal of shares in a Free Zone Person will be exempt if it is a holding company and substantially all its income is derived from shareholdings in subsidiary companies that meet the participation exemption condition.

FOREIGN BRANCH EXEMPTION

- Where a UAE company has a foreign branch, it is possible to elect to
 - (i) claim a foreign tax credit for taxes paid in the foreign country, or
 - (ii) claim an exemption for foreign branch profits.
- The election to claim a branch profit exemption is proposed to apply to all foreign branches of the UAE company and will be irrevocable. An exemption for foreign branch profits may not be available where the foreign branch is not subject to a sufficient level of tax in the foreign jurisdiction in which it is located.

OTHER EXEMPT INCOME

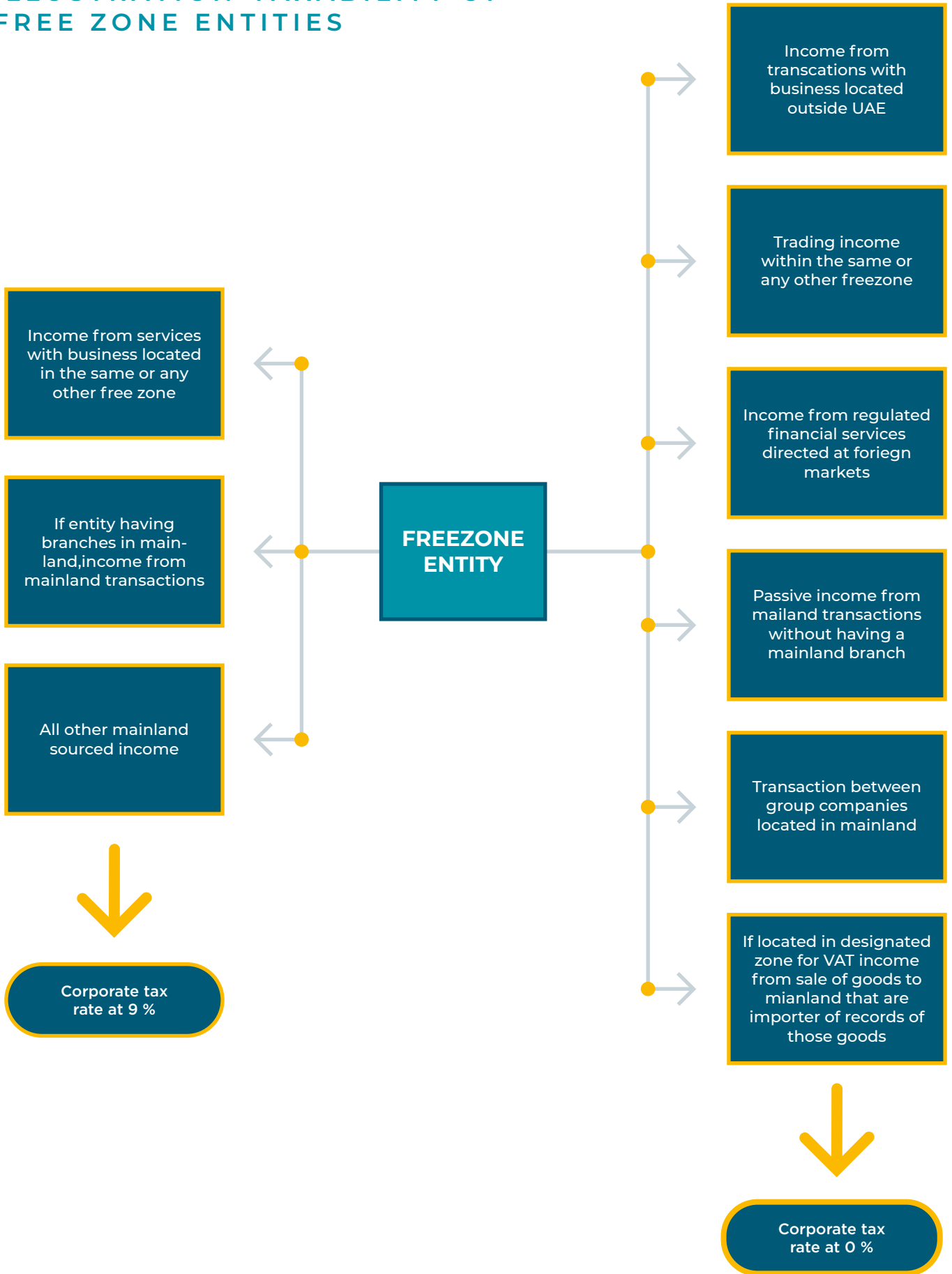
UAE CT regime will exempt income earned by a non-resident from operating or leasing aircraft or ships (and associated equipment) used in international transportation, provided the same tax treatment is granted to a UAE business in the relevant foreign jurisdiction under the reciprocity principle.

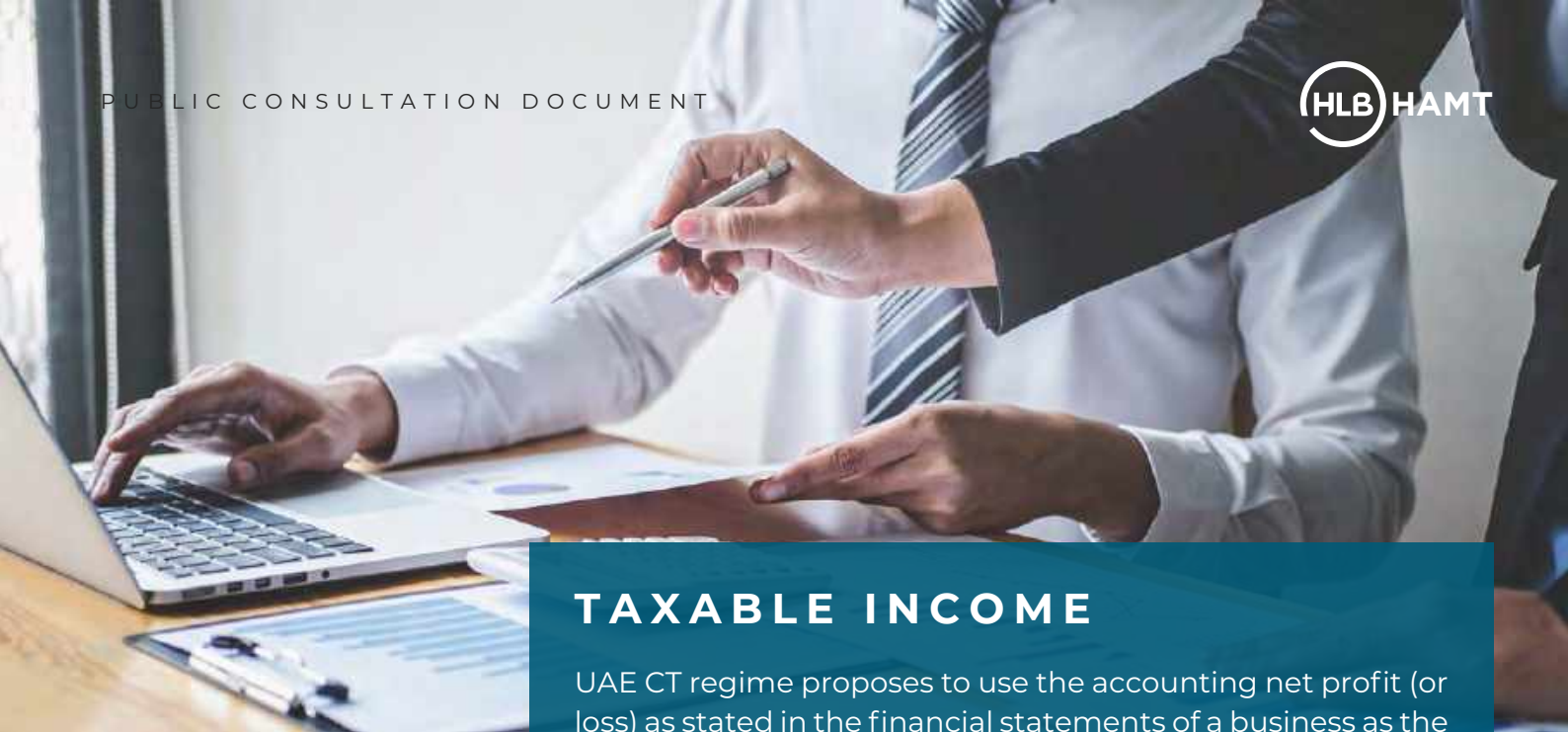


FREE ZONES

- The 0% CT regime will also apply to transactions between Free Zone Persons and their group companies located in mainland UAE but, payments made to the Free Zone Person by a mainland group company will not be a deductible expense.
- Free Zone Person located in a Designated Zone for Value Added Tax (VAT) purposes can benefit from the 0% CT rate on income from the sale of goods to UAE mainland businesses that are the importer of record of those goods.
- Free Zone Person can benefit from a 0% CT rate on income earned from transactions with businesses located outside of the UAE and from trading with businesses located in the same or any other Free Zone.
- Free Zone Person that has a branch in mainland UAE will be taxed at the regular CT rate on its mainland sourced income.
- If free zone entities have **ONLY** passive income (E.g., interest, royalties, & capital gains from shares in mainland companies) from mainland without having branches in mainland it will be taxed at 0%.
- Any other mainland sourced income will disqualify a Free Zone Person from the 0% CT regime in respect of all their income.
- Where a Free Zone Person benefits from the 0% CT regime in respect of mainland sourced income, such income will be within the scope of withholding tax (to be applied at 0%).

ILLUSTRATION-TAXABILITY OF FREE ZONE ENTITIES





TAXABLE INCOME

UAE CT regime proposes to use the accounting net profit (or loss) as stated in the financial statements of a business as the starting point for determining their taxable income. The financial statements should be prepared using accounting standards and principles that are acceptable in the UAE, and businesses will use their financial accounting period as their (annual) tax period.

UNREALISED GAINS AND LOSSES

Unrealised gains or losses on capital items are not considered when calculating taxable income. Revenue items are items that have a short-term impact on a business. Revenue assets are items other than capital items and can include items such as the goods a business sells. Unrealised gains or losses on revenue items will need to be considered when calculating taxable income.

INTEREST CAPPING RULES

UAE CT regime will cap the amount of net interest expense that can be deducted to 30% of a business's earnings before interest, tax, depreciation, and amortisation (EBITDA), as adjusted for CT purposes. This is in line with the interest limitation rules proposed by Action 4 of the OECD's Base Erosion and Profit Shifting project which have been implemented by countries around the world.

To reduce the administrative burden, businesses may be allowed to deduct up to a certain amount of net interest expenditure (safe harbour or de minimis amount) irrespective of the interest deductibility limit based on the EBITDA rule.

NON-DEDUCTIBLE EXPENSES

- Related party payments made to a Free Zone Person that is taxed at 0% on receipt of the income.
- Expenditure incurred to entertain customers, shareholders, suppliers & other business partners are capped at 50%.
- No deductions for penalties, recoverable VAT, donations to unapproved organizations / charities.



OFFSET OF LOSSES

Businesses can offset loss incurred against the taxable income of future periods, up to a maximum of 75% of the taxable income in each of the future periods.

CONDITIONS

Tax losses may be carried forward indefinitely provided the same shareholder owns at least 50% of the share capital. If there is a change in ownership, tax losses may still be available provided the new owners carry out same/similar business.

Further it's important to note that no tax loss relief will be available for the following losses:

- Losses incurred before the effective date of CT.
- Losses incurred before a person becomes a taxpayer for UAE CT purposes.
- Losses incurred from activities or assets which generate income that is exempt from UAE CT; or
- Losses incurred by a Free Zone Person that are not attributable to a PE in the mainland.

TAX GROUPS

The UAE CT regime will allow full consolidation for tax purposes (tax grouping) for essentially wholly owned groups of companies, and the transfer of losses.



CONDITIONS

- Parent company holds at least 95% of the share capital and voting rights of its subsidiaries.
- In case of subsidiary, owned indirectly by the parent company and other subsidiaries own at least 95% of its shares, or if it is a UAE branch of the parent company or one of its subsidiaries.
- Notice signed by the parent company & all subsidiaries will need to be submitted to the FTA.

Tax group's will be treated as a single taxable person with the parent company responsible for the administration and payment of CT on behalf of the tax group.

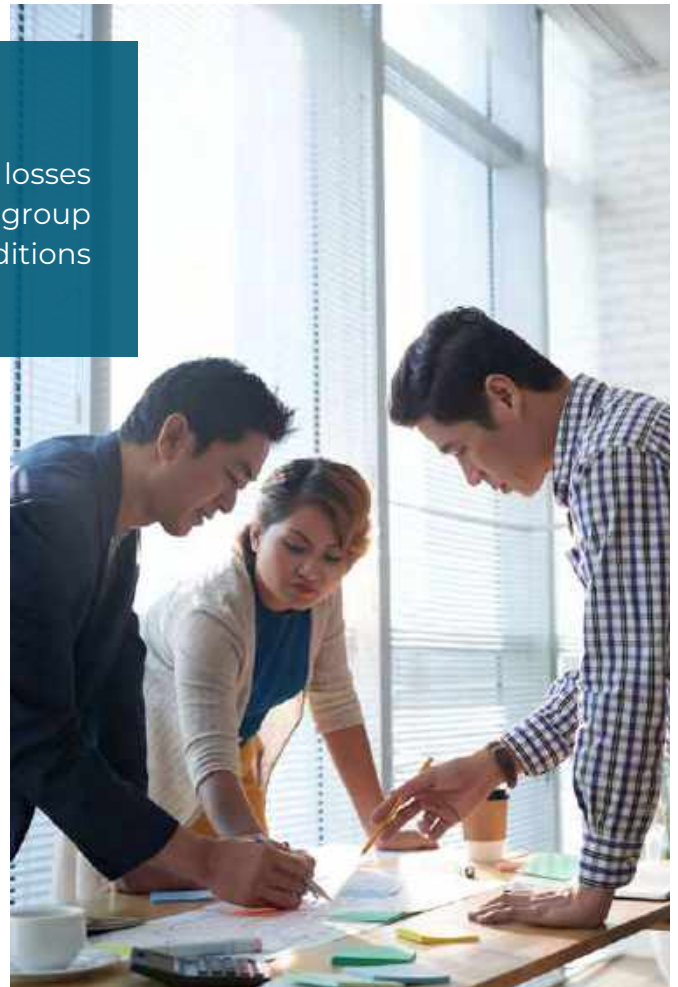
TRANSFER OF LOSSES

UAE CT regime can allow a transfer of tax losses from one group company to another group company with profits, provided certain conditions are met.

CONDITIONS

- Tax losses may be transferred to another UAE group company with profits, provided the UAE group companies are at least 75% commonly owned.
- No losses may be transferred from exempt companies or those which benefit from a 0% Free Zone CT regime.

Tax losses will be limited to 75% of the taxable income of the company receiving the transferred losses in the relevant period.



GROUP RELIEF

Proposed UAE CT regime will allow for an exemption or deferral of CT in respect of the transfer of assets or liabilities between members of a group. In addition, the CT regime will allow certain corporate reorganisation transactions (e.g., mergers) to be undertaken on a tax neutral basis, such that no taxable gain or loss arises.

Intra-group transfer relief will be available for transfers of assets and liabilities between UAE

resident companies that are at least 75% commonly owned, provided the assets and/or liabilities being transferred remain within the same group for a minimum of three years.

If the conditions for intra-group relief does not continue to be met, any gain or loss that would have arisen upon the initial transfer will be considered in transferor's tax returns



TRANSFER PRICING

The UAE CT regime will have transfer pricing rules to ensure that the price of a transaction is not influenced by the relationship between the parties involved. To achieve this outcome, the UAE will apply the internationally recognised "Arm's Length" principle to transactions and arrangements between related parties and with connected persons.

All Related Party transactions & transactions with Connected Persons will need to comply with transfer pricing rules and the arm's length principle as set out in the OECD Transfer Pricing Guidelines.

TRANSFER PRICING DOCUMENTATION

A business will also need to maintain a master and local file (with format & content consistent with the requirements prescribed under OECD BEPS Action 13) where the arm's length value of their Related Party transactions exceeds a certain threshold in the relevant tax period.

CORPORATE TAX RATES

0% for taxable income not exceeding AED 375,000.

9% for taxable income exceeding AED 375,000

SMALL BUSINESS RELIEF

In order to manage the compliance burden to start-ups and small business, The UAE CT regime proposed to provide relief for small businesses in the form of simplified financial & tax reporting obligations.

WITHHOLDING TAX

UAE CT is proposed to have a 0% (zero percent) withholding tax will apply on domestic & cross-border payments made by UAE businesses.

- UAE sourced income earned by a foreign company that is not attributable to a PE in the UAE of that foreign company.
- Mainland UAE sourced income earned by a Free Zone Person that benefits from the 0% CT regime, unless the income is attributable to a mainland branch of that Free Zone Person.
- Dividends and other profit distributions made by a Free Zone Person that benefits from the 0% CT regime to a mainland UAE shareholder in the Free Zone Person.

TAX CREDITS

UAE CT regime will allow a credit for the tax paid in a foreign jurisdiction against the UAE CT liability on the foreign sourced income that has not been otherwise exempted. This is known as "Foreign Tax Credit"



The maximum Foreign Tax Credit available will be the lower of:

- The amount of tax that paid in the foreign jurisdiction; or
- The UAE CT payable on the foreign sourced income.

ADMINISTRATION

A business subject to CT will need to register with FTA and obtain tax registration number within a prescribed period. Business will need to prepare and file one tax return and other supporting schedules.

DUE DATE OF FILING RETURN

Each tax returns along with supporting schedules will to be submitted within 9 months of the end of the relevant financial period. There will be no requirement for a business to file a provisional CT return and make advance payments of CT.

For example:

Financial Year	Due Date of Filing & Payment
1 Jul 2023 - 30 Jun 2024	31 Mar 2025
1 Jan 2024 - 31 Dec 2024	30 Sep 2025
1 Apr 2024 - 31 Mar 2025	31 Dec 2025

ASSESSMENT

The UAE CT regime will be based on a self - assessment principle. FTA may review a CT return filed & may issue an assessment within the timeframe prescribed in the Tax Procedures Law. A taxpayer may challenge an amended assessment issued by the FTA via the processes & procedures outlined in the Tax Procedures Law.

CLARIFICATIONS

Where there is uncertainty in relation to a proposed or entered into arrangement or transaction, a business may apply to the FTA for a clarification with regards to the correct or intended CT treatment.

DOCUMENTATION REQUIREMENTS

A business will be required to maintain financial and other records that explain the information contained within the CT return and other documents submitted to the FTA. The UAE CT regime will require a Free Zone Person to have audited financial statements if it wants to benefit from the 0% CT regime.



GOING FORWARD

We, HLB HAMT can guide you on the queries on public clarification points and on a high level how the proposed Corporate Tax regulations are going to impact on the business in UAE.

If you have any queries or questions, please use the below channels to contact us:

Email: tax@hlbhamt.com

Phone: +971 4 3277 775



JAY KRISHNAN
PARTNER
jk@hlbhamt.com



SUMESH KRISHNA
PARTNER
sumesh@hlbhamt.com



GIRISH NAIR
MANAGER
girish.g@hlbhamt.com

Corporate Office

HLB HAMT

Level 18, City Tower-2,

Sheikh Zayed Road

PO Box 32665

Dubai – United Arab Emirates.

