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UAE Corporate Tax
Things to keep in mind as in-house counsel

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Law Firm of the Year
The Oath Middle East Legal Awards 2023

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  - These slides were prepared for purposes of the In-house community presentation only and constitutes a high-level summary of the UAE tax landscape as at the date of the presentation.
  - The slide deck does not constitute formal tax advice and should not be relied upon as such.
  - These slides are subject to change as more legislative amendments and guidance documents from the FTA become available.
  - Attendees should not place reliance on this slide deck and are advised to obtain independent tax advice in relation to any of the issues discussed herein.

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Agenda

Agenda Item
1. Recap of Tax Concepts and Key Features
2. Selected Tax Considerations in Business Transactions a. Funding b. Corporate Structuring c. M&A d. Related Party transactions e. General Anti Abuse Rule (GAAR)
3. Tax Risk Management a. UAE Regulatory Environment b. Governance, Policies & Procedures c. Mitigating Current & Future Risk
4. Q&A

Recap

CORPORATE TAX

- Imposed on a *Taxable Person*
- *Resident* or *Non-Resident*
- Resident:
  - Juridical persons incorporated/established/recognised in the UAE (including FZ)
  - Foreign juridical persons effectively managed and controlled in/from UAE
  - Natural persons conducting Business or Business Activity
- Non Resident:
  - Permanent Establishment (PE)
  - State Sourced Income
  - Nexus in/to UAE (immovable property)

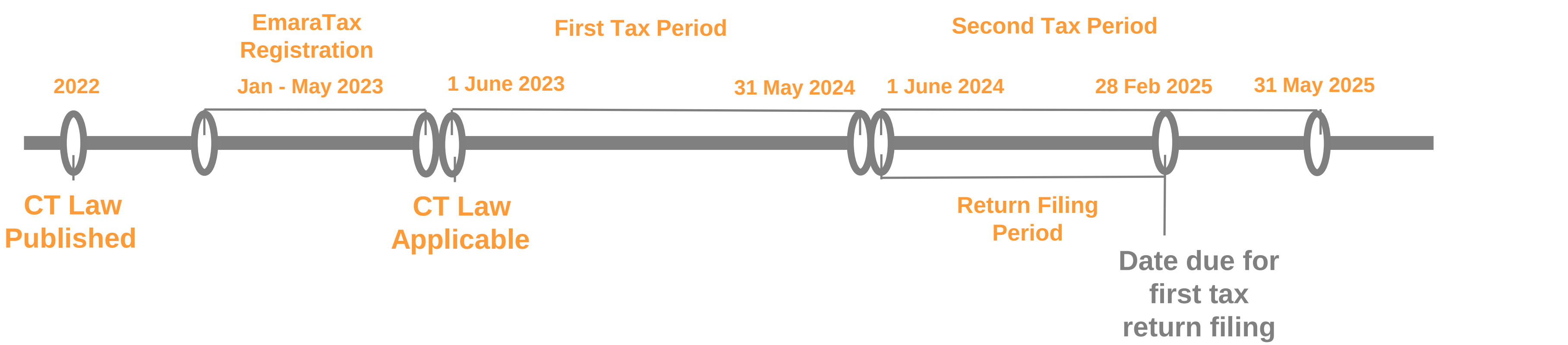
Recap

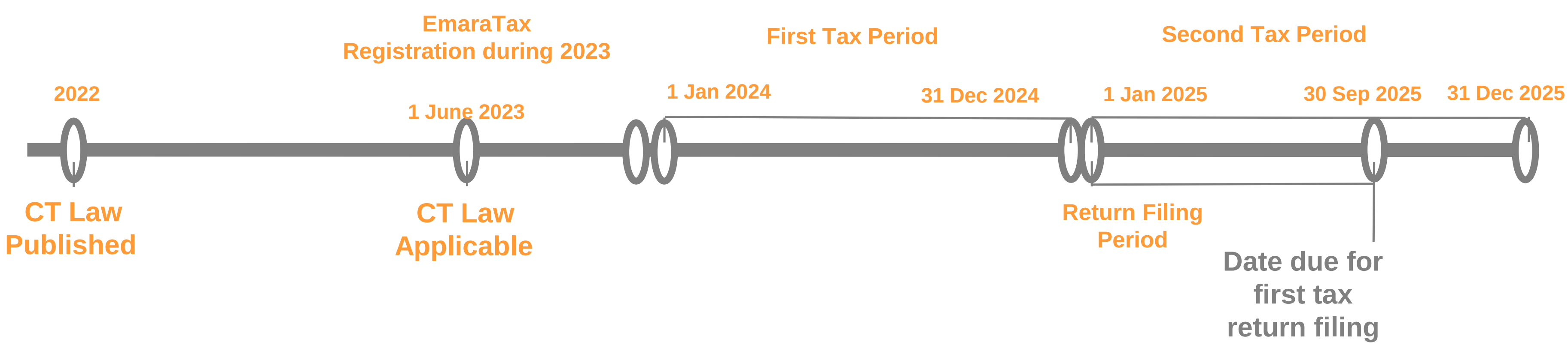
CORPORATE TAX

- **Tax Transparent vehicles**
  - Incorporated Partnership (separate legal personality from partners?) – Taxable Person
  - Unincorporated Partnership (General Partnership / JV) – transparent, each partner subject to CT
  - Foundation (taxable person) v Family Foundation (transparent)
  - Trusts (depends on trust - separate legal personality?)
- **Branches**
  - Single taxable person - treated as part of the head office

Timing

CT Law is applicable to a particular Taxable Person from their first financial year beginning on or after 1 June 2023.





Recap

- **Tax rates**:
  - tax free threshold – AED 375,000 (0%) ;
  - 9% for Taxable Income above tax free threshold;
  - different tax rate for large MNEs that meet specific criteria (TBC – 15%);
  - Qualifying Free Zone Person – Qualifying Income (0%); Non-Qualifying (9%).

Recap

- **Natural Persons:**
  - Business/business activities in UAE (AED 1m rev threshold), subject to following exclusions:
    - salary/wages
    - personal investment income
    - real estate investment income

Recap

- **Small Business relief:**
  - Businesses with turnover of less than AED 3,000,000 (both in the relevant and previous tax period) can elect to be treated as not having derived taxable income
  - Not available to QFZP.
  - Disadvantages - Inability to utilise the CT Law exemptions, deductions, reliefs and tax loss relief. Exempted from the TP documentation provisions in the CT Law.
  - Ends 31 December 2026

Recap

- **Exempt Entities**

  - Automatically Exempt Persons:
    - Government Entities;

  - Exempt if they notify the Ministry of Finance, and meet relevant conditions:
    - Extractive Businesses and Non-Extractive Natural Resource Businesses;

  - Exempt if listed in a Cabinet Decision and meet relevant conditions:
    - Government Controlled Entities and Qualifying Public Benefit Entities; and

  - Exempt upon application to, and approval by, the FTA:
    - Public and private pension or social security funds;
    - Qualifying Investment Funds;
    - Juridical persons incorporated in the UAE that are wholly owned and controlled by certain Exempt Persons; and
    - Any other Person as may be determined in a Cabinet Decision

Free Zone Taxation

- **Qualifying Free Zone Person**

- FZ Person – Juridical person incorporated/established/registered in FZ (including branch of non-resident)

- Requirements

  - derive Qualifying Income from relevant transactions
  - maintain adequate substance in the UAE
  - satisfy the *de minimis* requirement
  - not elected to be subject to Corporate Tax
  - comply with the transfer pricing rules and documentation requirements under the Corporate Tax Law; and
  - prepare and maintain audited Financial Statements for the purposes of the Corporate Tax Law.

Free Zone Taxation

- **Qualifying Income**
  - Income derived from transactions with **other Free Zone Persons**, provided **not Excluded Activities**;
  - Income derived from transactions with any **Non-Free Zone Person**, only in the case of **Qualifying Activities** that are **not Excluded Activities**; and
  - Income derived from the ownership or exploitation of **Qualifying Intellectual Property** (as prescribed in the relevant decision);
  - Any other income where the **de minimis requirement** is satisfied.

Recap

- **Exempt Income Streams**
  - Domestic dividends
  - Participation exemption
  - Foreign PE income
  - Non-resident operating aircrafts/ships in international transport

Dividend Exemption

- Domestic dividends and profit distributions **received from Resident** juridical persons are exempted from UAE CT (Article 22), without the requirement to meet any additional criteria.

- Dividend –

  - *“Any payments or distributions that are declared or paid on or in respect of shares or other rights participating in the profits of the issuer of such shares or rights which **do not constitute a return on capital or a return on debt claims**, whether such payments or distributions are in cash, securities, or other properties, and whether payable out of profits or retained earnings or from any account or legal reserve or from capital reserve or revenue. This will include any payment or benefit which in substance or effect constitutes a distribution of profits made in connection with the acquisition or redemption or cancellation of shares or termination of other ownership interests or rights or any transaction or arrangement with a Related Party or Connected Person which does not comply with Article (34) of the Corporate Tax Law”.*

Participation Exemption

- A Participation Exemption is available for dividends and profit distributions from foreign juridical persons (and capital gains on local shares) that meet the criteria for Participating Interests.

- A Participating Interest (Article 23(2)) is an ownership interest of 5% (or the aggregated acquisition cost of the ownership interest in that juridical person is equal to or exceeds AED 4 million) or more where:

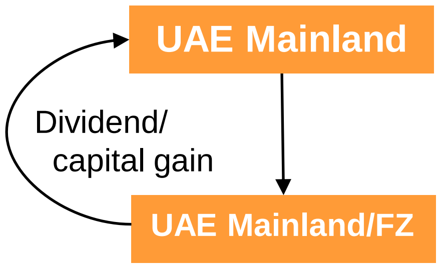
  a) the Participating Interest has been held or is intended to be held for at least 12 months;

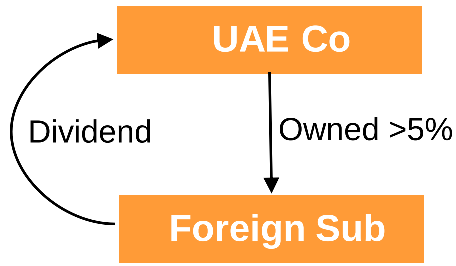
  b) the Participation is subject to Corporate Tax (or a similar tax) at a rate of not less than 9%;

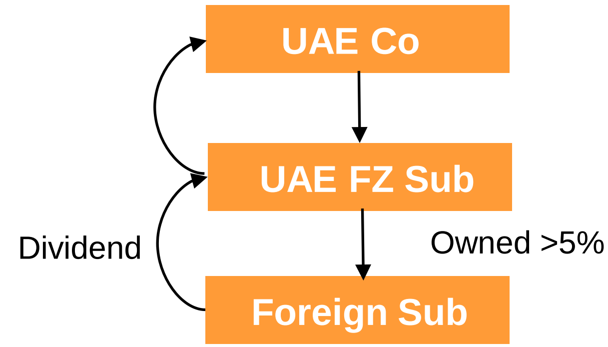
  c) the Participation gives a right to not less than 5% of profits and liquidation proceeds;

  d) Not more than 50% of the direct/indirect assets of the Participation consist of ownership interests/entitlements that would not have qualified for the participation exemption if held directly by the Taxable Person.

Participation Exemption







Domestic Dividend

Domestic dividends & capital gains from UAE companies exempt

Foreign Dividend/Capital Gain

Dividends & capital gains from foreign companies received by a UAE entity are exempt where:

- **UAE Co holds ≥ 5% ownership**
- **Foreign Sub paid ≥ 9% CT**

Foreign Dividend/Capital Gain

Capital gain from the disposal of shares in FZ Person exempted, subject to:

- **FZ Person is a holding company**
- **Substantially all of the income is derived from shareholdings in subsidiary companies that the meet the participation exemption requirements**

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Corporate Structuring

STRUCTURING

- Requires good understanding of tax landscape, entity type and anticipated operations/income streams
- Determine whether any exemptions (entity/income) applicable
- Any reliefs that could be utilised (corporate roll-over)
- Determine whether FZ tax holidays may be applicable
- Other requirements e.g. transfer pricing
- Applicable funding
- Explain and document relevant criteria / commercial rationale

FUNDING

- Understand tax treatment of debt vs equity
  - Debt (interest expense and income)
  - Equity (dividends exempt, but no deduction)
- Interest limitation rules
  - General vs Specific
- Utilisation of FZ Relief?
  - Financing of related parties

RESTRUCTURING

- **Possible reasons**
  - M&A
  - Utilisation of grouping rules
  - FZ potential income ‘tainting’
  - PE (taxable presence) and consequences
- **Implications**
  - Capital gains tax, VAT, claw backs etc.
  - Specific relief/exemptions that could be utilised?

Corporate Structuring

TRANSFERS WITHIN A QUALIFYING GROUP

- In summary, gains or losses in relation to transfers of assets or liabilities between two members of the same Qualifying Group (Article 26, Clause 1) need not be taken into account when calculating taxable income.
- Eligibility requirements
- Deemed disposal and acquisition at net book value
- Claw back
  - (Asset/liability is treated as having been transferred at **market value at date of original transfer.)**

Corporate Structuring

BUSINESS RESTRUCTURING RELIEF

- In summary, relief is available where a business (or part of a business) is transferred in exchange for shares (or equity interests) in the transferee, including where the transferor ceases to exist as a result of the transfer.
- Eligibility requirements
- Deemed disposal and acquisition values
- Claw back

M&A

Pre Transaction Planning

- Is pre transaction structuring or restructuring required?

Transaction

- Tax consequences of the transaction? CGT, VAT, foreign tax implications
- Is there tax relief available for the transaction by way of exemption or other relief?
- Is a group being joined or formed? Is an entity/entities exiting an existing group? Claw Backs?
- Tax due diligence on target
- Cover tax risks in transaction documents
- Prepared defence file for future FTA audit purposes

Managerial Decision Making

- Guided by governance & risk framework, informed by various aspects of financial, legal, regulatory and operational aspects

Share & Asset Sales

Share Sales

- Take over tax obligations of taxable person
- Importance of tax due diligence
- Determine if entity or transactional reliefs applicable
- Share sales are not subject to VAT
- Allocation of consideration

Business/Asset Sales

- Historic corporate tax obligations remain with seller
- VAT may apply
- VAT exclusion for transfer of going concern (subject to conditions)
- Allocation of consideration

Warranties & Indemnities

- Role of Warranty and Indemnity
- Consider requirements for definition of “Applicable Law”
- Define “Tax” broadly – Apart from Corporate Tax, ensure all transactional taxes/duties are covered – VAT, WHT, excise, customs
- Ensure Agreements provide adequate protection

Related Party Transactions

- Article 34 – All transactions/arrangements between Related Parties must meet the arm's length standard

- Non compliance with TP rules could lead to penalties (with regard to documentary requirements) and the **risk of an adjustment** to pricing which can lead to further tax liability / disallowance of deductions.

- Transfer Pricing is the **process** by which an arm's length result is determined in respect of related party transactions

    - Article 34 – Provides for a number of methods
    - FTA recently released UAE TP Guide (provides extensive guidance)
    - Also refer to the OECD TP Guidelines

Related Party Transactions

Related Party means any of the following:

a) **Two or more natural persons** who are related within the fourth degree of kinship or affiliation, including by way of adoption or guardianship.

b) **A natural person and a juridical person** where:
   1. the natural person or one or more Related Parties of the natural person are shareholders in the juridical person, and the natural person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or greater ownership interest in the juridical person; or
   2. the natural person, alone or together with its Related Parties, directly or indirectly Controls the juridical person.

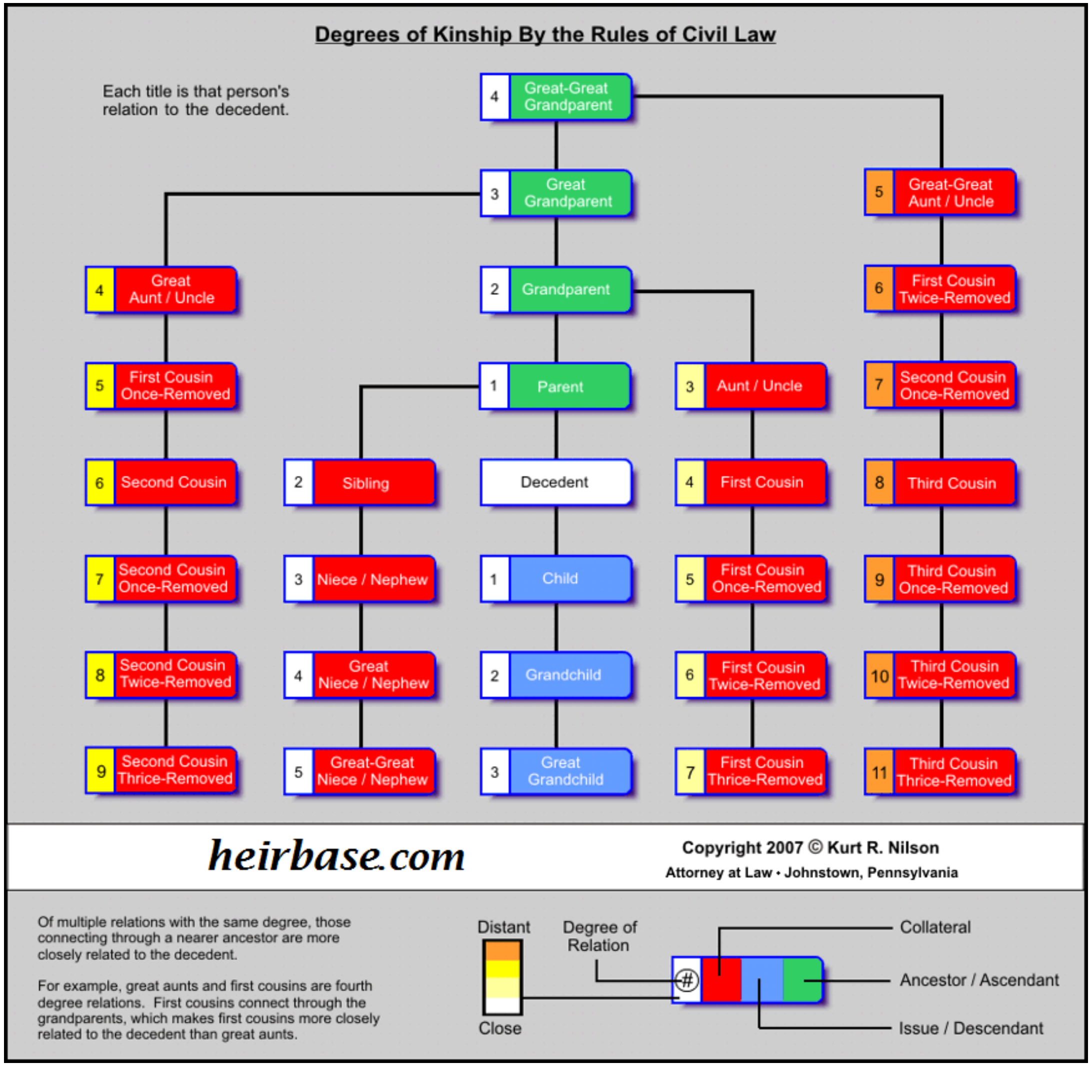
c) **Two or more juridical persons** where:
   1. One juridical person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or greater ownership interest in the other juridical person;
   2. One juridical person, alone or together with its Related Parties, directly or indirectly Controls the other juridical person; or
   3. Any Person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or great ownership interest in or Controls such two or more juridical persons;

d) **A Person and its Permanent Establishment** or Foreign Permanent Establishment.

e) Two or more Persons that are **partners in the same Unincorporated Partnership**.

f) **A Person who is the trustee, founder, settlor or beneficiary of a trust or foundation, and its Related Parties**.

Related Party Transactions



Source:
https://heirbase.com/degrees_of_kinship_chart/

Related Party Transactions

"**Control**" means the ability of a Person, whether in their own right or by agreement or otherwise to influence another Person, including:

a) The ability to exercise 50% (fifty percent) or more of the voting rights of another Person.

b) The ability to determine the composition of 50% (fifty percent) or more of the Board of directors of another Person.

c) The ability to receive 50% (fifty percent) or more of the profits of another Person.

d) The ability to determine, or exercise significant influence over, the conduct of the Business and affairs of another person."

Connected persons

- **Payments to Connected Persons (Article 36):** A payment or benefit provided by a Taxable Person to its Connected Person shall be deductible only if and to the extent the payment or benefit corresponds with the Market Value of the service, benefit or otherwise provided by the Connected Person and is incurred wholly and exclusively for the purposes of the Taxable Person's Business.

- A Person shall be considered a Connected Person of a Taxable Person if that Person is:

  a) **An owner of the Taxable Person**.
  b) **A director or officer of the Taxable Person**.
  c) **A Related Party of any of the Persons referred to in paragraphs (a) and (b)** of Clause 2 of this Article.
  d) Where the Taxable Person is a partner in an Unincorporated Partnership, a **Connected Person is any other partner in that same Unincorporated Partnership**, and any Person that is a Related Party of that partner.

- An owner of the Taxable Person is any natural person who directly or indirectly owns an ownership interest in the Taxable Person or Controls such Taxable Person.

- Shall not apply to:
  a) A Taxable Person whose shares are traded on a Recognised Stock Exchange.
  b) A Taxable Person that is subject to the regulatory oversight of a competent authority in the State.

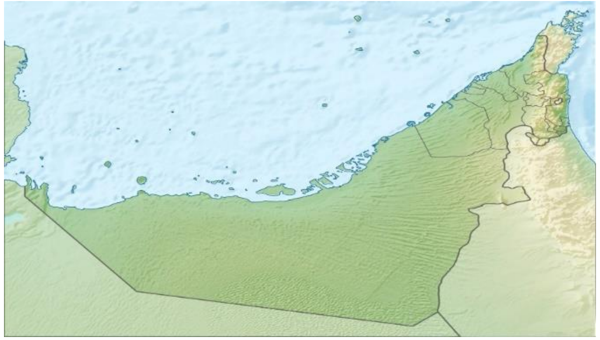
TP Documentation

- TP rules and documentary requirements aligned with the OECD TP Guidelines

- Documentation:
  - Art 55 of CT Law (audit request on 30 days notice)
  - TP Disclosure Form (materiality threshold awaited)
  - Master File (3.15bn / 200m)
  - Local File (3.15bn / 200m)
  - Country by Country Reporting (CbCR) (3.15bn)

- Further Guidance on required TP documentation – Refer to FTA Guide on TP

General Anti-Abuse Rule (GAAR)



- GAAR applies to:

  “a transaction or an arrangement if, having regard to all relevant circumstances, it can reasonably be concluded that:

  a) the entering into or carrying out of the transaction or arrangement, or any part of it, is **not for a valid commercial or other non-fiscal reason** which reflects economic reality; and

  b) the **main purpose or one of the main purposes** of the transaction or arrangement, or any part of it, is **to obtain a Corporate Tax advantage** that is not consistent with the intention or purpose of this Decree-Law.”

Tax Risk Management

UAE REGULATORY ENVIRONMENT

- Customs Duties (2003)
- FATCA (Foreign Account Tax Compliance Act – US/IRS regime) (2016)
- Common Reporting Standards (CRS) (2017)
- Excise Tax (2017)
- Value Added Tax (VAT) (2018)
- Economic Substance Regulations (ESR) (2019)
- Country by Country Reporting (CbCR) (2019)
- UAE Federal Corporate Tax (June 2023)

- Anticipated
  - OECD BEPS Pillar 1 – reallocation of consolidated proftits to sales jurisdiction (TBC)
  - OECD BEPS Pillar 2 – global minimum tax (15%) (TBC)

Risks & Mitigation – Corporate Tax

FEDERAL CORPORATE TAX – RISK

- Tax on business profit
- Risks
  - Incorrect tax calculation, transactions, treatment, categorization, adjustments
  - Leads to further tax liability plus penalties and interest
  - Tax disputes with FTA
- Mitigation – address through governance, policies, procedures

Governance, Policies & Procedures

Governance

- Allocates the overarching responsibility for tax, regulatory and risk aspects of business
- Allocates/delegates responsibility for each business aspect & risk category

Policies

- Documented rules of the business (by department)
- Allocates/delegates responsibility for each department requirement
- Sets out who makes decision, requirements for sign off, materiality limitations and escalation process

Procedures

- Sets out process and responsibilities for each task
- May address internal inter-departmental responsibilities

Practical Considerations

HOW TO HELP YOUR BUSINESS

- Encourage planning – it's never *too* soon!
- Understand relevant regulations
- Understand risks
- Set governance, policies and procedures
- Implement documentation to support transactional analysis
- Map out related and connected parties
- Get specialist tax and regulatory advice

Questions?