

**Sudit K. Parekh & Co. LLP**

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**Taxation of non-residents under  
the UAE Corporate Tax Regime**

## Provisions relevant for Non-residents

The UAE has introduced Corporate Tax (CT Law), which would be effective in the UAE from financial years beginning on or after 1 June 2023. Accordingly, it is imperative for foreign entities/ non-residents doing business in the UAE to evaluate the impact of CT on their operations and cash flows.

A non-resident in the UAE is subject to UAE CT on income attributable to its Permanent Establishment (PE) in the UAE or on UAE-sourced income not attributable to the PE or taxable income attributable to the nexus in the UAE. While the CT Law provides guidance on PE rules and UAE-sourced income, nexus rules are yet to be notified.

Furthermore, a non-resident entity having a Place of Effective Management (POEM) in the UAE would be considered as a resident of the UAE and would be liable to UAE CT.

In the next paragraphs, we have discussed the taxability of non-residents in the UAE.

### Permanent Establishment in the UAE

The concept of PE under the UAE CT Law is largely based on the Organization for Economic Cooperation and Development (OECD) model tax convention. As per the UAE CT Law, a non-resident shall be considered to have PE in the UAE if:

- It has a fixed place of business which would inter-alia include a branch, office, factory, workshop, etc.
- Has a building or construction site or place of assembly or installation or supervisory activities in connection therewith which exceeds six months.
- It has a dependent agent in the UAE who habitually exercises an authority to conclude or negotiate contracts without any material modification on behalf of the non-resident person.
- A fixed place PE would not be constituted if only preparatory and auxiliary activities are conducted in the UAE.

- A natural person will not be considered to constitute a PE for the foreign entity in the UAE if:
  - their presence is a consequence of a temporary or exceptional situation; or
  - where the natural person is employed by a non-resident; or
  - the activities being conducted in the UAE are not part of the core income-generating activities of the non-resident or its related parties; or
  - the non-resident does not derive UAE-sourced income.

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## Provisions relevant for Non-residents

### UAE-sourced income and the Nexus Rule

Income shall be considered as sourced from UAE if it is derived from:

- A resident person.
- PE of a non-resident.
- Derived from activities performed, assets located, capital invested, rights used, or services performed or benefitted in the UAE.

It would be pertinent to note that UAE-sourced income is widely defined, and it effectively covers any activity with the slightest link to the country. An illustrative list of activities that may be considered as UAE-sourced income is also provided under the law. The same is subject to certain conditions as may be determined by the Federal Tax Authorities (FTA). A few activities included in the said list are indicated below:

- Income from the sale of goods in the UAE.
- Income from movable or immovable property in the UAE.
- Interest on loans given to a resident in the UAE or secured by any property located in the UAE.
- Insurance premiums where the insured or insured asset is located in the UAE.
- Income from contracts wholly or partly performed in the UAE.

Even transactions between two non-resident persons will be covered if it involves any asset such as land, building, shares, or any event in the UAE.

In light of the above, non-residents earning UAE-sourced income may be liable to tax in the UAE. However, there appears to be a contradiction as per the FAQs issued with the final law in regarding taxation of foreign persons in the UAE. The FAQ's answer states that *“foreign entities that operate in the UAE through a permanent establishment or that are considered resident in the UAE for CT purposes will be subject to UAE CT. Merely earning UAE-sourced income would not trigger CT payable or require the foreign entity to register and file for UAE CT”*. However, no such specific exemption has been provided under the law. Considering the contradictory wordings within the FAQs and the law, clarity on treatment of UAE-sourced income is required.

At present a 0% withholding tax rate is prescribed on payment to non-residents towards UAE-sourced income. Furthermore, there are no withholding tax compliances as per the law today. However, since the withholding tax rate has been prescribed at 0%, we may see withholding tax rates increased in the future.

Also, it has been provided that the FTA would issue a cabinet decision shortly prescribing the nexus rules.

UAE CT laws specifically provide that all international agreements would prevail over local laws. Thus, where the UAE has entered into a Double Tax Avoidance Agreements (DTAAs) with any other country, the taxability of income of the non-resident from the UAE perspective would be governed under such agreement; the same is quite beneficial. It is pertinent to note that the UAE still does not have a DTAA with some of its neighboring countries such as Kuwait, Qatar, and other prominent countries, namely the US and Australia, amongst others. Thus, companies doing business in the UAE from these countries would have to be extra careful, especially in light of the UAE-sourced income rules and the nexus rules.

## Place of Effective Management (POEM)

The CT Law states that a non-resident entity effectively managed and controlled in the UAE shall be treated as a resident person for the purpose of CT and be taxable on its global income in UAE.

While the term POEM is not defined under the law, the FAQs released alongside the law state that POEM will have to be assessed on a case-to-case basis, and that the location where key managerial and strategic decisions (relevant to the non-resident entity) are made shall determine POEM.

Currently, no monetary limit/threshold has been provided for the applicability of POEM regulations. Accordingly, UAE companies with subsidiaries outside of the UAE or Key Managerial Persons located in the UAE for overseas entities needs to carefully conduct a thorough evaluation of POEM regulations.

While no specific guidelines have been provided for POEM, it could be relevant to refer to the criteria provided in OECD commentary which may help determine POEM of non-residents:

- The place where meetings of the Board of Directors or equivalent body of the company are usually held.
- The place where the Chief Executive Officer and other senior executives usually carry on their activities.
- The place where the senior day-to-day management of the entity is carried on.
- The place where the entity headquarters are located.
- The place where country laws govern the legal status of the entity.
- The place where accounting records are kept.





## Taxation of investment income in the hands of non-residents

### Dividends

UAE CT Law provides for an exemption with respect to dividends earned from UAE domestic companies. Thus, non-residents earning dividend income from investments in UAE corporates shall not be subject to tax in the UAE.

### Capital Gains

Based on a strict interpretation of the law, capital gains earned by non-residents on the sale of shares held in a UAE corporate shall be taxable in the UAE. Currently, the exemption is granted only with respect to capital gains earned by UAE corporate shareholders from the sale of investments held outside the UAE, subject to meeting participation exemption conditions.

It is pertinent to note here that since the introduction of the UAE CT Law, the Federal Tax Authorities have specified that non-residents earning investment income in the form of dividends, capital gains, interest, royalties, and other investment returns will not be subject to UAE CT. This is also specified in the FAQs. However, the same is not categorically coming out of the law. Considering the significant amount of foreign investments in the jurisdiction, a clarification on this front would be welcome for relevant stakeholders.



## Indian Investments in UAE – Impact Assessment

### Investment by Indian Companies/Limited Liability Partnerships (LLPs)

Indian companies/LLPs can invest in UAE companies/LLCs under the Overseas Investment Rules . Investment is permitted up to 400% of the investor's net worth as on the date of the last audited balance sheet. Investment is permitted in all sectors except for real estate activities, gambling, and dealings in financial products linked to the Indian Rupee, where RBI approval will be required. Furthermore, certain additional conditions exist for investment in the financial services sector.

Individuals can invest in the UAE within their Liberalized Remittance Scheme limits. However, individuals cannot invest in the financial services sector or have a step-down subsidiary.

Furthermore, portfolio investment (investment in less than 10% of the paid-up capital with no management control) in listed securities is permitted for Indian individuals as well as companies to the extent of 50% of the net worth on the date of the last audited balance sheet.

Latest trends suggest that Indian investors have invested either by way of equity contribution or loans close to USD 2,700 million in subsidiaries and joint ventures in the UAE in calendar year 2022. This is 1.5 times the investment made in calendar year 2021. These statistics indicate that India is viewing the UAE as a promising investment and growth destination. Thus, Indian investors must thoroughly evaluate the UAE CT Law and transfer pricing law. Indian companies should evaluate the structure, availability, and conditions for claiming tax exemption for a Free Zone entity, the capital structure of the UAE entity, need for restructuring of operations, etc.

In addition to the same, there could be requirements for re-alignment of transfer pricing policies between the Indian companies and UAE companies, meeting substance requirements in the UAE, creating tax efficiency in the UAE, evaluation of the availability of tax credit in India of taxes paid in the UAE, accounting aspects, etc.

While the law would develop over the coming months as various cabinet decisions and notifications are released, companies should prepare for the CT Law and transfer pricing implementation in advance.



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