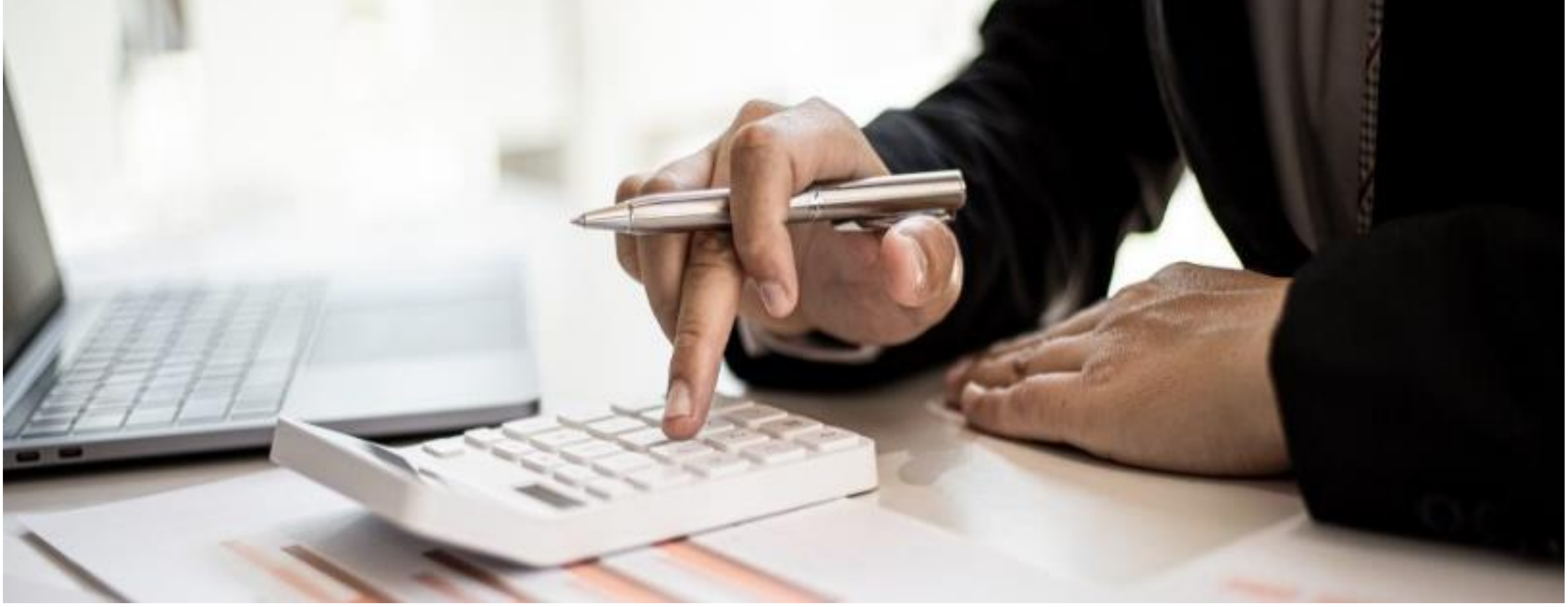

Corporate Tax in UAE

A quick look at what businesses need to know about the newly introduced corporate tax in UAE.

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Overview

Long known as a Tax-free country, the UAE has finally announced Corporate Tax on 31 January 2022. The law, regulations, and procedures are soon going to be promulgated and published.

UAE is a signatory to the Organization of Economic Cooperation and Development's (OECD) Inclusive Framework on Base Erosion and Profit Shifting (BEPS). UAE rolled out Economic Substance Regulations (ESR) and Country by Country Reporting in the year 2019, as part of the OECD framework. This was also done to avoid harmful tax practices amongst businesses.

Recently, OECD released a report. The report was on Pillar One and Pillar Two blueprints, addressing the BEPS Action 1 – "Addressing the Tax Challenges of the Digital Economy". The report was widely accepted by all the forums including G7 and G20. Pillar Two solution which deals with a minimum tax rate (15%), was accepted by G20 in July 2021.

The Corporate Tax Law is a Federal Law. All businesses and commercial activities (legal entities) in the UAE will be subject to tax. Exception: Businesses in the extraction of natural resources that are subject to the existing tax laws

Key Understandings:

- UAE's Corporate Tax proposes to incorporate global best practices and reduce the compliance burden on businesses.
- Corporate Tax will be paid on the taxable income, after making allowable adjustments as per the specification in the proposed CT Law.
- The income or profit would be as reported in the financial statement prepared as per internationally accepted accounting standards.

Salient Features of the Corporate Tax (CT)

Applicability

The Corporate Tax Law is a Federal Law. This means it would apply to all businesses and commercial activities (legal entities) in the UAE. **The exception, however, would be for businesses involved in the extraction of natural resources.** Such businesses will remain subject to the existing tax laws and rates (Emirates level corporate taxation). As we understand, the CT Law would also apply to the banking sector. For now, there is no exemption given to any specific industry.

Moreover, the UAE CT Law would apply to foreign entities and individuals, if they conduct any business or commercial activities in the UAE regularly.

CT Law would be effective from financial years commencing on or after 1 June 2023.

CT Law allows businesses to continue or choose their accounting year/ financial year. This is the same as the ESR compliance requirements. It is a welcomed move as many businesses will not be mandated to change their accounting year/financial year.

Unlike VAT registration, all entities need to register with Federal Tax Authority under the Corporate Tax Law.

Tax Rates

The Ministry of Finance has proposed the following tax rates:

- Taxable income up to AED 375,000 – **0%**
- Taxable income above AED 375,000 – **9%**

Different rates for multinationals.

- A Multinational that meets the specific criteria (as set in Pillar Two of the OECD BEPS project) would be taxed at a different rate. The criteria are a consolidated turnover of over Euro 750 million or AED 3.15 billion.

Tax Period

Corporate Tax Law would be effective from financial years commencing on or after 1 June 2023. E.g., if a company follows the calendar year as its financial year, i.e., 1 January to 31 December, its first corporate tax financial year would be 1 January 2024 to 31 December 2024. Similarly, if a company follows April to March as its financial year, its first corporate tax financial year would be from 1 April 2024 to 31 March 2025.

Treatment of Business Losses

CT law would provide for **set-off and carry forward of business loss**. A business will be allowed to carry forward its business losses and set it off against the taxable profits from the next years. This would be allowed once the conditions set in the Corporate Law are met. But the period up to which a business will be allowed to carry forward the losses needs to be discussed.

Grouping of Related Parties

CT Law allows UAE group of companies to form a tax group. It can be treated as a single taxable person once it meets the required conditions. In such a case, such a tax group would be required to file a single tax return for the entire group. Tax losses of one group company may be offset against the taxable income of the other group company, provided certain conditions are met.

Transfer Pricing

UAE businesses will **need to follow transfer pricing rules and documentation requirements** that are set with reference to OECD Transfer Pricing Guidelines.

Applicability to Free Zone businesses

Free Zones have provided businesses with corporate **tax incentives of up to 50 years**. CT Law applies to all businesses in the UAE including the Free Zones. CT Law will provide corporate tax incentives to all Free Zone businesses which follow all regulatory requirements. Such businesses should also not be conducting any business with mainland UAE.

Administration of Corporate Tax in UAE

The **Ministry of Finance will remain as the Competent Authority** for the purpose of bilateral/multilateral agreements and the international exchange of information for tax purposes.

The Federal Tax Authority will be responsible for the administration, collection, and enforcement of the CT Law.

CT law will prescribe the administrative mechanism such as:

- registration,
- compliance requirements and
- penalties for non-compliance of the CT Law

The Next Steps - As we await the publication of the Corporate Tax Laws, businesses can start to prepare.

GETTING READY

Accounting **Technology** **People**

The financial statement would be the basis for the tax calculations. The **Corporate Tax will be paid on the accounting net profits of the business**, after making appropriate adjustments as specified under the UAE Corporate Tax Laws.

Do you prepare your financial statements in accordance with internationally accepted accounting standards?

The management accounts usually do not follow the norms as prescribed by the accounting standards. Businesses need to ensure that the auditors prepare accounts according to accepted accounting standards (applicable to the business). In cases where the accounts are not audited, the management usually relies on the management accounts. They are largely an aggregation of the transactions for the period. These again, are not prepared as per any accepted accounting standards.

Currently, **the UAE has Excise tax and VAT**. Excise Tax (also known as “sin tax”) is levied only on sale of certain goods. VAT is a transaction tax, and the treatment differs based on the nature of the transaction. A transaction could be standard rated, zero-rated, exempt or out of scope for VAT purposes, accordingly. Corporate Tax, however, will be applicable on the profits of the business which includes all transaction types.

For example:

I. exports of goods or services attract VAT at zero rate.
II. Inter VAT group transactions are considered out of scope for VAT.
III. Residential accommodation rentals are exempted from VAT.

Going forward, business profit from the above transactions would attract corporate tax.

Accounting Process

First, it is a must to get the accounting process correct. A financial statement as per internationally accepted accounting standards is required to be prepared. This includes adhering to various Accounting Standards such as:

- IAS 18 on Revenue Recognition,
- IAS 12 on Income Taxes, to name a few.

Such a financial statement is the basis on which the Corporate Tax would be calculated.

UAE has no transfer pricing policies in place at present. Only certain information is provided to the authorities by way of Country-by-Country reporting and Economic Substance Regulation reporting obligations as part of BEPS minimum standards. OECD transfer pricing guidelines would likely be applicable in UAE.

On a global level, the tax authorities need the tax assesses to provide them with audited accounts, for filing purposes.

The proposed Corporate Law in UAE may also have similar requirements which is that the accounts are to be audited by an auditor in the UAE.

Technology

Mostly, businesses use accounting software for recording transactions and maintaining accounts. There will be a requirement to modify the Chart of Accounts regarding certain aspects discussed in the accounting process above.

People

Businesses will need to hire people with appropriate skill sets. The existing accounting resources might also need to upskill. Businesses also have the option to appoint advisors for accounting and corporate tax aspects.

How we can assist?

It is time for businesses to consider the impact of the newly introduced Corporate Tax. Our tax experts at KPI would be happy to guide you on what actions you need to take to follow the law, once it becomes effective.

Our Team

Suganth Ramasamy
suganth@kpi.co

Rajgopal Pai
rajgopal@kpi.co

Mahesh Shetty
mahesh@kpi.co

Prabhakar Kamath
kamath@kpi.co

Quick Links:

For more information on Corporate Taxation in UAE

→**See Frequently Asked Questions (FAQs)**
→**Learn More on Ministry of Finance Official Website**
→**Watch Recorded On-demand Webinar**