



# **Key Highlights of Explanatory Guide and Participation Exemption**

# Table of Contents

01

Recent Developments in CT

02

Important Definitions

03

Effective Management & Control

04

Effective Management & Control Vs  
Permanent Establishment

05

Withholding Tax Treatment

06

Transfer of losses

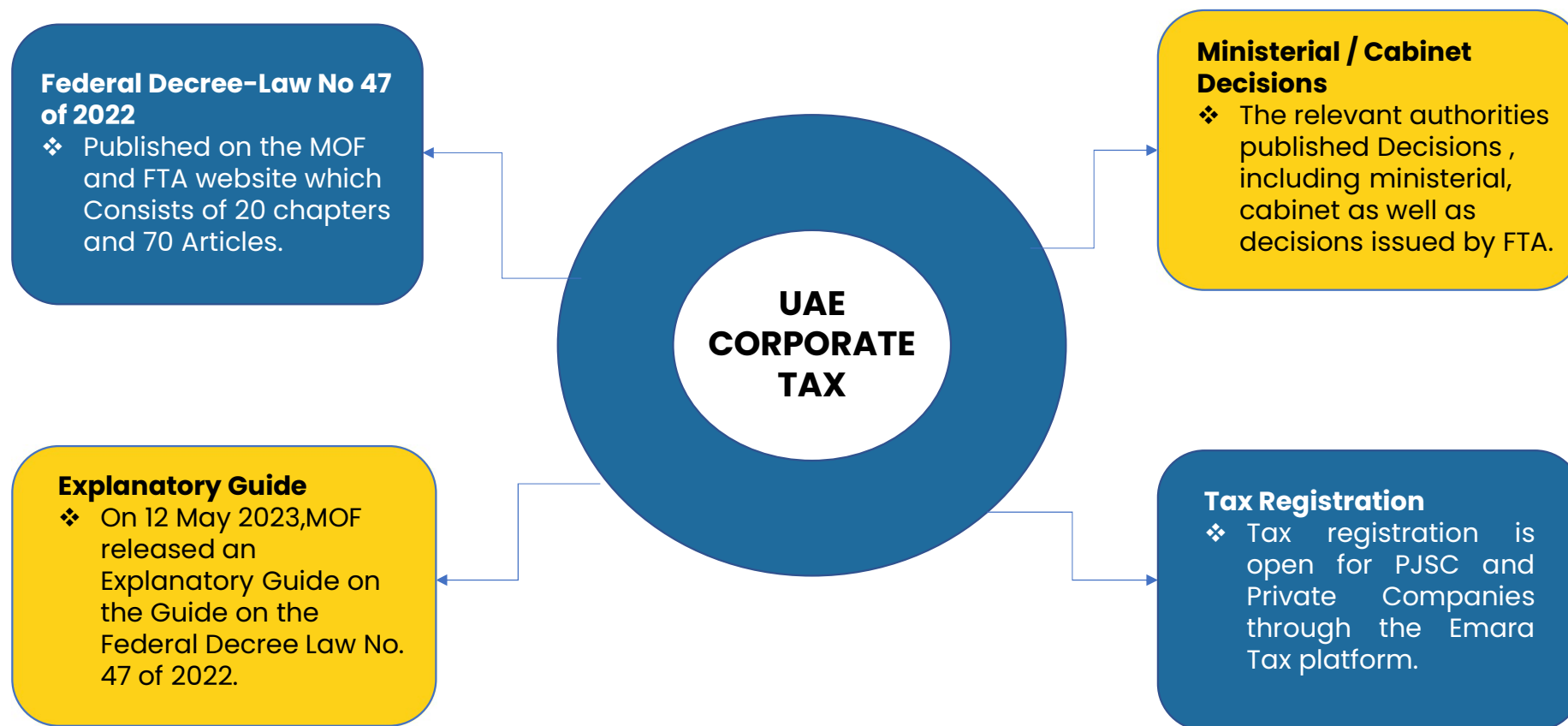
07

Deductibility of Expenditures

08

Participation Exemption

# Overview of Recent Developments



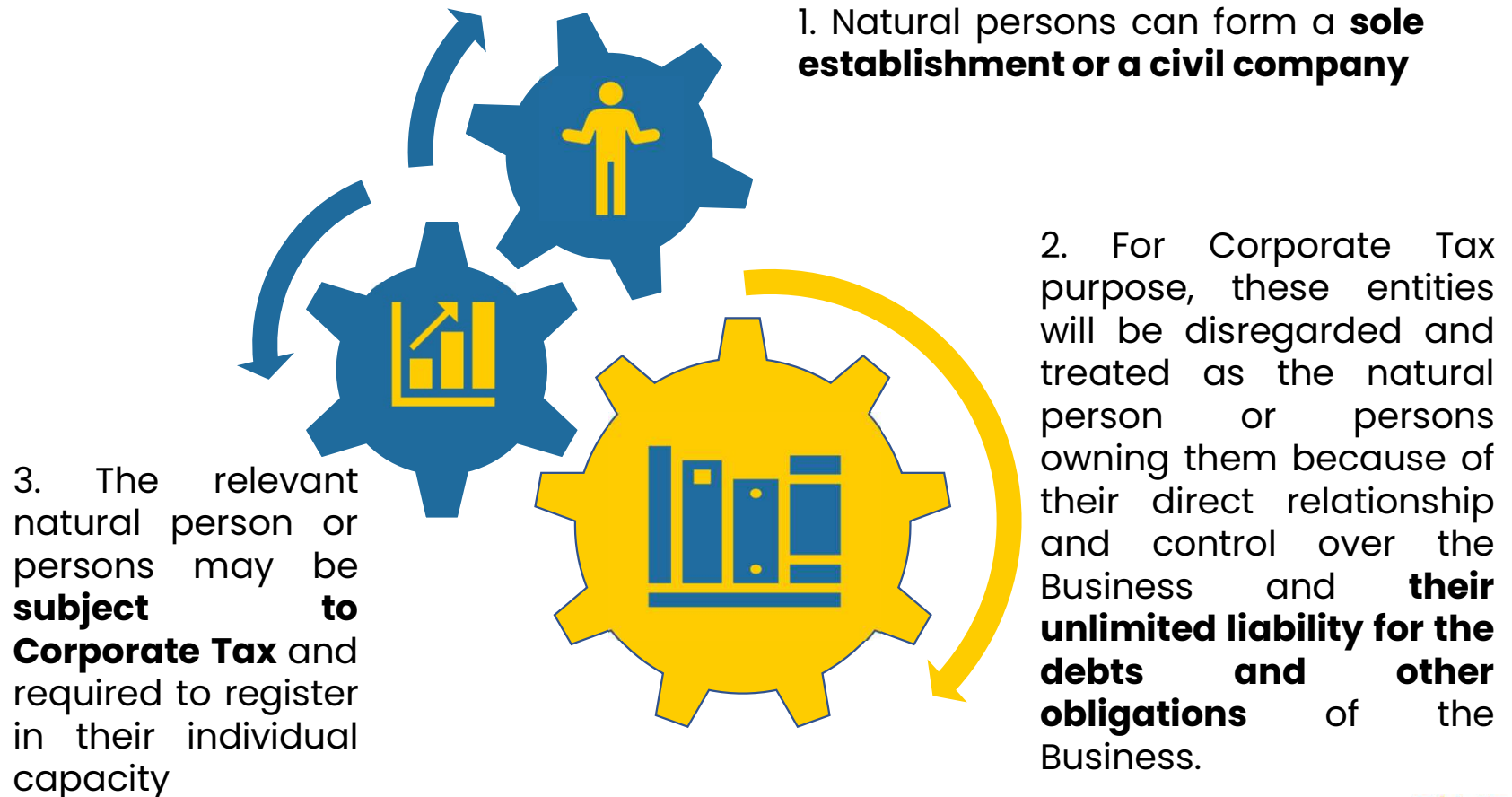
# Business and Business Activity

“Business” means any activity **conducted** with the **intention of generating profits**

**Short-term commercial activity** to be considered as Business for Corporate Tax purposes

“Business Activity” is **wider** than that of a “Business”, and **includes any transaction, step**, or other element or action undertaken by or as part of a Business, which may be carried out entirely or partially within the UAE.

# Person-Individual



# Taxation of Individuals

Ministerial  
Decision No. 49  
of 2023

**Resident or  
Non-Resident  
Individuals**  
shall be  
**subject to  
Corporate Tax**

- ❖ If conducting **business or business activities**
- and**
- ❖ Consolidated turnover **exceeds AED 1 million** in a calendar year.

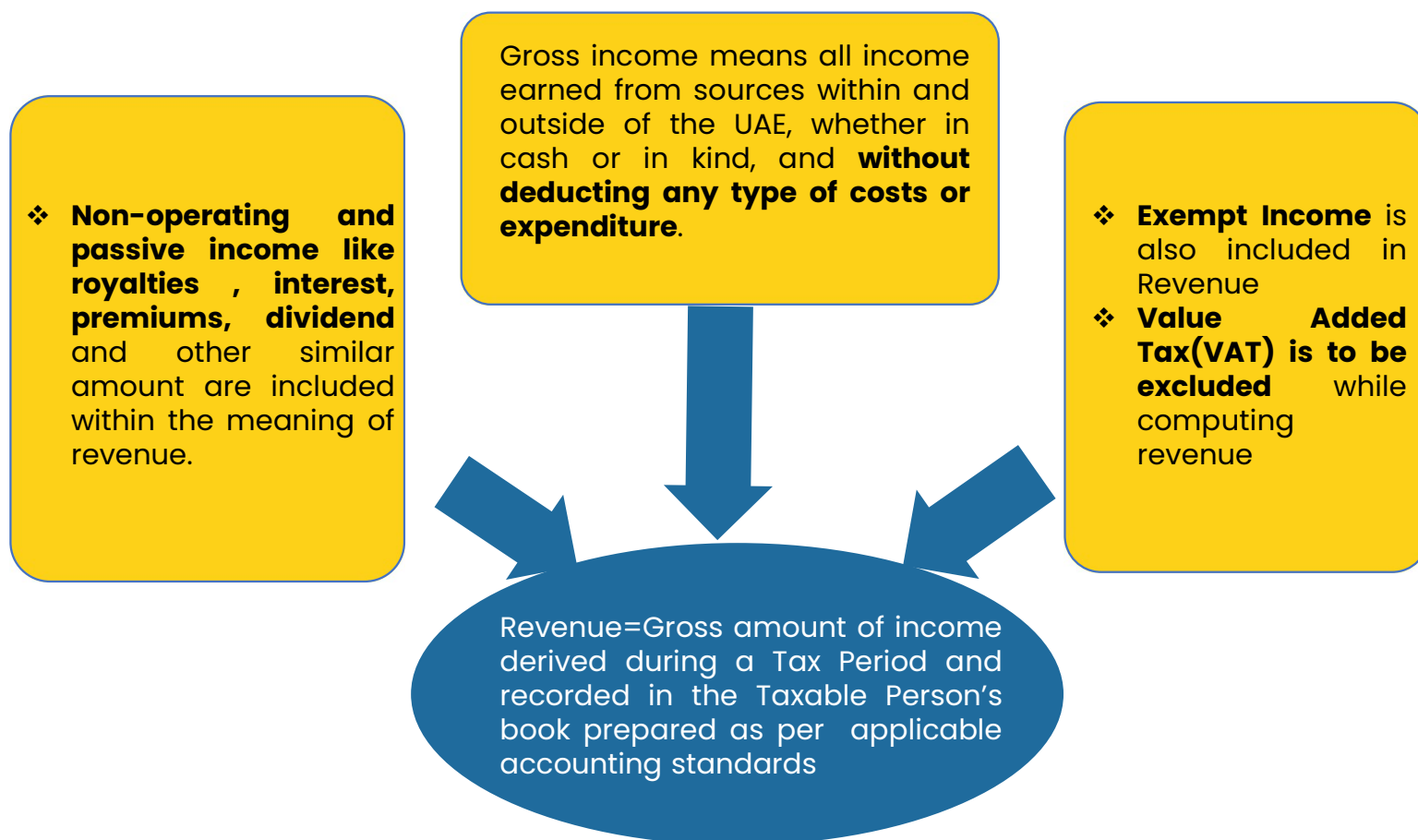
The taxability of business and business activity (other than the exclusions) **is not linked to license requirement**

# Taxation of Individuals

## Exclusions

- ❖ Wages- Salary and all allowances, bonus any other benefits **provided for in the employment contract.**
- ❖ Personal investment income earned in **personal capacity** that is **not** conducted or does not require to be conducted **through license** from licensing authority.
- ❖ Real estate Investment income from **sale, leasing, subleasing and rental** of land or real estate property in **personal capacity** that is **not** conducted or does not require to be conducted **through license** from licensing authority.

# Revenue





## Relevance of term Revenue under CT

Small Business Relief

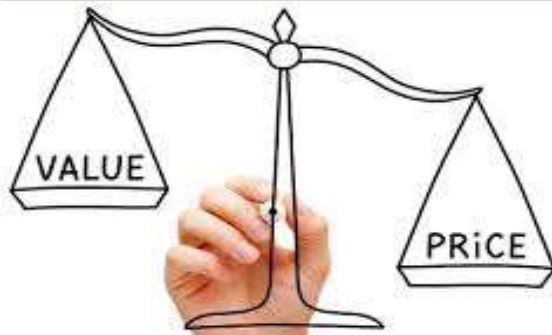
Audit Requirement for  
Financial statements

Resident or Non-  
Resident Natural  
Person Conducting  
business or business  
activity

Preparation of  
Financial  
Statements using  
the Cash Basis of  
Accounting

Maintaining Transfer  
Pricing  
Documentation

# Market Value

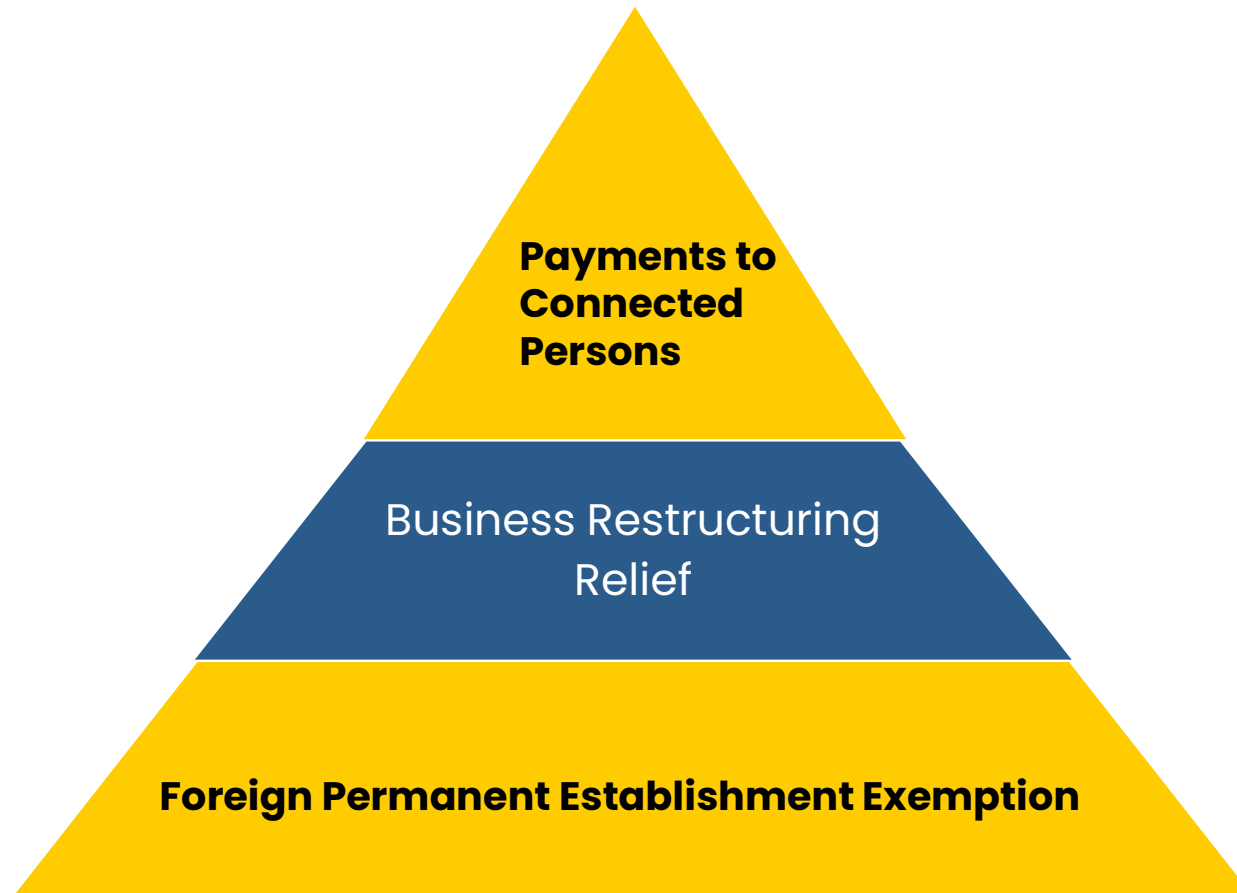


The Market Value of an asset, service or benefit provided is the value that the asset, service or benefit would ordinarily have in the **open market** at **the time and place** of the transaction taking place.



If it is not possible to determine Market Value of the actual asset, it is to be determined by reference to the consideration for a **similar asset, service or benefit in the open market** at that time, as adjusted for any differences between the transactions being compared or between the parties undertaking those transactions.

## Relevance of term Market Value under CT



# Effective Management and Control

## As per CT Law

Juridical persons that are incorporated, or otherwise established or recognized under the laws of a foreign jurisdiction, but that are effectively managed and controlled in the UAE, will be considered as Resident Persons for Corporate Tax purposes.

## As per Explanatory Guide

Key factor for determination of tax residence is where the **key management and commercial decisions concerned with broader strategic and policy matters** necessary for the conduct of the company's business as a whole are regularly and predominantly made i.e. ordinarily a place where Company's Board of Directors make these decisions

**Note:-For a juridical person to be considered effectively managed and controlled in the UAE, it is not necessary for its board members (or equivalent) to be domiciled or resident in the UAE.**

# Tax Residency Vs PE

## Tax Residency

Key management and commercial decisions concerned with broader strategic and policy matters necessary for the conduct of the company's business as a whole are regularly and predominantly made and given.

Foreign company could be a UAE tax resident taxed **at worldwide income**

## Permanent Establishment

A fixed or permanent place in the State includes a **place of management** where management and commercial decisions are taken.

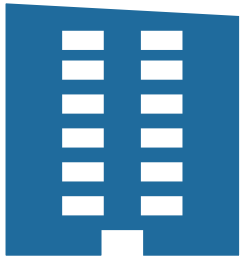
**Day to day management** which takes implementation decisions.

Foreign company could have a PE in UAE which is **taxed at attributable income in UAE.**

# Illustration

## Effective Mgmt & Control

ABC Company in BVI



BOD's residing in UAE



BOD are taking strategic decisions related to Product launch, Pricing strategies, Financing, mergers and acquisitions, etc. **in UAE.**

**Conclusion** : ABC Company is incorporated in BVI and BOD'S are residing in UAE and making **strategic and policy matters** necessary for the conduct of the business from UAE.

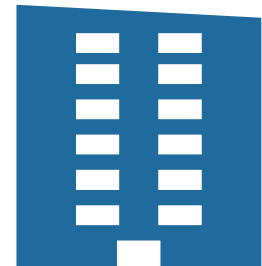
Therefore , ABC Company in BVI may be a UAE tax resident taxed at **worldwide income**

## PE

Employees residing in UAE



ABC Company in UK



Employees are taking decisions related to negotiation with customers, marketing function hiring of employees , etc. **in UAE**

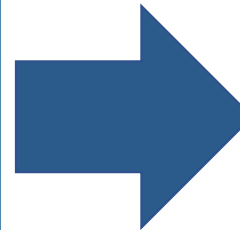
**Conclusion** : ABC Company is incorporated in UK and Employees are residing in UAE and making **day to day decisions** for the conduct of the business from UAE. Therefore , ABC Company in UK may be considered to have a PE in UAE and **taxed at income attributable to UAE.**

## Differences in the PE definition

Corporate Tax Law	OECD Model Tax Convention
1. Definition of Fixed Place PE includes-Place of Management where <b>management and commercial decisions</b> that are necessary for the conduct of the business are ,in substance made. As per Explanatory Guide , decisions related to <b>day to day operations</b> of the business.	1. <b>Place of Management</b>
2. It is also <b>not</b> required that the fixed place is owned or used exclusively by the Non-Resident Person or is at the <b>disposal</b> of the Non-Resident Person for an extended period of time.	2. Fixed place should be at the <b>disposal of the Non-Resident Person.</b>
3. 6 months threshold for a 'Construction PE'.	3. 12 months threshold for a 'Construction PE' .
4. Anti-fragmentation provisions exist in CT law.	4. Anti-fragmentation not provided
5. Services PE specifically not defined but employees covered under Agency PE	5. Service PE specifically defined
6. A 'Nexus PE' included specifically	6. A 'Nexus PE' has not been provided

# Withholding Tax treatment

- ❖ All the members of the Tax Group will remain responsible to comply with the provisions of the Corporate Tax Law regarding Withholding Tax.
- ❖ This means that as and when the Withholding Tax rate is increased from 0%, each member of the Tax Group will be responsible for deducting Withholding Tax and remitting amounts deducted to the Authority on payments subject to Withholding Tax made by them.
- ❖ It will not be the responsibility of the Parent Company to fulfil the Withholding Tax obligations on behalf of the Subsidiaries of the Tax Group.



## Tax group liabilities:

- ❖ Filing of one corporate tax return by the Parent Company and processing one payment;
- ❖ Separate payments of the withholding tax and potential separate filing of the withholding tax returns.



# Transfer of Tax Losses

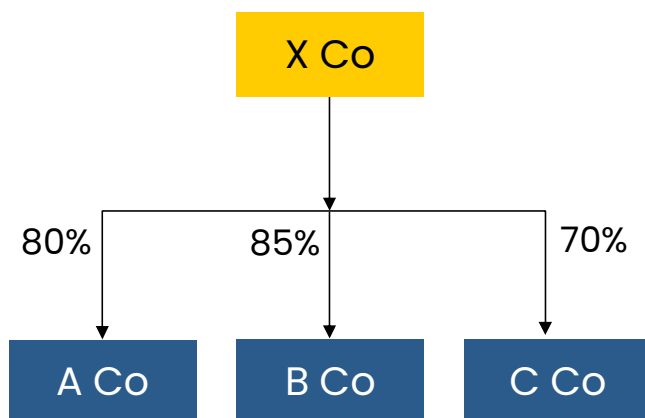
## As per CT Law- Special provision for transfer of losses

- ❖ Both taxable persons are **resident juridical persons**
- ❖ Either taxable person has a **direct or indirect ownership interest of at least 75%** in the other, or a third person has a direct or indirect ownership interest of at least 75% in each of the taxable person
- ❖ The **common ownership must exist** from the start of the tax period in which the tax loss is incurred to the end of the tax period in which the other taxable person offsets the tax loss transferred against its taxable income
- ❖ **None** of the persons are an **exempt person nor a Qualifying Free Zone Person**
- ❖ Both taxable persons should follow same financial year and same accounting standards.

## As per Explanatory Guide- Transfer of losses

- ❖ A **single Taxable Person** may transfer their Tax Losses to **more than one Taxable Person**.
- ❖ Tax loss used in subsequent periods cannot exceed 75% of taxable income for that period before utilizing any form of tax relief . However, the threshold of 75% applies separately to each recipient of the tax loss based on the taxable income, before utilizing any form of tax relief.

# Illustration



- ❖ X Co loss - AED 200 Mn
- ❖ A Co Profit - AED 150 Mn
- ❖ B Co Profit - AED 120 Mn
- ❖ C Co Profit - AED 130 Mn

(Amount In Millions)

PARTICULARS	COMPANY A	COMPANY B
Net taxable Income	150.00	120.00
Loss of X Co set off to the extent of 75% of Taxable Income	112.50	87.50
Net taxable Income	37.50	32.50
Tax rate	9%	
Exemption Threshold	0.375	0.375
<b>Tax Liability</b>	<b>3.34</b>	<b>2.89</b>

# Expenditure Deductibility–Entertainment Expenditure

## Entertainment Expenditure

Entertainment Expenditure incurred **for staff is fully deductible.**

Entertainment Expenditure incurred for **customer/shareholders/suppliers and business partners are 50% deductible**

### Example

- ❖ Distribution of Iftar kits of AED 15,000 to customers, suppliers, shareholders.
- ❖ Distribution of Iftar kits of AED 9,500 to employees.

### **Expenditure Deductibility as per CT Law–:**

- ❖ Entertainment expenditure of AED 15,000 for **customers, suppliers, shareholders is 50% deductible.**
- ❖ Entertainment expenditure of AED 9,500 for **employees is 100% deductible.**

# Compensation to Direct or Indirect Owners

Compensation paid  
to Direct or Indirect  
Owners

Compensation paid to direct or indirect owners that is not fixed and determinable but instead **contingent on the financial performance** of the taxable person is **not tax deductible**.

Issue of bonus shares or other non-cash entitlements in the Taxable Person to its direct or indirect owners is not deductible while calculating CT liability

# Deductibility of Interest Expenditure

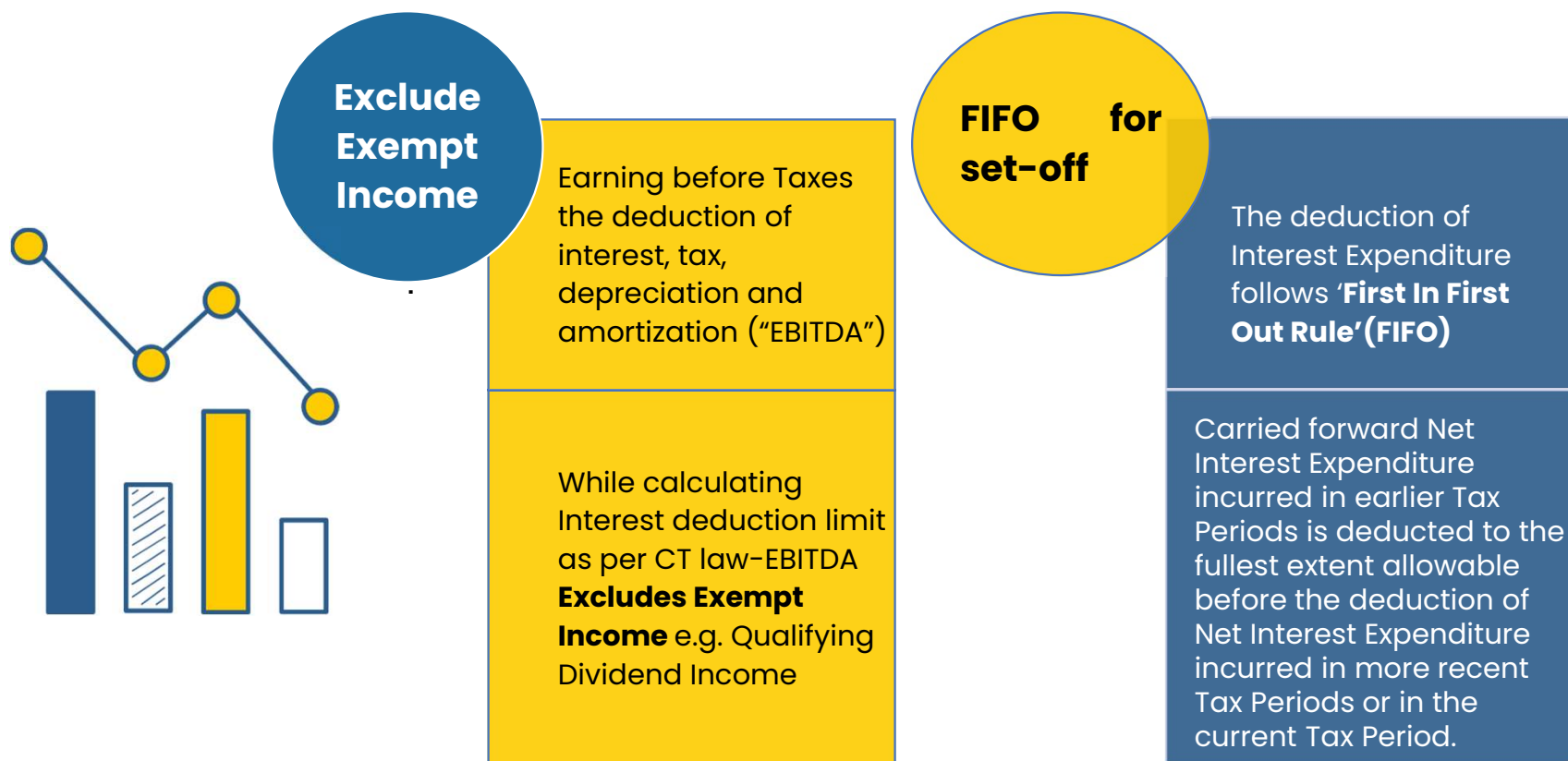
As per Explanatory Guide provides that while the interest definition is very wide, it is meant to be **compensation paid for use of money or for a debt obligation.**

Finance elements of **Finance/Non-finance lease** should be considered as interest and this includes both expenditure in relation to the finance cost elements and income received thereon.

Amount incurred in connection with raising finance such as **guarantee fees, arrangement fees, commitment fees or any other similar fees will be considered as interest.**

As per Ministerial Decision NO. 126 of 2023, if the Net Interest Expenditure for the relevant Tax period is **upto AED 12 Mn** then General Interest Deduction Limitation Rule will not apply (i.e. 30% of EBITDA)

# Deductibility of Interest Expenditure



# Condition for claiming Participation Exemption



Participating Interest **means a 5% or greater ownership interest** in the shares or capital of a juridical person



The Taxable person has to **hold the Participating Interest** for an uninterrupted period of **twelve (12) months**



The **Participation** is subject to **Corporate Tax of not less than 9%**



Taxable person is entitle to **receive atleast 5% of distributed profit and liquidation proceed**



**Not more than 50% of the participation assets** consist of ownership interest or entitlements that would not qualify for exemption under Corporate Tax.

# Ministerial Decision No. 116

This decision deals with Participation Exemption conditions under UAE CT Law. It's a very exhaustive decision and lays down clarifications on each of 3 conditions of being participating interest.



Ownership Interest to include Ordinary Equity Shares, Preference Shares, Redeemable Shares, Member / Partner interests, etc. However, these **interests should be classified as equity interest** as per Accounting Standard followed.



All types of **ownership interests to be aggregated for computing the 5% threshold** - this would even include interests held by members of Qualifying Group.



## Ministerial Decision No. 116

Even income from a **debt instrument, if classified as equity interest** as per Accounting Standard followed would be treated as income from Participating interest.

If the acquisition cost of ownership interest is equal to or more than **AED 4 Mn**, the 5% minimum ownership requirement will be considered satisfied for claiming Participation Exemption.

## Subject to Tax criteria

The entity in which ownership interest is held should be subject to a minimum tax rate of 9% in its home country.

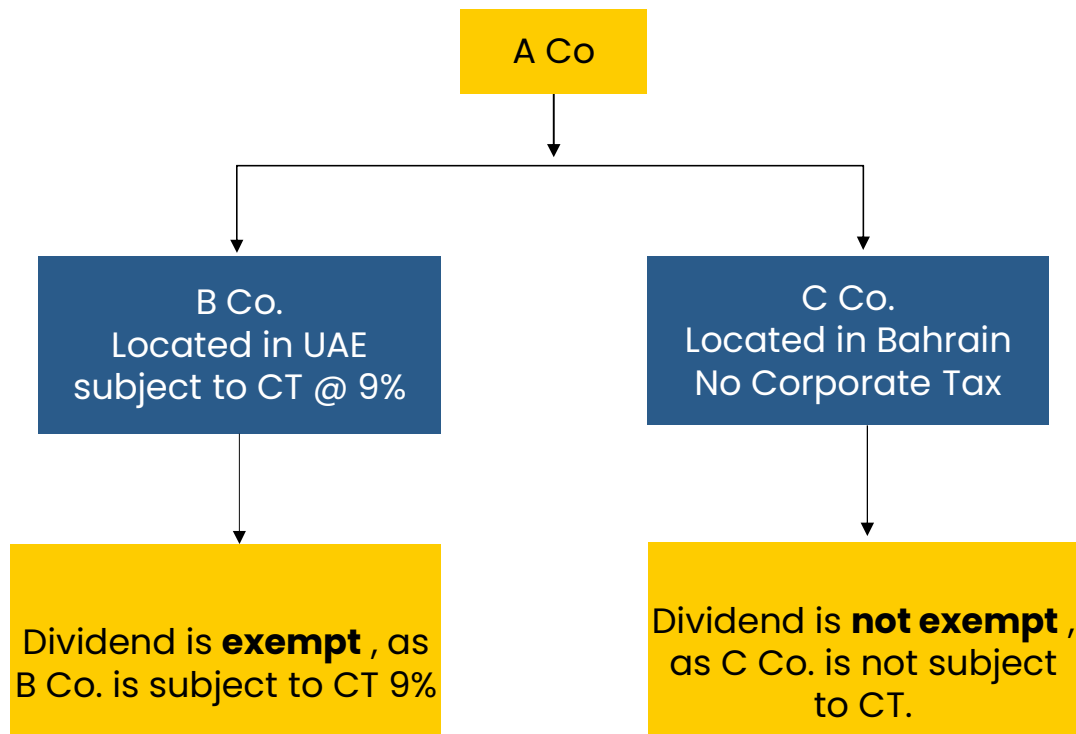
The tax is applied on a similar basis to UAE CT

The condition will be considered satisfied if Effective Tax rate ("ETR") of 9% or higher can be demonstrated.

If the participation is subject to tax on income, equity or net worth or a combination of any or all of these (eg. Zakat), ETR of 9% needs to be demonstrated based on accounting profits recalculated as per UAE accounting standards

# Illustration

A Co. hold Participation interest in the following Companies registered in two different countries.



# Illustration

A Co. hold Participation interest in the following two Companies :-

Particular	B Co.	C Co.
Ownership interest in Participation	3%	4%
Holding period	13 month	13 month
Participation subject to Corporate Tax	9%	15%
Acquisition Cost of ownership interest	5Mn	2.5Mn
<b>Will A Co. ownership interest qualify for Participation exemption?</b>	<b>Yes</b> , As per FTA Decision No. 116 of 2023, it state that <b>if acquisition cost is equal to or more than AED 4 Mn</b> , then only period of holding and participation subject to minimum Corporation Tax are required to meet.	<b>No</b> , Since the <b>acquisition cost</b> of ownership interest is <b>less than prescribed limit of AED 4 Mn</b> .

# Contact Us

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### Disclaimer

Please note that our views mentioned above are based on current prevailing regulatory regime in UAE and refers specifically to Federal Decree Law No. 47 of 2022. Our views or advise does not cover implications under any other laws or regulations that may govern the situation and are limited to the taxability consequences in UAE alone. For any other implications, we would recommend to obtain specific advice in that connection.

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**Thank You**