BDO

UAE ECONOMIC SUBSTANCE REQUIREMENTS

New regulations issued in the UAE create reporting obligations and require certain entities to maintain physical presence and employees in the UAE

Scope

The new economic substance rules apply to any entity which undertakes 'Relevant Activities'.

Relevant Activity is defined as banking, insurance, fund management, lease finance, headquarters services, shipping, holding company, intellectual property and distribution and service centers.

Entities owned partly or fully by the UAE government are excluded from the Regulations.

Economic substance requirements

In order to meet the economic substance requirements, an entity undertaking Relevant Activities is required to demonstrate that it is:

- Conducting its core income generating activity in the UAE
- Directed and managed in the UAE
- Employing adequate qualified full-time employees in relation to the activity in the UAE
- Incurring adequate operating expenditure
- Maintaining adequate physical assets

Outsourcing does not prevent the entity meeting the tests in this list. However, the entity must demonstrate an adequate level of expenditure incurred on outsourcing. It would also be required to demonstrate that the business providing the outsourced services has activity, employees, expenditure and premises in UAE which are adequate to provide the service.

In order to satisfy the "directed and managed" test, the entity's board of directors' meetings should be held in the UAE at an adequate frequency, meeting minutes should be maintained and kept in the UAE and a minimum number of directors should be physically present in the UAE during the meetings.

Pure holding companies, which earn income wholly from dividends and capital gains, are subject to lighter substance tests. In the event that such holding companies earn additional income from a Relevant activity, the portion of the income received from the Relevant activity would be subject to the normal substance requirements.

Reporting requirements

All entities will be required to report to the regulatory authority (The authority that issued the trade licence to the entity).

BACKGROUND TO THE CHANGES

On 30 April 2019, The Cabinet of Ministers issued Resolution No. 31 of 2019, ("the Regulations"), which introduces some important new requirements for international businesses.

Under the Regulations, a UAE entity which is engaged in "Relevant Activities" is required to meet certain economic substance requirements. If the requirements are not met, the entity may be liable to fines, penalties and the potential suspension, revocation or non-renewal of its license.

The Regulations support measures recommended by the Organization for Economic Cooperation and Development ("OECD") to combat harmful tax practices. Several other countries have implemented similar legislation during 2019.

ECONOMIC SUBSTANCE REQUIREMENTS- UAE

Information required will include:

- Whether or not the entity is carrying on a Relevant Activity.
- Whether or not all or any part of the entity's gross income in relation to the Relevant Activity is subject to tax in a jurisdiction outside UAE.

An entity carrying on a Relevant Activity is also required to submit a report with certain additional details within twelve months of the end of each financial year.

Penalties

Administrative penalties ranging from AED 10,000 to AED 300,000 may be levied on entities failing to satisfy the economic substance requirements, failing to report or reporting inaccurately. Continued non-compliance may result in suspension, revocation or non-renewal of an entity's license.

The impact on business

The regulations are applicable to any business based in the UAE, including entities owned by GCC nationals or businesses. However, it is likely to be international groups that will be most concerned about the potential impact and in particular, businesses that are carrying out Relevant activities in the UAE but which are managed remotely.

For UAE headquartered businesses and for businesses with genuine commercial activity in the UAE the impact may not be significant, but it is worth considering the implications in all cases.

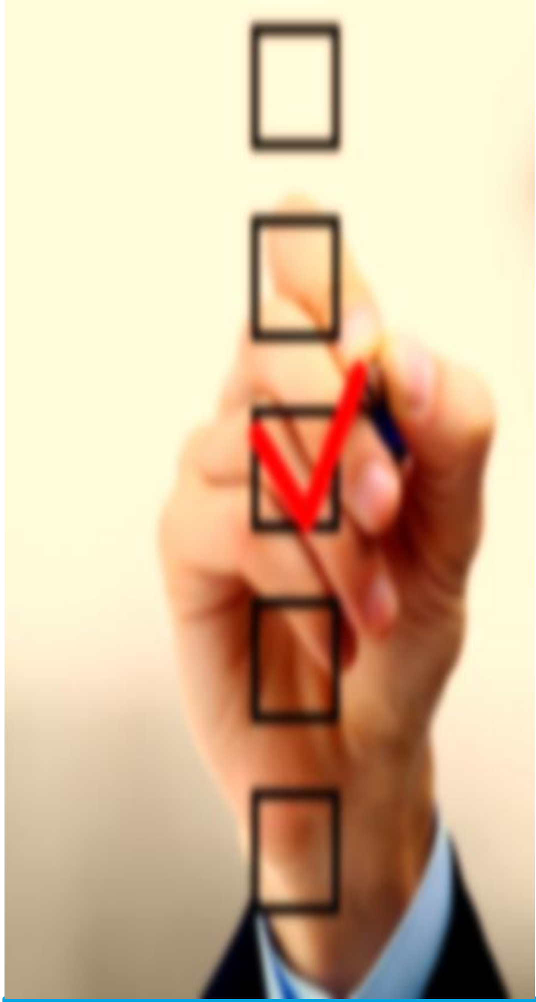
BDO comments

The introduction of substance requirements is a positive step by the UAE. It supports the OECD's Base Erosion and Profit Shifting (BEPS) Project. This project is aimed at preventing multi-national businesses from avoiding tax by shifting profits to low tax jurisdictions.

UAE entities, and multinational businesses with entities in the UAE, will need to review their UAE operations and substance. Failure to do so could result in penalties and the loss of tax treaty benefits.

The substance requirements introduced in the UAE, which are based on EU recommendations, are in line with those introduced by other jurisdictions such as Cayman Island, Jersey etc.

We are expecting further implementing regulations and guidance on the reporting requirements in due course.



How BDO can help?

Impact assessment

BDO can help you determine if your company would fall within the scope of the Regulations based on the constitution of the company as well as the activities and transactions undertaken by the company.

Gap analysis and planning

BDO can help identify gaps in the level of economic substance in the entities covered by the Regulation and provide implementable options to close the gaps.

Compliance

BDO can help businesses meet all the regulatory compliance, corporate structuring and reporting requirements in the Regulations, and mitigating the potential penalties.

For further information, please contact us:

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