

UAE Alert



Corporate Tax: 'Qualifying Income' Clarified

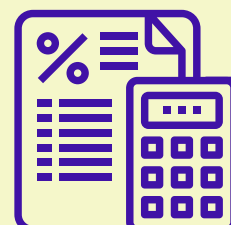
The UAE Corporate Tax (CT) Law has been implemented effective 1 June 2023. The CT law that was first released in December last year has a specific provision for Free zone companies in UAE which seeks to tax the income of Qualifying Free Zone Person (QFZP) as follows:

- 0% on Qualifying Income.
- 9% on Taxable Income that is not Qualifying Income.

Accordingly, a taxable person would be eligible for a 0% tax rate when they meet the conditions to become QFZP and earns 'Qualifying Income.'

However, what would constitute 'Qualifying Income' was not clarified in the CT law.

On the first day of implementation (i.e., 1 June 2023), the Ministry released the much-awaited clarification on the term 'Qualifying Income' vide Cabinet Decision no. 55 (CD 55) of 2023 and Ministerial Decision no. 139 of 2023 (MD 139).



Qualifying Income of a QFZP

Depending upon the source of the income, the Qualifying Income needs to be determined as follows:

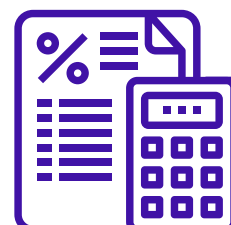
- **Transaction with a Free Zone person:** All revenue, except for the revenue from 'Excluded Activities'.
- **Transaction with a Non-free Zone person (including person outside the UAE):** Only such income that is derived from 'Qualifying Activities' and is not Excluded Activities.
- **Any other income:** Provided it meets the 'de-minimis' threshold limit of a) 5% of total revenue or b) AED 5 million, whichever is lower.

Additional clarification with respect to the above

1. Income attributable to a branch office/other office (either in the UAE or outside the UAE) of a qualified Free Zone that qualifies as a Permanent Establishment (PE) of a qualified Free Zone (either in the UAE or outside the UAE) would not be regarded as 'Qualifying Income.' For example, income derived by a branch of QFZP in the Mainland would not qualify as 'Qualifying Income.'
2. 'Qualifying Activities' has a wide coverage that includes most of the strategic areas of business activities, including manufacturing, processing, distribution for resale purposes, Holding of shares and securities, shipping business, logistics services, reinsurance services, fund/investment management services, etc. It also includes income from certain services to related parties,

such as headquarters services, treasury and financing services, etc. Additionally, any activities that are ancillary to the above activities would also qualify as Qualifying Activities.

3. Similarly, 'Excluded Activities' would include certain transactions with natural persons, activities of banking, insurance, leasing business, certain activities connected to immovable property and activities connected to intangible property. Additionally, any activities that are ancillary to the above activities would also qualify as Excluded Activities.
4. Furthermore, it is clarified that the Non-qualifying Income of QFZP could also enjoy a 0% CT rate provided that it meets the 'de-minimis' threshold limit, i.e., a) 5% total revenue of total revenue or b) AED 5 million, whichever is lower. Also, it has been clarified that the provision of the 'de-minimis' threshold would not apply to certain categories of income, such as revenue from the branch office in the Mainland/overseas and revenue from immovable property in some situations, etc.
5. Notably, a QFZP shall cease to be so from the beginning of the relevant tax period and for the subsequent four tax periods (in all five years) if:
 - a. Derives non-qualifying income beyond the 'de-minimis' level specified above; Or,
 - b. Fails to meet any of the existing conditions to become QFZP.



Our Comments

Effectively, a taxable person in UAE Free Zone shall meet the below conditions to enjoy a 0% CT rate:

- Maintain adequate substance in the State.
- Should not have elected to be subject to CT under.
- Transactions with related parties and connected persons must be at arm's length.
- Prepare audited financial statements.
- Derive 'Qualifying Income'.
- Non-qualifying Income (if any) should not exceed the 'de-minimis' level.

As the next step, a taxable person in UAE Free Zone would need to evaluate whether all the above conditions are satisfied. The definition of Qualifying Income is more activity-based rather than source-based (like foreign-sourced income) as contemplated by the industry.

Furthermore, it is also clarified that a taxable person in Free Zone should consult its regulatory authority to confirm whether it qualifies as Free Zone for the purpose of UAE CT.

Webinar



Are free zone companies free from UAE Corporate Tax?



Lokesh Gupta
Associate Director
Tax and Transfer Pricing

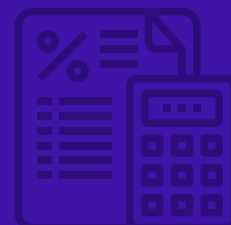


Nishit Parekh
Partner
Sudit K. Parekh & Co. LLP



6 June 2023 | 10:30 AM GST

Register Now



About Nexdigm

Nexdigm is an employee-owned, privately held, independent global organization that helps companies across geographies meet the needs of a dynamic business environment. Our focus on problem-solving, supported by our multifunctional expertise enables us to provide customized solutions for our clients.

We provide integrated, digitally driven solutions encompassing Business and Professional Services, that help companies navigate challenges across all stages of their life-cycle. Through our direct operations in the USA, Poland, UAE, and India, we serve a diverse range of clients, spanning multinationals, listed companies, privately-owned companies, and family-owned businesses from over 50 countries.

Our multidisciplinary teams serve a wide range of industries, with a specific focus on healthcare, food processing, and banking and financial services. Over the last decade, we have built and leveraged capabilities across key global markets to provide transnational support to numerous clients.

From inception, our founders have propagated a culture that values professional standards and personalized service. An emphasis on collaboration and ethical conduct drives us to serve our clients with integrity while delivering high quality, innovative results. We act as partners to our clients, and take a proactive stance in understanding their needs and constraints, to provide integrated solutions. Quality at Nexdigm is of utmost importance, and we are ISO/ISE 27001 certified for information security and ISO 9001 certified for quality management.

We have been recognized over the years by global organizations, like the International Accounting Bulletin and Euro Money Publications.

Nexdigm resonates with our plunge into a new paradigm of business; it is our commitment to **Think Next**.

USA Canada Poland UAE India Hong Kong Japan

www.nexdigm.com

Reach out to us at ThinkNext@nexdigm.com

Follow us on



Listen to our podcasts on all major platforms

This document contains proprietary information of Nexdigm and cannot be reproduced or further disclosed to others without prior written permission from Nexdigm unless reproduced or disclosed in its entirety without modification.

Whilst every effort has been made to ensure the accuracy of the information contained in this document, the same cannot be guaranteed. We accept no liability or responsibility to any person for any loss or damage incurred by relying on the information contained in this document.