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FAQs on Corporate Tax in the UAE

UAE introduces
Federal Corporate Tax
on business profits

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Introduction

The roots of taxation lie in the act of record keeping. Taxes have been an integral part of many economies for years now, however the tax landscape of the Gulf region had not gained momentum till 2015.

OECD and G20 published final reports outlining recommendations for Action Plan on Base Erosion and Profit Shifting ('BEPS') in 2015. Being the signatory to Inclusive Framework members and Multilateral Convention, UAE brought into force various regulations requiring disclosures of the organisational structure and nature of activities.

UAE introduced VAT on 1st January 2018 at a standard rate of 5% backed by a vision to reduce the economy's dependence on income sourced from hydrocarbons. In 2019, the country further introduced Country by Country Reporting (CbCR) and Economic Substance Regulation (ESR) and in 2020, it became mandatory to furnish details of the Ultimate Beneficial Owner (UBO). Each of these regulations are concrete steps taken by the UAE to comply with its commitment to BEPS.

In line with its commitment to the Global Minimum Taxation Regime, UAE recently introduced Corporate Tax and CT will apply equally to all categories of profit and net income reported in the financial statements prepared in accordance with internationally acceptable accounting standards. Corporate Tax coming into force in the UAE landscape catapults the country into being a part of a global financial ecosystem instead of limiting its potential as a tax haven.

Introduction of Corporate Tax (CT) in the UAE meets international standards for tax transparency and prevents harmful tax practices; further cementing the UAE's position as a global destination for business. Here are some Frequently Asked Questions pertaining to areas within the UAE business landscape likely to be impacted by Corporate Tax.

CEO's message on Corporate Tax in UAE

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Since 31st January 2022, the corporate corridors of UAE's private sector have been preparing and readying their entities for the announcement of the UAE Federal Corporate Tax Law which will pave the way for companies to align themselves with the new corporate tax regime.

The new corporate tax regime brings forth the need for businesses to put into place a proper accounting system and issuance of annual financial audit reports which will form the basis for calculation of Corporate Tax. Corporate tax conversations have dominated networking events, forums, seminars, webinars, and panel discussions since the beginning of 2022. The new UAE Federal Corporate Tax Law will govern the Corporate Tax regime which will come into effect by June 2023.

It is now time for businesses, tax advisors, audit firms, accounting software firms and many other players in the UAE economic environment to up their game and deliver towards a seamless implementation of corporate tax in the UAE. In this period of transition, it is imperative that stakeholders and business owners walk the extra mile to evaluate their corporate structures, assess their audit readiness and ensure they complement the corporate tax regime is a compliant manner.

We are ready to handhold businesses as the waves of change sweep the UAE's economic environment with the UAE Federal Corporate Tax Law coming into play. We aim to leave no stone unturned in helping you understand the nuances of corporate tax through our digital channels of communication. The UHY James team is here to help.

Free Zones

Whether all the business transactions undertaken by the taxable person in free zone shall be subject to CT?

Free zones in the UAE offer various tax incentives, however as per Article 3 and Article 18 of the federal decree law no. 47 of 2022, the qualifying freezone person shall be subject to corporate tax at 0% on the Qualifying income and others shall be taxed at 9%

The freezone person shall be considered as Qualifying freezone person after fulfilling the following conditions:

- Maintain adequate substance in UAE
- Derives Qualifying Income as specified in a decision by the Cabinet
- Non-election to be subject to Corporate Tax at 9%
- Compliant with Arm's Length Principle and Transfer pricing documentation for related party transactions

What are the consequences of non-fulfilment of Qualifying freezone conditions and for how many years, the tax incentive shall be allowed to Qualifying freezone person?

A Qualifying Free Zone Person that fails to satisfy any of the given conditions at any time during a Tax Period shall cease to be a Qualifying Free Zone Person from the beginning of that Tax Period and shall be taxed at a rate of 9% on taxable income.

The given rate of 0% and 9% shall apply to a Qualifying Free Zone Person for the balance tax incentive period stipulated in the applicable legislation of the respective Free Zone. Further, the period may be extended at the suggestion of the Minister, but any one period shall not exceed (50) fifty years.

Transfer Pricing

When shall Transfer Pricing rules be applicable on UAE entity?

When Taxable Person has an arrangements or transaction with its Related Parties and/or Connected Persons as on the effective date of the relevant tax period.

Who is connected person?

The person shall be considered a Connected Person of a Taxable Person if that Person is:

- An owner of the Taxable Person.
- A director or officer of the Taxable Person.
- A Related Party of any of the Persons referred above.

Will TP rules be applicable on connected persons

Yes, the business transactions undertaken with related parties including connected person in UAE shall be covered under the ambit of Transfer Pricing rules specified in the Decree law.

Whether domestic companies being a member of tax group needs to undertake TP compliances?

Intra-group transactions carried out between tax group member entities shall not be required to comply with TP rules.

How to determine the market value of the payment made to connected person and relatives?

Market value can be agreed through an arm's-length free market transaction between persons who are not related or connected by securing supporting documents from approved source or database for bench marking.

Who needs to maintain master file and local file and is there any specific form for Master file and local file?

The Taxable Person who is undertaking related party and/or connected persons transactions, needs to maintain master file and a local file in the form prescribed by the Authority. The transaction limits to trigger the preparation of respective files is yet to be specified by the Authorities.

When TP compliance document be required to be submitted to the Authorities?

Upon request by the Authority, a Taxable Person shall provide the relevant documents within (30) thirty days following the request by the Authority, or by any such other later date as directed by the Authority.

What we need to consider to choose or apply the TP method for the transaction or arrangement?

The following has to be reviewed and supported while choosing the TP methods

- The contractual terms of the transactions
- The characteristics of the transactions
- The economic circumstances in which it is conducted.
- The functions performed, assets employed, and risks assumed by the Related Parties entering into it
- The business strategies employed by the Related Parties entering in to it

Special relief to Small Businesses

Revenue of the Taxable Person for the relevant Tax Period and previous Tax Periods does not exceed a threshold to be set by the Minister and meets all other conditions prescribed by the Minister can claim special relief.

Entities claiming the relief may lose the benefit of

- Exempt Incomes specified in the Decree Law shall be added back considering the revenue threshold
- Reliefs available on transfers within qualifying group and business restructuring will be added back
- General Deductions are not allowed in computation of revenue.
- Tax Losses shall not be allowed to carried forward and adjust in the subsequent tax periods.
- Transfer pricing documentation requirement will not be applicable.

Authority may request any relevant information or records from the Taxable Person within the timeline prescribed by the Authority.

Related Party Transactions

If income is adjusted for the related party transaction, corresponding adjustment to other related party is allowed?

Yes, the Authority shall make a corresponding adjustment to the Taxable Income of the Related Party that is party to the relevant transaction or arrangement.

If foreign tax authority makes an adjustment, how UAE income can be adjusted?

The taxable person in UAE can make an application to the Authority to make a corresponding adjustment to its Taxable Income.

Tax Grouping

Conditions for Tax grouping

- Parent company holds at least 95% (directly or indirectly) of the share capital and voting rights of its subsidiaries,
- The Parent Company is entitled to at least 95% (directly or indirectly) of the Subsidiary's profits and net assets
- All group members must be resident juridical person
- Exempt person or a Qualifying Free Zone Person shall not be a tax group member,
  All group members must have the same financial year and prepare their financial statements using the same accounting standards.

Benefits of forming tax group

- Tax group is treated as a single taxable person leading to compliance cost savings
- Loss is allowed to offset against the Taxable Income of the Tax Group
- Intra-group transaction shall not be subject to TP compliances

Any provision to offset the tax losses of group companies (taxable person) not forming Tax group?

Offset of tax losses from taxable income of another taxable person in a same group can be allowed subject to following condition,

- Taxable person is resident juridical person
- Either of Taxable Person has at least 75% (direct or indirect ownership interest) in the other, or a third Person has at least 75% (direct or indirect ownership interest) in each of the Taxable Persons,
- Ownership interest must exist from the start of the Tax Period in which the Tax Loss is incurred till the end of the Tax Period in which offsets shall be done
- No loss transfers from exempt companies or Qualifying FZ person
- Taxable person(s) must have the same financial year and prepare their financial statements using the same accounting standards.

When a member entity of tax group can be de-registered from tax group?

A group member entity can leave the Tax Group in the following circumstances:

- With the approval by the Authority of an application by the Parent Company and the respective Subsidiary.
- Where the respective tax group member entity, no longer meets the conditions to be a member of the Tax Group.

Exempt Taxpayers

Are all the companies subject to corporate tax provisions?

No, Following is the list of entities which are not subject to applicability of corporate tax provisions.

- Government Entity (other than conducting a Business or Business Activity under a Licence issued by a Licensing Authority.
- Government controlled entity (other than conducting a Business or Business Activity that is not its Mandated Activities)
- Businesses engaged in the extraction and exploitation of UAE natural resources (other than contractors, subcontractors, suppliers or any other Person used or contemplated to be used in any part of the performance of the Extractive Business)
- Non-Extractive Natural Resource Business (subject to conditions)
- Qualifying Public Benefit Entity under Article 9 of this Decree-Law
- Qualifying Investment Funds under Article 10 of this Decree-Law
- Public pension, Private pension, social security fund that is subject to regulatory compliances
- A juridical person (wholly owned and controlled by an Exempt Person)

Disallowable Expenses

List of disallowable expenses are:

- 50% of entertainment, amusement, or recreation expenditure (expenditure incurred for entertaining the customers, shareholders, suppliers or other business partners)
- Fines and penalties, other than amounts awarded as compensation for damages or breach of contract
- Bribes or other illicit payments.
- Dividends, profit distributions or benefits of a similar nature paid to an owner
- Amounts withdrawn from the Business by a natural person
- Donations, grants or gifts made to an entity that is not a Qualifying Public Benefit Entity.
- Tax on income imposed on the Taxable Person outside the UAE Recoverable VAT
- Related party expenses in excess of Arm's Length Pricing (ALP)
- Expenditure incurred in deriving Exempt Income
- Non-business expenditures
- Interest capping up to 30% of business EBITDA excluding any exempt income (Excluding Natural Person business, banks, Insurance business)
- Corporate Tax imposed
- Remuneration paid to partner/owner and connected person in excess of market value.

Whether tax depreciation needs to be calculated separately other than book depreciation?

No, there is no provision in the Federal Decree Law no. 47 of 2022 for maintaining separate books of accounts for taxation.

What is considered for deriving deductible Net Interest Expenditure (NIE) and can it be carry forward?

Net Interest Expenditure for a particular Tax Period is as follows

- Interest expenditure incurred during the Tax Period + NIE carried forward (if any) (-) the taxable Interest income derived during that same period.
- Further, the amount of NIE disallowed in a particular tax period may be carried forward and deducted in the subsequent (10) Tax Periods.

Tax Loss carry forward and Off set

Losses incurred before effective date of Law or person becomes taxable person will be allowed to be claimed for tax loss relief?

No, any book loss incurred before the effective date of CT and/or before becoming taxable person will not considered for tax loss relief (i.e., carry forward and offset).

What are the conditions for carry forward of loss?

To carry forward a loss, both the conditions must be satisfied

- 50% of the shareholders capitals are same (from the tax period when tax loss was incurred till Tax Period in which the Tax Loss or part thereof is offset) and,
- If there is any change in ownership, then same or similar business or business activity shall be carried on

***Exception** : Continuity of shareholding is not required for the Businesses listed on RSE*

Others

Is Rental income earned by the individuals investing in the UAE real estate is subject to CT?

On conjoint reading of Article 1, Article 11, Article 12, a natural person who conducts a Business or Business Activity in the State is considered as taxable person and income earned is subject to corporate tax.

Investment in real estate (by natural person) should not be considered as business unless the substance of passive income identified as business income, we can expect a clarification in Executive Regulation.

Further on looking small business relief, threshold of revenue that can be earned without application of the Corporate Tax has to be watched out.

Is capital expenditures incurred during the tax period allowed for deduction?

Capital expenditure incurred during the tax period is not allowed however, amortisation of the capital expenses/ deprecation of the capital assets should be allowed over the deferred period as deductions.

Whether Audited financial are mandatory as per the provisions of tax law?

The Minister may issue a decision requiring categories of Taxable Persons to prepare and maintain audited or certified financial statements.

Taxable Person has to submit the financial statements used to determine the Taxable Income for a Tax Period in the form and manner and within the timeline prescribed by the Authority.

Can we apply for Advance pricing agreement

A Person may make an application to the Authority in the form and manner prescribed by the Authority.

- For a clarification regarding the application of this Decree-Law
- Transaction or an arrangement proposed or entered into by the Person

Tax return period for the entites operations started newly during the year and related compliances under CT?

Tax return has to be submitted for the Financial Year or part thereof of the 12 months period for which it required to prepare the financial statements.

Transition Rules and its impacts

The opening balance sheet balances shall be prepared taking into consideration the arm's length principle in accordance with Article 34 of this Decree-Law.

As a result stock in hand procured from the related parties and/or connected persons in the beginning of the tax year should be at the arm's length price.

Exempt Income

- Dividends and other profit distributions received from Resident Person.
- Dividends and other profit distributions received by having Participating Interest in a foreign juridical person
- Any other income earned by having Participating Interest
- Income of a Foreign Permanent Establishment subject to conditions specified in the decree law
- Income derived by a Non-Resident Person from operating aircraft or ships in international transportation Establishment subject to conditions specified in the decree law

Our Tax Team

Tax being an integral part of the UAE's business and economic landscape we have on board a team of efficient Tax Advisors wielding solid expertise and strong technical insights into Direct Tax and Indirect Tax. Having diverse industry experience enables our tax team (Partner, Directors, Managers and consultants) to gain a ringside view into the challenges facing businesses.

Our team carries a combined experience of almost 50 years which is instrumental in helping clients navigate taxation related challenges. We strongly believe our taxation services provide businesses with partner level engagement that helps stakeholders get an eagle's view into the regulatory overview of the business.

For Direct & Indirect tax related queries reach out to us at tax@uhy-ae.com

Overview of services

Audit & Assurance
- Financial Statement Audits
- Information System Audits
- RERA Regulatory & Compliance Audits
- Retail Sales Audit

Internal Audit
- Risk Assurance
- Forensic Audits
- Standard Operating procedures
- Business Efficiency Reviews

Corporate Finance
- Financial Due Diligence
- Valuation and Pricing
- Purchase Price Allocation
- Business Modelling
- Fund Raising

Technology & Cybersecurity
- Information Security Audit
- Cybersecurity Assessment
- Data Protection
- Automation
- ERP Consulting

Strategy & Transformation
- Strategic Consulting
- Profitability Enhancement
- Organizational Transformation

Company Incorporation
- Business Setup
- Company Liquidations
- Tax Residency Certificate
- Trademark Registration
- Visa Assistance

Direct Tax
- Corporate Tax Advisory and Compliances
- Transfer Pricing Advisory and Compliances
- ESR Advisory

Indirect Tax
- VAT Advisory and Compliances
- Tax Audit Assistance
- Excise Tax Advisory and Compliances

Accounting & Bookkeeping
- IFRS Review & Implementation
- Payroll Processing
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