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CHARTERED ACCOUNTANTS

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UAE: Corporate tax FAQ

1) What is Corporate Tax?

The Federal Decree-Law No. 47 of 2022 on the Taxation of Corporations and Businesses (hereinafter referred to as the "Corporate Tax Law") was issued by the United Arab Emirates ("UAE"), on 09 December 2022 Corporate Tax is a form of direct tax levied on the net income of corporations and other businesses.

Corporate Tax will be effective for all financial years beginning after 1st June 2023. For example, if Company A has a financial year end of 30th June, then their first tax year would be from the 1st of July 2023 to 30th June 2024. If Company B has a year end of 31st December, then their first tax year would be from 1st January 2024 to 31st December 2024.

2) Who must pay Corporate Tax?

Broadly, Corporate Tax applies to the following "Taxable Persons":

- UAE companies and other juridical persons that are incorporated or effectively managed and controlled in the UAE
- Natural persons (individuals) who conduct a Business or Business Activity in the UAE as specified in a Cabinet Decision to be issued in due course; and
- Non-resident juridical persons (foreign legal entities) that have a Permanent

Establishment in the UAE:

Juridical persons established in a UAE Free Zone are also within the scope of Corporate Tax as "Taxable Persons" and will need to comply with the requirements set out in the Corporate Tax Law.

However, a Free Zone Person that meets the conditions to be considered a Qualifying Free Zone Person can benefit from a Corporate Tax rate of 0% on their Qualifying Income.

Non-resident persons that do not have a Permanent Establishment in the UAE or that earn UAE sourced income that is not related to their Permanent Establishment may be subject to Withholding Tax (at the rate of 0%). Withholding tax is a form of Corporate Tax collected at source by the payer on behalf of the recipient of the income. Withholding taxes exist in many tax systems and typically apply to the cross-border payment of dividends, interest, royalties, and other types of income.

3) What are the rates and tax slabs?

Corporate Tax will be levied at a headline rate of 9% on Taxable Income exceeding AED 375,000. Taxable Income below this threshold will be subject to a 0% rate of Corporate Tax. Corporate Tax will be charged on Taxable Income as follows:

Resident Taxable Persons	
Taxable Income not exceeding AED 375,000 (this amount is to be confirmed in a Cabinet Decision)	0%
Taxable Income exceeding AED 375,000	9%
Qualifying Free Zone Persons	
Qualifying Income	0%
Taxable Income that does not meet the Qualifying Income definition	9%

4) What income is exempt from Corporate Tax?

The Corporate Tax Law also exempts certain types of income from Corporate Tax. This means that a Taxable Persons will not be subject to Corporate Tax on such income and cannot claim a deduction for any related expenditure. Taxable Persons who earn exempt income will remain subject to Corporate Tax on their Taxable Income.

The main purpose of certain income being exempt from Corporate Tax is to prevent double taxation on certain types of income. Specifically, dividends and capital gains earned from domestic and foreign shareholdings will generally be exempt from Corporate Tax. Furthermore, a Resident Person can elect, subject to certain conditions, to not take into account income from a foreign Permanent Establishment for UAE Corporate Tax purposes.

Certain types of businesses or organizations are exempt from Corporate Tax given their importance and contribution to the social fabric and economy of the UAE. These are known as Exempt Persons and include:

Automatically exempt	• Government entities • Government controlled entities that are specified in a Cabinet decision
Exempt if notified to the Ministry of Finance *(and subject to meeting certain conditions)*	• Extractive Businesses • Non-extractive Natural Resource Businesses
Exempt if listed in a Cabinet Decision	• Qualifying Public Benefit Entities
Exempt if applied to and approved by the **Federal Tax Authority** *(and subject to meeting certain conditions)*	• Public or private pension and social security funds • Qualifying Investment Funds • Wholly-owned and controlled UAE subsidiaries of a Government Entity, a Qualifying Investment Fund, or a public or private pension or social security fund

In line with the tax regimes of most countries, the Corporate Tax Law taxes income on both a residence and source basis. The applicable basis of taxation depends on the classification of the Taxable Person.

- A “Resident Person” is taxed on income derived from both domestic and foreign sources (i.e. a residence basis)

- A “Non-Resident Person” will be taxed only on income derived from sources within the UAE (i.e. a source basis).

Residence for Corporate Tax purposes is not determined by where a person resides or is domiciled but instead by specific factors that are set out in the Corporate Tax Law. If a Person does not satisfy the conditions for being either a Resident or a Non-Resident person, then they will not be a Taxable Person and will not therefore be subject to Corporate Tax.

5) What expenses can businesses deduct in their tax returns

In principle, all legitimate business expenses incurred wholly and exclusively for the purposes of deriving Taxable Income will be deductible, although the timing of the deduction may vary for different types of expenses and the accounting method applied. For capital assets, expenditure would generally be recognized by way of depreciation or amortization deductions over the economic life of the asset or benefit.

Expenditure that has a dual purpose, such as expenses incurred for both personal and business purposes, will need to be apportioned with the relevant portion of the expenditure treated as deductible if incurred wholly and exclusively for the purpose of the taxable person's business. Certain expenses which are deductible under accounting rules may not be fully deductible for Corporate Tax purposes. These will need to be added back to the Accounting Income for the purposes of determining the Taxable Income. Examples of expenditure that is or may not be deductible (partially or in full) include:

6) What if my company is not profitable?

The FTA will allow for tax losses to be carried forward and be offset against future taxable income. However, only tax losses incurred from an entity's first tax period will be eligible for this benefit. As such, for an entity with a Gregorian calendar fiscal year, any losses before 1st January 2024, will be disallowed.

Types of expenditures	Limitation to deductibility
• Bribes • Fines & penalties (other than amounts awarded as compensation for damages or breach of contract) • Donations, grants or gifts made to an entity that is not a Qualifying Public Benefit Entity • Dividends and other profits distributions • Corporate Tax imposed under the Corporate tax Law • Expenditure not incurred wholly and exclusively for the purpose of the Taxable person's Business • Expenditure incurred in deriving income that is exempt from Corporate Tax	No deduction
• Client entertainment	• Partial deduction of 50%of the amount of the expenditure
• Interest expenditure	Deduction of net interest expenditure exceeding a certain de minimis threshold up to 30% of the amount of earnings before the deduction of interest, tax, depreciation and amortisation (except for certain activities)

7) What about Tax Groups?

Two or more entities can apply to form a Tax Group, primarily to benefit from intercompany transactions offsetting and being able to file only one tax return for all entities under the tax group. A tax group may only be formed if the following conditions are met:

a. The Resident Persons are juridical persons.

b. The Parent Company owns at least 95% (ninety-five percent) of the share capital of the Subsidiary, either directly or indirectly through one or more Subsidiaries.

c. The Parent Company holds at least 95% (ninety-five percent) of the voting rights in the Subsidiary, either directly or indirectly through one or more Subsidiaries.

d. The Parent Company is entitled to at least 95% (ninety-five percent) of the Subsidiary's profits and net assets, either directly or indirectly through one or more Subsidiaries.

e. Neither the Parent Company nor the Subsidiary is an Exempt Person.

f. Neither the Parent Company nor the Subsidiary is a Qualifying Free Zone Person.

g. The Parent Company and the Subsidiary have the same Financial Year.

h. Both the Parent Company and the Subsidiary prepare their financial statements using the same accounting standards.

8) When does the CT have to be paid?

All Taxable Persons (including Free Zone Persons) will be required to register for Corporate Tax and obtain a Corporate Tax Registration Number. Entities can register with the FTA from **1st January 2023**.

Taxable Persons are required to file a Corporate Tax return for each Tax Period within **9 months** from the end of the relevant period. The same deadline would generally apply for the payment of any Corporate Tax due in respect of the Tax Period for which a return is filed.

9) Do I have to pay tax if my company is in a Free Zone?

A company located in a Qualifying Free Zone may be subject to 0% Corporate Tax on Qualifying Income, if it meets all the following conditions:

a. Maintains adequate substance in the State

b. Derives Qualifying Income

c. Has not elected to be subject to Corporate Tax

d. Complies with Articles 34 (Arm's Length Principle) and 55 (Transfer Pricing Documentation) of Decree-Law

e. Meets any other conditions as may be prescribed by the Minister

10) What is Qualified Income?

Simply put, Qualified Income is any income that is generated outside the UAE by a UAE Qualifying Free Zone Company. Qualifying Income will be defined by a decision from the Minister, however we expect this income to be like out-of-scope transactions for VAT, for example, third port sales.

11) What is Transfer Pricing/Arm's Length?

Transfer pricing refers to a set of principals in place to price transactions between related parties, or parties with similar ownership or control. For example, a simple transfer pricing principal in a business could be Cost+20% for any sales made to a related entity. The Arm's Length Principal is a transfer pricing concept, that requires that all related party transactions, be carried out at the same prices that they would be if the transaction was between un-related parties.

Related party transactions can include, management remuneration, salaries to family members and shareholder's loan accounts, apart from just sales and purchases between related entities

Documentation: We recommend all Companies understand these concepts, and have appropriate documentation in place, to support all related party transactions, as we believe they will be central to the Corporate Tax Regime in the UAE.

12) What records need to be maintained and how long do records need to be maintained.

All records and documents must be maintained for a period of (7) seven years following the end of the Tax Period to which they relate that:

a) Support the information to be provided in a Tax Return or in any other document to be filed with the Authority.

b) Enable the Taxable Person's Taxable Income to be readily ascertained by the Authority.

13) Are audited financial statements required?

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

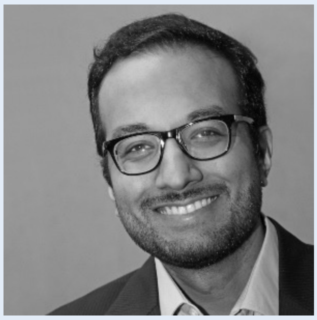
14) What next?

The authority will release Executive Regulations and Ministerial Decrees to further clarify details in the Law.

However, we believe all companies should begin preparing for Corporate Tax implementation within their entities at the earliest.

The team at MGI Salim Rajkotwala Chartered Accountants can assist companies with this implementation exercise and help clients be better prepared to comply with the Corporate Tax regime well-before its actual effective date. We can also assist companies with Corporate Tax registration, which will begin from the 1st January 2023.

Contact us:



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