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Emirati IP box regime for an embedded income

In October 2023, the UAE retrospectively introduced tax benefits for the ownership and exploitation of intellectual property. Income from patents or software and other qualifying IP assets can be in the scope of the 0% Corporate Tax rate. The regime is guided by the OECD guidelines highlighted in the final BEPS report on Action 5.

The benefit is available not only for purely IP business, but also for businesses that use IP to manufacture products or provide services, generate income from an exploitation of software and other IP in trading, etc. Embedded income (or notional royalties) can also be zero-rated.

Embedded IP income and 0% rate

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The Minister: Overall Income - royalties or any other income derived from Qualifying Intellectual Property as determined according to the provisions of the Corporate Tax Law, **including embedded intellectual property income derived from the sale of products and the use of processes directly related to the Qualifying Intellectual Property** as determined in accordance with the arm's length principle under Article 34 of the Corporate Tax Law.



In our recent webinar, we dwelled on the uncertainties and complexities that companies may face in when applying these provisions.

There is limited guidance from the authorities on the application of the above Ministerial rule. Therefore, we refer to international experience. This approach

is relevant because these practices are based on OECD guidelines and clarify the meaning of commonly used terminology.

Embedded IP international experience


Portion of income from sale

'...Where the sales price of a product or service', Overall Income from IP includes an amount 'which is attributable to a qualifying asset, such **portion of the income from those sales** as, on a just and reasonable basis, is **attributable to the value of the qualifying asset**'


Embedded royalties

actual embedded royalties

any amounts attributable to the sale of copyrighted materials relating to a qualifying asset then only the **portion of the sales price** which relates to those embedded royalties will form part of the overall income from the qualifying asset.

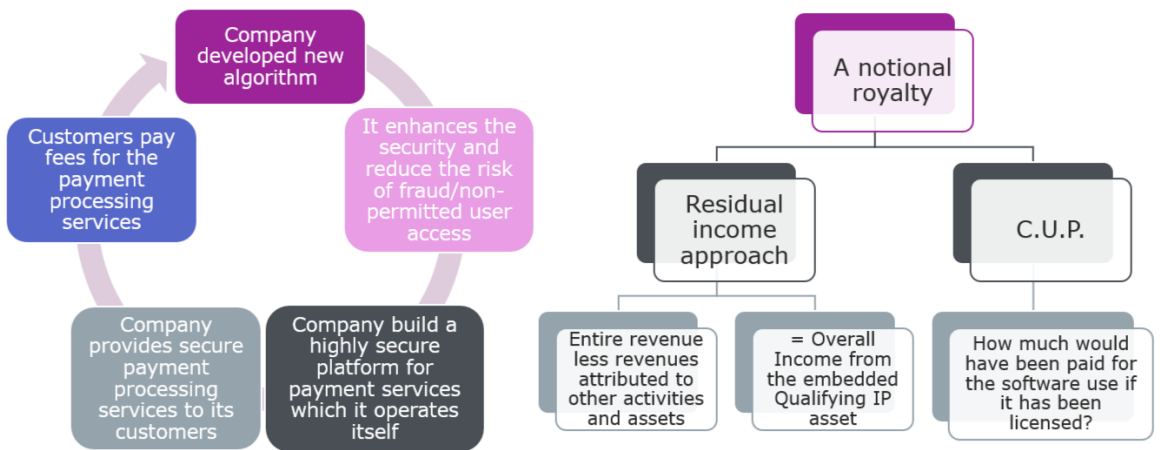


Tax and Duty Manual
Guidance Notes on the Knowledge Development Box
Part 29-03-01
This document should be read in conjunction with Chapter 5 of Part 29 of the Taxes Consolidation Act 1997
Document last reviewed November 2022



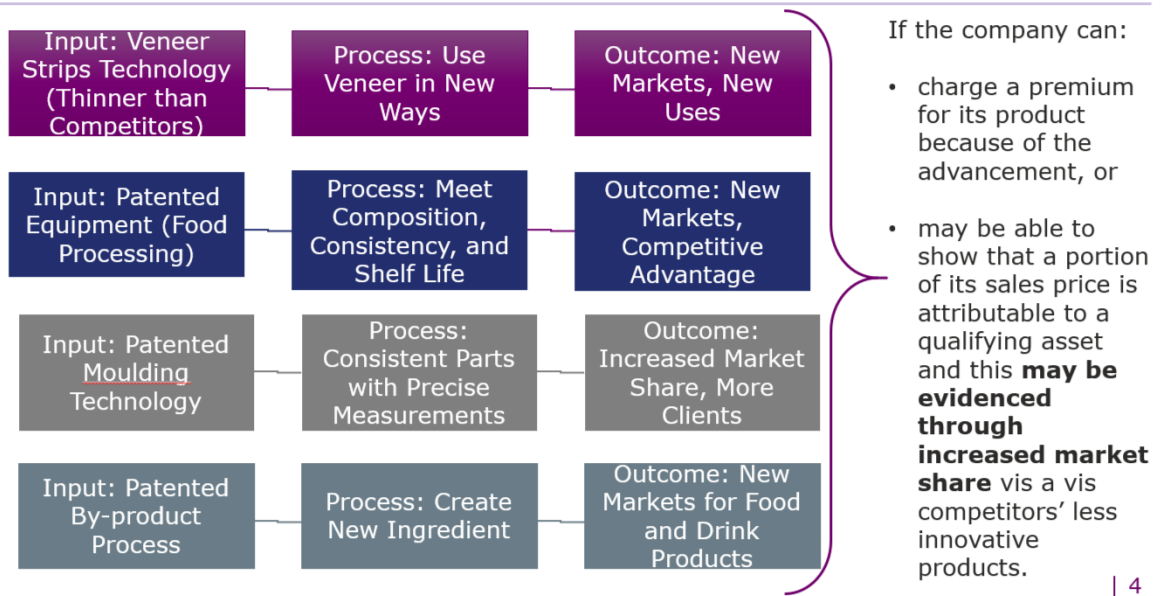
We dwelled on specific scenarios (see slide below on the left) and addressed the tools available to allocate incomes to qualifying IP assets.

Transfer Pricing to identify Embedded Income



As shown in the examples below, the OECD's approach, which the UAE intends to implement, does not prevent the application of benefits for embedded IP, even if there is no separate charge for it.

Embedded IP: international practice



Nevertheless, the benefit is only allowed in scenarios where the IP is integrated into processes to generate income, rather than to reduce costs.

Embedded IP: when the benefit is not allowed



Research Ltd ... come up with a new process, for which they obtain a US patent following substantive examination for novelty and inventive step. Research Ltd uses the process to make its R&D procedures more effective and reduce costs. ... From Research Ltd.'s perspective, as the process **reduces costs, rather than being reflected in the sales price of the resulting product, it is not a qualifying asset in respect of which it is in receipt of any income.**

However, the FTA's interpretation of the embedded income provisions introduces risk, as demonstrated below.

The risks inherent to embedded royalties

MoF: Overall Income - royalties or any other income derived from Qualifying Intellectual Property as determined according to the provisions of the Corporate Tax Law, **including embedded intellectual property income derived from the sale of products and the use of processes directly related to the Qualifying Intellectual Property** as determined in accordance with the arm's length principle under Article 34 of the Corporate Tax Law.

FTA: This requires a **separately identifiable income stream** that is **directly attributed to the intellectual property**, such as royalties, licence fees, and capital gains.



Income that is generated indirectly when embedded intellectual property is used to contribute to a product or service for which no separate remuneration is received from the intellectual property would not be considered to generate income from the ownership or exploitation of intellectual property for purposes of the de minimis requirements.

Likely to result in a disqualification



Keep in touch with us to stay updated on further developments.

Disclaimer

Pursuant to the [MoF's press-release](#) issued on 19 May 2023 "a number of posts circulating on social media and other platforms that are issued by private parties, contain inaccurate and unreliable interpretations and analyses of Corporate Tax".

The Ministry issued a reminder that official sources of information on Federal Taxes in the UAE are the MoF and FTA only. Therefore, analyses that are not based on official publications by the MoF and FTA, or have not been commissioned by them, are unreliable and may contain misleading interpretations of the law.

See the full press release [here](#).

You should factor this in when dealing with this article as well. It is not commissioned by the MoF or FTA. The interpretation, conclusions, proposals, surmises, guesswork, etc., it comprises have status of the author's opinion only. Like any [human](#) job, it may contain inaccuracies and mistakes that I have tried my best to avoid. If you find any inaccuracies or errors, please let me know so that I can make corrections.