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Overview of the Corporate Tax Guide CTGDTI1: **Determination of Taxable Income**

The Guide can be accessed here

2024

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Step 1. Determination of Accounting Income

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Basis of Accounting

Cash Basis of Accounting*

An accounting method under which the Taxable Person recognises income and expenditure when cash payments are **received and paid**

* before the revenue exceeds AED 3,000,000, or, in exceptional circumstances and pursuant to an application. **Case Study 6.**

A Taxable Person shall apply the **International Financial Reporting Standards** (IFRS).

A Taxable Person deriving Revenue that does not exceed AED 50,000,000 may apply **International Financial Reporting Standards for small and medium-sized entities** (IFRS for SMEs).

Accrual Basis or Accounting

An accounting method under which the Taxable Person recognises income when earned and expenditure when **incurred**

Taxable Persons deriving Revenue exceeding AED 50 million during the relevant Tax Period are required to maintain **audited Financial Statements**

Step 2. Accounting Income → Taxable Income

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Article 20(2) of the Corporate Tax Law. *The Taxable Income for a Tax Period shall be the Accounting Income for that period, and to the extent applicable,* ***adjusted*** *for the following*

Accounting Income

+/-	unrealised gain or loss
+/-	exempt income (exempt losses)
+/-	reliefs
+	non-deductible expenditure
+/-	adjustments for Related Party transactions not at arm's length
-	incentives/special reliefs*
+/-	adjustments specified in a Ministerial Decision

Taxable Income before Tax Loss relief

-	tax loss relief set-off

→ Taxable Income

**none at present*

Step 3. Taxable Income ➡ Tax Payable

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Taxable Income subject to Corporate Tax × Tax Rate = **Corporate Tax Liability**

- Withholding Tax Credit*
- Foreign Tax Credit

Corporate Tax Payable (Refundable)

**none at present*

Unrealized gains and losses

<table>
<tr><th colspan="3">Article 20(3) of the Corporate Tax Law
Election of basis for the accounting of gains and losses</th></tr>
<tr><td>Realization basis in relation to all assets and liabilities that are subject to fair value or impairment accounting under the applicable accounting standards</td><td>Realization basis in relation to all assets and liabilities held on capital account at the end of a Tax Period, whilst taking into account any unrealized gain or loss that arises in connection with assets and liabilities held on revenue account at the end of that period</td><td>no election</td></tr>
<tr><td colspan="2">To calculate the Taxable Income, Accounting Income must be adjusted by the amounts of gains and losses in relation to assets and liabilities according to the election made by a Taxable Person</td><td>No adjustments for an amounts of gains and losses recognized in FS.</td></tr>
</table>

✓ Realization basis can be elected only by a Taxable Person that prepares financial statements on an accrual basis

Case Study 7a.

Adjustments for the realization basis in relation to all assets (1), in relation to only for assets and liabilities held on capital account (2) and when no election of realization basis was made (3). Examples of adjustments by: unrealized gain on land, unrealized loss on inventory, impairment loss on shares (not sold).

Exempt Income

Domestic dividends	Exempt income, no additional conditions
Dividends and other profit distributions received from foreign juridical persons	Exempt income if the recipient has a Participating Interest in a foreign juridical person *(Article 23(2) of the Corporate Tax Law)*
Other income and gains received from the capacity of the shareholder as specified in *Article 23(5) of the Corporate Tax Law*	Exempt if they are derived from a Participating Interest
Income and associated expenditure derived from Foreign Permanent Establishments	Exempt based on the election of the Taxable Person

Expenditure incurred in relation to the acquisition, transfer, sale, etc. of the whole or part of the Participating Interest will not be deductible. Instead, this expenditure should be capitalized as part of the acquisition cost of the Participating Interest.

Deductible and non-deductible expenditure (1)

To be deductible expenditure must be incurred **wholly and exclusively** for business purpose
+ must not be capital nature

No deduction:
- expenditure/loss not for a business purpose
- expenditure incurred in deriving Exempt income

If expenditure is incurred for **more than one purpose**, the proportion of the expenditure that is incurred for non-Business purposes is not deductible for Corporate Tax purposes and must be added back when determining Taxable Income

Case Study 1
for the treatment of expenditure incurred for more than one purposes while determining Taxable Income

Deductible and non-deductible expenditure (2)

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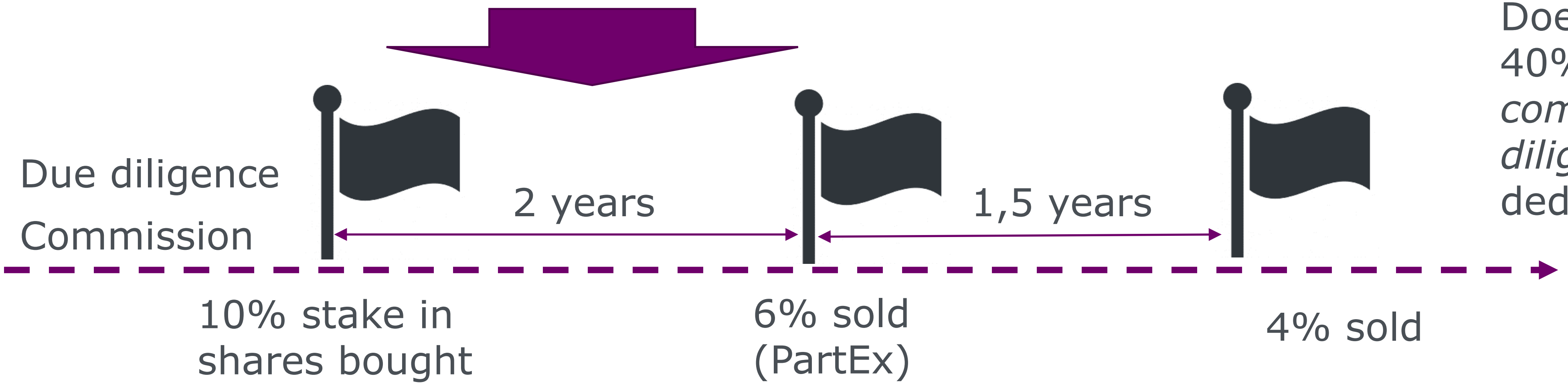
The Guide clarifies details of treatment for the following types of expenditures

Capital expenditure paragraph 4.5.6 of the Guide	not deductible expenditure. Shall be deductible in the calculation of gains or losses upon the realisation of the asset or liability	paragraph 4.5.6 of the Guide, Case Study 1, 6, 7a
Pre-incorporation or pre-trade expenses	will be allowed as a deduction to the extent to which it is recorded in the income statement once the company is incorporated	paragraph 4.5.7 of the Guide new
Creation & reversal of provisions (bad debts, write-off and recovery)	will be allowed as a deduction, as long as it satisfies the requirements for deductibility of expenditure under the Corporate Tax Law	paragraph 4.5.7 of the Guide new
Entertainment expenditure	50% deduction rule and exceptions. Incidental expenses, commercial hospitality, marketing or advertising expenditure	paragraph 4.5.10 of the Guide

Capital Expenditure

'No deduction shall be allowed for depreciation, amortisation or other change related to capitalised expenditure, where such expenditure would not have been deductible had it been an expenditure that is not capital in nature'.

*'Expenditures that are **capital in nature** that **have not been deducted** for the purpose of calculating the Taxable Income, other than those under the above bullet point, shall be deductible in the calculation of gains or losses upon the realisation of the asset or liability.'*



Does this mean that 40% of the *commission* and *due diligence* are non-deductible?

FTA’s comments on allocation of indirect expenditures

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Allocation keys – to assign or distribute costs across different departments, products, services, or divisions

In many cases, an allocation that prorates expenses based on Revenue will be considered as a reasonable allocation.

Other allocations keys approved in the Guide:

HEADCOUNT | FLOORSPACE | USAGE | TIME SPENT | OTHER

If the expenditure incurred for more than one purpose cannot be apportioned on a fair and reasonable basis, it will not be allowed as a deduction

FTA’s Criteria to check if allocation key is appropriate

Cause and effect: An allocation should be consistent with identifiable cause-and effect relationships (e.g., machinery running hours may be an appropriate allocation key to allocate maintenance costs).

Benefits derived: An allocation should be commensurate with the benefits received.

Logic and fair representation: for the benefit that the expense generates for each income component.

Consistency: The allocation key should also be used consistently for each Tax Period, unless there is a change in fact pattern which may justify a change in allocation or methodology.

Employment Related Expenditure

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… it is not relevant whether an employee is paid wholly in cash or also receives other benefits, such as a car for personal use (for spouse and children). In other words, the cost is wholly and exclusively for Business purposes as rewarding employees is wholly a Business purpose.

Personal Car

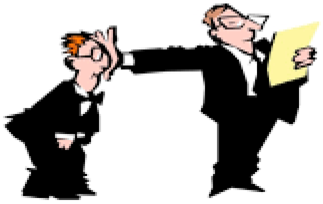
Flight allowance

Entertainment of employees

Family Insurance

Other

In these situations, '*the personal use should be viewed in the same way as the employee spending their cash salary on items for their personal benefit…*



Arm's Length

FTA's Example: '*the salary or bonus paid to* ***directors or officers*** *of a company* ***or an owner*** *of the Taxable Person would be deductible when determining Taxable Income, but only insofar as this salary corresponds with the Market Value rates for such services rendered*'.

Employee benefits for home working

NEW

✓ Expenses incurred due to an exclusively work-from-home arrangement are **deductible**

Case Study 1

Home office setup and a portion of **utility bills** are **deductible**

-

incurred wholly and exclusively for the Business of the employer

No clarifications on what consists the home office setup?

- new or past broadband expenses
- phone use
- online subscriptions (Zoom, Microsoft Office etc.)
- printer and supplies
- office supplies
- repairs and maintenance
- furniture (can be depreciated?)

How to allocate (e.g. for the utility bills)

Interest Expenditure.
General Interest Deduction Limitation Rule (GIDLR)

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Interest expenditure

↓

General rules for deductibility *(Articles 28 and 29 of the Corporate Tax Law)*

↓

General Interest Deduction Limitation Rule *(Art. 30 of the Corporate Tax Law)*

Basic components to apply General Interest Deduction Limitation Rule
1. To know the Meaning & Components of '**Interest**'. *Paragraph 4.6.1 of The Guide*
2. To calculate **Net Interest Expenditure**: Interest expenditure less Interest income + adjustments. *Paragraph 4.6.3 of The Guide*
3. To calculate **30% of adjusted EBIDTA**. *Paragraph 4.6.4 of The Guide*
4. Note **de minimis** – AED 12 million

Case Study 2, 4.

All the key and necessary requirements for compliance with the GIDLR are established in the Corporate Tax Law and the Ministerial Decision № 126 of 2023. The Guide combines these rules into a single document, explains them in user-friendly language, and provides practical examples of calculating the specified amounts and necessary adjustments.

Tax Loss

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Year 1

Company A
(1) reflects Tax Loss
(2) transfers* Tax Loss
to Company B

transfer

Company B

Deducts Company A's tax loss up to 75% of Company B's Taxable Income

Year 2

Company A
(1) must deduct remaining loss up to 75% of Company A's Taxable Income
(2) transfers remaining Tax Loss to Company B

transfer

Company B

Deducts Company A's tax loss up to 75% of Company B's Taxable Income

Notes

- a Taxable Person must use Tax Loss in the next Tax Period (cannot carry them forward)
- before transferring the Tax Loss to the other Company a Taxable Person must deduct it itself (up to 75% of the Taxable Income)
- a Taxable Person must first utilise its own brought forward Tax Losses before it can utilise a Tax Loss transferred to it
- there's a limitation rule on carry forward of Tax Loss in case of the change in ownership

Case Study 3, 5.

** the conditions to transfer the Tax Loss are set in Art. 38(1) of the Corporate Tax Law*

Tax Credits

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A Foreign Tax Credit – a Tax paid under the laws of a foreign jurisdiction on income or profits that may be offset against the Corporate Tax liability in UAE

The amount of Foreign Tax Credit is the lower of the following:

- the actual amount of tax paid on foreign source income in the foreign jurisdiction

- the amount of the Corporate Tax due in the UAE on the foreign source income*

** the amount of the Corporate tax Due on the foreign source income = X * Y/ Z, where:*
X= Corporate Tax due on total Taxable Income of the Taxable Person before any Foreign Tax Credit,
Y= Relevant net foreign source income, and
Z= Total Taxable Income of the Taxable Person

- any foreign tax that is similar to corporate tax
- the same tax period
- foreign source income must be included in the Taxable Income of the Taxable Person

Taxation of Non-Resident Persons

Permanent Establishment

Nexus

(i.e. Immovable Property situated in the UAE)

A Non-Resident Person is subject to Corporate Tax in UAE in relation to the Taxable Income that is attributable to Permanent Establishment or nexus

Separate entity approach. Arm's length principle between a Person and it's PE

How to attribute the profit between the PE and its parent:
Step 1. Conduct a functional analysis to identify the functions performed by the PE on one side, and the head office on the other side, treating each as separate to the other. This analysis should also take into account the assets used and the risks assumed by the PE and the head office, respectively
Step 2. Determine the compensation relating to arrangements or dealings between the PE and the head office, commensurate with their respective functions performed, assets deployed, and risks assumed

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