THE Inward Investment and International Taxation Review

Twelfth Edition

Editor
Tim Sanders

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Twelfth Edition

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PREFACE

In January 2021, the 11th edition identified and described two material global tax trends that emerged in 2020: the response of economies to the covid-19 pandemic and the taxation of the digital economy. These two trends evolved through 2021 and can be expected to occupy centre stage in 2022 and beyond.

In 2020 and 2021, governments sought to bolster economies hit by the pandemic through a series of measures ranging from furlough schemes, postponing tax deadlines and deferring tax payments to relaxing residence rules. In 2021 and into 2022, governments will face the difficult balancing act of continuing to support their economies and encourage growth on the one hand, while needing to raise money from damaged economies to pay for such support and reduce the size of large deficits on the other, without such tax raising stifling any recovery. Precisely how each jurisdiction will deal with this balance remains uncertain and is a key area to observe in 2022. At this stage it appears that, while we may see some limited tax rises, more rigorous tax enforcement is likely to play a material role.

On 1 July 2021, a statement was made by the G20 Finance Ministers that on 8 October 2021 resulted in the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS 2) that contains details of how Pillars 1 and 2, which seek to address the issues raised by the digital economy, will be applied in practice. Pillar 1 deals with the reallocation of certain profits from very large multinational enterprises to market jurisdictions, while Pillar 2 deals with a global minimum tax. Among significant points to note is that under Pillar 1 it is intended that a new multilateral convention will be drafted and available for signature in 2022 that will remove unilateral digital services taxes and similar measures. Some jurisdictions that have applied a unilateral solution, notably the United Kingdom, Austria, France, Italy and Spain, have committed to transition from existing digital services taxes to the new multilateral approach solution. Under Pillar 2, the minimum tax rate is set at 15 per cent rather than the previously proposed rate of 'at least 15 per cent'. This has already had an impact, with Ireland announcing an increase in its minimum corporate rate to 15 per cent. While a remarkable amount of progress has been made in a short time, there are still important technical issues to be addressed quickly if the timetable, which proposes implementation in 2023, is to be adhered to. However, there is sufficient detail in the proposals for businesses likely to be affected to consider starting the process of reviewing their internal procedures and processes to ensure they can be compliant.

It is hoped that this volume will prove to be a useful guide to the tax rules in the jurisdictions where clients conduct their businesses. Each chapter aims to provide topical and current insights from leading experts on the tax issues and opportunities in their respective jurisdictions. While specific tax advice is always essential, it is also necessary to have a broad understanding of the nature of the potential issues and advantages.

The views expressed in this book are those of the authors and not of their firms, the editor or the publishers. Every endeavour has been made to ensure that what you read is the latest intelligence.

Tim Sanders
London
January 2022

Chapter 30

UNITED ARAB EMIRATES

Danielle Lobo and Silvia A Pretorius[1]

I INTRODUCTION

The United Arab Emirates (UAE) was established in 1971 under a written constitution as a federation of the seven emirates of Abu Dhabi, Ajman, Dubai, Fujairah, Ras Al Khaimah, Sharjah and Umm Al Quwain. The significance of the UAE economy is based on the discovery, in the 1950s in Abu Dhabi and the 1960s in Dubai, of major quantities of crude oil and the subsequent generation of very substantial revenues from its export, especially following the price increases in 1973.

Abu Dhabi is the federal capital of the UAE, and the site of a number of federal ministries, the UAE Central Bank, and other government institutions and agencies.

Under the Constitution of the UAE, each of the seven emirates retains a very substantial measure of control over the conduct of governmental affairs within the emirate. The important subjects over which the federation exercises control are defence, foreign affairs, communications, education and health. In addition, the federation has legislative authority with regard to a number of matters, including commercial and corporate law. The individual emirates retain control over all matters not specifically stated in the Constitution to be under federal authority.

The UAE attracts substantial foreign direct investment (FDI). Although FDI flows plunged 35 per cent globally in 2020, investment into the UAE increased 11 per cent to almost US$20 billion, and the UAE was the world's 15th-biggest recipient of FDI in 2020, ranking one place above the United Kingdom and seven places higher than the prior year, according to the United Nations Conference on Trade and Development.[2] Key advantages for investing and doing business in the UAE include the fact that the UAE has a stable economic and political background, and that it provides a unique geographical location for worldwide business opportunities. Many financial institutions and international industrial companies have taken advantage of the location's appeal. Other factors include no income tax (with limited exceptions), fast population growth in recent years and the absence of exchange control or of any constraint relating to repatriation of funds.

Despite the recent global economic crisis, the UAE has in excess of 97 billion barrels of proven oil reserves, or about 8 per cent of the world's proven oil reserves, and Abu Dhabi commands one of the wealthiest sovereign investment funds in the world. Furthermore, the UAE has one of the highest incomes per capita in the world, and the UAE ranked 16th out of 190 countries in the 2020 Doing Business ranking published by the World Bank. The

1 Danielle Lobo is a partner and Silvia A Pretorius is a senior associate at Afridi & Angell.

2 'UAE was the world's 15th-biggest recipient of foreign investment last year', Khaleej Times, 21 June 2021.

UAE is the highest-ranking economy in the Middle East and North Africa, and joined the World Bank's top 20 ranking out of 190 economies for the first time in 2019. All of these factors should see the UAE continue to have a per capita income in the foreseeable future that is among the highest in the world, and continue to remain a preferred jurisdiction for inward investment.

II COMMON FORMS OF BUSINESS ORGANISATION AND THEIR TAX TREATMENT

The types of business entity most commonly used in the UAE by inward-investing corporates and non-residents are companies or branch offices of foreign companies created under UAE Federal Law No. 2 of 2015 on Commercial Companies, as amended, (the Companies Law). Another commonly used option is establishing an entity in one of the many free zones in the UAE.

Prior to discussing these various corporate structures in more detail, it is important to note that there is no federal income tax law in the UAE, and although all but one of the emirates have statutory income tax laws providing for tax on corporate bodies that are still technically effective with certain exceptions (principally oil-producing businesses and banks), a foreign business currently investing inwardly can safely conclude that its activity will not be subject to taxation.

i Corporate

The Companies Law applies to all companies established in the UAE, and to foreign companies with one or more branches in the UAE. It regulates existing branch offices of foreign companies and contains regulations for the establishment of new branch offices of foreign companies.

The Companies Law provides for the organisation of five types of businesses: joint liability company, simple partnership company, limited liability company (LLC), public shareholding company and private shareholding company.

The LLC is the preferred choice of corporate vehicle in the UAE. An LLC must have at least one and not more than 50 owners. The Companies Law does not apply to sole proprietorships or to non-commercial entities.

The UAE has recently introduced some significant changes to the foreign ownership restrictions (or foreign investment restrictions). Federal Decree Law No. 26 of 2020 (Decree Law) came into force on 2 January 2021 and significantly amends the Companies Law. The general long-standing requirement for 51 per cent of the shares in a mainland or onshore company to be held by one or more UAE nationals (natural or legal persons) has been removed. This amendment now means that it will be possible for foreign investors to own up to 100 per cent of shares in UAE companies. The Decree Law also removed the requirement for foreign branches to appoint a local service agent.

A Foreign Investor is defined in the recently enacted Cabinet Decision No. 55 of 2021 On the Determination of the List of Strategic Impact Activities (Cabinet Decision No. 55) as a 'Physical or moral person not holding the State's nationality and who invests in the State'. The UAE extends national treatment to Gulf Cooperation Council (GCC) nationals from other GCC countries.[3]

Under the Decree Law, local licensing authorities (i.e., the relevant economic departments) of each Emirate were granted the authority to determine a list of activities for which up to 100 per cent foreign ownership is permitted (FDI Activity). All general partnership interests must be owned by UAE nationals. However, certain sectors such as oil and gas, utilities and companies carrying on activities with a 'strategic impact' will continue to be subject to restrictions on foreign ownership. Strategic Impact Activities include:

a security and defence activities and activities of a military nature;
b banks, money changers, finance companies and insurance activities;
c printing currencies;
d telecommunications;
e Hajj and Umrah services; and
f Quran Memorisation Centres.

Cabinet Decision No. 55 also provides that in relation to fisheries-related services, the contribution percentage of UAE nationals for this activity will be 100 per cent. The aforementioned Strategic Impact Activities will be subject to the approval and requirements of the relevant regulatory authority in terms of:

a determining the percentage of the UAE nationals' contribution and/or the percentage of the Foreign Investor's contribution to the capital;
b determining the participation of UAE nationals' and/or Foreign Investor's to the membership of the Board of Directors (if any); and
c any other conditions or rules deemed proper by the relevant authority.

Foreign investors may now own and control 'onshore' companies (i.e., companies outside of the UAE's free zones (including the financial free zones)) without the need to employ nominee or similar structures. Furthermore, entities with a single shareholder, which previously had to be wholly owned by UAE nationals, are now eligible to be 100 per cent owned by foreign investors on the assumption that they are licensed for an FDI Activity.

The Companies Law gives the shareholders considerable freedom in structuring the memorandum of association for an LLC, and particularly those provisions regarding the management and governance of the LLC. Inter alia, parties are free to include provisions allowing a minority shareholder to retain considerable management control of the LLC. An LLC may be licensed to conduct any lawful activity, except for the business of insurance, banking and investment of money for the account of others.

As mentioned above, a branch of a foreign company is now, pursuant to the Decree Law, no longer required to have a sponsor (termed a national agent). The national agent is not the same as a commercial agent. The provisions of Federal Law No. 18 of 1981 Regulating Commercial Agencies Law (the Commercial Agencies Law) are discussed below.

The term 'free zone' refers to one of the many areas designated as such within the UAE. Free zones are often established to cater to particular types of businesses.

3 The GCC Member States are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the UAE.

Foreign companies are generally permitted to establish branches in free zones. Legislation in each of the free zones also permits the incorporation of corporate entities that exist and operate outside the purview of the Companies Law. Such free zone companies can be 100 per cent foreign owned. The establishment of a free zone branch or a corporate entity is handled by the relevant free zone authority. Free zones generally guarantee freedom from corporate and income taxes for a specified period.

Conceptually, companies operating in a free zone are treated as offshore or foreign companies for non-export purposes and are not permitted to conduct business activities within the rest of the UAE without complying with the rules generally applicable to the establishment of a foreign business presence. Normal import duties are payable on sales by free zone companies to customers within the UAE.

In 2005, the Emirate of Dubai launched the Dubai International Financial Centre (DIFC). The DIFC represents a radical development, in that it is designed to operate independently of UAE civil and commercial laws generally, and it has its own legislation and court system modelled generally on English common law. The language of the DIFC is English, and a majority of DIFC judges have common law experience. Similarly, the Abu Dhabi Global Market (ADGM) was established pursuant to Abu Dhabi Law No. 4 of 2013 as a financial free zone in the Emirate of Abu Dhabi, with its own civil and commercial laws. The ADGM commenced operations in 2015.

As an alternative option, many foreign companies will appoint a commercial agent to offer their goods and services to consumers in the UAE through local agents and distributors. The Commercial Agencies Law governs the relationship between foreign principals and local agents and distributors. It offers significant protections to the local party if the agency or distributorship is registered with the Ministry of Economy. To register the agency or distributorship, the agent or distributor must be a UAE national or a company wholly owned by UAE nationals. The statutory protections to the local party flowing from registration include, inter alia, exclusivity, restrictions on the foreign party's right to terminate or withhold renewal of the relationship, and the right to receive compensation on termination or non-renewal of the relationship. Although there are a number of disadvantages to registration of an agency or distributorship from the foreign party's perspective, certain government departments may insist on dealing only with registered agents or distributors.[4]

ii Non-corporate

All general partnership and limited partnership interests can only be owned by UAE nationals. They are not subject to any taxation and are not fiscally transparent as, unlike other companies, they are not required to have their annual financial statements audited by accountants registered in the UAE and to submit such audited statements to the Ministry of Economy.

4 Many agency relationships in the UAE are not registered, and non-registration generally works to the foreign principal's advantage.

III DIRECT TAXATION OF BUSINESSES

i Tax on profits

There is no federal income tax law in the UAE, or any federal taxes on income (except as noted further below in this section). Accordingly, the pre-federation income tax decrees of the individual emirates remain applicable.

Corporate income tax statutes have been enacted in each of the emirates, but they have not been implemented. Instead, corporate taxes are collected with respect to branches of foreign banks (at the emirate level) and courier companies (at the federal level). Further, emirate-level 'taxes' are imposed on the holders of petroleum concessions at rates specifically negotiated in the relevant concession agreements. There is no personal income tax.

Dubai and certain other emirates impose taxes on some goods and services (including sales of alcoholic beverages, hotels, restaurant bills, and residential and commercial leases).

On 27 November 2016, the Member States of the GCC signed the Unified VAT Agreement for the Cooperation Council for the Arab States of the Gulf (the GCC VAT Framework Agreement). The GCC VAT Framework Agreement provides that each GCC state will be allowed to introduce its own value added tax (VAT) regime, providing that common principles are adopted by all GCC states.

The UAE has introduced a number of new laws to be able to prepare for the implementation of VAT. The Federal Tax Authority was established under Federal Law No. 13 of 2016 and will be in charge of managing and collecting federal taxes and related fines, distributing tax-generated revenues and applying the tax-related procedures in force in the UAE.

Following on the Federal Tax Authority, the Tax Procedures Law was then issued as Federal Law No. 7 of 2017. The Tax Procedures Law establishes the framework for federal taxes administration in the UAE.

Thereafter, Federal Decree-Law No. 8 of 2017 (the VAT Law) was issued, and a dedicated tax website launched for the Federal Tax Authority. The VAT Law is based on the common principles agreed in the GCC VAT Framework Agreement and sets the general rules for the implementation of the new tax and includes some details on the goods and services subjected to VAT, as well as those that will receive special treatment. The VAT Law introduced a 5 per cent VAT starting January 2018, and this is imposed on a taxable supply of goods or services for consideration and deemed supplies by a taxable person conducting business in the UAE and the import of taxable goods. The supplier of the goods or services, the importer of taxable goods and the taxable person registered for VAT who acquires goods will be required to account for VAT. Registration is mandatory for any taxable person if the total value of its taxable supplies made within the UAE exceeds the mandatory registration threshold of 375,000 dirhams over the previous 12-month period or if it is anticipated that the taxable supplies will exceed the threshold in the next 30 days. VAT registration will be optional if the mandatory registration threshold requirement (375,000 dirhams) is not met, but the voluntary registration threshold (187,500 dirhams) has been exceeded. The VAT Law provides for tax grouping, which allows companies with common control or ownership to be combined together into one entity for the purposes of VAT. Zero-rated supplies include certain exports, international transportation, supply of certain education and healthcare services and related supplies, certain investment grade precious metals, supply of crude oil and natural gas, supply of newly constructed residential properties within three years of completion and supply of certain land, sea and air means of transportation.

Exempt supplies will include certain financial services, residential supplies, bare land and local passenger transport. Provision is made for reverse charging VAT on certain transactions between entities within the GCC.

While the VAT Law provides a framework for implementation of VAT in the UAE, the operative provisions are contained within the VAT Law's Executive Regulations, issued as Cabinet Decision No. 52 of 2017. The Executive Regulations provide additional legislative and procedural guidance to the application of VAT within the UAE, specifically where it concerns the tax treatment of free zone entities. Cabinet Decision No. 52 of 2017 also outlines supply of goods and services in all cases, including supply in special cases, supply of more than one component and exemption related to legal supply. The regulation also defines the mandatory and voluntary tax registration thresholds, exceptions from registration, tax grouping, as well as the process to apply for deregistration.

Revenues from the UAE's value added tax exceeded government expectations in 2018, reaching 27 billion dirhams compared to the government's original projection of 12 billion dirhams, and accounted for 1.7 per cent of the UAE's 2018 nominal GDP.[5]

Separately, the Ministry of Finance (MOF) has announced that it is still studying reforms to the UAE corporate tax regime, that the tax rate is under study and that businesses will be given at least one year to prepare for any changes. As there are still many stages to go through before a corporate tax law is enacted, there is still no firm timeline in place for the implementation of this corporate tax law.

Each emirate, except for Umm Al Quwain, has an income tax decree. The income tax decrees of the emirates of Fujairah (1966), Sharjah (1968), Ajman (1968), Dubai (1969) and Ras Al Khaimah (1969) are based on and broadly similar to the Emirate of Abu Dhabi Income Tax Decree of 1965 (together, as amended, the Income Tax Decrees), which will be the basis for discussion here.[6] No other taxes are imposed on corporate income.

Taxable persons are defined as juristic entities or any branches thereof,[7] wherever organised, that conduct trade or business[8] at any time during the tax year through a permanent establishment[9] based in the respective emirate, whether directly or through the agency of

5 'UAE's VAT collections exceeds expectations by a wide margin in 2018', Khaleej Times, 3 June 2019.

6 The official language in the UAE is Arabic; as such, all legislation is promulgated in Arabic. The discussion in this chapter is based largely on unofficial translations of this legislation, although the official Arabic texts of the Abu Dhabi Income Tax Decree of 1985 (as amended) (Abu Dhabi ITD) and the Dubai Income Tax Decree of 1969 (as amended) (Dubai ITD) have been consulted. Some of the material differences in treatment between the Abu Dhabi ITD and the Income Tax Decrees of the other emirates are indicated in these footnotes.

7 Abu Dhabi ITD, Article 2(3) refers to a 'body corporate', a term that does not refer solely to corporations. Dubai ITD, Article 2(3) refers to any 'body having juristic personality' as being a taxable person.

8 Conduct of trade or business encompasses the sale of goods or rights therein; the operation of any manufacturing, industrial or commercial enterprise; the leasing of property; and the rendering of services. The simple purchasing of goods or rights therein is excluded (Abu Dhabi ITD, Article 2(4)). Dubai ITD, Article 2(6)(e) specifically includes the production of petroleum or other hydrocarbons. The Fujairah Income Tax Decree of 1966 (Fujairah ITD), Article 1 provides that only entities engaged in oil production or extraction of other natural resources are taxable persons.

9 'Permanent establishment' is defined as a branch, place of management or other place of business. It does not include an agency relationship unless the agent is authorised, and habitually exercises this authority, to conclude contracts on behalf of the principal (Abu Dhabi ITD, Article 2(10)).

another juristic entity, unless exempted.[10] The Income Tax Decrees make no distinction between resident and non-resident corporations, but instead define a taxable person as, inter alia, having a permanent establishment within the respective emirate.

Banks

The principal difference in the treatment of local and foreign commercial banks is that local banks are not subject to any taxation on their income, whereas foreign banks may be subject to taxation at the emirate level. Additionally, a foreign bank may not establish more than eight branches in the UAE. The tax paid by banks varies from emirate to emirate and also within each emirate where certain banks are allowed to make annual payment of an agreed sum without reference to the level of profits or losses. In Abu Dhabi, banks are required to pay a tax of 20 per cent on net profits.

The government of Dubai issued Regulation No. 2 of 1996 (Regulation No. 2) setting out guidelines to be used by branches of foreign banks in calculating income tax due to the government of Dubai from taxable income arising from the conduct of business in the Emirate of Dubai.

Foreign banks operate in the Emirate of Dubai without local equity participation pursuant to special arrangements with the government. Generally, foreign banks are required to pay 20 per cent of their net profits to the government of Dubai as an income tax. Regulation No. 2 enumerates the permissible deductions that foreign banks may take in determining taxable income. For example, a foreign bank may not deduct more than 2.5 per cent of its total revenue in any year for head office charges and regional management expenses combined. Furthermore, centralised or shared expenses (including regional management expenses) of foreign branches of banks operating in Dubai may be deducted on a prorated basis. Head office expenses must be reflected in the Dubai branch's books and certified by the external auditors of the bank's head office.

The guidelines also set out acceptable methods for calculating 'doubtful debts', losses, amortisation of assets and capital expenditures. Losses may be carried forward and set off against taxable profits in the next tax year. Losses, however, may not be deducted from a previous year's tax obligation.

Branches must file an annual tax declaration together with audited financial statements. The financial year for foreign banks operating in Dubai must be 1 January to 31 December. Taxes are due and payable to the Dubai Department of Finance no later than 31 March of the following year. The penalty for late payment has been fixed at 1 per cent for each 30-day period that such payment is in arrears.

Oil companies

The revenue of oil-producing companies is subject to the payment of both a royalty and an income tax. Royalties are calculated as a percentage of total revenue derived from production, while the income tax is calculated on net profit after depreciation.

In the Emirate of Abu Dhabi, the Supreme Petroleum Council (SPC), created pursuant to Abu Dhabi Law No. 1 of 1988, was designated as the supreme authority responsible for petroleum affairs in Abu Dhabi in charge of formulating and implementing policy in the oil sector. However, Law No. 1 of 1988 did not delegate to the SPC any powers of the Ruler to,

10 Abu Dhabi ITD, Article 2(3).

inter alia, levy taxes on petrochemical activities in Abu Dhabi according to the Abu Dhabi ITD. Accordingly, any royalties levied by the SPC on concessions in the Emirate of Abu Dhabi are not taxes levied in accordance with the Abu Dhabi ITD, but duties levied pursuant to the SPC's role as a petroleum policy and regulatory body, and distinct from the power of the sovereign or ruler of Abu Dhabi to impose taxes.

A taxpayer's taxable income is defined as its net income arising in the respective emirate from the conduct of trade or business, after making permitted deductions.[11] Taxable income is to be computed by the method of commercial accounting regularly used by the taxpayer for its own records, provided that such method fairly reflects taxable income. Such a method may be on either a cash basis or an accrual basis.[12]

Costs and expenses incurred in the production of income are treated as deductions.[13] Such deductions include:

a the direct costs to the taxable person of producing goods sold or of providing services rendered by it;[14]

b other costs and expenses incurred by the taxable person for the purpose of carrying on trade or business;[15]

c a specified annual allowance in respect of depreciation, obsolescence, exhaustion or amortisation of physical and intangible assets;[16]

d uninsured losses sustained by the taxable person in connection with carrying on trade or business;[17] and

e any net operating loss of the taxable person incurred in carrying on trade or business that is carried forward from a previous tax year.[18]

Deductions allowed to a taxable person dealing in oil[19] as costs and expenses incurred for the purpose of carrying on trade or business are specifically defined[20] to include certain costs and expenses incurred for the exploration for and development of petroleum or other hydrocarbons,[21] and certain royalties paid on crude petroleum dealt in by such taxable

11 Abu Dhabi ITD, Articles 2(5) and 6.

12 id., Articles 5(1) and 5(2).

13 id., Article 6(1). In Dubai, banks are expressly permitted to treat as deductions head office overhead expenses charged to branches in Dubai (government of Dubai, Circular to All Banks Subject to Dubai Tax, 24 December 1984).

14 Abu Dhabi ITD, Article 6(1)(a).

15 id., Article 6(1)(b).

16 id., Article 6(1)(c).

17 id., Article 6(1)(d).

18 id., Article 6(1)(e). Dubai ITD does not provide for loss carry-forward, but does provide for deduction of losses on sales of certain depreciable property (Article 4(1)(d)), and of 10 per cent of certain expenses incurred prior to commencing trade or business in Dubai (Article 4(1)(e)).

19 'Dealing in oil' is defined by Abu Dhabi ITD, Article 2(15) as 'dealing [. . .] in oil or in rights to oil'.

20 But not in Dubai ITD.

21 id., Article 6(2)(a)(i).

person,[22] but not to include any sums included in the credit aggregate[23] or certain sums paid to the ruler of the respective emirate as the ruler's share in profits from oil under an agreement between the taxpayer and the ruler.[24]

The following amounts may not be deducted from the taxable income of a taxable person dealing in oil: expenses deemed to be contributions to capital by agreement with the ruler of the relevant emirate,[25] sums included in the credit aggregate,[26] and certain sums paid to the ruler of the respective emirate as the ruler's share in profits from oil under an agreement between the taxpayer and the ruler.[27] No non-deductible business expenses are specifically enumerated with respect to taxable persons not dealing in oil.[28]

An annual deduction in respect of the depreciation, obsolescence, exhaustion or amortisation of physical and intangible assets calculated as a reasonable percentage of the original cost of such assets, and any additions thereto, are allowed. For certain specified assets, a straight-line depreciation in percentages stipulated in the Abu Dhabi ITD is presumed reasonable, subject to proof to the contrary.[29]

The total of deductions for depreciation and losses in any tax year in respect of any asset may not, when added to the total of deductions previously allowed in respect of that asset, exceed the actual cost to the taxable person of such asset.[30]

The Income Tax Decrees do not specifically address accounting issues relating to stock and inventory as a discrete category of asset. Therefore, valuation of stock and inventory may be accomplished by the method of commercial accounting regularly used by the taxpayer in maintaining its own records, provided that it fairly reflects the taxpayer's taxable income.[31] The Income Tax Decrees do not specifically refer to the depreciation of stock and inventory.[32]

As the Income Tax Decrees do not specifically address the treatment of reserves, such treatment is to be governed by the method of commercial accounting regularly followed by the taxpayer in keeping its own records, provided that such method fairly reflects the taxpayer's taxable income.[33]

22 id., Article 6(2)(a)(ii). The royalty payable under all concession agreements is 14.5 per cent pursuant to Article 1 of Federal Decree No. 55 of 1974.

23 Abu Dhabi, ITD Article 6(2)(a)(iii). Article 2(18) provides as follows:
. . . credit aggregate' means in relation to oil of a producing company the aggregate value of all royalties (other than royalties on Crude Petroleum equal to one eighth of the value, or such greater amount as may from time to time be agreed between the Ruler and such producing company, at the applicable posted price in Abu Dhabi, of crude petroleum produced in Abu Dhabi and exported therefrom) and rentals, and of all taxes (other than the tax imposed by this Decree), duties, imposts and other exactions of a like nature and of any payments in lieu of any tax which accrue from or are paid by whomsoever to the Ruler or to any State, governmental or other public authority in Abu Dhabi (whether central or local) in respect of the relevant income tax year in connection with the production, transportation, sale, shipment or export of such oil.

24 Abu Dhabi ITD, Article 6(2)(a)(iv).

25 id., Article 6(2)(a)(i).

26 id., Article 6(2)(a)(iii). See footnote 25 for a definition of credit aggregate.

27 Abu Dhabi ITD, Article 6(2)(a)(iv).

28 The corresponding non-deductible business expenses apply to all taxpayers under Dubai ITD, Article 4(1)(b).

29 Abu Dhabi ITD, Article 6(1)(c)(i).

30 id., Article 6(c)(iii).

31 id., Articles 5(1) and 9.

32 id., Article 6(1)(c).

33 Abu Dhabi ITD, Articles 5(1) and 9.

The Income Tax Decrees do not provide that dividends paid affect the taxpayer's taxable income; nor do they require a dividend-paying taxpayer to withhold a portion of the dividend as a withholding of the recipient's income tax.

Dividends received and income from capital gains are treated no differently from other types of income.

Losses

Net operating losses not allowed to be deducted from a taxpayer's income in a tax year may be carried forward indefinitely.[34]

Rates

Taxable amount (dirhams)	Zero to 1 million	1,000,001 to 2 million	2,000,001 to 3 million	3,000,001 to 4 million	4,000,001 to 5 million	5,000,001 and over
Rate	–	10%	20%	30%	40%	50%

The rates[35] of tax payable on income of oil-producing taxpayers in the emirates are as follows:

a Ajman and Fujairah: 50 per cent;[36]

b Abu Dhabi and Dubai: 55 per cent;[37] and

c Sharjah: 65 per cent.[38]

Ras Al Khaimah has no separate provision governing petroleum-producing taxpayers.[39]

Administration

All foreign companies, public and private shareholding companies, LLCs and share partnership companies are required to have their annual financial statements audited by accountants registered in the UAE, and to submit such audited statements to the relevant authority. Branch offices of foreign companies are required to prepare their annual accounts on an independent basis for operations in the UAE, and to maintain the necessary books and documents of account within the UAE. Pursuant to the Companies Law, every LLC or joint-stock company is now required to keep its accounting books in its head office for a period of at least five years from the end of the financial year of the company.[40]

34 id., Article 6(2)(e). In Dubai, banks are not permitted to make general provisions for bad debts but are permitted to make specific provisions in respect of doubtful customer accounts (government of Dubai, Circular to All Banks Subject to Dubai Tax, 24 December 1984). A bank may carry forward losses no more than two years (id.).

35 Abu Dhabi ITD, Article 4(1); Ajman Income Tax Decree of 1968 (Ajman ITD), Article 4(1); Dubai ITD, Article 2(19)(a); Sharjah Income Tax Decree of 1968 (as amended) (Sharjah ITD), Article 4(1). Fujairah ITD omits this progressive tax on non-petroleum producing entities. Under the Dubai ITD, a taxpayer whose income reaches a particular tax bracket has the rate of that bracket imposed on his or her entire income. In contrast, the other income tax decrees impose the progressive tax rates only on that portion of the taxpayer's income that falls into the relevant brackets.

36 Ajman ITD, Article 4(2); Fujairah ITD, Article 1; Ras Al Khaimah Income Tax Decree of 1969 (as amended), Article 4(2).

37 Abu Dhabi ITD, Article 4(2); Dubai ITD, Article 2(19)(b).

38 Article 4(2), Sharjah ITD.

39 Ras Al Khaimah Income Tax Decree of 1969 (as amended), Article 4.

40 Companies Law, Article 26.

Within three months of the end of each tax year (1 January to 31 December), taxable persons are required to file a provisional income tax return. Taxable persons with taxable income below the threshold of 1 million dirhams are exempted unless specifically directed to file. The returns are filed with the respective director of tax appointed pursuant to the Income Tax Decrees.[41]

Income tax is to be paid in quarterly instalments based upon the provisional declaration. Within nine months of the end of the tax year, taxable persons are required to file a final income tax declaration. Discrepancies between the provisional and final declarations are to be reconciled by adjustment of the final quarterly tax instalment and, if necessary, a partial tax refund.[42]

Failure to file the declaration or to pay income tax without reasonable cause incurs liability for a fine of 1 per cent of the amount payable for each 30-day period or portion thereof during which the failure continues. Extensions of time for filing may be granted upon proof of a justifiable reason.[43]

The director of tax has power to inspect relevant books and records.[44] Penalties for falsification of records or making false statements include imprisonment or a fine, or both. A taxable person affected by such falsification, if legally responsible, is also liable to a fine.[45]

Disputes as to the application of the tax laws are subject to the jurisdiction of the UAE courts or, by agreement, to arbitration.[46]

ii Other relevant taxes

Establishment of a branch office or an LLC in the UAE will entail payment of various fees in the course of the licensing and registration process. Although these fees are not taxes as such, the amounts involved can be significant and should be taken into consideration as a potential cost of doing business in the UAE.

Customs duties are generally low. Under the GCC agreement to impose uniform rates for customs duties, the UAE imposes a uniform 5 per cent customs duty on the import of goods from outside the GCC.[47] Limited exemptions apply to military and security purchases and some foodstuffs.

Federal Decree Law No. 7 of 2017 introduced an excise tax in the UAE on certain products and became effective as of 1 October 2017. A reasonably high rate of tax on a limited number of goods is imposed by way of an excise tax. This includes a 50 per cent excise on carbonated drinks and a 100 per cent excise on energy drinks and tobacco products.

The Federal Tax Authority announced that the excise tax will be imposed upon electronic smoking devices and tools and sweetened beverages with effect from 1 January 2020, in accordance with the Cabinet and MOF decisions issued in this respect.[48]

41 Abu Dhabi ITD, Article 8(1).
42 id., Article 8(2).
43 id., Article 8(3).
44 id., Article 11.
45 id., Article 12.
46 id., Article 13.
47 In 2003, the GCC became a customs union (i.e., a free trade area with a common 5 per cent external customs tariff).
48 Cabinet Decision No. 52 of 2019 On the Excise Goods, Tax Percentages Imposed Thereon, the Way of Calculating the Excise Rates and Ministerial Decision No. 236 of 2019.

IV TAX RESIDENCE AND FISCAL DOMICILE

i Corporate residence

Tax residency is not clearly defined under UAE law in the absence of any enforced income tax legislation. The Income Tax Decrees make no distinction between resident and non-resident corporations, but instead define a taxable person as, inter alia, having a permanent establishment within the respective emirate. In addition, double taxation treaties provide a basis for determining tax residency under the applicable treaty. Eligible foreign companies can obtain tax residency certificates from the Federal Tax Authority.

ii Branch or permanent establishment

Entities incorporated outside of the UAE can have a fiscal presence through licensed branches in the UAE. Indeed, a branch of a foreign company is treated the same as a company incorporated in the UAE under the Income Tax Decrees, as both constitute permanent establishments in the UAE. However, with limited exceptions (discussed above), there are no UAE tax consequences as a result of such fiscal presence.

Tax residence may be relevant to tax considerations in the foreign company's home jurisdiction under the relevant double taxation treaty.

V TAX INCENTIVES, SPECIAL REGIMES AND RELIEF THAT MAY ENCOURAGE INWARD INVESTMENT

i Holding company regimes

While the Companies Law has introduced the concept of a holding company, whereby a holding company can be incorporated as either a joint-stock company or an LLC, and can establish subsidiaries inside the UAE or abroad, or has control of existing companies by holding shares or stocks enabling such holding company to control the management of the subsidiary and to have influence on the resolutions of the subsidiary,[49] the applicable laws and regulations in the UAE do not provide for any special holding company regimes.

ii IP regimes

Similarly, there are no special IP regimes in the UAE.

iii State aid

Tax law should be considered in the context of any major project, notwithstanding that the UAE is generally a tax-free jurisdiction. The tax treatment that will be extended to the project should be negotiated in detail and in advance. For major projects, tax holidays or the extension of national treatment may be available for a specified period of time.[50]

Some entities that would otherwise be taxable persons have been expressly exempted by the respective rulers,[51] by federal legislation or by their location in a free zone. For other

49 Companies Law, Article 266.

50 The reason for seeking a tax holiday is to guard against the possibility of income tax being implemented before completion of the project.

51 See, for example, the order exempting the Middle East Bank from income tax, Dubai Official Gazette No. 129 of 1979. Such exemptions are expressly contemplated by the Income Tax Decrees (Abu Dhabi ITD, Article 2(3) and Dubai ITD, Article 2(3)).

taxable persons, the Income Tax Decrees have in practice only been enforced against oil companies and certain foreign banks.[52] This selective application, however, is neither codified nor assured for the future.

As discussed above, free zones in the UAE generally provide inward investors guaranteed freedom from corporate and income taxes for a specified period.

iv General

As noted above, the UAE is essentially a tax-free jurisdiction, and the absence of corporate or personal income tax is one of the UAE's most attractive features for foreign investors.

VI WITHHOLDING AND TAXATION OF NON-LOCAL SOURCE INCOME STREAMS

i Withholding on outward-bound payments (domestic law)

There are currently no withholding taxes on dividends, interest and royalties paid out by a company or other business entity.

ii Domestic law exclusions or exemptions from withholding on outward-bound payments

There are currently no withholding taxes and, accordingly the issue of exemptions does not apply.

iii Double tax treaties

The UAE has an extensive and growing list of double taxation treaties with more than 90 countries.[53] Under these treaties, profits derived from shares, dividends, interest, royalties and fees are taxable only in the contracting state where the income is earned. Although corporate income tax is not levied in the UAE, the provisions of the treaties do not state that such income must be taxed to qualify for benefits. Thus, dividend income paid by a UAE company to a company that has a double taxation treaty with the UAE may not be taxable in the hands of the foreign parent corporation; however, it is wise to study the text of the treaties themselves before assuming anything about the tax treatment of untaxed income flows originating in the UAE.

52 As noted previously, courier companies are also taxed by the federal government.

53 This network includes treaties with Albania, Algeria, Antigua and Barbuda, Andorra, Angola, Argentina, Armenia, Austria, Azerbaijan, Barbados, Belarus, Belgium, Belize, Benin, Bermuda, Bosnia and Herzegovina, Botswana, Brazil, Brunei, Bulgaria, Burundi, Canada, Cameroon, Chile, China, Colombia, Comoros, Costa Rica, Croatia, Cyprus, the Czech Republic, Egypt, Equatorial Guinea, Ethiopia, Fiji, Finland, France, Gabon, Gambia, Georgia, Germany, Ghana, Guinea, Guinea-Bissau, Greece, Honduras, Hong Kong, Hungary, India, Indonesia, Iraq, Italy, Japan, Jersey, Jordan, Kazakhstan, Kenya, Kosovo, Kuwait, Kyrgyzstan, Latvia, Lebanon, Libya, Liechtenstein, Luxembourg, Macedonia, Maldives, Malaysia, Malta, Mauritius, Mexico, Moldova, Mongolia, Montenegro, Morocco, Mozambique, the Netherlands, New Zealand, Nigeria, Pakistan, Palestine, Panama, the Philippines, Poland, Romania, Russia, Rwanda, Saint Kitts and Nevis, Saudi Arabia, Senegal, Serbia, the Seychelles, Singapore, Slovakia, Slovenia, South Korea, South Sudan, Spain, Sri Lanka, Sudan, Suriname, Switzerland, Syria, Tajikistan, Thailand, Tunisia, Turkey, Turkmenistan, Ukraine, the United Kingdom, Uruguay, Uzbekistan, Vietnam, Venezuela, Yemen and Zimbabwe .

It is possible to make an application and pay a fee to obtain a tax residency certificate issued by the Federal Tax Authority to confirm a company's residence in the UAE, and to qualify for the benefits that may accrue to it in another tax jurisdiction with which a double tax treaty has been signed.

iv Taxation on receipt

As noted previously, the UAE is essentially a tax-free jurisdiction, and most businesses are not taxed at all. Companies falling into the small list of exceptions (foreign banks, foreign petroleum companies and courier companies) are not subject to taxation on receipt.

VII TAXATION OF FUNDING STRUCTURES

i Thin capitalisation

There are no thin capitalisation rules (restrictions on loans from foreign affiliates) applicable in the UAE.

ii Deduction of finance costs

For most types of business, the absence of corporate taxation in the UAE renders the issue of deductions meaningless. However, for foreign banks and oil companies, there may be relevant considerations relating to deduction of finance costs. These will vary depending on the emirate and the type of business. For example, for foreign oil companies in Abu Dhabi, finance costs may be deductible if they reflect costs incurred in the production of income and are computed by the method of accounting regularly used by the company, provided such a method fairly reflects taxable income.

iii Restrictions on payments

Any rules that may prevent the payment of dividends are not tax-driven and would depend on the provisions in a company's constitutional documents (such as its articles of association) or whether the shareholders have specifically agreed conditions that may prohibit paying dividends (e.g., unless the directors are satisfied the paying company can pay debts as they fall due).

iv Return of capital

There are no applicable tax rules or regulations relating to equity capital and, accordingly, no UAE tax consequences.

VIII ACQUISITION STRUCTURES, RESTRUCTURING AND EXIT CHARGES

i Acquisition

Foreign companies acquiring interests in a local business generally use foreign entities for the acquisition.

UAE tax considerations are not relevant to the structuring of the financing of the transaction. Share capital must be paid in cash at the time the shares are issued. Some investors contribute capital through a combination of equity and shareholder loans. The reasons for using shareholder loans rather than equity are generally to lower statutory reserve requirements and facilitate return of investments to shareholders without having to go through the process of applying to reduce the share capital of the company.

ii Reorganisation

There is no taxation levied when a business in the UAE merges with (or demerges from) an existing local business.

iii Exit

Should a business decide to exit from the UAE, this will not give rise to any taxes or penalties as such. It will, however, attract fees in the course of the deregistration process, and the amounts involved can be significant.

Where an inward investor has done business in the UAE through a local agent or distributor (and which has been registered pursuant to the Commercial Agencies Law), the statutory protections to the local party flowing from such registration include, inter alia, exclusivity, restrictions on the foreign party's right to terminate or withhold renewal of the relationship, and the right to receive compensation on termination or non-renewal of the relationship.

IX ANTI-AVOIDANCE AND OTHER RELEVANT LEGISLATION

i General anti-avoidance

There are no applicable general avoidance rules owing to the fact that the majority of businesses are exempt from taxation.

ii Controlled foreign corporations

There are no controlled foreign corporation rules in the UAE.

iii Transfer pricing

No transfer pricing rules apply in the UAE.

iv Tax clearances and rulings

It is possible to obtain advance tax rulings to secure a measure of certainty. Although the UAE is generally a tax-free jurisdiction, taxes are imposed on foreign oil companies.[54] The tax treatment that will be extended to, for example, a specific petroleum project must be negotiated in detail and in advance, and a legislative relief required to implement the desired tax relief must be validly obtained under local law. For major projects, tax holidays or the extension of national treatment may only be available for a specified period of time.

54 As discussed above, foreign banks and courier companies are also subject to taxation.

X YEAR IN REVIEW

In recent years, the International Monetary Fund and the World Bank have recommended the introduction of taxes in various oil-rich Gulf nations to reduce subsidies and consider adopting alternative sources of revenue, and potential changes in taxation policy. The UAE has acted on this advice. Examples include the establishment of the Federal Tax Authority and the implementation of VAT and the excise tax. Rumours about corporate income tax have thus far been premature.

The European Union maintains a blacklist of non-cooperative jurisdictions for tax purposes. The UAE was added to the blacklist in March of 2019. In response, the UAE Cabinet issued Cabinet Resolution 31 of 2019 Concerning Economic Substance Regulations (the Economic Substance Regulations), which came into effect on 30 April 2019 and on 11 September 2019, the MOF issued the Guidance on the Economic Substance Regulations (together, the 2019 Economic Substance Regulations and Guidance). In October 2019, the UAE was removed from this blacklist. The 2019 Economic Substance Regulations and Guidance have now been repealed and replaced by UAE Federal Cabinet Resolution No. 57 of 2020 and Ministerial Decision No. 100 of 2020, respectively.

The UAE issued Federal Decree No. 24 of 2019 for the ratification of the country-by-country reporting (CbCR) agreement. Thereafter, on 30 April 2019, Cabinet Resolution No. 32 of 2019 was issued introducing the requirements on CbCR in the UAE. Recently, the MOF issued Cabinet Resolution No. 44 of 2020 (Resolution 44 of 2020), concerning the organisation of reports submitted by multinational enterprises (MNEs), which repealed and replaced Cabinet Resolution No. 32 of 2019. CbCR is part of Action 13 of the base erosion and profit shifting initiative led by the Organisation for Economic Co-operation and Development and the G20 industrialised nations. Under Resolution 44 of 2020, the reporting entity definition has been amended to specify that the ultimate parent entity (UPE) of an MNE group, tax resident in the UAE, is the only entity of the MNE group required to comply with CbCR obligations. The purpose of CbCR is to eliminate any gap in information between the taxpayers and tax administrations with regard to information on where the economic value is generated within the MNE group, and whether it matches where profits are allocated and taxes are paid on a global level.

Each UPE of an MNE group, tax resident in the UAE, is required to notify the competent authority that it is the entity responsible for filing the country-by-country report. The former Resolution provided a wider scope of application for the notification, whereby all constituent entities of an MNE group, tax resident in the UAE, were required to comply with such notification. As such, only the UPE is henceforth required to file the notification. Identical to the former Resolution, the notification is to be submitted no later than the last day of the group's reporting fiscal year. Each reporting entity of an MNE group, tax resident in the UAE, is required to file the country-by-country report in the UAE within 12 months following the last day of the reporting fiscal year of the MNE group. All provisions in respect of the surrogate parent entity were removed under Resolution 44 of 2020.

In Cabinet Resolution No. 9 of 2016, the UAE government committed to sign the Multilateral Convention on Mutual Administrative Assistance in Tax Matters, signed on 21 February 2017, and the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information (MCAA), signed in Abu Dhabi on 22 February 2017. Pursuant to Federal Decree No. 48 of 2018 on the Ratification of the Multilateral Administrative Agreement for the Automatic Exchange of Information, the MCAA was ratified.

The MCAA contains the rules on the exchange of information between the UAE competent authority (CA) and partner jurisdiction CAs. The confidentiality, safeguards and the existence of the necessary infrastructure for an effective exchange are all covered by the MCAA. The MCAA provides for collaboration on compliance and enforcement, whereby a CA will notify the other CA when the first-mentioned CA has reason to believe that an error may have led to incorrect or incomplete information reporting or there is non-compliance by a reporting financial institution with the applicable reporting requirements and due diligence procedures consistent with the Common Reporting Standard (CRS). The notified CA will take all appropriate measures available under its domestic law to address the errors or non-compliance described in the notice. The UAE's Council of Ministers Resolution No. 17 of 2012 on the collection and exchange of information for the purposes of international tax agreements provides the legislative basis for the implementation of the CRS. The Collection and Exchange of Information in Implementation of the International Tax Conventions Purposes authorises the MOF to collect and exchange information and data on natural persons and legal entities licensed to operate in the UAE. The MOF released its Guidance Notes for the Common Reporting Standard in 2016. The Guidance Notes provide that, under the CRS, the UAE has opted for the 'widest approach': reporting financial institutions are required to perform due diligence procedures and report information on all accounts held by an account holder who is resident for tax purposes in a jurisdiction other than the United States or the UAE. The United States is excluded because jurisdictions will be reporting to the United States under the Foreign Account Tax Compliance Act.

The MOF's Guidance Notes for the Common Reporting Standard provides that the following authorities are appointed as the regulatory authorities for the purposes of implementing the provisions of the MCAA and the CRS:

a the Central Bank in respect of a financial institution subject to its supervision under applicable laws and regulations;

b the Securities and Commodities Authority in respect of a financial institution subject to its supervision under applicable laws and regulations of the Securities and Commodities Authority;

c the Financial Free Zone Authority designated by the relevant financial free zone as a regulatory authority in respect of a financial institution registered in such financial free zone:
- the ADGM: Financial Services Regulatory Authority; and
- the DIFC: Registrar of Companies (RoC); and

d the MOF, in respect of any financial institution not otherwise regulated by any of the aforementioned regulatory authorities.

XI OUTLOOK AND CONCLUSIONS

The UAE has long been a tax-free haven, but this is starting to change. Following the implementation of VAT and an excise tax in recent years, the introduction of the Economic Substance Regulations is another indication of the UAE's willingness to change its tax rules. Furthermore, lower oil prices and a desire to diversify the economy have changed the landscape. The introduction of VAT has resulted in a change to the way business is conducted and administratively maintained in the UAE. Although the rate of VAT imposition is set at a low 5 per cent initially, there have been rumours (if not expectations) that the rate will be increased. However, the UAE's Minister of State for Financial Affairs has ruled out increasing

VAT and excise tax over the next five years,[55] and an official from the MOF reiterated this position.[56] Moreover, it is possible that corporate tax may be introduced in the future, although the MOF says that the UAE has no plans to do so.[57]

55 'No VAT, excise tax increase over next five years in UAE', Khaleej Times, 11 February 2018.

56 'UAE has 'no income tax plans' says senior government official', The National, 7 November 2019.

57 ibid.

Appendix 1

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