

UAE CORPORATE TAX



Navigating Your First Tax Period:

Demystifying Deductible Vs. Non-Deductible Expenses for a Smoother Filing Experience

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III. Deductible & Nondeductible Expenditure

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I. First Tax Period

5 KEY POINTS FROM PUBLIC CLARIFICATION – CTP003

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First Tax Period for a Juridical Person incorporated in the UAE

1

Incorporated **before June 1, 2023**: The first Tax Period shall be the first financial year **commencing on or after June 1, 2023**

Incorporated **on or after June 1, 2023**: The first Tax Period shall be from the date of incorporation to the end of the financial year, which will be **above 6 months but not more than 18 months**



Date Of Incorporation

1st May 2023

1st July 2023

1st June 2023



FY adopted by the company

Jan - Dec

Jan - Dec

Jan - Dec



First Tax Period

1st Jan 2024 – 31st Dec 2024 [12 months]

1st July 2023 – 31st Dec 2024 [18 months]

1st June 2023 – 31st Dec 2023 [7 months]

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Treatment of Thresholds- When First Tax Period is more or less than 12 months:

2

Example:

- ✓ **ABC LLC** incorporated on 1/8/2023, the First FY will be 17 months ended 31/12/2024.
- ✓ **EFG LLC** incorporated on 1/6/2023, the First FY will be 7 months ended 31/12/2023.

[Assuming the FY year adopted - JAN to DEC]

There is no pro-rating of the various thresholds prescribed under the Corporate Tax Law when the first Tax Period is different than 12-months period:

- ✓ Small Business Relief threshold - 3 M
- ✓ Basic tax rate of 0% for profit up to AED 375K
- ✓ Mandatory Audit threshold of AED 50M
- ✓ Mandatory TP documentation threshold of AED 200M
- ✓ De-minimus Criteria of AED 5 Million for a QFZP

Exception- General Interest Deduction Limitation Rule (currently set at AED 12 million)

Tax Period	Interest Deduction Limit
12 Months	12 Million
8 Months	08 Million
17 Months	17 Million

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First Tax Period

for a Non-Resident Person with PE in the UAE

3

Existed **before June 1, 2023**: The first Tax Period shall be the first financial year **commencing on or after June 1, 2023**

Existed **on or after June 1, 2023**: The first Tax Period shall be from the date it began operation in the UAE, till the end of the financial year, which will be **above 6 months but not more than 18 months**

 Type of PE in the UAE	 FY adopted by the Entity	 Started Operation in the UAE	 PE effective date	 First Tax Period
Fixed Place of Business	Jan - Dec	1st July 2023	1st Jan 2024	1st July 2023 till 31st Dec 2024
*Dependent Agent	Jan - Dec	1st July 2023	1st July 2023	1st July 2023 till 31st Dec 2024

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*a Person habitually exercising an authority to conduct Business or Business Activity on behalf of the Non-Resident Person



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For a Juridical Person subject to the Commercial Companies Law:



- Cease to exist before Tax period: It is not required to register for Corporate Tax
- Cease to exist after Tax period: A company is obliged to register for Corporate Tax and the first Tax period will come to an end on the cessation date.
- Deregister within 3 months from the date of triggering the event.

 FY adopted by the company	 Cease to Exist	 First Tax Period	 Registration
<p>Jan - Dec</p>	<p>1st Feb 2024</p>	<p>1st Jan 2024 – 31st Dec 2024</p>	<p>Register & then Deregister</p>
<p>Apr - Mar</p>	<p>1st Feb 2024</p>	<p>1st Apr 2024 – 31st Mar 2025</p>	<p>NA</p>

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II. Determination of Taxable Income

[CT GUIDE – CTGDTI 1]

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Starting Point - Accounting profits or loss as per

(a) financial statement prepared in accordance:

- IFRS OR
- IFRS [SME] OR

(b) Income & Expenditure Stt maintained – if cash basis is followed.

Following adjustments to be made to accounting profits/loss to arrive at the taxable income:

Accounting Income		XXXXXX
i. Unrealized gain or loss	XXXXX	
ii. Exempt income/loss	XXXXX	
iii. Qualifying Relief [Q.G. Relief / S.B. Relief]	XXXXX	
iv. Treatment of Expenditure	XXXXX	
v. Transfer Pricing adjustments	XXXXX	
vi. Incentives/ Special Relief	XXXXX	
vii. Adjustments as per MD	XXXXX	XXXXXX
Taxable Income before Tax Loss Relief		XXXXXX
Tax loss relief		XXXX
Taxable Income Subject to Corporate Tax		XXXXXX

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III. Demystifying Deductible & Non-Deductible Expenses

7 KEY POINTS FROM CT GUIDE – CTGDTI 1

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EXPENDITURE

DEDUCTIBLE



- Incurred '**wholly and exclusively**' for the taxable person's business purposes
- Is **not capital** in nature.
- Is **incurred** in the Tax Period

NON - DEDUCTIBLE



- **Incurred for another** Taxable Person's Business
- Incurred for deriving **Exempt Income**
- **Non-Arm's Length** Expenditure
- Portion of the expenditure which is **not for the purpose of business**

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ILLUSTRATIVE LIST

DEDUCTIBLE



- **Bad Debts** as per IFRS / IFRS for SMEs
- Donation to **QPBE**
- Any **Local taxes** that are not in the nature of CT, eg. municipal and property taxes
- **Irrecoverable** input VAT

NON - DEDUCTIBLE



- **Bribes** / Illicit payments
- **Dividend** / Profit distribution to owners
- **Corporate Tax**
- **Emirate-level taxes**

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1



EXPENDITURE

DEDUCTIBLE



- **Employee cost** (provided reasonable)
- Connected Persons cost **subject to ALP**
- Cost of benefit provided to the employees [eg: **Car, Telephone allowance** etc.]
- Cost of **entertainment expenses** for employees
- Expenditure of associated cost for an employee **working from home**

TAXABLE



- Shared employee cost that is **not for that taxable person's business**
- Incurred for the **private events** (e.g. wedding related)
- Connected Person Expenditure **beyond ALP**

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DEDUCTIBLE



- Incurred wholly and exclusively for the Taxable Person's Business are deductible
- **Staff party** expenses
- Expenditure incurred for Event on rewards for **meeting performance targets**
- Conferences for **employees, their spouses and children** (such as team building events or seasonal events – eg Annual Day), expenditure including catering.



TAXABLE



- **Staff wedding event** expenses – personal in nature.

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DEDUCTIBLE



- Contributions made to a **private pension fund** in respect of its employees who are Pension Plan Members.
- Contribution to be **“PAID”**
- **Up to 15%** of the **“TOTAL”** remuneration

NON - DEDUCTIBLE



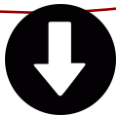
- Contributions in **excess of 15%**
- **Provision created** in the books but not actually “paid”

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Manpower Vs. Visa Facilitation Services

[VATP 038- Public Clarification]

Employment visas are held by one entity while the employees work under the supervision and control of another entity.



Company A is regarded as supplying manpower services irrespective of whether the employees' salaries and benefits are paid by Company A or Company B.

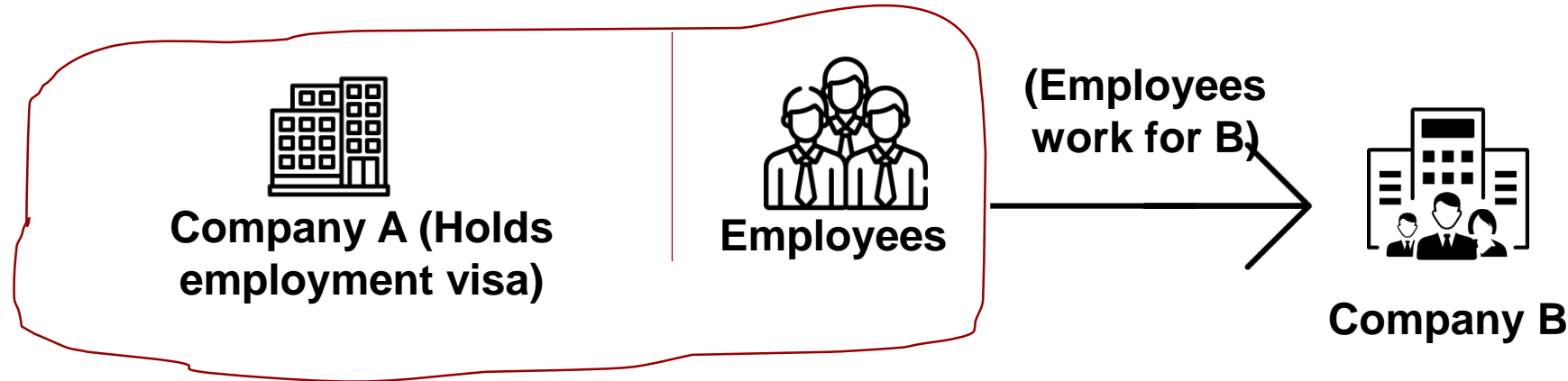
If A & B are **not in same VAT group**, **A has to charge B, 5% VAT** for the supply of services (includes the salary & other benefits to the employees and the service charge if any)

As fa as **Corporate Tax** is concerned, the value of such supply should be at **ALP**.

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Manpower Vs. Visa Facilitation Services

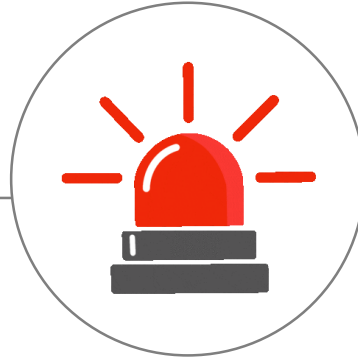
[VATP 038- Public Clarification]



⚡ A supply would not be regarded as a supply of manpower services but rather as a **supply of visa facilitation services** if all of the requirements set out below are met

- 1** If A & B are part of the **same corporate group** but are not part of the same tax group.
- 2** A's activities **do not** include the **supply of manpower**
- 3** A is not responsible for any of the **obligations related to the employee**
- 4** "A" sponsors these employees to exclusively work for & **under the supervision and control, of B**

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In order for this condition to be met, “A” and “B” **must be part of the same corporate group** from a commercial/accounting perspective.

The reference to “corporate group” **differs from the tax group** concept used for Corporate tax purpose, but relates to companies operating within the same corporate structure, which includes **common ownership of the companies** in line with Article 9(2) of the Executive Regulation.


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Expenditure Incurred For More Than One Purpose




- Proportionate based on **Fair and Reasonable basis**




- **Allocation Keys** used for assigning expenses on fair and reasonable basis




- Allocation keys need to be determined on basis of:
 - ✓ Cause & Effect
 - ✓ Benefits Derived



- Factors based on which **allocation keys can be** determined:
 - ✓ headcount
 - ✓ floor space
 - ✓ Usage
 - ✓ time spent
 - ✓ or any other measurable & reasonable basis



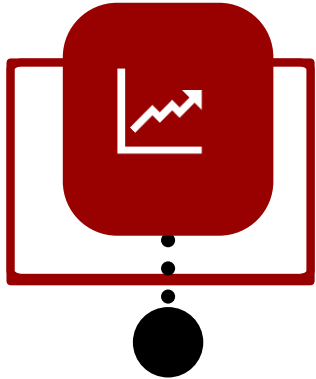
- The selected allocation key must be **used consistently** for each Tax Period



- If expenditure incurred for more than one purpose **cannot be apportioned on a fair and reasonable basis, it will not be allowed** as a deduction for CT purposes.

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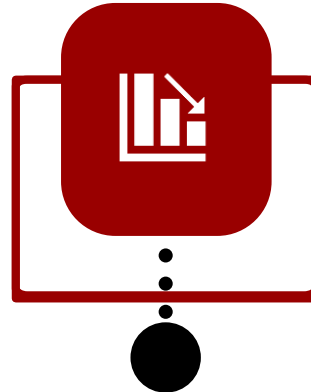
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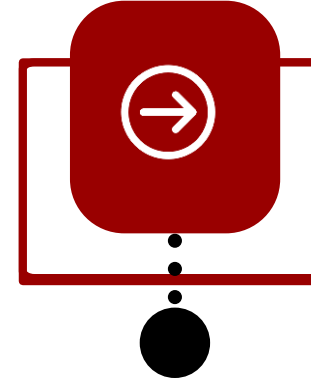
- It creates an **enduring benefit to business** hence non- deductible



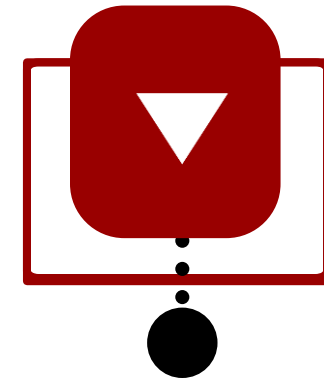
- **Depreciation** on capital asset is a deductible expenses



- **Low value capital asset** can be expensed based on accounting policy



- **Directly attributable cost** incurred for asset need to be capitalized



- Depreciation on Capital expenditures would not be allowed where such **expenditures are generally non- deductible**
- Example:
 - ✓ (1) **Fines levied by the Govt.**
 - ✓ (2) **Commission to RP over Arm's length capitalized)**

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Pre- incorporation

- Pre-Incorporation expenses are **generally reimbursed to the Shareholders/Promoters**:
 - ✓ feasibility studies,
 - ✓ registration fees,
 - ✓ legal and professional fees in relation to incorporation documents, etc.
- **Allowed in the first Tax Period if**
 - ✓ It is accounted **as per IFRS**
 - ✓ has not been **claimed** as deductible expenditure **by another Taxable Person**



Post Incorporation – *(before commencement of operations)*

- pre- trading
- *product development*
- *marketing and advertising expenses,*
- *office setup costs,*
- *utilities,*
- *expenses for hiring and training employees*

Allowed as an expenses in the Tax Period when it is incurred

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Provision for expenditure

DEDUCTIBLE



- Provisions created for **legal or constructive obligation** (e.g. ECL)
- Amount of obligation can be **estimated reliably**
- Is as per applicable **IFRS / IFRS for SMEs**

TAXABLE

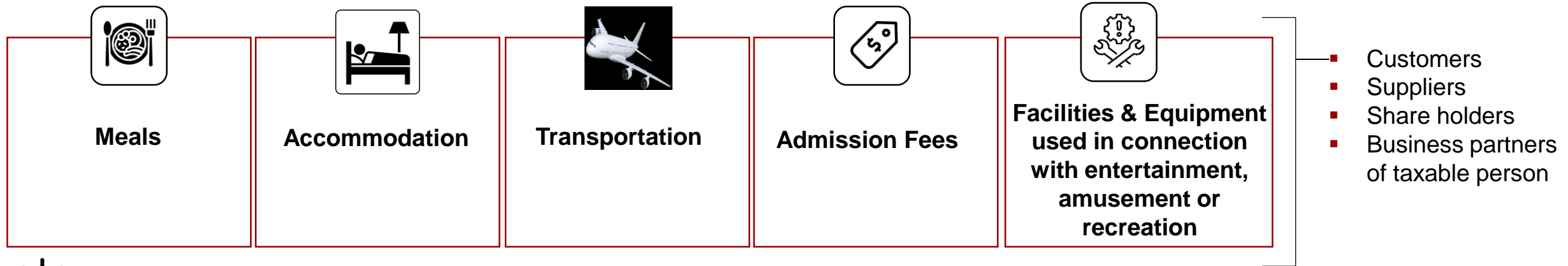


- Provision of **illegal payment / fine / penalty**
- **Reversal of provision** (even if created prior to first Tax Period)
- **Receipt of written off** bad debts (in the year of recovery)

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The following are the entertainment expenses subject to 50% deduction rule:



Key Aspects:

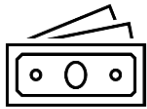
Entertainment expenditure usually serves to build relationships and promote the Business in a **more informal or social setting.**



Examples:

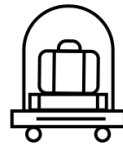
Hospitality at restaurants, cultural events, sporting events, hotel stays and similar trips

Fully Deductible



Incidental Expenses

- Expense incurred which is incidental to a Business purpose - not entertainment expenditure.
- Example
 - ✓ Food and refreshments in **an office setting**
 - ✓ A retailer provides complimentary refreshments to prospective customers



Commercial Hospitality

- Commercial hospitality as part of Business or Business Activity,
- Example:
 - ✓ airline provides a washbag or in-flight entertainment,
 - ✓ hotels provide packaged or mid-week promotions



Marketing and Advertising Expenditure

- marketing expenditure,
- advertising,
- online promotion,
- attending trade shows
- direct marketing campaigns
- Business Advertising its own product or services for generating publicity
- Sponsoring an event –provided not to entertain customers

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Key Takeaways:



- Entertainment expenditures **incurred for employees are allowed as deduction** without any adjustment



- Benefits provided** to employees which are **personal in nature are allowed as deduction**



- Entertainment expenditure incurred for the **business partners**, shareholders, customers, suppliers are allowed to **the extent of 50%**



- Entertainment expenditure incurred for the **family members of shareholders** are **NOT** allowed as deduction

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DEDUCTIBLE



- Compensation for:
 - ✓ damages or **breach of contract**
 - ✓ due to **negligence** of the company.
 - ✓ a **breach of warranty** or for failure to perform
 - ✓ **delay in performing** a trading contract or construction contract
 - ✓ for **extension of time for** performance of contract

NON - DEDUCTIBLE



- Fines for infraction/**breach of any laws, rules or regulations** or is imposed as punishment
 - ✓ Traffic fines
 - ✓ VAT Penalty
 - ✓ Other Statutory penalties

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ECAG

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June 2024

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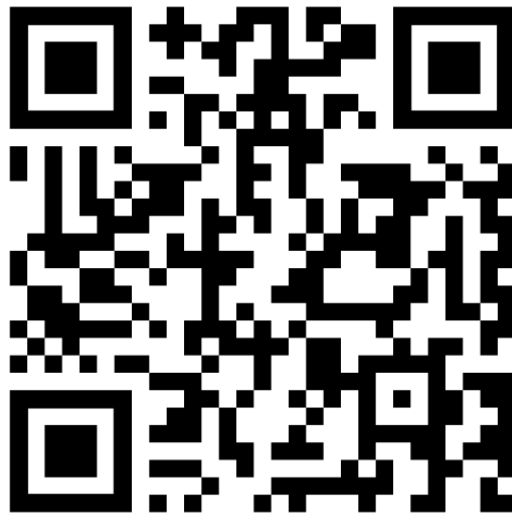
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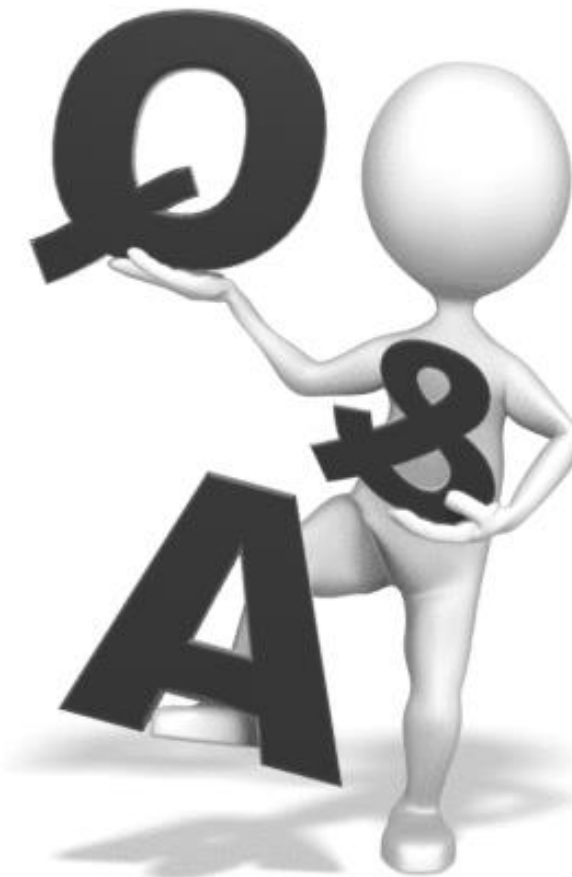


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