



## Client Alert

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### **Complying with the new UAE Economic Substance Resolution**

***The key impact of the Resolution is the obligation of companies carrying out relevant activities to meet the specified Economic Substance requirements and to conduct annual compliance reporting. Non-compliant companies could risk fines and penalties, suspension, withdrawal or non-renewal of licenses, and the disclosure of their position to other foreign authorities. Companies in the UAE carrying out the relevant activities must file their first report within 12 months from the end of their fiscal year.***

#### **Why has the UAE issued the Resolution?**

In March 2019, the European Union (EU) published an updated list of non-cooperative tax jurisdictions (the **EU blacklist**), which included the United Arab Emirates (UAE) for not delivering on its commitment "to comply with the EU's good governance criteria". Since then the UAE has issued new legislation under Cabinet Resolution No. 31 of 2019 (the Resolution) which specifies the requirements for companies to have economic substance or a presence in the UAE. Although the Resolution was published on 19 June 2019, compliance with the requirements has been in force since 30 April 2019.

#### **Which entities does the Resolution apply to?**





Under the Resolution, the Economic Substance requirements apply to companies that generate income by carrying out the following relevant activities in the UAE, whether onshore or in the free zones including financial free zones:

- Banking;
- Insurance services;
- Investment fund management;
- Finance leasing;
- Headquarter activities related to (i) conducting management decisions, (ii) incurring operational expenditures on behalf of group entities, and (iii) coordinating group activities
- Shipping;
- Intellectual property services;
- Holding company activities; and
- Distribution and service center activities provided to non-UAE related persons including (i) transporting and storing spare parts, materials or ready-for-sale goods, (ii) managing inventories (iii) taking orders, and (iv) providing consulting or other administrative services.

### **What are the requirements for companies under the Resolution?**

Companies in the UAE that carry out any of the above activities must:

1. **Maintain actual Economic Substance**, in particular:
  - Carry out the Core Income-Generating Activity (**CIGA**) in the UAE;
  - Be directed and managed in the UAE; and
  - Have an adequate level of qualified full-time staff, operational expenditure and physical assets present in the UAE to conduct the CIGA. This requirement may also be met if there is an adequate level of expenditure incurred on outsourcing these to third party service providers in the UAE.
2. **Prepare and submit a compliance report to the regulatory authority** which should include information on the:



- Type of CIGA conducted;
- Amount and type of income arising from the CIGA;
- Amount and type of operating expenses and assets to conduct the CIGA;
- Location of place of business and, if applicable, plant, property or equipment;
- Number of full-time employees with qualifications and staff responsible for carrying out the CIGA; and
- A declaration of compliance with the Economic Substance test.

The compliance report must be submitted within 12 months from the end of the company's fiscal year. The form and method of submission will be determined by the regulatory authority (which shall be identified in a Cabinet decision) in due course.

More lenient Economic Substance requirements apply to holding companies that derive their income from dividends and capital gains only. There are additional reporting requirements in case the CIGA is a "high risk" intellectual property business or in case the CIGA is outsourced.

### **What are the repercussions for non-compliance?**

Non-compliant companies could risk fines and penalties, suspension, withdrawal or non-renewal of licenses, and the disclosure of their position to other foreign authorities.

An administrative fine of not less than AED 10,000 and not more than AED 50,000 shall be imposed when the Economic Substance requirements are not met or for failure to provide information or for providing inaccurate information. A penalty of not less than AED 50,000 and not more than AED 300,000 shall be imposed in the subsequent year for recurring non-compliance. In addition, the regulatory authority may decide to suspend, withdraw or not renew the commercial license of the company.

If the regulatory authority decides that the company has not met the Economic Substance requirements, the information submitted by the company shall be provided to the Ministry of Finance, which in turn,



shall share the information with foreign authorities subject to provisions in international agreements (e.g. double tax treaties). The information submitted by companies that carry out "high risk" intellectual property activities are in all cases reported to the Ministry of Finance and the relevant foreign authority.

### **What does this mean for you?**

Companies in the UAE should:

1. Assess whether their activities qualify as CIGA under the Resolution; and if so,
2. Analyze whether they meet the specific Economic Substance requirements for the CIGA.

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