How taxing has it become to invest in the UAE

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***"I want a government that toils 24 hours a day, just like airlines. I want it to be close to people, welcoming all clients akin to that welcome received by hotel guests. I want the citizens to be able to process all their government transactions in one place, on a mobile one stop shop."* – His Highness Sheikh Mohammed Bin Rashid Al Maktoum**

Introduction

The government of every country has the right to legislate and enact laws for their territory and choose the best form of tax system that may suit the needs of their economy. The quote above, by the Prime Minister of the United Arab Emirates and the Ruler of Dubai, demonstrates an intention to make the UAE the best possible place for residents and investors alike. However, due to the forces of globalisation, every country is required to align its governance and legal systems with international standards to promote capital inflows into the country.

OECD measures on tax policy

One of the key changes in legal systems across the globe has been in relation to establishing stable tax policies and fair tax regimes. The Organisation for Economic Co-operation and Development ('OECD'), an intergovernmental economic organisation, has been a key driver in stimulating economic progress, world trade, transparency, and certainty in tax policies across the globe. As a means of guiding global tax authorities and corporate taxpayers in relation to anti-tax avoidance measures, the OECD published a package of measures in 2015 to prevent tax base erosion and reduced profit sharing (so-called 'BEPS'). According to the OECD, revenue losses from BEPS are estimated at between US$100 billion and US$240 billion annually.

Some of the 15 key measures to address BEPS concerns listed by the OECD include:

- Provisions to prevent treaty shopping/abuse;
- Provisions relating to standardized country-by-country reporting, so as to provide tax authorities with a global view of where a company's economic activities are reported and the ability to evaluate transfer pricing and other BEPS risks; and
- A peer-review process, including a commitment to transparency through the obligatory exchange of information and changes to the transfer pricing guidelines to ensure that the transfer pricing of corporates is aligned with their economic activity.

A Multilateral Convention on Mutual Administrative Assistance in Tax Matters ('Convention') was developed by the OECD and the Council of Europe in 1998 and was amended in 2010 to align it with international standards on exchange of information. The Convention provides for administrative assistance in tax matters, including:

- Exchanges of information on request;

- Spontaneous exchanges of information;
- Automatic exchanges of financial account information;
- Tax examinations abroad; and
- Assistance in tax collection.

Common Reporting Standards ('CRS') were developed after a request from the G20. They were approved by the OECD Council in 2014, and require countries to obtain information from banks and financial institutions and automatically exchange that information with other countries on an annual basis. The CRS sets out the details of the financial information to be exchanged, the extent of reporting required by banks and financial institutions, as well as common due diligence (know your client) procedures to be followed by banks and financial institutions in relation to the determination of a customer's tax status and domicile.

BEPS and greater disclosure proposals are focused against tax strategies that companies use to take advantage of the differences in each country's tax rules, shifting profits to low-tax or no-tax jurisdictions, even though a company may have little or no economic activity there.

UAE policy alignment with global standards

While the UAE is not an OECD member, the OECD project has generated considerable interest in the region due to the changing global tax landscape and international pressure on aligning tax policies. The Convention was signed by the UAE on 21 April 2017 with a commitment by the UAE to its first exchange of information by 2018. The UAE also joined the Global Forum on Transparency and Exchange of Information for Tax Purposes in 2010. The UAE Ministry of Finance's commitment to implementing higher standards in relation to the exchange of information is demonstrated two-fold. First, through its continuing effort to establish infrastructure to implement an automated system to collect and exchange information; second, through its negotiation of memoranda of understanding with related authorities to enable financial institutions to submit periodic reports according to data protection laws. These efforts to implement international standards have led to the UAE obtaining a seat on the International Steering Committee ('ISC') for the exchange of information.

With the recent inclusion of the UAE by the European Union in a list of countries it considers guilty of offering unfair tax avoidance schemes, the UAE is actively considering implementing measures to prevent tax BEPS. In a statement by the UAE Government in response to its inclusion in the EU tax havens list, it commented that the UAE is working to adhere to the EU's requirements in relation to exchange of information and to implement policies to avoid BEPS, which will be finalised by October 2018, so as to be removed from the EU's list. The UAE has in the recent past demonstrated its commitment through additional rules and regulations being imposed on financial institutions by the UAE Central Bank in relation to reporting on financial crimes and ensuring compliance. There will likely be no significant impact in the long term as a result of its inclusion in the EU's tax havens list. In any event, the EU finance ministers have not been able to agree on sanctions/measures that could be imposed on the jurisdictions in the list.

Impact on businesses in the UAE

With increased disclosure norms and reporting requirements being imposed in the UAE, there is no doubt that businesses in the UAE will be affected. The question here is whether there is a positive or negative effect. The immediate concern is that increased reporting requirements may usher in a sense of negative sentiment, at first, as currently the UAE has no corporate tax regime. However, in reality the increased reporting requirements should be viewed positively as increased reporting obligations in the UAE are likely to result in negligible impact on the multinational corporates in their home country. This is because the UAE is not a typical low/no-tax jurisdiction where no economic activity actually takes place.

Another advantage of implementing the OECD proposals for businesses in the UAE would be certainty with regards to determination of tax domicile or residence. For example, many multinationals in the UAE may be facing issues or hurdles in obtaining tax treaty benefits in their home countries on account of the UAE being a no-tax jurisdiction. However, with implementation of the OECD proposals, certainty will be accorded to the tax residence of companies in the UAE affording tax treaty benefits for the profits and income generated in the UAE. Therefore, increased reporting requirements are likely only bound to align the UAE more closely with international standards, making it a secure jurisdiction for multi-national corporates to invest in and carry on business operations due to certainty in according tax residence to the entities in the UAE.

The reporting requirements of the BEPS proposals, which may include the implementation of transfer pricing provisions in some form, may prove to be a challenge for businesses in the UAE. Currently there is a lack of awareness and experience in the region on undertaking transfer pricing audits and assessments. Transfer pricing is the rate at which two related parties in the same group carry out transactions with each other, which is determined by a myriad of factors, including what an arms-length price for a similar transaction would be. Businesses implementing transfer pricing guidelines and complying with greater disclosure norms (if BEPS proposals were to require so in the UAE) may be required to incur greater compliance costs in the first few years. However, this may only be an initial inconvenience where corporates are able to quickly adapt their supply chains and revenue streams to be in accordance with globally adopted transfer pricing guidelines and reporting requirements.

Conclusion

The recent inclusion of the UAE in the EU’s list of tax haven countries and UAE’s committed efforts to adopting tax policies in line with international standards is a sign for businesses in the UAE to simplify and rationalise their group structures. UAE businesses should now also focus on maintaining proper accounting records and information to avoid the risk of being unfairly taxed on account of providing inaccurate or inadequate data.

As part of the World Bank’s 2018 ranking, the UAE ranks 21st out of 189 countries on ease of doing business, with a marked improvement over its previous year’s ranking. With the country being focused on complying with global standards on tax policies, the ease of doing business is only likely to improve due to the impact of archetypal inefficiencies caused by uncertainties being minimised.