Tax update | **The UAE's corporate tax law**

The United Arab Emirates | 15 December 2022

keypoint

The UAE published its corporate tax law on 9 December 2022, fundamentally changing the tax landscape for businesses - including free zone businesses - in the UAE. Key findings from our review of the law and other legislation include:

Tax rate

- ≤AED375,000 or qualifying income of a free zone person - 0%
- >AED 375,000 or non-qualifying income of a free zone person - 9%

Exempt persons

- Government entities or entities controlled by the government (excluding income from business activity)
- Persons engaged in an extractive business or a non-extractive natural resource business (subject to emirate-specific tax) - excluding income from business activities >5% of total revenue
- Qualifying public benefit entities set up for religious, charitable or scientific purposes
- Qualifying (regulated) investment funds traded widely or on the stock exchange
- Pension and social security funds

Taxable persons and base

- Resident persons:
  - Juridical persons incorporated in the UAE (including free zones) or incorporated overseas but managed and control from UAE
  - Natural persons conducting business in the UAE
  - Branches of juridical or natural persons
- Non-resident persons:
  - With a permanent establishment (PE) in the UAE
  - Who derives UAE income
  - With a nexus in the UAE
- Tax base of resident persons – income earned inside and outside the UAE
- Tax base of non-resident persons - income attributable to PE or nexus in the UAE or any other UAE income
- Permanent establishment
  - Non-resident persons with a fixed or permanent place from where business is conducted
  - A business conducted by a third person on behalf of a non-resident person
  - A business related to the nexus in the UAE
- Note: A permanent place used for storing goods, merchandising or preparatory or ancillary activity to the main business is not a PE

Taxable free zone persons

- Maintains adequate substance
- Derives qualifying income
- Elected not to be subject to corporate tax (Exemption from CT (0%) is limited to 50 years)

Taxable income

- Accounting income reported in stand-alone financials prepared under UAE accounting standards, adjusted for gains/losses, tax reliefs & deductions, prices charged between related parties, losses, exemptions and incentives
- Small business relief - Taxable resident persons can decide not to receive income subject to CT if revenue for the current and preceding tax periods is <AED375,000

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Exempt income

- Dividends and profit distributions received from a resident juridical person
- Dividends, capital gains, foreign exchange or impairment gains/losses and any other income distributions from a participating interest (shares or capital) in a juridical person provided:
    1. Participation interest is ≥ 5% AND
    2. The taxable person has held (or intends to hold) the interest for a minimum continuous period of 12 months AND
    3. The juridical person is subject to a corporate tax ≥9% where the taxable person is resident AND
    4. ≤50% of the participating or ownership interest would have been exempt from corporate tax if it was held directly by the taxable person
- Resident persons can elect to exclude a foreign PE's income and expenditure if the PE is subject to CT ≥9% in the foreign jurisdiction

Business restructuring relief

- No gains or losses arise on:
    - Transfers of assets or liabilities between two taxable persons (resident or non-resident juridical persons) within the same qualifying group who are part of a 75% ownership structure. If a transferred asset is disposed outside of the qualifying group or the taxable persons leave the qualifying group within two years, the transfer will be treated as having taken place at market, not book, value
    - Transfers of a business in return for shares for genuine commercial reasons. A subsequent disposal of the shares to a third person outside of the qualifying group within two years will be treated as taking place at market, not book, value

Deductible expenditures

- Revenue expenditure exclusively for business purposes (excluding donations, fines, bribes, dividend or profit distributions and taxes) is deductible from income.
- Tax deductible interest expense is capped at 30% of earnings before interest, tax, depreciation and amortisation (EBITDA). Unrelieved interest expense can be carried forward and offset against future interest income for up to 10 tax periods.
- Deductible business entertaining expenditure is capped at 50% of the expense incurred.
- Payments to related parties are deductible, if business related and at market value

Related party transactions

- Transactions between related parties must be undertaken at market value – which must be determined by applying one or more of the prescribed transfer pricing methodologies taking into account contractual terms, functions performed, assets employed, risks undertaken and business strategy.
- The Federal Tax Authority (FTA) can amend a taxpayer's income if it determines that prices are below market value.
- Parties can be related through ownership, control, influence, birth or marriage

Loss relief

- Taxable persons can offset a loss against income of a subsequent tax period, capped at 75% from the date that the person was subject to corporate tax.
- Tax losses can be transferred between two resident juridical persons who are subject to corporate tax at the main rate with the same financial year-end and who are members of a 75% ownership structure.

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- Tax losses can be carried forward to a subsequent tax period provided the taxable person is under the common ownership (minimum 50%) or the taxable person is conducting the same or similar business following a major (more than 50%) change in ownership.

Tax groups

- Resident parent companies can decide to form a tax group with other resident persons provided:
  1. All persons are juridical and have the same financial year end AND
  2. The parent owns - directly or indirectly - ≥95% of shares, voting rights or net assets AND
  3. Neither the parent nor the subsidiary are exempt or qualifying free zone persons
- Tax groups are treated as a single taxable person
- Parents and subsidiaries are jointly and severally liable for the tax payable by the group.
- There are conditions under which subsidiaries can enter or leave groups and controlling the offset of tax losses between group members on entry or exit

Tax payable

- Corporate tax payable is net of withholding tax credits, foreign tax credits or any other credit, expressed in UAE dirhams.
- Non-resident persons are subject to a withholding tax of 0% on the gross amount of UAE-sourced income not attributable to the person's PE.
- Withholding tax credit in excess of the tax payable amount will be refunded.
- Foreign tax credits will be the lower of the tax credit or tax payable.

Tax payments and refunds

- Taxable persons must pay due corporate tax within nine months of the end of the relevant tax period.
- Taxable persons can apply for refunds of excess withholding tax credits or overpaid corporate tax.

Anti-abuse rules

- The FTA can disregard any tax advantage gained by taxable persons who enter into a transaction or arrangement to avoid tax

Tax registration and deregistration

- The FTA will stipulate the conditions under which a person can register or deregister for corporate tax.

Tax filings and rulings

- Taxable person must file a tax return within nine months of the end of the relevant tax period.
- Tax periods are the 12-month period (or part) for which the financial statements have been prepared. Taxable persons can apply to change their tax period.
- Parent companies must file tax returns on behalf of groups.
- The FTA can request persons to file financial statements and report transactions with related parties to determine tax liabilities
- The FTA can ask taxable persons to submit transfer pricing master and local files within 30 days (or any other timeframe).
- Taxable persons must maintain books and records for seven years from the end of the relevant tax period.
- Taxable persons can apply for a ruling on the law's application or agree an advance pricing agreement.

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Violations and penalties

- The FTA will issue rules on tax assessments and penalties for non-compliance.

Transitional rules

- The opening period balances of the first taxable period will be the closing period balances for the period before the introduction of the law, adjusted for the arm's length principle

Other provisions

- The law applies to tax periods starting on or after 1 June 2023.
- The law does not override international agreements.

Disclaimer

This summary is based on a review of the UAE's corporate tax law published by the UAE's Federal Tax Authority and other publications. Several provisions within the law will be ratified by ministerial decisions or tax authority rulings. Please contact your adviser for specific tax advice.

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