



## FACT SHEET: UAE ECONOMIC SUBSTANCE

### LAW BRIEFING

#### How does the Economic Substance Law affect your business in the UAE?

##### Overview

On 30 April 2019, the UAE Cabinet issued the Cabinet of Ministers Resolution No. 31 of 2019 Concerning Economic Substance Regulations in the UAE, (**ESR**), with a further guidance issued on the application of the ESR on 11 September 2019, requiring all in-scope UAE entities (**Relevant Entities**) that carry on certain activities (**Relevant Activities**) to have demonstrable economic substance in the UAE. The ESR is now in force and UAE entities are required to comply with them.

The ESR creates the basis for the UAE to meet the requirements of the European Union Code of Conduct Group (business taxation) in respect of economic substance and in particular, to ensure that the jurisdiction does "not facilitate structures or arrangements aimed at attracting profits which do not reflect real economic activities and substantial economic presence".

The introduction of the ESR demonstrates the UAE's ongoing efforts on meeting the highest international standards on taxation, including the OECD's requirements.

#### When did the ESR become enforceable?

Existing entities were required to comply with the ESR from 30 April 2019 with the first economic substance declaration (the **Report**) due in 2020 within 12 months from the end of their financial year.

#### What is the reportable financial year?

The first reportable financial year starts from 1 January 2019 onwards. Where an entity starts its financial year on 1 January 2019, ending 31 December 2019, the assessable period shall be 1 January 2019 to 31 December 2019 and the Report would need to be submitted by 31 December 2020. Whereas for an entity with a financial year starting 1 April 2019, ending 31 March 2020, the assessable period shall only be from 1 April 2019 to 31 March 2020 and the Report can be submitted by 31 March 2021. As for new entities, the compliance is required upon receiving its license, with the first Report due within 12 months from the end of their first financial year.

#### How will the monitoring and enforcement be carried out?

You will be asked to confirm whether you are undertaking a Relevant Activity. All Relevant Entities will be required to prepare and submit the Report to the regulatory authority, which should include information on the type of key essential activities that generate the income of the entity being carried out [known as the Core Income Generating Activity (**CIGAs**)], amount and type of income arising from the CIGAs, location and place of business and the number of full-time employees.

#### Do the requirements vary depending on the Relevant Activities?

Yes, there are certain exceptions in the ESR, depending on the type of activity undertaken by the company, for example

- > Relevant Entities undertaking certain "high-risk intellectual property" business will be subject to relatively higher standards of economic substance and more detailed reporting requirements;
- > Relevant Entities undertaking equity holding company business are subject to relatively reduced level of economic substance requirements.

Summary of ESR Reporting Dates for Relevant Entities

Date of Incorporation of the Relevant Entity	Financial Year	Assessable Period	Report Due
Relevant Entities incorporated before 30 April 2019	1 January 2019 – 31 December 2019	1 January 2019 – 31 December 2019	31 December 2020
	1 April 2019 – 31 March 2020	1 April 2019 – 31 March 2020	31 March 2021
	Other	From the start date until the end date of the first financial year ending after 30 April 2019	12 months from the end of the first financial year ending after 30 April 2019
Relevant Entities incorporated on or after 30 April 2019	As per the Relevant Entity's Memorandum and Articles	From the date of incorporation to the end of the first financial year	12 months from the end of the first financial year



### Is your entity captured by the ESR?

**Q1: Are you registered as a UAE onshore or free zone or offshore company via the following?**

- Limited liability company
- Limited partnership
- Sole establishment
- Private joint stock company
- Branch office of a foreign company
- Representative office of a foreign company

Entities that are directly or indirectly at least 51% owned by the Federal or an Emirate Government Entity, or a UAE Government body or authority, are exempt from the ESR.

**Q2: Does your entity generate income?**

If your current activity is generating income, then continue to Q3.

**Q3: Is the income being generated from any of the below "relevant activity"?**

- Banking Business
- Insurance services
- Fund Management business
- Headquarters business
- Holding company business
- Intellectual Property holding business
- Shipping business
- Distribution and service Centre business, and
- Finance and leasing business

If the answer is yes to Q1, Q2 and Q3, your entity will need to satisfy the "Economic Substance Test" requirements below:

- be directed and managed in the UAE
- have adequate qualified employees in the UAE
- have adequate operational expenses in the UAE
- have physical assets in the UAE
- conduct the CIGA in the UAE

Alternatively, the test can be met by outsourcing the above requirements to third-party service providers in the UAE.

### What are the implications of non-compliance?

Annual administrative penalties of AED 10,000 – AED 300,000 can be imposed on entities if they fail to comply with the ESR, or if they provide inaccurate or false information to the regulatory authority. Licenses may be suspended, withdrawn or not renewed.

### Are there any implication with exchange of information?

Besides the fines, the ESR stipulates that the tax authorities may exchange information on non-compliant UAE registered companies with the tax authorities in the State where their holding companies and UBOs are resident.

*For all core requirements introduced by ESR outsourcing to a corporate service provider (CSP) all or part of the requirements (i.e. occupy non-executive functions, and /or coordinate the handling of meetings, maintenance of records, undertaking all or part of the conduct of the CIGA) is permitted. This option comes with a caveat as certain important conditions must always be met by the CSP (i.e. having adequate levels of resources in the UAE in connection with the CIGA) for the Relevant Entity to satisfy the Economic Substance Test in these circumstances.*

### Our Recommendation

We highly recommend taking immediate action to assess your company's standing against the provisions of the ESR. As a first step, determine the specifics on your company's activity, for example, does your holding company conduct other activities that will fall under the scope of the substance requirements or, alternatively, how to interpret the notion of "Distribution or Service Centre" and confirm whether the services you are providing are connected? These are the type of questions we can help you answer following a diagnostic of your current status.

### How can we help you?

Banks Legal Consultancy can support you in assessing the qualification of your company for the test. We propose to undertake a diagnostic on your company's status vis-à-vis the ESR and advise you on the necessary level of economic substance for your entity to meet compliance tests (assuming you are required to do so). We will at the same time audit your corporate arrangements with the view to bringing in necessary level of corporate substance.



### Have you considered that you can have the substance adequately outsourced to you?

We offer a one stop shop service – [see our bespoke corporate packages](#) to provide local economic substance for your entity.

We are happy to discuss the implications on your business of the additional obligations that have recently been triggered by the introduction of the ESR in the UAE. Following our review, we will identify potential gaps (if any) and help you to define a strategy and implement the most cost and time effective solution.



## About us

Founded in 2009 by the Managing Partner Nathan Banks, Banks Legal & Corporate Services is a legal and corporate services consulting firm based in the United Arab Emirates. With over 100 years of combined professional experience in the UAE, our lawyers harness leading international law firm experience with extensive knowledge of the GCC legal and business landscape. Our clients are broad, encompassing a variety of industries and sectors, and range from individuals to family offices, SME's and reputed listed multinationals.

Whilst specializing in all core areas of law, providing strategic commercially focused business advice, Banks Legal & Corporate Services also provides an extensive suite of corporate services through Banks Corporate Services.

Core to our values is a strong commitment to client service and responsiveness and we pride ourselves on quickly identifying legal issues and providing pragmatic solutions. As an entrepreneurial minded firm, we take the time to understand client instructions from the perspective of their business in order to add value beyond the specific scope of work.

Our dedicated multi-cultural and multi-lingual team includes civil and commercial lawyers and staff from across the globe with international law firm experience. With our strategic presence spanning across the region with offices in Abu Dhabi, Dubai and Ras Al Khaimah and regional co-operation arrangements with reputable professional services firms, we are very well placed to provide clients with key support and legal services, who do business throughout the GCC and wider Middle East & North Africa region.

## Team



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