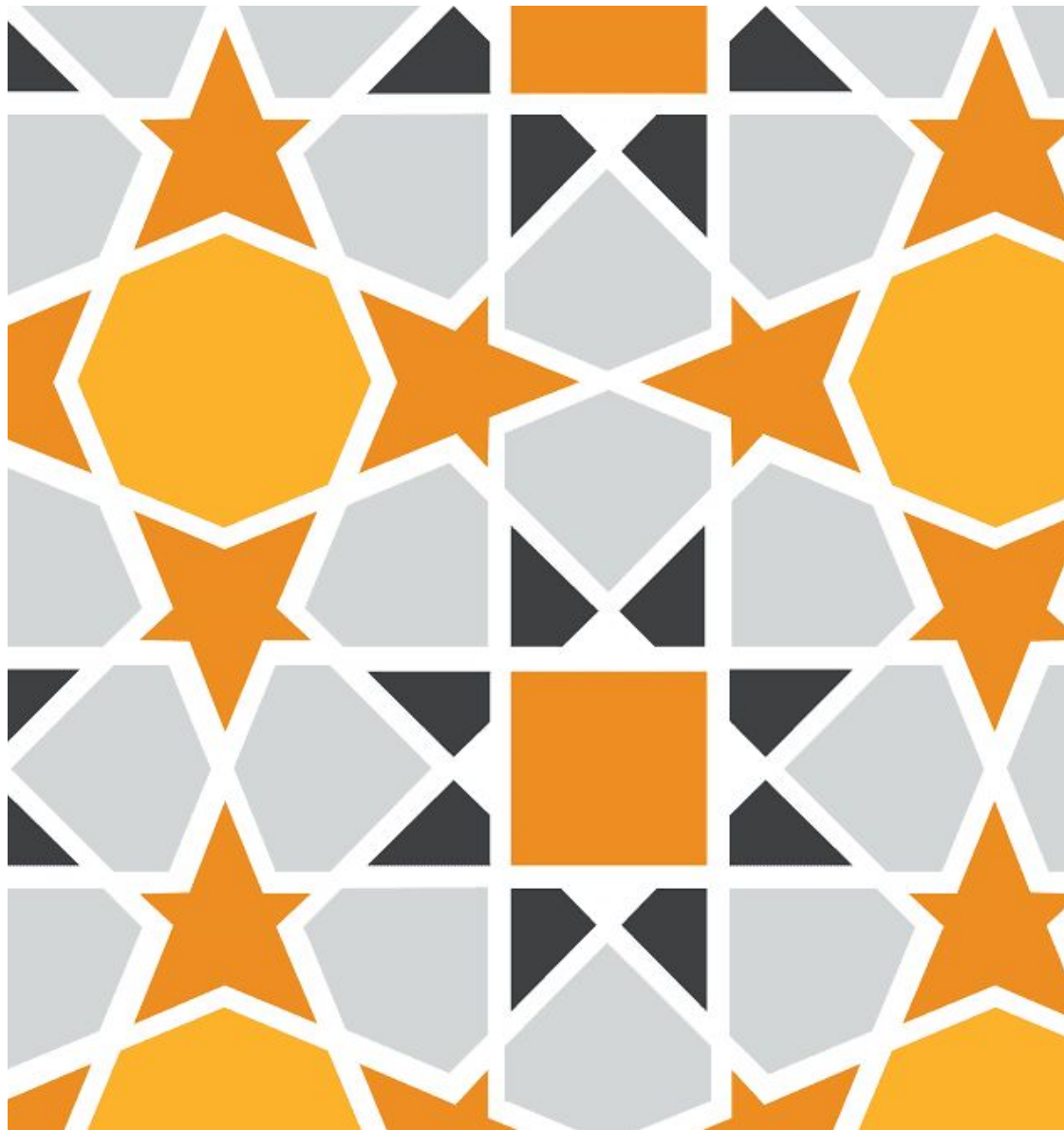


Cabinet of Ministers  
issued Decision No. (98)  
of 2024 (“**Decision**”),  
introducing key  
amendments to the UAE  
Economic Substance  
Regulations (“**UAE  
ESR**”)

October 2024





## In brief

The Cabinet of Ministers issued Decision No. (98) of 2024 (“**Decision**”), introducing key amendments to the United Arab Emirates (“**UAE**”) Economic Substance Regulations, amending certain provisions under Decision No. (57) of 2020 (“**UAE ESR**”).

These significant changes to the UAE ESR regime bring significant relief to UAE businesses, particularly in the context of the Federal UAE CT Law (which is effective for each taxable person’s new financial year beginning on or after 1 June 2023, is applicable across all Emirates and applies to all business and commercial activities, except to certain exempt persons).

In short, we understand UAE ESR will no longer be applicable for the financial year started on or after 1 January 2023 but will remain applicable for the financial years 1 January 2019 to 31 December 2022 (“**ESR Period**”).

## In detail

### *Amendments brought by the Decision*

Any entity that meets the definition of a Licensee (as defined by the UAE ESR) during the ESR Period (1 January 2019 to 31 December 2022), such entities are expected to:

1. Comply with the ESR reporting obligations for the ESR Period, including:
  - a. Submission of the Economic Substance (“**ES**”) notifications and/or ES annual reports;
  - b. In case an entity did not submit the ES notification and/or ES annual report for the ESR Period, such entity would need to make such filings at the earliest.
2. Demonstrate adequate substance in the UAE (if applicable) and other applicable requirements as outlined in the Decision.

Therefore, any entity that meets the definition of a Licensee on or after 1 January 2023 are no longer required to comply with the Decision. For illustrative purposes, please see below examples.

#### **Example 1** (1 January 2023 - 31 December 2023)

Company A has a financial period starting 1 January 2023 and ended on 31 December 2023. Considering the Decision, we understand there is no obligation to file the ES notification, ES annual report or demonstrate adequate substance for period starting 1 January 2023 and ending 31 December 2023.

#### **Example 2** (1 July 2022 - 30 June 2023)

Company B has a financial period starting 1 July 2022 and ended on 30 June 2023. Considering the Decision, we understand there is no obligation to file the ES notification, ES annual report or demonstrate adequate substance for period starting 1 July 2022 and ending 30 June 2023:

- In accordance with the Decision the ESR is applicable to the financial years beginning from 1 January 2019 and ending on 31 December 2022. Considering the financial year end of Company B ended after 31 December 2022 [on 30 June 2023], Company B should not be required to file the ES Notification and/or ES Annual report for FY23.

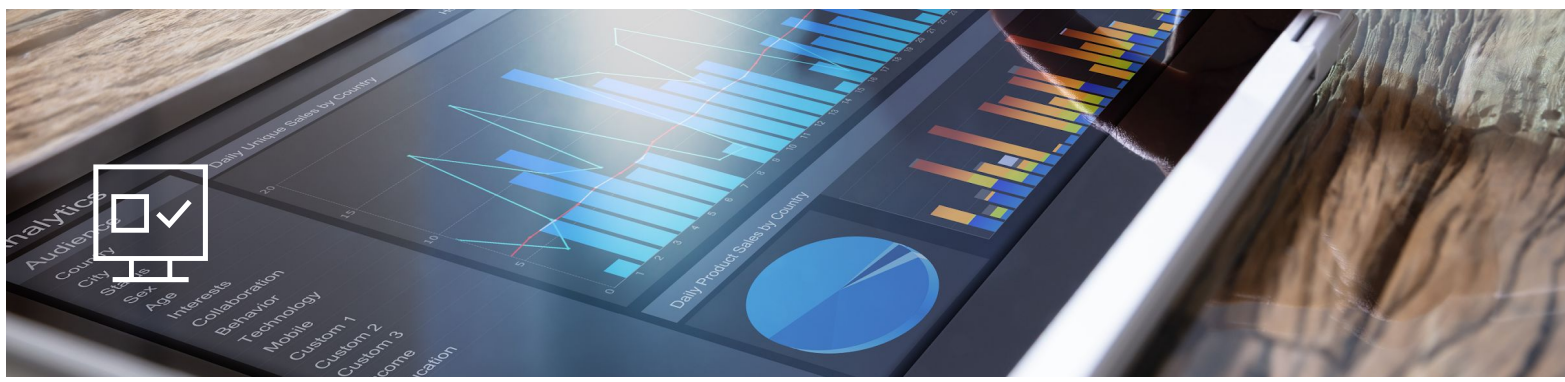
#### **Example 3** (1 January 2022 - 31 December 2022)

Company C has a financial period starting 1 January 2022 and ended on 31 December 2022. Considering the UAE ESR, Company C is required to comply with all provisions outlined in the Decision, including filing of the ES notification, ES annual report and demonstrating adequate substance, if applicable.



*In short, UAE ESR will no longer be applicable for the financial year started on or after 1 January 2023 but will remain applicable for the financial year starting on or after 1 January 2019 through to 31 December 2022.*





### Practical considerations

- **Administrative penalties** - If a Licensee has received an administrative penalty for non compliance with the ESR during any of the financial years commencing after the ESR Period, the Decision states such administrative penalties will be cancelled by the Federal Tax Authority (“FTA”) and any amounts collected would be refunded. According to the UAE ESR Frequently Asked Questions (“FAQ”), Q73, Licensees that are due a refund can request a refund through the e-refund portal on the UAE Ministry of Finance website (although Q73 strictly applies to refunds if an appeal is granted, the UAE Ministry of Finance may use a similar procedure for refunds where administrative penalties are cancelled).
- **Reporting already undertaken for periods on or after 1 January 2023** - we await whether the relevant authorities will provide any guidance, especially with respect to the status of filings that have been already submitted by Licensees for periods after the ESR Period. Our expectation is that the authorities would likely disregard such filings and they would not be further considered but we would await further guidance on this matter.
- **Ongoing document retention and ESR portal access** - the FTA has a 6-year period to review and determine whether Licensees have met the Economic Substance Test (i.e., the assessment of the substance compliance for the reportable period ended on 31 December 2019 can be conducted by the FTA until 31 December 2025; for the reportable period ended on 31 December 2020, until 31 December 2026 etc.). Licensees are expected to maintain supporting documentation (including access to the ESR portal) for at least for 6 years following the end of the reportable period.
- **Expected audit activity** - considering the limited timeframe for the ESR audit period, we expect to see increased audit activity with respect to whether Licensees have complied with the Economic Substance Test during the ESR Period.

### Federal Corporate Tax (“CT”) regime considerations

Even though the ESR would not be applicable for financial years commencing on or after 1 January 2023, the UAE free zone entities and branches (“Free Zone Persons”) that wish to avail the 0% CT rate benefit as Qualifying Free Zone Persons may still be required to comply with certain substance obligations from a UAE Federal Corporate Tax perspective. Specifically, a Free Zone Person may qualify for 0% corporate tax rate in case it meets certain conditions, one of which is the requirement to maintain “adequate substance” in a free zone. The “adequate substance” condition would require the Free Zone Person to:

1. Undertake Core Income Generating Activities in a Free Zone;
2. Have adequate assets and adequate number of full-time qualified employees in the Free Zone and incur an adequate amount of operating expenditure.

The determination of adequate substance is highly subjective and would depend on the nature and size of the business of the Free Zone Person.

Therefore, businesses are expected to continue compliance with economic substance requirements and maintain adequate substance in line with existing laws and regulations.

### Next steps

We recommend that entities to engage in specific discussions about their ESR position during and post ESR Period. Consider the following actions with respect to the ESR:

- **ESR compliance from 2023 onwards:** Entities will not be required to comply with ESR obligations for any financial periods starting on or after January 1, 2023.
- **Meet ESR reporting requirements for 2019 - 2022:** If your entity had ESR reporting obligations for financial years between 2019 and 2022, ensure all necessary filings (i.e., ES Notifications and ES Annual reports) are completed accurately for this period.
- **Assess adequate substance:** Free zone entities should review their operational structure to ensure it aligns with other UAE tax compliance standards (i.e., UAE Federal Corporate Tax).
- **Verify eligibility for administrative penalties cancellation:** Confirm whether your entity is eligible for the waiver and/or refund of any of the administrative penalties to be paid or already paid.
- **Monitor further clarifications:** Stay updated for further information on what ESR compliance obligations need to be met for the penalty waivers to apply.



# The takeaway

*UAE ESR will no longer be applicable for the financial year started on or after 1 January 2023 but will remain applicable for the financial year starting on or after 1 January 2019 through to 31 December 2022. Entities should review the applicability of the ESR on their operations and take the appropriate actions as prescribed in the regulations.*

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## Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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