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Public Consultation Document

UAE Corporate Tax

Foreword

This is Aurifer's reply to the Public Consultation initiated by the UAE Ministry of Finance in regard to the implementation of Corporate Income Tax in the UAE as of June 2023. Under no circumstances can the contents of this document be considered as tax advice. The input we have shared is meant to assist the Ministry in considering certain positions, as well as best practices abroad.

Aurifer would like to commend and congratulate the Ministry on a succesfull communication campaign so far, and we wish the Ministry an equally succesful implementation.

For our comments below, we have followed the outline of the Public Consultation document.

The contents of this document was submitted via the regular public consultation process on 20 May 2022.

Input Aurifer on Section 3 – Taxable Person

3.1. Natural persons

In 3.4., it is clarified that natural persons can indeed fall inside the scope of corporate income tax, when the activity they conduct requires the individual to obtain a commercial license or equivalent permit from the relevant competent authority (DED or Free Zone registration) in the UAE.

We assume that this objective registration criterion is guided by administrative simplification, and therefore, for clarification purposes, it would be helpful to state explicitly that the UAE MoF and FTA will not consider situations where in addition to the regular license, a natural person must obtain approvals from other regulatory bodies.

For example, for attorneys, architects and real estate agents, their respective registration with their governing bodies does not constitute the criterion for them to be subject to corporate income tax.

Where a person is required to be licensed to conduct an activity, and has made his license available to a business, the person and the business will therefore not be taxed twice. For example, when a real estate agent has passed the exam to become a real estate agent, and incorporates a business to that effect, the business will be taxed in scope of the corporate income tax. The income which the real estate agent derives from that business would then therefore be considered personal income as salaries and bonuses.

In 3.3., reference is made to a situation where individuals are partners in an unincorporated partnership that conducts business in the UAE. It is observed that the consultation document does not explicitly state that, despite not having an individual license, natural persons which are part of an unincorporated partnership will be taxed under Corporate Income Tax, neither does it state that the unincorporated partnership is itself subject to CIT or other obligations (registration, reporting, …). It may be helpful to receive such clarity.

Additionally, there is no reference made to whether an incorporated partnership is automatically subject to Corporate Income Tax.

In 3.5 reference is made to a number of situations where income earned by an individual is outside of the scope of corporate income tax. Reference is made there to dividends, investment income and rental receipts.

It is observed that the text does not explicitly refer to passive income (dividends, interest, royalty), and neither to capital gains (for real estate or otherwise). Presumably, if no license is required to exercise an activity of buying and selling properties, even if this is done at a relatively high volume for high value, that income would still not be taxable under the UAE CIT.

It may be advisable to consider another criterion for so-called professional speculation, as opposed to regular speculation, although we acknowledge this a hard position to maintain, and such a substance over form approach has its disadvantages.

In regard to interest and royalties, we assume that the same principles would apply. Where the individual does not require a license to conduct the activity, these are not taxed under the corporate income tax.

Further, the text refers to trusts, but we assume that the same principles would apply if the income is earned by a foundation, an SPV or an otherwise structure set up only to receive passive income, which would otherwise be earned by a natural person.

3.2 Legal persons

In section 3.7 we note a reference to the managed and controlled criterion for legal persons incorporated in a foreign jurisdiction. We assume that this criterion is used as opposed to the incorporation criterion. It may therefore be advisable to explicitly exclude such reference to the incorporate criterion, and to the fact that the UAE will not consider it.

As to the transparency of limited and general partnerships, and other unincorporated joint ventures and associations, we note and observe that when those partnerships are made up of natural persons, given the design of the UAE rules, to the extent that those natural persons do not require a license for their activity, the income will not be taxed in their hands1.

In Section 3.8 reference is made to the flow through treatment for collective investment funds, and in Section 3.22 and following again. We assume there is no distinction to be made between the funds referred to in Section 3.8 and 3.22.

In Section 3.9, it is stated that foreign unincorporated partnerships' CT treatment will be aligned with the tax treatment in the foreign jurisdiction. It would be helpful to understand whether the Ministry would consider the legislation applicable in DIFC and ADGM as foreign legislation or UAE legislation, given the fact that these free zones are apply partially or wholly English law.

In addition, it is unclear whether the incorporation or the transparency is the many criterion. There are situations, such as in the UK, where a partnership is incorporated, but nonetheless transparent from a tax point of view[2].

Following the same philosophy and intent of the proposed regime, we may consider to also apply a transparency regime to a branch of a foreign incorporated partnership, which is incorporated but transparent.

We would conclude from this that if a British or American LLP is treated as transparent in their home jurisdiction, there will be no taxation in the hands of the UAE branch of such a foreign LLP. Depending on the specific situation of the partners, there may be taxation at that level, e.g. when those partners are tax resident abroad and are subject to personal income tax.

In regard to foreign unincorporated partnerships which are considered non transparent in the foreign jurisdiction and therefore taxed, we understand that the UAE will therefore also tax those partnerships.

3.3 Exempt persons

In regard to Section 3.11, a number of the situations listed also cover lists which exist for VAT purposes, whether for example for designated government bodies[3], or listed charities[4]. It may be advisable to align the business criterion for both VAT and Corporate Income Tax, for administrative simplification purposes.

We note also the absence of the Emirati banking decrees in the list, and would assume therefore that these will co-exist with the Federal Corporate Income Tax, as was indicated in the FAQs. The mechanism for such coexistence is yet to be defined.

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[1] Inspiration on the tax treatment of partnerships can be found in the OECD Partnership report, OECD, *The Application of the OECD Model Tax Convention to Partner- ships*, Issues in International Taxation No. 6 (Paris: OECD, 1999), as incorp- orated into the April 2000 update of the OECD Model Tax Convention and Commentary.

[2] Various authors, "Characterization of Other States' Partnerships for Income Tax", *Bulletin – Tax Treaty Monitor, July 2002, IBFD.*

[3] Article 10, 2 of the UAE VAT law juncto article 57 of the UAE VAT Law.

[4] Article 57 of the UAE VAT Law.

3.4. Government and Government owned entities

In regard to Section 3.13 it is stated that "The UAE CT regime will allow UAE subsidiaries of these Government-owned companies that undertake part or whole of the sovereign or mandated activity or ancillary activities to apply for an exemption from UAE CT." We have observed that the same mechanism is not always straightforward to apply for VAT purposes, and that the process can be burdensome. This may put some strain on the attractiveness of such an exemption.

3.5 Natural resources

From the drafting of the commentary, we would assume that midstream and downstream activities are excluded from the exemption. It is however unclear how businesses would be treated which would have upstream exempt income, and e.g. downstream taxed income.

It may also be considered to find a mechanism which allows UAE Emirate businesses active in the natural resources sector to more easily access treaty relief under Double Tax Treaties negotiated by the UAE.

3.6 Charities and Public Benefit Organisations

In section 3.20, it is stated that "Whether an organisation qualifies for a CT exemption is at the discretion of the Ministry of Finance. However, no exemption from UAE CT will be available to organisations that undertake commercial activities that are not directly related to their stated purpose, or whose income and donations are or may be used for the personal gain of persons associated with the organisation (e.g., the founders and fiduciaries)."

The UAE will not impose any taxation on non profit organisations, such as many other countries do. Charities and Public Benefit Organisations will be closely looking at the interpretation of the commercial activities that are allowed for Charities and Public Benefit Organisations. One may consider situations such as sponsorships, a gift shop, a bake sale, etc. which would generate revenues.

Generally speaking, the limitation for charities and public benefit organisations does not mean such organisations cannot engage in commercial activitiy or are not allowed to intend to achieve a budget surplus, as long as this balance is not distributed as dividends (or similar) or payments to the founders.

According to an OECD report[5], in a number of countries philanthropic entities must reinvest their surplus towards activities aimed at fulfilling their worthy purpose. If philanthropic entities engage in too much commercial activity or do not reinvest the surplus into a worthy purpose, countries may choose to tax the commercial activity, as well as the remaining surplus, or strip the entities of their preferential tax status altogether.

We would generally expect that the UAE would not tax non-commercial income, such as income from philanthropic gifts and government grants, or grants from supporting funds. Income from philanthropic gifts includes donations from individuals and corporations and testamentary transfers from individuals.

Commercial income is income derived from the supply of goods or services in return for some form of payment. When a corporation makes a payment as sponsorship (i.e. in return for publicity) to a philanthropic entity, it may, in some countries, be considered commercial income. That is to say that to the extent that the publicity resulting from sponsoring a philanthropic entity is a service, such income could be considered commercial.

Most countries would exempt all income, or only exempt non-commercial income[6]. For example, Belgium would exempt income, except for real estate income, and income from capital and movable goods.

[5] OECD (2020), Taxation and Philanthropy, OECD Tax Policy Studies, No. 27, OECD Publishing, Paris, https://doi.org/10.1787/df434a77-en.

[6] OECD (2020), Taxation and Philanthropy, OECD Tax Policy Studies, No. 27, OECD Publishing, Paris, https://doi.org/10.1787/df434a77-en, table 3.4. Those countries are Australia; Austria; Belgium; Bulgaria; Canada; Chile; Finland; Germany; Greece; Ireland; Israel; Italy; Latvia; Malta; Mexico; the Netherlands; New Zealand; Norway; Portugal; Romania; Singapore; the Slovak Republic; Slovenia; South Africa; Sweden; Switzerland; the United Kingdom, and the United States.

The MoF can consider thresholds, e.g. the income via ancillary commercial activities cannot exceed 20% of overall income, or 35,000 EUR annually[7]. Austria, Germany and the United States do so for commercial income. France, Hungary, Mexico, the Netherlands, Norway, the Slovak Republic, and South Africa do so for income of charitable entities overall.

3.7 Investment funds

We note in Section 3.24 that the transparency or "pass through" for investment funds organised as limited partnerships where partners have unlimited liability is automatic. However, for other regulated investment funds and Real Estate Investment Trusts, the application of an exemption is subject to approval by the FTA.

An automatic qualification of a fund that meets the criteria, and which is any case regulated by the DFSA, FSRA or SCA would however be a recommended consideration, and one with less administrative work for the FTA. Further, it is stated that such entities would be exempt, which may suggest that this is a different situation than transparency. It is unclear whether that suggestion is intended.

Pass through or transparent entities have important advantages in terms of market neutrality (when compared to other traditional forms of investment)[8]. It is currently unclear whether the investment fund will have reporting obligations vis-à-vis the FTA, and if so, what those would look like.

There is currently also no reference as to an important matter for investment funds, which is capital gains. Investment funds might divest, and as a result realise a gain. A fully transparent regime, would impose capital gains potentially on the investor in the fund, where that participation does not qualify for an exemption under the participation exemption. There are a number of complexities associated with the application, such as but not limited to the capacity of the investor (professional or not? Exempt government body or not?), the residence of the investor and the potential for treaty access for the fund[9].

In regards to non-transparent funds, which are therefore subject to tax, the Ministry may consider from a policy point of view, nonetheless for non exempt income, give credits to the investors of the UAE CT paid.

A couple of important benchmarks and points of comparison are[10]:

Country	Taxation of investment funds
UK	Investment funds subject to corporate income tax, where capital gains are exempt from taxation. Investment funds may be structured as partnerships.

[7] Which is the threshold set by Germany below which an entity's commercial income is not subject to corporate income tax.
[8] Tax Law Design and Drafting (volume 2; International Monetary Fund: 1998; Victor Thuronyi, ed.) Chapter 22, Taxation of Investment Funds, https://www.imf.org/external/pubs/nft/1998/tlaw/eng/ch22.pdf consulted on 7 May 2022. See also Committee on Fiscal Affairs, "The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles", https://www.oecd.org/tax/treaties/41974553.pdf, consulted on 8 May 2022.
[9] It may be recommended to include a provision in DTT's expressly conforming access of investment funds to the network.
[10] https://research.ibfd.org/#/doc?url=/data/tns/docs/html/tns_2008-06-23_cit_1.html
https://research.ibfd.org/#/doc?url=/collections/bit/html/bit_2019_05_e2_3.html
https://books.google.co.uk/books?hl=en&lr=&id=t0gWUkE3v00C&oi=fnd&pg=PR5&dq=uk+taxation+investment+fund&ots=YNxNYAjpVl&sig=akDZUawj-KGlwn6L3be2UoscTx8&redir_esc=y#v=onepage&q=uk%20taxation%20investment%20fund&f=false
https://uk.practicallaw.thomsonreuters.com/w-021-0312?transitionType=Default&contextData=(sc.Default)&firstPage=true

Germany	1. Mutual investment funds: Subject to 15% CIT at fund level for certain income. Fund distributions also taxed at investor level. 2. Special investment funds: 15% CIT for certain German income at fund level (but transparency option if investor taxation documented) 3. Funds with legal form of partnership: Complete transparency Changes made in 2018. Pre-2018 investment funds all generally treated as transparent (but fund still taxed on deemed distribution income). Complexity of taxation of deemed distribution income drove the reform.
France (SICAV vs FCP) (SICAVs): Investment companies with variable capital (FCP): Unincorporated open-ended funds	FCP (considered as 'groups of persons'): considered as non-taxable entity. Capital gains tax exemption provided no individual investor holds >10% of the FCP. SICAV –within the scope of CIT (i.e. need to register and report), however they benefit from a full tax exemption. Taxation is also imposed at investor level.
Luxembourg	Both SICAV and FCPs are exempt from all taxes. All distributions by Luxembourg funds (domestic or foreign) non-taxable.

Finally, given the important regional investments of UAE investment funds, it may be advisable to propose within the GCC a passporting mechanism for tax purposes, with mutual recognition of the transparency of investment funds. This could however exacerbate the issue of conduit arrangements using the UAE if the vehicle is fully transparent.

3.8 Free Zones

In Section 3.8 the applicable tax regime to free zone businesses is described. The principle under the Corporate Income Tax Law which will be implemented with effect from June 2023, is that the UAE will honour the tax incentives currently being offered to Free Zone persons that maintain adequate substance and comply with all regulatory requirements.

Presumably the reference to substance is a reference to the Economic Substance Regulations introduced in 2019 by way of Cabinet Decision No. 57 of 2020. It would be helpful if it is clarified whether for example a free

zone business with a mainland branch can count its mainland substance towards the substance required for ESR purposes.

In addition, it is assumed that when a Free Zone business loses its tax exemption, the substance requirements are no longer applicable. In any case, the UAE may consider other substance criteria which are more aligned with international treaty requirements.

An irrevocable election can be made to be subject to CIT, however we would advise flexibility in that election, given that group structures and organisations may change, and therefore also the drivers in regard to electing to apply the exemption or not.

The CT exemption only continues to apply if the business solely transacts with other Free zone businesses (in the same free zone or another) or with third countries.

What constitutes transacting with the mainland is interesting to note, as:

- Free zone businesses in a Designated Zone for VAT purposes are not considered transacting with the mainland, if the buyer is the importer of record.
- Conversely, assumed, though not made explicit, services rendered to the mainland are considered, and therefore such FZ businesses involved in these services will loose their tax exemption.

We noted that it is not allowed to provide services to mainland businesses, despite a longstanding tolerated situation where free zone businesses provided their services to mainland businesses.

As regarding goods, there are a number of situations to be considered:

- Free Zone businesses do not control the status of the Free Zone as a Designated Zone. Such a status needs to be applied for by the Free Zone Authority, and is subject to approval. Moreover, Free Zones can loose or gain Designated Zone status with retroactive effect. This has an adverse impact on legal certainty in regard to the application of the tax exemption.
- There is a stark contrast with traders in a free zone (e.g. commodity traders), who may buy in mainland to sell in mainland, or to bring those goods into a free zone. Those seem to be excluded from the tax exemption, whereas they are conducting the same trade, just in the opposite direction.
- Retail sales in the Designated Zone look to be at an advantage. For VAT purposes, they are subject to VAT, but when conducted by a Free Zone business with mainland and free zone branches, the mainland branches' income is subject to CT, and the free zone branches in a designated zone are not.

Certain transactions are further allowed to be conducted with the mainland, such as situations where a free zone business earns passive income, i.e. interest, royalties, dividends and capital gains from mainland companies. This is good news for holding companies in free zones. Trading and transactions seem to be used interchangeably in the Public Consultation Document, however these may cause confusion for services supplied by Free Zone businesses.

Transactions from a Free zone to a group company in mainland are also allowed without losing the benefit of the 0% CT. However, payments made to a Free zone business will not constitute a deductible expense for CT purposes.

In regard to Free Zone businesses with a branch in mainland UAE, the Ministry may consider further guidance on how to allocate income and profits to such branch, but also what documentation or supporting evidence would be required.

So far, we have not identified an anti-abuse rule preventing a free zone company to make the charge to a business abroad, for that business to subsequently charge the mainland business, this nonetheless creating a deductible expense.

Group Treasury Centres often established in Free Zones may considered the non-deductibility on a group level a disadvantage. This may bring groups to reconsider their structure, and put their regional headquarter in a different country with a low level of taxation (e.g. Bahrain), and where payments would nonetheless be deductible. Additionally, the non-deductibility looks limited to UAE Free Zones. A business who relocates their Group Treasury Centre for example to a KSA Free zone, or a HQ, may continue to benefit from tax exempt income on the one hand, and deductibility on the other hand.

From a policy perspective, the UAE may consider an anti-abuse rule considering this situation, which may for example consist of defining a Free Zone in a broad enough manner in order for it to encompass foreign free zones as well, as no or only nominal tax jurisdictions in which activities may be relocated.

Input Aurifer on Section 4 – Basis of taxation

4.1 Residents

In terms of the effectivement management and control criterion, there is a great deal of potential uncertainty around the topic. The UAE may consider safe harbour rules, with a check the box list, or at least guidance regarding focus on Board, Management or otherwise.

In Section 4.6 it is clarified that when income earned abroad is not exempt, income taxes paid in the foreign jurisdiction can be taken as a credit against the CT payable in the UAE on the relevant income to prevent double taxation.

We note here the reference to the "relevant income" to mean that credits can only be compensated for the taxation of a specific type of income, e.g. if royalties are subject to a withholding tax abroad, they'll be able to be credited specifically against the taxation of the royalty income in the UAE.

We would expect as well that where a withholding applies on dividends, and the receiver benefits from the participation exemption, the taxpayer cannot credit the withholding tax on dividends, because the specific income is not taxed in the UAE.

What will be helpful for tax payers to know, is whether they can still avail such a credit, when the UAE tax payer does not decide to avail the benefits of the double tax treaty. In such a case for example, the UK does not allow a tax payer to take the credit[11]. Further also, when a tax is withheld in violation of the double tax treaty, it would be advisable to take a position as to whether the credit would be available or not.

4.2. Non-residents

In the public consultation document, there is a reference to a 6 month's period for a building site to constitute a fixed PE, whereas the OECD standard is 12 months, and the document explicitly refers to the OECD as its source. It may be considered to clarify why this deviation was maintained.

Although it may seem petty as well, the Ministry may consider making the calculation of the duration as precise as possible, taking into account calendar days etc.

We noted in Section 4.14 in regard to a fixed place of business that an employee's home office can constitute a Permanent Establishment.

In regards to the use of home offices, the OECD's commentary states: "Even though part of the business of an enterprise may be carried on at a location such as an individual's home office, that should not lead to the automatic conclusion that that location is at the disposal of that enterprise simply because that location is used by an individual (e.g. an employee) who works for the enterprise."[12] We assume that there will still be a

[11] HMRC's Foreign Notes states "If a DTA does not give the other country the right to tax the income, you cannot claim FTCR and must claim relief in the other country.", https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1062228/sa106-notes-2022.pdf, consulted on 15 May 2022.

[12] Paragraph 18 of Commentary to Article 5 of the OECD's 2017 Model Tax Convention.

factual judgment to be made, and that the UAE will take into account the OECD's guidance on remote working[13].

The OECD stated in that note that "The exceptional and temporary change of the location where employees exercise their employment because of the COVID-19 crisis, such as working from home, should not create new PEs for the employer." Considering that a home office could constitute a PE would significantly hamper the UAE's competitiveness, and further also not be aligned with the remote working visa which the UAE promotes.

The question is further raised whether a Free Zone business which is applying the CT exemption, will have a taxable PE in mainland if some of its employees have a home in mainland.

In Section 4.14 the extraction of natural resources is considered a PE, but we assume that at the same time that income will be exempt, if falling inside one of the above referred to exemption situations.

In Section 4.15, there is a reference made to a situation where in a fixed place there are only preparatory and auxiliary activities. Examples given are then limited marketing and promotional activities. We assume that representative offices of foreign businesses would qualify for this exception to a PE. However, those representative offices do have a license from the DED or free zone. We assume therefore, that despite the fact that these entities are incorporated, given that their license does not allow commercial activities, they will not constitute a PE and not fall inside the scope of CT. The Ministry may consider clarifying this situation in the legislation or guidance.

In Section 4.20 it is stated that Free Zone businesses can have a PE in mainland. However, it is not stated in which way the profit attribution will take place in regard to the PE. We assumed that this could potentially be linked with the sourcing rules, or that the PE will follow a Separate Entity Approach.

Finally, the Ministry may consider clarifying in its guidance that it will not adopt the concept of a (virtual) services PE, in the same way as Saudi Arabia.

In Section 4.23, wide ranging sourcing rules are stated, which would trigger a payment of withholding taxes at 0%. However, although likely implicit, it stops short of stating that businesses which do not meet the PE threshold will not be subject to 9% CIT. For example, income derived from an asset (e.g. a commercial building), is income sourced from the UAE, but given that it would not amount to a PE, it would not be subject to CIT.

[13] OECD Policy Responses to Coronavirus (COVID-19), OECD Secretariat analysis of tax treaties and the impact of the COVID-19 crisis, paragraph 5. https://www.oecd.org/coronavirus/policy-responses/oecd-secretariat-analysis-of-tax-treaties-and-the-impact-of-the-covid-19-crisis-947dcb01/, consulted on 10 May 2022.

Input Aurifer on Section 5 – Calculation of taxable income

In Section 5.4, reference is made to the Gregorian year as the default year. Will the Ministry accept shorter accounting years as well, for example for businesses which are just starting off?

In section 5.5., reference is made to accounting standards. In absence of UAE GAAP, a reference is made to IFRS.

In regard to startups and small businesses, it is potentially considered to use alternative financial reporting standards. It may be taken into account that for such businesses cash flow is always important, and therefore a business could be proposed to use cash accounting. However, to the extent that there is a solid bad debt regime, and given that the UAE will not require prepayments from businesses for corporate tax, there is much less of a need of such a regime. We would therefore rather advocate to not have an exemption to the standard regime.

If the UAE would nonetheless implement separate standards for certain tax payers, we would advocate that these are unified for all tax payers.

In Section 5.12 it is mentioned that income from investment in other companies would be exempt. Is this an implicit reference to passive income, or is it rather an introduction to the participation exemption or the foreign branch profit exemption, the next sections in the document.

In Section 5.16 reference is made to holding 5% shares. There is no reference made to the number of votes, or the situation where a person might own less than their beneficial ownership. Will those situations be considered as well and qualify for the participation exemption, or will regard solely be held to the shares themselves? It is usual in other jurisdictions to also consider voting rights and economic ownership.

In Section 5.22, it is stated that the exemption for foreign branch profits is unavailable if the foreign branch is not subject to a sufficient level of tax in the foreign jurisdiction. Will the criterion here be the same as the UAE default rate of 9%? This is currently not stated, whereas in section 5.16, that same criterion is made explicit.

In regard to section 5.38 there is discussion around an indefinite carry forward of losses whereas the FAQ had stated at least 5 years.

In Section 5.25 we note the capping deductible interest at 30% of EBITDA for most businesses. What will be the position taken by the UAE towards special transactions such as profit participating loans and convertible loans?

The 30% of EBITDA rule can be problematic for commodity traders, operating at low margins, and with a high financing cost. Given that EBITDA is a measure based on margin, rather than revenue, 30% of the EBITDA can potentially only be a very small amount. Therefore, the added tax cost of financing would make this type of trade finance less attractive, and may even lead to situations where a business is required to pay tax, even though it's turning a loss. The same consideration, i.e. low margins and high financing needs, which has lead to an exclusion of the financial sector from this limitation, can also be taken into account to exclude commodity traders from the interest deduction limitation.

While the OECD in BEPS Action 4 prescribes to ignore for the purposes of the calculation of the 30% of EBITDA the amounts under derivative instruments or hedging arrangements which are not related to borrowings, for example commodity derivatives14, this is insufficient for commodity trading.

As an alternative, a consideration can be given to a by-industry approach to the interest safe harbour amount, or a group wide approach. Suggestion is to include an industry threshold as percentage on overall active income (or revenue), under which all of the interest expense is to be deductible for CIT purpose. This threshold is to be an additional threshold to 30% of EBITDA. The total threshold applicable for deductible interest calculation in this case would be the higher of the two, industry-specific and general threshold.

The UAE may also consider the unlimited carry forward of losses, and grandfathering rules for existing loans at the time of implementation of corporate income tax.

As an additional thought, the EU is currently considering addressing the debt bias by introducing a notional interest deduction for equity15, a concept pioneered by Belgium. It favours businesses using own resources in financing projects, and is seen as a stable factor.

We noted in terms of the deductibility of expenses a business test and a limitation of entertainment expenses in a broad sense to 50%, amongst others. The Ministry may consider as well taking a position for the following types of expenses:

- UAE Corporate tax itself,
- Royalties, management fees, or other fees that are not at arm's length price,
- Congresses, excursions, and similar
- Vehicles available for personal use

Further, the question may be raised how to consider the deductibility of municipality taxes, Emirate taxes, and payments made to related parties and connected persons.

In Section 5.39 there is reference made to the business continuity criteria not being applicable to businesses listed on a recognized stock exchange. Will the UAE also consider UAE businesses that are listed on a foreign stock exchange? If so, what would be the criteria to consider the foreign exchange?

Finally, on the accounting front, the question may arise whether the UAE will be implementing different depreciation and amortization rates for tax purposes and for accounting purposes.

We note the absence of any specific IP or R&D regime, which could enhance the UAE's stance internationally endorsing the knowledge economy activities.

[14] Paragraph 39 of OECD (2017), Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4 - 2016 Update: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. http://dx.doi.org/10.1787/9789264268333-en.

[15] Commission Proposal for a Council Directive on laying down rules on a debt-equity bias reduction allowance and on limiting the deductibility of interest for corporate income tax purposes, COM(2022) 216, https://ec.europa.eu/taxation_customs/system/files/2022-05/COM_2022_216_1_EN_ACT_part1_v6.pdf, consulted on 19 May 2022.

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Input Aurifer on Section 6 – Groups

6.1. Tax Groups

According to Section 6.1 of the Corporate Tax (CT) Public Consultation Document, a tax group can be formed by a UAE resident group of companies if the parent company holds at least 95% of the share capital and voting rights of its subsidiaries. A subsidiary can also be part of the tax group if it is owned indirectly by the parent company and other subsidiaries own at least 95% of its shares, or if it is a UAE branch of the parent company or one of its subsidiaries.

In the first place, we welcome the flexibility offered by the rules set out in the consultation document regarding the formation of tax groups and appreciate the opportunity offered to group companies to be treated as a 'single taxable person' for Corporate Tax purposes (or "fiscal unity").

However, we note that, in practice, in some cases, two or more UAE resident companies are owned by a non-resident parent company, which holds at least, directly or indirectly, 95% of their share capital and voting rights.

In this situation, we suggest that the facility of the formation of the tax group should be extended to the UAE registered companies, even though > 95% of their share capital or voting rights is held, directly or indirectly, by a non-resident parent company.

In such a scenario, the representative of the group, who will be responsible for administration and payment of Corporate Tax, could be one of the UAE resident companies (instead of the non-resident parent company) as elected by the Tax Group and subject to conditions similar those required for a classical tax group (except for the location of the non-resident parent company).

The non-resident parent company should be subject to a tax on profits equivalent (or more) to the UAE corporate tax in its jurisdiction.

All the group companies (including the non-resident parent company) should have the same 12-month fiscal year, except where not allowed under foreign legislation.

Accordingly, if these conditions are met, one of the companies established in the UAE and at least 95% owned by the non-resident parent company, could be the representative/head of the tax group formed with its "sister' and "cousin" companies established in the UAE.

However, only UAE resident companies would be treated as members of the UAE horizontal tax group, i.e. only their taxable results would be consolidated for UAE corporate tax purposes. Further, the joint liability for members of a tax group, foreseen in Section 6.9, can be limited to the UAE resident companies (who will be members of the tax group), and should not be extended to the non-resident parent company.

We believe, such a tax consolidation scheme, by allowing companies established within the UAE to benefit from a tax group, regardless of the place of establishment of their parent-company, would enable the UAE to reinforce its position as an international business hub and global financial center, remain a competitive and productive economy and continue to attract foreign investment.

The UAE would not be alone in granting such an advantage, as e.g. the Netherlands extends grouping to the situation where the parent is established in another EU Member State[16].

In Section 6.8, as mentioned before, we noted that the parent company is responsible for the administration and payment in regard to the corporate income tax due by the group (although we are advocating allowing the situation of a foreign parent with delegating the responsibilities to a UAE entity).

For VAT purposes, when grouping companies, a responsible person has to be appointed. This is not necessarily the parent company. For simplification purposes, and especially when there are no excluded exempt or free zone entities, it may be advisable to align the concepts of the representatives for the VAT and CIT group.

In terms of the capital requirements to constitute a tax group, these are put at 95% common ownership. For VAT purposes, this is only 50%, and side agreements have to be analysed for their economic benefits. It may therefore be considered as well for CIT purposes, that potential side agreements are analysed, or structures which give the beneficial ownership largely to one party (while complying with the requirement to have >95% economic interest).

In terms of the joint liability for members of a tax group, foreseen in Section 6.9, for CIT purposes this can be ring fenced, subject to FTA approval, to certain members. However, for VAT purposes, this is not explicitly allowed. While the joint liability exists for both taxes, from a contractual point of view, nothing prevents members of a tax group or VAT group to reassign internally potential liabilities of the group. The Ministry may therefore consider removing this provision.

6.3 Group relief

In regards to Section 6.16, we noted transfers of losses are possible between group companies. We assume however that such losses are not possible internationally? Such a transfer is not possible in New Zealand for a similar regime[17]. When the UK was a part of the European Union, under certain conditions, losses from group companies in other EU countries were transferable. Given the UAE's membership of the GCC, it may consider extending a similar benefit to other GCC group companies.

[16] https://www.belastingdienst.nl/wps/wcm/connect/bldcontentnl/belastingdienst/zakelijk/winst/vennootschapsbelasting/fiscale_eenheid_vennootschapsbelasting/fiscale_eenheid_vennootschapsbelasting, consulted on 17 May 2022.

[17] See https://www.ird.govt.nz/income-tax/income-tax-for-businesses-and-organisations/income-tax-for-companies/losses-for-companies/transferring-losses-to-another-company, consulted on 15 May 2022.

Input Aurifer on Section 7 – Transfer pricing

7.1. Related Parties

In Section 7.4 it is indicated what the definition will be of a Related Party. It may be advisable to explicitly state that such definition is independent from the accounting definition of a related party according to IFRS. It may further also be considered to state what means of proof are required to be provided, and whether by default entities will be considered related, or unrelated.

Further, there are multiple potential definitions of control, and therefore the Ministry may duly consider those different definitions, to select one simple criterion.

7.2. Connected Persons

In Section 7.7, the Ministry may consider a relaxation for persons who have an interest in an entity, but which is not controlling. In such a case, the risk which these provisions are aiming to mitigate, i.e. base erosion through high pay out of salaries, may not materialize.

In Section 7.6, for connected person, there is a reference made to what constitutes a market value for payments or benefits. Although theoretically a great concept to apply, such is the arm's length principle that it is not always easy to apply. The Ministry may therefore consider independent benchmarks to this extent, or to determine safe harbours. Overall, apart from of the considerations with respect to exemptions and free zones, the Ministry may consider not imposing any domestic transfer pricing rules, or to exempt domestic transfers from transfer pricing documentation. Many EU countries have done so. Especially for small businesses, this would be helpful.

Still on the topic of connected persons, it may not be easy to trace kinship to the fourth degree, and this may simply not be known to businesses.

In Section 7.11, a reference is made to a controlled transaction disclosure form, a type of reporting as well in use in Saudi Arabia and Qatar. Experience has taught however, that the use of such a form is limited in case of an audit. In any case, at best, such a form would be a conversation starter. Following the philosophy of reducing the administrative burden on businesses, the Ministry may consider removing this requirement.

Input Aurifer on Section 8 – Calculation of CT liability

In Section 8.5 reference is made to relief for small businesses. As it stands though, the compliance obligations foreseen in the Public Consultation Document suggest very limited compliance requirements.

To the extent that these compliance requirements stay at the same level, the UAE may, for simplicity reasons, consider not to have a deviating regime for small businesses. Every such regime has difficulties with scoping, e.g. when a turnover threshold is foreseen, the concentration of businesses right below the threshold is usually higher than average.

In Section 8.6 of the Public Consultation Document, a 0% WHT is foreseen. This may cause an issue in future tax treaties where the preamble mentions that the tax treaty should not lead to double non-taxation. This would especially be the case with OECD countries.

In Section 8.7, no reference is made to payments from Free Zone Persons to non-residents, including dividend, interest, capital gains, other gains (including derivatives trading).

In regard to section 8.11 on foreign tax credits, we refer to our comments higher on Section 4.1.

Input Aurifer on Section 9 – International tax developments

According to Section 9.2 of the CT Public Consultation Document, we understand that the UAE is, at present, working with other members of the Inclusive Framework to implement the Pillar Two proposals. We commend the UAE for implementing BEPS 2.0, because it goes a certain way in mitigating adverse circumstances of base erosion and profit shifting planning structures.

There are many policy options made available to the UAE under BEPS 2.0. We discuss them below.

Pillar One

Under Pillar One, 25% of residual profits of an in-scope multinational business with a global annual turnover in excess of EUR 20 billion and profitability over 10% would be allocated to market jurisdictions.

For example, even if Pillar One would grant taxing rights to the UAE, the UAE could choose not to exercise these taxing rights. However, this would be at odds with the desire to tackle potential profit shifting by large businesses falling inside the scope of Pillar One. In addition, the relatively modest potential revenue from Pillar One is nonetheless an easy addition to the UAE's federal budget.

The UAE could therefore consider adopting the Pillar One rules, based on the model legislation prescribed by the OECD in regard to profit allocation the market jurisdiction, and the taxable base, and the future multilateral treaty to be signed. Subsequently, it could limit itself to applying the same standard corporate income tax rate at 9% as it does for domestic businesses.

Presumably, given this concerns nonresident businesses, the free zone exemptions would not apply, even if there are clients established in a free zone.

Further, the UAE may consider stressing that businesses in scope of Pillar One would not be considered as having a Permanent Establishment in the UAE as a result of their obligations under Pillar One.

We assume further that the UAE will therefore not adopt article 12B proposed by the UN to tackle the same issue[18], nor take any unilateral measures to addressed the same problem.

Pillar Two

In terms of Pillar Two, the mechanism is designed as such that where the jurisdictional ETR falls below the 15% minimum threshold, with the adjusted calculations, the country of the Ultimate Parent Entity will have the right to apply a top up tax.

It is expected that most jurisdictions where businesses would fall foul of the minimum 15% Effective Tax Rate, would introduce a Qualified Domestic Minimum Topup Tax (QDMTT). The policy driver behind this is that the revenue will be taxed regardless of whether the jurisdiction would apply the QDMTT or not. Indeed, no special tax system would have to be imposed on multinational companies within the scope of Pillar Two, if a QDMTT is incorporated into the domestic law of the UAE.

[18] As John W. Mpoha advocates, the implementation of article 12B of the Revised UN Model is plagued by a number of issues, see J. W. Mpoha, Article 12B of the UN Model (2021): A simplified solution for developing countries to tax income from the digital economy?, Bulletin for International Taxation, 2022 (Volume 76).

In terms of the timing, the Ministry may consider aligning itself with the EU and the US. It would add great complexity, and make perhaps the UAE unnecessarily a frontrunner, if the UAE implemented Pillar Two before the largest economies it deals with. In the last proposal under the French presidency of the Council, it is only proposed to implement Pillar Two by 31 December 2023[19] (the UTPR even later).

Although simple in concept, Pillar Two is complex in its execution and burdensome in its reporting. The UAE may choose to satisfy itself with the QDMTT, while relying on the reporting made by a foreign UPE in the tax jurisdiction of residence of the foreign UPE. This will constitute an important simplification for the FTA, but also for the tax payer. The foreign tax jurisdiction has an incentive in ensuring the information return filed by the UPE is correct, as any jurisdictional ETR's below the threshold may allow the foreign jurisdiction to collect additional taxes.

The information return should therefore be of good quality, and the UAE can consider not requesting additional information from groups falling inside the scope of Pillar Two.

In order to constitute a QDMTT, the minimum tax must compute profits and calculate any top-up tax due in the same way as the Pillar Two rules themselves. In that respect, the QDMTT must be implemented and administered in a way that is consistent with the OECD model rules.

Moreover, with regard to the calculation of the effective tax rate, the top-up tax rate, and, if applicable, the top-up tax, we suggest that the OECD model rules be adopted by the UAE identically in order to ensure harmony and simplicity in the application of the rules at the international level. The UAE may even consider for businesses in scope of Pillar Two to solely consider the Pillar Two rules for the calculation of the taxable base, rather than those businesses having to operate two sets of rules.

It may be advisable as well to clarify if, in the view of the Ministry, there is any interaction with the Free Zone exemptions or not.

Several academics have raised the issue of the compatibility of Pillar Two with the bilateral Double Tax Treaties[20]. It would be helpful for businesses to learn what the UAE's position in this regard is.

Further, outside of the implementation of BEPS 2.0, the UAE may consider reconsidering some of its Treaty positions. For example, now that the UAE will become a taxing country, it may add limitations to benefiting from treaty relief if the income in the source state benefits from a special tax regime[21]. In addition, the UAE may consider reviewing its MLI positions. Where today, the UAE has largely opted out of optional provisions, those provisions have become more important now that the UAE will become a taxing country.

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[19] Draft Council Directive on ensuring a global minimum level of taxation for multinational groups in the Union, French presidency compromise text, 28 March 2022, consideration #21, https://data.consilium.europa.eu/doc/document/ST-7495-2022-INIT/en/pdf, consulted on 15 May 2022.

[20] Chand, Vikram and Turina, Alessandro and Romanovska, Kinga, Tax Treaty Obstacles in Implementing the Pillar Two Global Minimum Tax Rules and a Possible Solution for Eliminating the various challenges (November 19, 2021). Available at SSRN: https://ssrn.com/abstract=3967198 or http://dx.doi.org/10.2139/ssrn.3967198.

[21] See Paragraph 85 OECD Commentary to Article 1 2017 Model, "Provisions could be included in a tax treaty in order to deny the application of specific treaty provisions with respect to income benefiting from regimes that satisfy the criteria of a general definition of "special tax regimes". For instance, the benefits of the provisions of Articles 11 and 12 could be denied with respect to interest and royalties that would be derived from a connected person if such interest and royalties benefited, in the State of residence of their beneficial owner, from such a special tax regime".

Input Aurifer on Section 10 – Administration

In regards to Section 10.1, the Ministry may consider clarifying whether the Federal Tax Procedures Law will apply.

In 10.3 a reference is made to a business ceasing its activity. Such moment is not always easy to define, and therefore the Ministry may consider objective criteria to determine whether a business has ceased its activity, in order to avoid disputes on the matter.

The reference in 10.8 on CIT returns only being due after 9 months leaves ample time to finalise Financial Statements and prepare the return, and is therefore very welcome. The Ministry may also consider the possibility for tax payers to amend their CIT returns post submission. This is possible e.g. in the UK up to one year after the submission.

The reference in 10.14 to clarifications, or rulings how they are more commonly referred to elsewhere, being binding on the FTA is very welcome, in the same vein as clarifications for VAT, for which the FTA considers itself administratively bound.

The Ministry and the FTA may also consider granting Advance Pricing Agreements for Transfer Pricing purposes. Other jurisdictions in the region do not necessarily grant those, and therefore, if the UAE does, it gives it a substantial competitive edge over its regional competitors.

Equally so, given the position of the UAE as an international and relatively open economy, it may be considered to sufficiently consider dispute resolution mechanisms, especially internationally, in order to ensure investor confidence.

In 10.15, for simplicity purposes, the Ministry may consider prescribing rules closely aligned with the VAT rules for record keeping purposes, to simplify matters administratively for tax payers.

In 10.16, reference is made to the auditing of Financial Statements. In some countries, auditors need to sign off on a tax return. Experience has taught that having a tax return also signed off by an auditor does not improve the quality of the corporate tax return, and creates confusion as to the role of an auditor. Auditors are not tax experts. There are multiple potential conflicts of interest, and a lack of governance and problems of independence render the task of an auditor complicated. We would therefore advocate not to implement a rule requiring an auditor to sign off on the tax return.

Additionally, where financials are required to be audited, but they are not, the UAE may consider how it will implement a sanction mechanism for unaudited financials.

In Section 10.17, there is reference made to grandfathering rules. It may be advisable to consider including a reference to unrealized gains, and leave these untaxed under grandfathering rules.

Input Aurifer on Other

We have noted that so far, there have been no anti abuse rules yet communicated in a general sense (there seem to be some specific some). In other words, there is currently no suggestion of a GAAR. If the UAE were to implement such a GAAR, we would suggest that this is carefully balanced against economic operations, and that any planning structure can be the subject of a ruling with the FTA.

We would recommend for sensitive operations, that the clarifications process is opened to situations where structuring could be debatable, in order to ensure certainty for tax payers.

We note that there are not proposed provisions around exchange of information, although article 4, 12 of the FTA Establishment Law foresees in this, or mutual assistance for tax collection. Although these types of provisions can be found back in article 26 and 27 of the OECD Model Tax Treaties, it is important from a legislative point of view that there is domestic legislation confirming these powers. There are also no provisions around joint audits conducted by the FTA and other foreign tax authorities, which may be very helpful in cases of cross border fraud.