

# UAE Free Zone Qualifying Conditions – A Snapshot

June 2023

## Background

UAE introduced federal decree-law on corporate tax, called the Federal Corporation Tax ('CT') on 9th December, 2022. In the previous editions of UAE Transfer Pricing ('TP') bulletin we had provided an overview of the salient features of UAE regulations and clarifications provided via different ministerial decisions published subsequently.

In this edition, we dive further into two new decisions that together specify the main features of the CT Law as it applies to juridical persons operating out of free zones in the UAE. These include Cabinet Decision No. 55 of 2023 published on May 30, 2023 on determining qualifying income, as well as Ministerial Decision No 139 of 2023 published on June 1, 2023 on Qualifying Activities and Excluded Activities. Below is a summary of the key aspects of these decisions.

## Snapshot

The UAE CT Law introduced a category of taxpayers that can be subject to corporate tax at the reduced rate of 0 – the Qualifying Free Zone Persons (QFZPs). Further, it is stated that this zero per cent corporate tax (CT) is applicable on the qualifying income (QI) of the QFZP, and the non-qualifying income (NQI) of the QFZP is subject to tax at nine per cent.

### Qualifying Income

The Free Zone CT regime is intended to apply only to income derived from activities that are performed exclusively in or from within a Free Zone. This is reflected in the definition of 'Qualifying Income' which includes:

- Income derived from transactions with other Free Zone Persons, except for income derived from "**Excluded Activities**".
- Income derived from transactions with a Non-Free Zone Person, but only in respect of "**Qualifying Activities**" that are not **Excluded Activities**.
- Any other income provided that the QFZP satisfies the "**de minimis**" requirements.

## **Qualifying Activities**

The 'Qualifying Activities' include manufacturing of goods or materials; processing of goods or materials; holding of shares and other securities; ownership, management, and operation of ships; reinsurance services; fund management services that are subject to the regulatory oversight of the competent authority in the UAE; and wealth and investment management services that are subject to the regulatory oversight of the competent authority in the UAE. They also include headquarter services to related parties; treasury and financing services to related parties; financing and leasing of aircraft, including engines and rotatable components; logistics services; distribution in or from a designated zone that meets the relevant conditions; and any activities that are ancillary to the above-mentioned activities.

## **Excluded Activities**

The "excluded activities" with few exceptions and conditions includes the activities with natural persons, banking activities, insurance activities, financing and leasing activities, ownership, or exploitation of immovable property (other than commercial property located in a free zone, where the transaction in respect of such commercial property is conducted with other free zone persons) and intellectual property assets, and any activity that is ancillary to any of these activities.

## **De minimis Requirement**

Earning income from 'Excluded Activities' or earning any other income that is not 'Qualifying Income' will disqualify the Free Zone Person from the regime, subject to de minimis requirements. To satisfy the de minimis requirements, the non-qualifying revenue earned by a Free Zone Person must not exceed the lower of either 5% of their total revenue or AED5,000,000. The Decision also provides information on how the above limit should be calculated.

## **De minimis Requirement (contd)**

Revenue attributable to a domestic or foreign permanent establishment of the Free Zone Person and revenues attributable to immovable property located in a Free Zone that cannot benefit from the Free Zone Corporate Tax regime will not count towards the de minimis threshold. Instead, the associated taxable income will be subject to the regular UAE Corporate Tax regime at 9%.

## **Substance Requirement**

The decisions also provide clarity on how to maintain substance in the UAE Free Zone, the business needs to undertake its core income-generating activities in the Free Zone, and satisfying this condition will take into account whether the business; has adequate assets in the Free Zone; has an adequate number of qualified employees in the Free Zone; incur adequate amount of operating expenditures in the Free Zone.

## **Other Conditions**

- Observing the above limit, along with maintaining the audited financial statements has been listed as one of the conditions to benefit from the QFZP.
- Where the de minimis requirements are not met or the Free Zone Person does not continue to meet any of the other qualifying conditions, the Free Zone Person will no longer be able to benefit from the Free Zone Corporate Tax regime for a minimum period of five (5) years. During this period, the Free Zone Person will be treated as an ordinary Taxable Person and be subject to Corporate Tax at the rate of 9% on their Taxable Income above AED 375,000.

## AMICUS COMMENTS

Much awaited clarity has now been provided on which incomes of a free zone entity / person would be considered as “Qualifying Income” subject to tax at 0%. The decisions provide much-needed guidance and understanding of conditions that need to be satisfied by a taxpayer to obtain the QFZP status. It is to be noted that both these decisions (Cabinet Decision No. 55 of 2023 and Ministerial Decision No. 97) should be read in conjunction with each other to obtain a full understanding of the proposed rules.

For transactions with related parties one important qualifying condition is that transactions must be at arm’s length if Free Zone Benefit of Nil Corporate Tax is to be availed.

In light of this significant development, it would be advisable for a free zone entity / person to conduct an impact assessment of these clarification at the earliest.

## ABOUT AMICUS

Amicus is legal and tax consulting firm with focus on corporate finance, re- structuring, private equity, international taxation, transfer pricing and goods and services tax. The Firm's tax team also represents clients in assessments and litigation including Tax Tribunal and Higher Courts.

The Firm focuses on providing efficient, effective, solution- oriented advice and representation based on specialist knowledge and experience. Amicus' boutique tax practice has been consistently ranked as a leading practice by Legal 500, Asia Law and World Tax (ITR).



## Our Locations

**Delhi** I-1, Jangpura Extension  
New Delhi-110014

**Tel: 011-4155 3433**  
**011-4054 1821**

**Noida** 620, Tower B, Advant Business Park,  
Plot #7, Noida-Greater Noida Expressway,  
Sector 142, Noida,  
Uttar Pradesh - 201305

**Tel: +91 120 429 2578**

**Mumbai** DBS Business Center, Bldg. No., 213,  
Raheja Chambers, 2nd Floor, Free  
Press Journal Marg, Nariman Point,  
Mumbai - 400021. INDIA

**Tel: +91 22 4050 9490**

**Email: [info@amicusservices.in](mailto:info@amicusservices.in)**

**Web: [www.amicusservices.in](http://www.amicusservices.in)**

### **Key Contacts:**

[ashutosh@amicusservices.in](mailto:ashutosh@amicusservices.in)

[shivi@amicusservices.in](mailto:shivi@amicusservices.in)

[madhav@amicusservices.in](mailto:madhav@amicusservices.in)

[kinshuk@amicusservices.in](mailto:kinshuk@amicusservices.in)