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Autumn 2023

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FINER POINTS ON FREEZONES

UAE Freezones and Corporate Income Tax

LEXIS MIDDLE EAST
GULF TAX

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THE FINER DETAILS

Corporate Income Tax may have come into force on 1 June 2023 but as we had expected supporting legislation providing greater detail on this subject has continued to be issued over the summer. This list has included Ministerial Decision No. 139/2023 Concerning Qualifying Activities and Excluded Activities for the Purposes of Federal Decree-Law No. 47/2022 on the Taxation of Corporations and Businesses and Cabinet Decision No. 55/2023 On Determining Qualifying Income for the Qualifying Free Zone Person for the Purposes of Federal Decree-Law No. 47/2022 on the Taxation of Corporations and Businesses - two Decisions which have been key to understanding how exemptions will work for those operating in the UAE freezones. In the past one of the key benefits of establishing a business in the UAE freezones, a benefit which has been widely promoted, has been the tax incentives and tax holidays which have applied to legal entities registered in these zones. However, ever since UAE authorities announced their plans to introduce corporate income tax it has been clear although a special regime and 0% rate will apply there in some circumstances there will also be freezone companies that end up paying the standard 9% tax rate. Freezone businesses and their advisers have lots of questions on exactly how this will work in practice. Some of these have been answered in these two new Decisions, and by further information on this area which was given at the special awareness sessions run by the authorities during the summer. We decided as a result to focus in this issue on exactly what is known at present on this complicated issue. However, there are still a number of unanswered questions including exactly which of the UAE freezones will be classed as Designated Freezones for these purposes. The MOF also issued a consultation on this subject which ended in August asking for feedback and examples of potential issues which could be faced as a result of the requirements in these Decisions and on areas taxpayers would like more guidance, so there could yet be more changes on the way in this important area.

Claire Melvin - Editor

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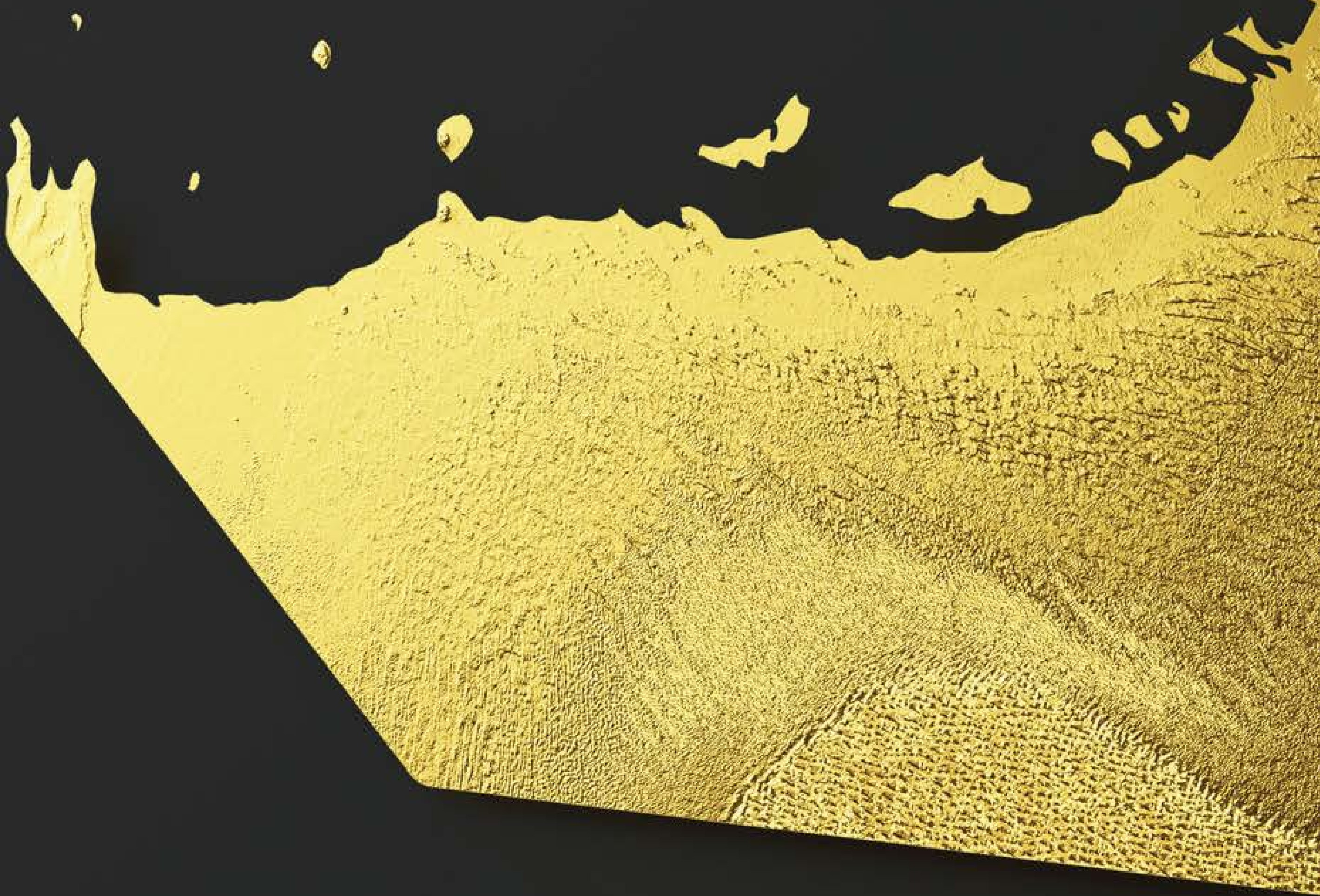
FINER POINTS ON FREEZONES

Mourad Chatar of Value Square explains how Cabinet and Ministerial Decisions issued since the UAE Corporate Income Tax Law was issued have led to some surprises on how liabilities of those in the free zones will be determined.



Since the UAE issued Federal Decree-Law No. 47/2022 On the Taxation of Corporations and Businesses in October 2022, over 20 Cabinet and Ministerial Decisions have been issued by the Ministry of Finance (MoF) in order to provide more detail on how the tax regime will work in practice. These have included Decisions intended to clarify how the income tax regime will operate in practice for persons in the UAE freezones.

These Decisions have included Cabinet Decision No. 55/2023 On Determining Qualifying Income for the Qualifying Free Zone Person for the Purposes of Federal Decree-Law No. 47/2022 which was issued on 30 May 2023 which provides a definition of qualifying income for qualifying free zone persons and Ministerial Decision No. 139/2023 On Qualifying Activities and Excluded Activities for the Purposes of Federal Decree-Law No. 47/2022 which defines qualifying activities and excluded activities for qualifying free zone persons. These Decisions provide additional detail on what are and are not qualifying income and activities for the purpose of determining if a free zone entity will be required to pay corporate income tax.

QUALIFYING FREEZONE PERSONS

A form of corporate tax relief operates in the Freezones which allows a free zone person classed as a qualifying free zone person to benefit from a 0% corporate income tax rate on its qualifying income while paying the standard 9% corporate tax rate on certain income from specific sources. Article 18 of Federal Decree-Law No. 47/2022 provided a definition of who would be classed as a qualifying free zone person. This is a free zone person who maintains adequate substance in the UAE, derives qualifying income, has not elected to opt out of the free zone corporate tax regime, complies with transfer pricing rules and documentation requirements, and also meets any other conditions which might be prescribed by the Minister.

Cabinet Decision No. 55/2023 then determines what income is considered as qualifying income and taxable at 0% and what income earned by a qualifying free zone person will be taxable at 9%.

QUALIFYING INCOME AND ACTIVITIES

Cabinet Decision No. 55/2023 introduced the concept of qualifying and excluded activities in the free zone context for the first time. Previously in the 2022 Consultation on UAE Corporate Income Tax the terms onshore versus offshore had been used. Typical offshore sourced income would be when a free zone entity is engaged in trading of goods, i.e. buying and selling goods from and to foreign third parties with or without physically moving through a UAE free zone such as the Jebel Ali Free Zone. However, these terms are no longer being used in the legislation and that has come as a surprise to many in the business community.

Instead, there is Qualifying Income which includes Income from transactions with another free zone person (who can be a person in any UAE free zone, so parties to the transaction do not need to be in the same free zone), except for income from excluded activities. It can also include income from transactions with any person, including a domestic or foreign person in the case of qualifying activities, except for income from excluded activities, or any other income subject to meeting the de-minimis requirement (which is also explained in Cabinet Decision No. 55/2023).

Therefore, whether an activity is classed as qualifying or not is key to understanding if income is to be treated as qualifying income for the purpose of the 0% corporate income tax rate. Ministerial Decision No. 139/2023 contains a list of qualifying activities. These are manufacturing or processing goods or materials; holding shares and other securities; ship ownership, management and operation; reinsurance services, wealth and investment management or fund management services subject to regulatory oversight of the competent UAE authority; headquarter or treasury and financing services to related parties; financing and leasing of aircrafts, including engines and rotable components; logistical services or activities that are ancillary to activities noted above. Article 2(1)(k) of Ministerial Decision No. 139/2023 also states that the distribution of goods in or from a Designated Zone to a customer that resells such goods or materials, or parts of them or processes or alters such goods or materials or parts of them for the purposes of sale or resale is treated as a qualifying activity but it is key to note that this only applies in Designated and not all free zones.

EXCLUDED ACTIVITIES

The Ministerial Decision also specifically lists a number of activities which are classed as excluded activities. These are banking activities subject to the regulatory oversight of the competent UAE authority; transactions with natural persons unless they involve ship ownership, management, and operation; qualifying fund management, wealth and investment services; or qualifying aircraft financing and leasing activities.

Insurance activities subject to the regulatory oversight of the UAE competent authority (unless classed as qualifying reinsurance activities) are also excluded as are finance and leasing activities subject to the regulatory oversight of the UAE competent authority, unless they are treasury and financing services to related parties or involve the financing and leasing of aircraft.

In addition, ownership or exploitation of immovable property, other than commercial property located within a free zone where the transaction involving that property is conducted with another free zone person; ownership or exploitation of intellectual property assets which give rise to separately identifiable income such as royalties or licence fees and activities that are ancillary to excluded activities, are also treated as

Mourad Chatar
Managing Partner
Value Square

excluded activities.

Activities are treated as ancillary activities it they serve no independent function but are necessary for the performance of the main qualifying or excluded activity.

DE MINIMIS REQUIREMENT

Cabinet Decision No. 55/2023 also introduced the concept of the de minimis requirement which aims to prevent a free zone person from losing their qualifying status because a small or incidental amount of income comes from an excluded activity or other non-qualifying income.

The de-minimis requirement is met when the qualifying free zone person's relevant non-qualifying revenue does not exceed either the lower of 5 million AED or 5% of total revenue. If the de-minimis requirement is met, the income in question is treated as qualifying income and benefits from the 0% Corporate Income Tax rate.

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RELEVANT LEGISLATION

Article 4(1) of Cabinet Decision No. 55/202

The de minimis requirements shall be considered satisfied where the non-qualifying Revenue derived by the Qualifying Free Zone Person in a Tax Period does not exceed a percentage of the total Revenue of the Qualifying Free Zone Person in that Tax Period as specified by the Minister, or an amount specified by the Minister, whichever is lower.

(Source: Lexis Middle East Law)

FURTHER CLARIFICATIONS

In June 2023, the MoF held a series of awareness sessions on the free zone corporate income tax regime to help explain and discuss Cabinet and Ministerial Decisions implementing the corporate tax regime in UAE free zone areas.

While most of the clarifications given at those sessions were a reiteration of points in the existing legislation there were areas where further clarification was given.

For example, the adequate substance test was illustrated and further defined through an example. In Article 18 of Federal Decree-Law No. 47/2022 one of the conditions for being a qualifying free zone person is maintaining adequate substance in the UAE. At one of the awareness sessions, it was explained that adequate substance would be employees performing work in a free zone, operating expenditures incurred solely in a free zone and having assets located in a free zone. However, it was said if a person in a free zone had their employees working in the mainland, had their operating expenditure in the mainland and their assets in the mainland, the adequate substance test would not be met.

It was also a clarification on the de minimis rule that even if the requirement is met, the portion of revenues that are not qualifying income would not be subject to the free zone corporate income tax regime. Many businesses had thought that once the de minimis requirement was met all the income would be subject to free zone corporate tax regime.

There has also been a clarification that designated free zones mentioned in the definition of Included Activities will be those listed for VAT purposes which basically refers to gated free zones. This would mean from a strict reading and interpretation of this guidance, a trading activity generating offshore income and performed by a free zone entity that is not in a Designated free zone would not qualify as an eligible activity for the free zone corporate income tax regime. Therefore, a confirmed list of these Designated free zones is eagerly awaited.

WHAT IS NEXT?

However, it unlikely that these two Decisions will be the last word on the free zone corporate income tax regime. With questions on which freezones will constitute a Designated Freezone still unanswered, a defined list is eagerly awaited.

The definition of a qualifying free zone person found in Article 18 of Federal Decree-Law No. 47/2022 also allows the Minister to prescribe additional eligibility requirements, which have not yet been issued. In addition, following on from the free zone awareness sessions which were held in June, the MOF issued a consultation which ended on 9 August 2023 (following an extension) on how this regime should operate. The consultation document summarised the provisions found in Cabinet Decision No. 55/2023 and Ministerial Decision No. 139/2023 but did not provide any details of proposed changes. Those responding to the consultation were asked to provide examples, data or other information on their views on how this area should be approached as well as their opinions about the areas they would prioritise for further Ministry of Finance and the Federal Tax Authority guidance on this subject, which appears to indicate there is more to come on this subject.

E-INVOICING: WHAT NEXT?

With the introduction of new tax regulations, regulators across the GCC have also been rolling out new technology to increase compliance. Ekansh Agrawal and Shashank Chandak of KPMG look at how tax regulators across the GCC are tackling this via mandatory e-invoicing.

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Manager in the tax team,
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Shashank Chandak
Associate Director in the tax team.
KPMG Bahrain

Across the GCC we have recently seen the introduction of new direct and indirect taxes, and other tax related filing or disclosure requirements. The next obvious step for the regulators is to ensure higher levels of compliance and a growing number of them have been looking into how technology can help with this which has led to the growing popularity of electronic invoicing or e-invoicing, a system which is already being used by tax regulators across the world, as an effective tool for digitalisation, and a means of automating indirect tax compliance, improving enforcement and increasing tax collections.

Although the reasons for implementing an e-invoicing system can vary from tax authority to tax authority it is safe to say that reducing the tax collection gap and preventing shadow economy transactions are the main reasons. However, rolling out e-invoicing can also be a part of a larger government initiative to enhance sustainability by reducing paper use or a broader digital transformation agenda.

TYPICAL SYSTEMS

A typical e-invoicing regime involves the generation of invoices in a standard electronic format, which are digitally signed. These electronically signed invoices are then transmitted over to the tax authority's platform which validates the e-invoice. Validation by the tax authority's platform can either happen real-time before the final e-invoice is issued (which is known as the clearance model) or in periodic batches (which is known as the post-audit model).

APPROACH IN SAUDI

Saudi Arabia was the first GCC country to implement e-invoicing which it did within just three years of introducing VAT. E-invoicing in Saudi has been introduced in a phased manner. In Phase 1

(which went live for all businesses without exceptions in December 2022) businesses in Saudi had to generate and store their invoices electronically. Phase 2 then saw taxpayers' systems being integrated with the tax authority's system. Unlike phase 1, phase 2 which kicked off in January 2023 has been rolled out in multiple waves in order to allow SMEs time to gradually adapt to the new system. During the generation phase, businesses have had to update their existing invoice templates to capture additional information such as time stamps, QR codes, address/date which is required by the system in a particular format, while ensuring that all invoices are generated electronically and among other things, are tamper proof. The integration phase on the other hand involves a holistic review of a business's ERP systems so that they are integrated with the tax authority's portal in real time or on a batch basis.

Where a business makes B2C supplies,

THE PHASES

Phase	Wave	Taxpayers in scope	Effective date
Generation phase	N/A	All taxpayers	4 December 2021
Integration phase	First wave	Taxpayers with taxable revenue exceeding SAR 3 billion	1 January 2023
Integration phase	Second wave	Taxpayers with taxable revenue exceeding SAR 500 million	1 July 2023
Integration phase	Third wave	Taxpayers with taxable revenue exceeding SAR 250 million	1 October 2023
Integration phase	Fourth wave	Taxpayers with taxable revenue exceeding SAR 150 million	1 November 2023
Integration phase	Fifth wave	Taxpayers with taxable revenue exceeding SAR 100 million	1 December 2023
Integration phase	Sixth wave	Taxpayers with taxable revenue exceeding SAR 70 million	1 January 2024
Integration phase	Seventh wave	Taxpayers with taxable revenue exceeding SAR 50 million	1 February 2024
Integration phase	Eighth wave	Taxpayers with taxable revenue exceeding SAR 40 million	1 March 2024

RELATED NEWS

MOF Projects Announced
The UAE Ministry of Finance has announced a number of projects it intends to work on. These include strategies for local supply, climate data transparency, CT reforms, public-private partnerships, and the introduction of an advanced e-billing system. The MoF plans include developing an innovative e-billing system which would be implemented nationwide. The current aim is to complete the project by July 2025.
(Source: Lexis Middle East Law)

it is mandatory for them to be able to report all invoices generated throughout the day to the tax authority's portal using an authorised API. The tax authority then performs a validation check on the invoice data and confirms the status of the check to the taxpayer.

Taxpayers will be brought into the integration phase gradually. Taxpayers will be notified in advance to ensure they are ready. Although, it has been some time since the initial adoption of e-invoicing in Saudi Arabia, we are still noticing cases of non-compliant invoice formats and situations where XML and PDF formats do not have the necessary QR code. It is critical to note that any failure to comply with the e-invoicing requirements can lead to hefty fines and penalties being levied.

OTHER GCC COUNTRIES

At present, Bahrain appears to be next GCC country which is getting closer to implementing an e-invoicing regime. The Bahraini tax authority released an RFP last year seeking proposals for the implementation of an e-invoicing regime. Although there are no confirmed details of when this will be rolled out at this stage, it is anticipated that as was the case in Saudi implementation will be rolled out in a phased manner and the framework is likely to resemble the Saudi approach.

In UAE VAT has been in place as long as it has in Saudi but when it comes to e-invoicing steps have not yet been taken. However, the Ministry of Finance did recently announce five major strategic initiatives to increase the country's competitiveness which specifically included an e-invoicing system. As a result, more details on a future e-invoicing system are likely to be issued soon. In Oman there is currently no news on a potential introduction of an e-invoicing system. While, in Qatar and Kuwait, which do not have a VAT regime yet, there is less chance of e-invoicing being rolled out.

KEY CHALLENGES

Although every business will most likely face its own set of unique challenges when implementing an e-invoicing system, there are some common ones. A critical one, which will come at the very beginning is selecting the right e-invoicing solution and implementation partner which suits the organisation's unique requirements and workflows. A wrong choice can lead to unforeseen costs. Here a common bottleneck is a lack of adequate knowledge of the e-invoicing system. Often the IT and finance departments are very well trained on using the new system, but actual end users who need to generate e-invoices can in some cases not be so well trained. This can lead to large numbers of errors which can include the sort of errors which will lead to monetary penalties under the local regulations.

A successful implementation will also normally require crucial changes to be made to existing accounting or ERP systems. This can include accurate validation and authentication of various mandatory data input fields, and ensuring data points are being captured in the exact formats which have been specified by the tax authority. This can require significant investment in terms of money and time.

Another challenge businesses can face is the generation of the QR code, as this will potentially be an additional requirement, with its own set of challenges.

In most jurisdictions, the tax authorities have prescribed different e-invoicing rules and requirements for B2B and B2C transactions.

As a result, the process of segregating B2B and B2C invoices has to be automated, to some extent in order to avoid manual effort.

WHAT'S NEXT

When looking at how to tackle e-invoicing, should it be adopted in a jurisdiction your business operates in, it is best to look at the lessons learnt by those in jurisdictions where it is already required.

Businesses need first to carefully monitor the tax authority's announcements on e-invoicing, in particular if a phased approach is to be used, when it will apply to them.

They should then define their own digital strategy, assess their readiness, and have identified any additional technical requirements, they will need to have in place. They will also need to have standardised their data entry processes and have ensured they have implemented adequate controls to ensure compliance.

For most organisations implementing e-invoicing is a large-scale digital transformation, so before starting, the leaders of the business must work towards establishing the right organisational culture where stakeholders embrace change, understand their role and the importance of the transformation.

Continuous communication and alignment at all levels is also key to achieving the required cultural change. It will also mean developing people and investing in upskilling the workforce, while maintaining institutional knowledge.

This can be made easier by emphasising the importance of training at all levels and leading by example, even if that means taking away people from their daily tasks for a brief time. Businesses may also have to look outside the organisation and recruit talent with the necessary skills.

Finally, the success of any organisation in its e-invoicing transformation will largely depend on how well it is able to leverage new technological tools, while moving away from outdated processes without a significant disruption to their day-to-day operations.

WHAT'S CHANGED
CLARIFICATION PROCEDURE

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KEY TAKEAWAYS
Clarifications can be a useful tool in achieving UAE tax compliance. They can provide businesses with certainty on their tax positions, and comfort in the event of a future tax audit. The FTA appears to borrow the interpretation of tax laws from the most common tax jurisdictions when providing Clarification decisions. If a Clarification is requested before a tax audit, it may save the taxpayer penalties and higher taxes.

CHANGE

In June 2023 the UAE Federal Tax Authority (FTA) published an updated guide on Private Tax Clarification procedures, Private Clarifications Tax Procedures, TPGPC1. In the updated guide it is added from June 2023, taxpayers must pay a 1,500 AED fee per application, or 2,250 AED if the application involves more than one tax. The guide has also been updated to assist taxpayers in submitting Clarification applications through the Emaratax portal.

RELEVANCY

If taxpayers are unsure about the tax treatment of their transactions in UAE, they can ask the FTA for a Clarification. Clarifications are legally binding decisions by the FTA on a technical tax issue and are comparable to tax rulings used in other countries. They can be submitted on technical tax matters such as VAT and Excise Tax but there is currently no way to submit a Clarification on Corporate Income Tax, although the FTA has indicated it will be possible later. Customs Duties matters in the UAE involving the import of goods are not covered by this process but businesses can request advance rulings from the customs authorities in the respective Emirate on customs matters. The FTA normally responds to a Clarification Request within 45 business days. Anyone can submit a private Clarification to the FTA on tax matters involving their business in the UAE. It is not necessary for them to be UAE tax registered. Tax agents or legal representatives can also submit a private Clarification to the FTA on behalf of those they represent. FTA Clarification decisions are beneficial to both taxpayers and tax professionals. The decision only applies to the requesting taxpayer and to the specific transaction or transactions it has been requested for. However, it will provide an insight into the FTA's perspective on a tax technical issue which may not be publicly available. The information may also be useful to other taxpayers where there is a similar fact pattern. From our own experience of VAT Clarifications for our clients the FTA has tended to explain tax concepts in the UAE in a way that is most consistent with international best practice and appears to be influenced by VAT case law issued by the European Court of Justice.

REMEMBER

- A taxpayer cannot in principle dispute or appeal a Clarification Decision. However, if the taxpayer feels the facts of their case have not been properly interpreted by the FTA they can submit a new Clarification request.
- UAE tax returns are self-assessments so taxpayers must apply the correct tax treatment and pay the correct amount of tax to the FTA. Only summary numbers are reported (with no underlying calculations) in tax returns but the FTA may review the underlying calculations in a tax return during a tax audit. The Clarification process allows taxpayers to get confirmation on technical tax matters and prevent errors in their tax returns prior to a tax audit. Therefore, they are very useful tools, as taxpayers who are able to resolve mistakes proactively before they are found by the FTA in a tax audit may avoid higher penalties and possible disputes with the FTA.
- If a Clarification confirms a taxpayer has reported a transaction in the correct way in their tax return, they will be safe from tax assessments or penalties for that transaction. If the facts have been presented correctly when the Clarification request was sent, the FTA will be administratively bound to follow that Clarification decision.
- If a Clarification decision differs from the taxpayer's original interpretation of the transaction, it may impact the taxpayer's tax return. In such cases, the taxpayer should consider whether a correction of their historical tax returns is necessary, and what would be the best correction method. Taxpayers who fail to comply with an FTA Clarification decision, could find themselves facing various administrative penalties if there is a later tax audit.

TAX NEWS ROUND-UP

COVERING RECENT KEY DEVELOPMENTS – REGION-WIDE

UAE

TAX PROCEDURES

New legislation, Cabinet Decision No. 74/2023 On the Executive Procedure of Federal Law No. 28/2022 on Tax Procedures has been issued. This Cabinet Decision repeals and replaces the previous Executive Regulations on Tax Procedures (Cabinet Decision No. 36/2017) and includes updated definitions, processes and procedures. With the exception of Article 12(2) of Cabinet Decision No. 74/2023 (which covers requirements to be registered as a tax agent which take effect on 1 December 2023) its provisions came into force from 1 August 2023. The changes cover areas including the accounting records and commercial books that must be maintained as well as the period and manner of record keeping. There are also provisions on the registration, responsibilities and deregistration of tax agents, who must be able to communicate with their clients in either English or Arabic or both, verbally and in writing.

PENALTIES

Cabinet Decision No. 75/2023 has been issued on Administrative Penalties for Violations Related to the Application of the Corporate Income Tax Law Federal Decree-Law No. 47/2022 and came into effect on 1 August 2023. Violations which are subject to Administrative Penalties include failure to register for corporate income tax purposes, failure to file and pay due corporation tax within the set deadlines and in circumstances where the taxable person either files an incorrect tax return or fails to maintain required records. Cabinet Decision No. 75/2023 also mentions voluntary disclosure penalties, and appears to suggest that the UAE Corporate Income Tax regime will have a voluntary compliance system similar to the VAT one.

INVESTMENT FUNDS

Cabinet Decision No. 81/2023 On Conditions for Qualifying Investment Funds for the Purposes of Federal Decree-Law No. 47/2022 on the Taxation of Corporations and Businesses has provided clarification on whether investment funds can apply for exemption from UAE corporate tax (at the discretion of the UAE tax authority). This Cabinet Decision applies equally to all investment funds, including real estate investment trusts (REITs), regardless of their place of incorporation. It allows investments funds, including REITs, to undertake an analysis (based on prescribed metrics) in order to understand if they might be eligible for an exemption. If following that analysis the required conditions are met, an application must then be made and approved by the UAE tax authority. After that happens the fund can qualify for the exemption.
However, even if approval is granted, the investment fund still has to register for UAE corporate income tax and make an annual corporate income tax filing. However, its income streams should not be subject to UAE corporate income tax. These obligations would then pass on to the investors. Article 10(1) of Federal Decree-Law No. 47/2022 details conditions for an Investment Fund to be able to make the application but further conditions are detailed in Cabinet Decision No. 81/2023. Specific conditions also apply in the case of a REIT.

OMAN

TAX INVOICES

The Omani Tax Authority has reported action it has taken against a VAT registered company which was avoiding issuing tax invoices for VAT evasion purposes, breaching Article 67 of Oman Sultani Decree No. 121/2020. An administrative violation report was issued against the company, resulting in a fine of 3,000 Rials. The employee who was responsible for the violation was also summoned to appear at the Oman Tax Authority's headquarters. Under Article 100 of Oman Sultani Decree No. 121/2020 potential penalties for this offence are imprisonment for a period of not less than two months and of not more than one year and/or a fine not less than 1,000 Rials but not more than 10,000 Rials.

SAUDI ARABIA

RETT WAY

Saudi Arabia Ministerial Decision No. 712/1442 On the Approval of the Implementing Regulation of the Tax Imposed on Real Estate Dispositions has been amended by Saudi Arabia Ministerial Decision No. 1331/1445. The changes largely reflect proposals detailed in a consultation in June 2023. Article 3(a)(16) of Saudi Arabia Ministerial Decision No. 712/1442, under which the transfer of real estate by a natural person to a Saudi company fully owned by that person, is exempt from Real Estate Transfer Tax (RETT), has been extended to include transfers of real estate by a natural person to an investment fund established in Saudi Arabia. In this case in order to qualify the

TAX TREATY UPDATE

Oman: Oman has ratified a Double Tax Treaty with Egypt.
Qatar: Qatar has signed a Double Tax Treaty with Uzbekistan.
Oman: Oman has signed a Double Tax Treaty with Cyprus.
Kuwait: Kuwait has been in discussions with Ecuador on a Double Tax Treaty.
Oman: The Omani Consultative Assembly has approved the signing of an income and capital tax treaty with Kazakhstan.
UAE: Federal Decree No. 91/2023 has ratified a Comprehensive Economic Partnership Agreement or (CEPA) with Turkey which will reduce and eliminate tariffs and non-tariff trade barriers on goods traded between the countries.

fund must be fully owned directly or indirectly by the transferor, and there must be no change in the fund's ownership for five years from the transfer date. Article 3(a)(17) of Saudi Arabia Ministerial Decision No. 712/1442 , under which transfers of real estate between companies that are fully owned by the same person are exempt from RETT, has also been amended so it applies where the real estate disposal is between two companies established in Saudi where one company is fully owned by the other. The exemption also now includes real estate transfers between Saudi companies and investment funds established in Saudi Arabia fully owned by these companies and real estate transfers between companies and investment funds established in Saudi that are owned by the same persons. In order to qualify there can be no change to the ownership of the fund or company for five years from the transfer date.

TAX RULING REQUESTS

The Zakat, Tax and Customs Authority (ZATCA) has published a Guideline on Tax Ruling Requests. This guidance applies to natural and legal individuals, and their representatives and agents, who wish to submit a request for a Tax Ruling to confirm the application of tax laws in Saudi Arabia. An important change is that the rulings issued by ZATCA are now binding. Rulings can be sought on VAT, income tax (including withholding tax), and other relevant tax matters on ongoing or planned economic activity. ZATCA also has discretion to issue optional Tax Rulings, which are not necessarily in response to a specific request but are general clarifications on matters the authority believes will benefit all taxpayers.

VAT CHANGES

A series of small changes has been brought in to Saudi's VAT Implementing Regulations Saudi Arabia Administrative Decision No. 3839/1438 by Saudi Arabia Administrative Decision No. 01/04/23/1444. As a result, for example, online stores are now required to display their VAT registration certificates in a way that makes them clearly visible to the general public. There have also been changes to the rules on when an international means of transport qualifies for the 0% VAT rate under Article 34(4) of Saudi Arabia Administrative Decision No. 3839/1438. This now states supply of a qualifying means of transport can be zero-rated, if the customer provides the Authority or supplier with a certificate stating the supplied means of transport qualifies according to the provisions of that Article, and the supplier keeps that certificate. Before issuing that certificate the customer is also required under Article 34(9) of Saudi Arabia Administrative Decision No. 3839/1438 to verify the eligibility of every transportation means and if they meet the conditions and terms in Article 34.

EGYPT

NON-RESIDENT VAT

Following, Egypt Ministerial Decision No. 160/2023 legislative amendments have been made which enable non-resident companies and platforms, with transactions involving digital and remote services inside Egypt to register for tax purposes there. Their transactions are subject to VAT, as a result of Egypt Law No. 3/2022 which amended the 2016 Egyptian VAT Law. A simplified electronic registration form has been put in place to make it easier for non-resident companies and platforms to register and the authorities have also issued a guide on VAT on digital and remote services provided by non-residents.

YEMEN

IMPORTED GOODS

The Houthi Ministry of Finance has imposed a 100% levy on items imported through government-controlled ports and land crossings, including Aden and Al-Mukalla. This means any products passing through these ports or crossings will be subject to the same tax and customs fees as those imported through the Hodeidah port when they pass through Houthi checkpoints. Traders will have to pay these taxes in cash at Houthi checkpoints in Sanaa, Taiz and Al-Bayd before they can enter markets controlled by the Houthis.

IN BRIEF

UAE: The final deadline for notified financial companies to submit their tax returns ended on 15 August 2023...

Turkey: Following the imposition of taxes on short-term rental services in the tourism sector police teams and tax offices in tourist areas are assessing all reports of unregistered transactions...

Saudi Arabia: Guidance on the cancellation of fines and financial penalties for those facing difficulties because of COVID 19 has been issued extending the amnesty until 31 December 2023...

Qatar: The National Committee for the Customs Clearance System is looking at ways to improve the clearance system and reduce the time for goods to be cleared in Qatar...

Turkey: It has been proposed that Motor Vehicle Tax on vehicles which are already registered and are to be registered by 31 December 2023 will be collected twice...

UAE: A new Foreign Account Tax Compliance Act (FATCA) and Common Reporting System (CRS) reporting portal has gone live..

Saudi Arabia: Educational programmes which are equivalent to educational certificates can be VAT exempt if they last at least two and no more than three years...

Jordan: The Parliamentary Financial Committee has recommended establishing a joint committee to look into the issue of goods which are either confiscated by or left with the Customs Department...

UAE: The Federal Tax Authority (FTA) has announced they have started to accept explanation requests on electronic registration for business tax ...

Saudi Araba: The Zakat, Tax and Customs Authority (ZATCA) has issued new requirements and procedures for importing motorbikes from outside Saudi Arabia...

Iraq: The Ministerial Council for Economy has announced a reduction in the customs tariff imposed on live animals imported for slaughtering to 4%..,

Egypt: The poultry sector has been included in the industrial and productive sectors for whom the state General Treasury assumes property tax responsibility until the end of December 2024...

Turkey: Products and services that were subject to an 8% VAT are now subject to a new 10% rate, while those which previously had a 18% VAT rate now have a 20% rate...

FOCUS ON M&A

The introduction of Corporate Income Tax to the UAE has had a significant impact on how Mergers and Acquisitions (M&A) will work there. Tax considerations are driving key strategic decisions on M&A. For example, the introduction of Corporate Income Tax in the UAE may reshape a company's valuation and transaction structure, primarily due to the UAE's now higher tax rates. The appeal of using UAE based companies for cross-border transactions may change along with tax obligations. There could also be increases in transaction costs, as companies may now need tax professionals to assess potential tax ramifications, and deal timings and financing strategies could be impacted. Factors like a company's headquarters' location, profit distribution, and tax-efficient transaction structuring may need reassessment and as a result, companies may want to alter their M&A strategies. In this context it is also important to remember that UAE Corporate Income Tax also applies to revenues sourced from the UAE by non-resident entities. So foreign investors who have assets or investments in the UAE, which they are looking to divest, may also have to consider the new Corporate Income Tax regime.

APPROACH TO DUE DILIGENCE

The introduction of Corporate Income Tax in the UAE means increased scrutiny of tax-specific matters will be needed in the due diligence phase before any M&A activities. Purchasers will need to dig into the fiscal ramifications of UAE Corporate Income Tax on the entity, tax adherence, and will also have to pinpoint potential tax risks and liabilities. They will also need to think about structures which will maximise tax efficiency after the purchase. These steps will all be essential in ensuring appropriate decision-making and smooth post-deal integration of the newly purchased business.

Capital cost estimation also needs be a key part of any due diligence. The Corporate Income Tax rate can play a pivotal role in deciding the capital distribution between equity and debt. However, determining the effective tax rate can be tricky given the potential discrepancies between accounting profit and taxable profit and the need to understand interactions with specific tax rules, such as the distinct interest deduction limitation rule.

Another consideration is valuation and the deal structure. Taxes levied on earnings can alter a company's valuation. Increased tax costs will diminish a company's profit margins and cash flows and could deflate their worth. Therefore, these variations can influence deal negotiations and pricing. As a result, purchasers may have to recalibrate their propositions or reconsider the transaction's financial viability.

Related party transactions will also need to be carefully reviewed. These can lead to everything from adjustments in cash flow statements to reshaping of transaction structuring. For example, there is a specific interest deduction rule that restrains the interest deduction on loans acquired from affiliated entities in cases including dividend distributions, capital contributions, and share buybacks.

Deal timing is also key as the introduction of new income tax rules can prompt businesses to expedite or postpone M&A ventures. In the UAE, this could mean some entities with accounting years that start on 1 January are currently looking to hasten the finalisation of transactions before the tax system fully activates for them. Although it should be noted that anti-abuse provisions have been introduced to limit purely tax driven transactions with no business rationale. It may also be helpful to consider including a tax risk clause in any agreement as these are now becoming more common.

SHARE DEAL OR ASSET DEAL METHODS

Under a share deal, any existing and potential tax risk the target has remains with the target and therefore rests with purchaser once they own the target. So, where a share deal approach is being considered very thorough due diligence is needed to unearth any contingent tax liability and provide suitable justifications to those risks. However, share deals are also a privileged way of tax planning, which allow for tax loss transfers that can be used to offset against taxable income in subsequent periods. This is similar to the tax-loss harvesting used in other tax jurisdictions to offset gains and losses on securities. These kinds of strategies can be helpful to M&A transactions parties, although the UAE Corporate Tax Law (Federal Decree-Law No. 47/2022) provides that tax losses can only be carried forward and used, if the same person or persons has continuously owned at least a 50% ownership interest in the taxable person, from the start of the tax period in which the tax loss is incurred to the end of the tax period in which the tax loss or part of it is offset against taxable income of that period.

With asset deals, the target company's liabilities are not transferred to the asset purchaser but there are always some tax aspects to consider, particularly on realised capital gains, and the different options to tax them. Federal Decree-Law No. 47/2022 provides favourable business restructuring relief, under which a taxable person may transfer an asset to another taxable person in exchange for shares or other ownership interests of the transferee.

Alternatively, the taxation of realised capital gains would be limited, to the portion attributable to the period starting from the start of the first taxable period. The assessment starting from the introduction of Corporate Income Tax will be important in determining the way asset deals are structured.

TIMING OF IMPACT

For companies with a year end on or just after 1 June 2023, considering M&A these issues already apply but there could be a retroactive impact on M&A transactions dating back to end of 2022, as the General Anti-Abuse Rule applies to transactions or setups initiated on or after the date Federal Decree-Law No. 47/2022 was published in the Official Gazette which was 10 October 2022. M&A transactions currently in the pipeline should have already taken into account revised cashflow forecasts as a result of the introduction of corporate income tax, a recalibration of estimations of capital costs and past tax adjustments which may have to be reassessed and adjusted to accommodate Corporate Income Tax effects.

FINANCING

Tax changes will also impact M&A deal financing structures. For example, UAE Corporate Income Tax will affect the after-tax cost of debt and the volatility of equity indexes, and so the cost of equity. This can influence capital structure decisions of acquiring companies and impact the overall financial feasibility of the transaction. The limitation of tax deductibility of interest charges on debt will also influence the allocation capital versus debt when financing a transaction.

GROUPS

Under UAE tax group provisions the parent and each subsidiary are jointly and severally liable for corporate tax payable by the tax group for tax periods when they are group members. This could be an obstacle to potential purchasers of companies in a group as the liability associated with the target could be extended to other former group companies. Limitation of joint and several liability to some, and not all group companies, is subject to the authority approval. This limitation request could become a standard prerequisite in M&A transactions involving tax group member targets.

This article was written by Mourad Chatar and Ismail El Koundi of Value Square.

TAX PROFESSIONAL PROFILE

GLOBAL HEAD OF TAX, TREASURY & CUSTOMS – LOGISTICS

SUSTAINABLY MINDED

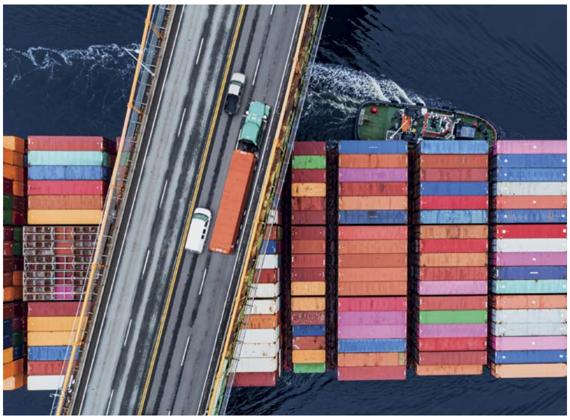
Rajpal Bal, Global Head of Tax, Treasury & Customs at Aramex explains the impact sustainability has on his company's strategy and tax planning.

ABOUT YOU?

I have a degree in Accounting and Finance from Oxford Brookes University and am an ICAEW Fellow and qualified with the CTA. I also have Non-Executive Director and Executive Leadership qualifications from Hult Business School. I began my training with a medium sized accountancy firm that eventually led me into tax as I wanted to create value for clients, save them money and give them certainty on the taxes they would be paying. For around 17 years I have been working in tax in a range of different companies, headquartered in different parts of the world where tax is viewed differently - that has given me a balanced view in my current role when assessing tax positions, the approach with tax authorities and risk management.

ABOUT YOUR CURRENT ROLE?

I currently work for Aramex, a global logistics company headquartered in the UAE with a presence in over 65 countries. Aramex has a strong presence in the MENA region but also good coverage in the US, Asia, Africa and Oceania region. Aramex's services include domestic and international express delivery services for packages and documents, a freight forwarding product and logistics and supply chain solutions. As part of my role, I have to be able to manage relationships with both external and internal stakeholders, depending on the country I am dealing with. As part of my role, I have to educate my peers, the board and management on tax and why it is important for it to be part of the organisation's decision-making process. My role involves not just financial areas but there is also a broader remit which covers areas such as ESG, risk and how external investors view you as a business, which can depend on your approach to tax. On the tax side I lead a team of five based in the UAE, India and Jordan and am responsible for all aspects of tax (including corporation tax, transfer pricing, VAT and Customs. As part of my tax role, I am responsible for Effective Tax Rate (ETR) management for the company and set the tax strategy. I am also having to implement OECD BEPS 2 across all 65 countries. In addition, have worked on Advanced Pricing Arrangements, audit and risk management and led audits with the tax authorities globally. Group M&A and tax structuring is another of my responsibilities,



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along with tax governance and risk management for the Aramex group. On the treasury side I manage a team of 30 in the UAE and India. That includes monitoring cash and liquidity, work with rating agencies, putting in place robust treasury management systems and payment solutions, managing relationships with banks, and optimising funding structures to support M&A, short term financing and other financing needs. Post pandemic the tax authorities have become more eager to recoup revenue, which has made tax audit defence a larger part of the role. At present, our biggest challenges are the introduction of Corporate Income Tax in the UAE and OECD BEPS 2. Our specific function has to be to ensure our tax compliance is fully up to speed given there are still many areas of uncertainty on both these subjects.

With UAE corporate income tax, we have had to do a lot of planning before implementation on the tax. However, extensive pieces of legislation are still being issued so you have to be able to get to grips with a lot of information, very quickly.

OECD BEPS 2 is being rolled out in a country by county basis. That has meant we have had to ensure we have the correct technology to ensure compliance and measure impact on our business. We have needed the correct data capture and have had to check we are correctly modelling impact. You also need to understand the global rules but also ensure tax pick up is right at a country level.

SUSTAINABILITY

Aramex is a market leader on sustainability and tax

PRACTITIONER PERSPECTIVE

Rami Alhadhrami of BDO looks at the impact ESG can have on tax for GCC companies.

Rami Alhadhrami
Partner – Tax & Regulatory Services
BDO in Kuwait

ESG – short for environment, social and governance, is a framework used to assess an organisation's practice in these areas. Tax plays an important role in each of the ESG principles but there is often a misunderstanding of the relationship between tax and ESG issues, particularly in the GCC where there are limited environmental taxes and related incentives. Oman has recently provided an exemption from VAT and customs on Electric Vehicles but there are no special tax incentives for investing in green energy and no single use plastic tax in the GCC. However, environmental taxes and incentives, such as carbon taxes on greenhouse gas emissions and tax incentives for green energy adoption are increasing across the globe and may impact GCC companies with operations abroad (for example in the EU or UK). Despite these limited environmental tax incentives in the GCC, there can still be tax implications to consider. For example, as ESG strategies can affect a company's supply chain and business model, there may be transfer pricing implications.

With the social part of ESG, taxes serve as a means by which companies can contribute to the societies in which they operate. The governance part of ESG is also of growing importance when it comes to tax, globally and regionally, as tax governance essentially entails establishing a tax policy, tax principles and a tax risk framework to ensure adherence to tax principles. Another key aspect of tax governance is tax transparency. Stakeholders and the wider community are increasingly interested in what Multinational Enterprises (MNEs) pay in tax and where. There are mandatory tax reporting measures such as OECD and EU Country by Country Reporting (CBCR), and the EU Directive on cross-border tax arrangements (DAC 6) which can impact some GCC groups operating in the EU. In addition, some businesses have also decided to publish wider tax statements and adopt voluntary transparency standards such as the Global Reporting Initiative (GRI). The Saudi Exchange has included tax transparency as part of its ESG Guidelines, and as a result companies are assessed on several tax criteria including their Effective Tax Rate (ETR) and their tax controversies. Tax disclosures can also be relevant when it comes to M&A as an investor's ESG programme could cover an assessment of the investee entity's tax framework. Deciding on how and what tax information a company shares with stakeholders can also have an impact on the reputation and perceptions of its ESG statements. The inclusion of tax-related metrics and disclosures within ESG frameworks can help stakeholders understand a company's dedication to responsible and sustainable practices.

Companies may, however, face challenges in meeting the demand for tax transparency (and for reporting on tax incentives and environmental taxes, as applicable). Data gathering and analysis is often a key issue with tax transparency reporting and process automation may be needed to collect the required tax data for analysis.

Internationally, the ESG regulatory landscape is developing rapidly. In June 2023, the International Sustainable Standards Board formally approved new Global Sustainability Disclosure Standards (IFRS S1 and IFRS S2) and in July 2023, the EU Commission adopted European Sustainability Reporting Standards. In most GCC counties, there are no mandatory annual sustainability reporting obligations for companies and reporting tends to be voluntary. However, regulatory bodies in some GCC countries have issued ESG reporting guides..

in January 2023 the GCC Exchanges Committee launched voluntary Unified Sustainability Metrics ESG guidelines for local listed entities and some GCC listed companies have begun ESG implementation and started issuing sustainability reports. In view of this ESG momentum, tax function leaders will need to ensure their tax strategy and operations correctly intersect with their corporate ESG vision and commitments. Implementing a responsible tax programme takes time and careful consideration of an entity's overall approach to tax is needed.

has had to be part of our discussions in this area. For example, we have had to look at our transparency on tax disclosures, where this is documented and how is it communicated internally and externally. We have also had to know what our carbon footprint is and think about our position on carbon tax policies. We have had to think about tax policies which are related to health and/or social justice areas. Another area which has come up has been which voluntary reporting frameworks we are planning to report under, and what tax disclosures will be required by those frameworks. You also have to consider whether you plan on engaging with ESG rating agencies, standard setters and regulators as they design and refine the tax metrics. How we benchmark ourselves against other companies on ESG generally and tax specifically has also been a consideration. The tax credits and incentives we use also come up, as does how tax credits are reflected in our ESG disclosures. The way ESG is factored into our supply chain decisions and the potential role tax has in those discussions is another consideration, along with the impact energy and environmental taxes have on our supply chain.

We are also always aware of the potential future carbon, labour or health-related tax policy changes that could impact our business. Finally, it is important that we know how ESG-related taxes are impacting our revenue targets and competitiveness. In order to fully understand that, it is also important that we are measuring this impact.

ANY QUESTIONS?

HOW DOES TAX RETENTION OPERATE?

Rami Alhadhrami of BDO Kuwait explains the retention requirements which apply to every entity trading or doing business in Kuwait.

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Under Kuwait income tax regulations, every entity trading or doing business there is required to retain 5% of the total contract value or from each payment made, to any party with whom they enter into contracts or transactions. The retained amount must be held, in trust, by the payer (i.e. customer) until the payee (i.e. the vendor) submits a retention release letter (RRL) issued to them by the Kuwait Ministry of Finance (MOF). In addition, on rare occasions, if the payee has failed to meet its Kuwaiti income tax requirements, the MOF may also request the payer to remit the retained amounts directly to MOF's account.

Foreign companies often make mistakes with this regime. For example, many wrongly assume that the 5% which has been retained by their customer is some type of Withholding Tax (WHT), and as a result they do not try to claim a refund or check whether they now have a tax filing obligation in Kuwait. It is important to note that there are significant penalties in Kuwait both for late filing and for late payment of tax. The 5% retention is not a payment in lieu of paying taxes and does not provide an exemption from filing income tax returns. Mistakes can also be made by some entities who are involved in a Kuwaiti project and may not realise that as the client they have to retain 5% from payments to their contractors even if they are not present in Kuwait.

APPLICATION

Kuwait tax retentions (KTRs) apply to all public and private bodies, whether they are local or foreign entities, who trade or do business in Kuwait. The KTR requirements have been broadly drafted and capture all types of payments – there are no exclusions provided in the KTRs.

In practice, certain types of payments are scrutinised in particular by the MOF when it comes to tax retentions. These are transactions involving services of all types, intercompany expenses, where equipment or labour is being hired and royalties, licences and subscriptions, and payment for supplies of goods (particularly if they contain an installation or training element). While there are some similarities between Withholding Tax (WHT) and Kuwaiti tax retentions, there are specific differences between these two, which should be noted. For example, unlike WHTs, which must normally be deducted and then deposited with the government by the person withholding the taxes, in Kuwait, the payer themself is usually required to hold the retentions until the payee provides a RRL that they have obtained from the MOF and after which the retentions can be released to the payee. It is also worth noting that a Kuwaiti tax retention is not a type of tax and, therefore, is not covered in Kuwaiti tax treaties.

ARE TAX RETENTIONS REFUNDABLE?

Kuwait tax retentions can be refunded once the payee has obtained an RRL from the MOF and they have submitted this RRL to their Kuwaiti customer.

OBTAINING AN RRL

The process and timeframe for obtaining an RRL will ultimately depend on the company's taxability in Kuwait and their Kuwait related contract. For example, GCC companies owned by an individual can typically submit a request for a RRL to the MOF, along with their corporate documents. The RRL will often then be issued in one to four weeks, subject to MOF approval. However, if the company is a foreign (non-GCC) company the process is more complicated and will depend on whether the contract is a taxable contract or a tax exempt contract. If a taxable contract, the foreign entity executing that contract will normally have to register with the MOF, file an income tax return, comply with MOF tax inspection and obtain a tax assessment. Once that assessment has been issued, if there are no outstanding taxes, the company will then be able to proceed to apply for an RRL for revenue which was covered in that assessed year. In contrast if the foreign company is executing a tax exempt contract and they have no presence in Kuwait and do not make visits to Kuwait, as would be the case for a pure supply contract, they normally will be able to apply for and obtain an RRL without having to go through the tax compliance process detailed above.

FAILURE TO FOLLOW THE RULES

If an entity has failed to make the necessary retentions, the MOF has a right to demand from them the tax debt which would have been payable by the payee (if that payee fails to settle their due tax). In addition, in the case of a foreign company which has tax filing obligations in Kuwait, non-compliance with KTR requirements can lead to disallowances of amounts paid without tax retention.

Contributor
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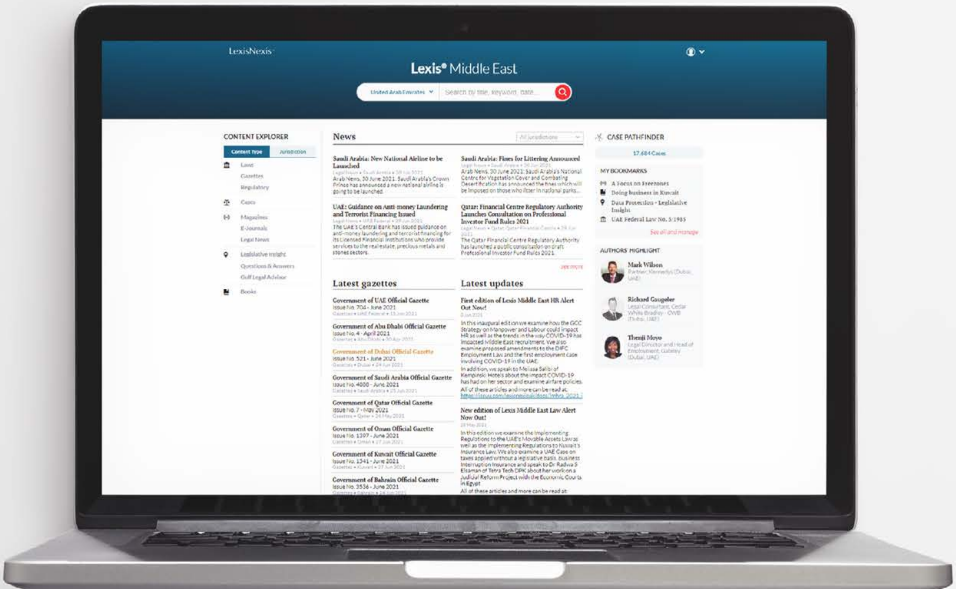

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