Corporate Tax in the UAE

Tax Accounting Considerations

April 2023

Enacted or substantively enacted status of law

In brief

As companies begin to focus on financial reporting in 2023, there are important corporate income tax considerations to evaluate and assess. The UAE Federal Corporate Tax Law is now considered as enacted for the purposes of International Financial Reporting Standards ("IFRS"). Despite no current income tax accounting being required yet, companies need to consider whether to account for deferred income taxes for reporting periods ended on or after 16 January 2023. To assist companies in navigating the accounting for deferred income tax impacts during the interim reporting period, this alert highlights some key areas to consider.

In Detail

About the Corporate Tax Law

On 10 October 2022, the Corporate Tax Law appeared in the Official Gazette (becoming legally effective 15 days later). On 9 December 2022, the UAE Ministry of Finance ("MoF") published the full text of the law Federal Decree-Law No. 47 of 2022 on the Taxation of Corporations and Businesses (the "Corporate Tax Law", the "Law"). This means businesses will be subject to UAE Corporate Tax ("Corporate Tax") from the beginning of their first financial year that starts on or after 1 June 2023. Per the Cabinet of Ministers Decision No. 116 published on 16 January 2023, a standard rate of 9% (nine percent) will apply to taxable income exceeding a threshold of AED 375,000, and a rate of 0% (0 percent) will apply to taxable income not exceeding that threshold.

Enactment and substantive enactment

International Accounting Standard 12 Income Taxes (IAS 12) requires *companies to measure deferred tax assets and liabilities at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period*. With the Cabinet Decision specifying the tax threshold having been issued, the Law is now assessed and considered to be "enacted" effective 16 January 2023

Based on the above, companies have to assess the deferred tax implications and the estimated deferred tax [Deferred Tax Assets (DTA) / Deferred Tax Liabilities (DTL)] for reporting periods on or after 16 January 2023, including interim reporting.

Key considerations for interim tax accounting

Transitional Rules

A Taxable Person’s opening balance sheet for corporate income tax purposes will be the prior period closing accounting balance sheet for many financial statement line items, subject to any conditions or adjustments prescribed by future Cabinet Decisions. For these initial reporting periods, this should generally simplify calculation of deferred tax for taxpayers. However, the transitional rules include some areas requiring further consideration, such as:

- this principle is “subject to any conditions or adjustments that may be prescribed by the Minister”;
- the balance sheet of any company should be prepared taking into consideration the arm’s length principles, i.e. where there are intercompany balances, their recorded value should be after the applications of transfer pricing principles.

Further considerations could arise where companies have not previously prepared standalone financial statements, or where there are material tax sensitive consolidation adjustments.

Potential Exemptions

Although the Law potentially exempts many companies (or subjects them to tax at a rate of 0%), some of these companies could be viewed as taxable as the Law currently stands. This is particularly applicable where exemptions are conditional on the specific approval of the Cabinet or Tax Authority. Free Zone Entities will also need to assess their legal position carefully because such entities will have been promised tax free status by the local Emirate / Free Zone, but the definitions of “Free Zone” and “Qualifying Income” remain outstanding from the Law. Despite the apparent intent in Articles 3 & 18 to exempt certain activities of “Qualifying Free Zone Persons” from the Law, the missing definitions make it challenging to demonstrate qualification for this relief.

Potential Adjustments

Companies should continue to assess the impact of cabinet decisions on their corporate tax profile as these are published to ascertain the potential deferred tax implications. Some relevant considerations could include the items below (not an exhaustive list). It should be noted that certain adjustments will depend on the election option available for taxpayers under the Law.

- General & specific provisioning including the expected credit loss (ECL) provisions
- Impairment provisions for inventories / property plant and equipment and other provisions recognized as per the IFRS requirements
- Fair value unrealized gains / losses & foreign exchange gains / losses being recognized
- Interest related deductions
- Carry-forward tax losses
- Tax group consolidation related adjustments

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Key considerations for interim tax accounting

Disclosures

While the details required to be disclosed during interim periods may be limited compared to annual requirements, companies should ensure that significant income-tax related items are included in the disclosures of the financial statements.These may include:

- *an explanation of changes in the applicable tax rate (s) compared to the previous accounting period (IAS 12,18d).*
- *an entity shall include the following information, in the notes to its interim financial statements, if not disclosed or elsewhere in the interim financial report : the nature and amount of changes in estimates of amounts reported in prior interim periods of the current financial year or changes in estimates of amounts reported in prior financial years (IAS 34,16Ad)*

For those companies that have already issued financial statements with a balance sheet date falling on or after 16 January 2023 on the basis that the Law is not yet enacted - this view can be accepted as a management judgement made in uncertain circumstances and therefore is not considered an error. Analysis of the status of the Law following the 16 January 2023 Cabinet Decision has necessarily taken an extended period of time. Making reasonable estimates and judgments in uncertain circumstances is required by IFRS and does not represent an error. Deferred taxes should be recorded in the next reporting period as a change in estimate.

How we can help you

We are here to help guide you on the impact of the Law from a tax accounting perspective. Together, we can navigate the complexities and take the actions required to make sure you are compliant with the requirements of IFRS. Our Team of dedicated finance and accounting professionals along with the subject matter experts from the corporate tax team will assist you in reviewing tax balance sheet accounts and related deferred tax provisioning computations.

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Thank you

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