

RAK ICC

Economic Substance Requirements Guidance

Background

As part of the UAE's commitment as a member of the OECD Inclusive Framework, and in response to an assessment of the UAE's tax framework by the European Union Code of Conduct Group on Business Taxation, the UAE issued Economic Substance Regulations, (the "Regulations") on 30 April 2019. Further guidance on the application of the Regulations was issued on 11 September 2019. Amendments to the Regulations were made by Cabinet of Ministers Resolution No. (57) of 2020 on 10 August 2020, and updated Guidance was issued on 19 August 2020 (Ministerial Decision No. (100) of 2020). The Regulations require UAE onshore and free zone companies and certain other business forms that carry out any of the defined "Relevant Activities" listed below to maintain and demonstrate an adequate "economic presence" in the UAE relative to the activities they undertake ("Economic Substance Test").

Relevant Activities:

1. Banking Business
2. Insurance Business
3. Investment Fund Management Business
4. Lease - Finance Business
5. Headquarters Business
6. Shipping Business
7. Holding Company Business
8. Intellectual property Business ("IP")
9. Distribution and Service Centre Business

Application in RAKICC

The ESR applies in RAK ICC and requires entities that carry on one or more "Relevant Activities", to have economic substance in the UAE in relation to these activities, and to comply with notification and return filing obligations.

The Regulations apply to financial years commencing on or from 1 January 2019. Entities that are within the scope of the Regulations are required to submit an annual Notification form, and complete and submit an Economic Substance Report within 12 months from the end of their financial year (e.g. 31 December 2020 for entities with a financial year ending 31 December 2019). An entity is not required to meet the Economic Substance Test and file an Economic Substance Report for any financial period in which it has not earned income from a Relevant Activity or if it meets the conditions for being exempt. A Notification form will need to be submitted regardless. Failure to comply with the Regulations can result in penalties, spontaneous exchange of information with the Foreign Competent Authority (as defined in Article 1 of the Regulations), as well as other administrative sanctions such as the suspension, revocation or non-renewal of the entity.

Exemptions

The following Exempted Licensees are exempt from filing an Economic Substance Report and the requirement to demonstrate substance in the UAE:

- A Licensee that is tax resident outside the UAE;
 - An Investment fund and its underlying SPVs / investment holding entities;
 - A wholly UAE resident-owned business that is not part of a multinational group and that only carries on business in the UAE
 - A branch of a foreign entity that is subject to tax on all of its Relevant Income in a foreign jurisdiction
- Sufficient evidence must be submitted along with the Notification form to claim any of the above exemptions.

However, exempt RAK ICC entities must still file an economic substance annual notification.

Annual notification

All RAK ICC entities conducting relevant activities are required to submit a Notification electronically on the new Ministry of Finance Portal and entities that carry out Relevant Activities, that have already submitted a Notification directly to RAK ICC, are required to re-submit a Notification once it is available.

Economic Substance Report

RAK ICC entities that are not exempt and undertake a relevant activity from which they earn income during a relevant financial year, are required to:

Meet economic substance requirements.

File an Economic Substance Regulations Return “ESR Report”.

The ESR Report is due within 12 months of the end of the licensees’ financial year (Accounting Reference Period).

Note: if a licensee is exempt or carries on a relevant activity but does NOT derive income from that activity, it does NOT need to file an ESR Report.

What are the penalties for non-compliance?

Failure to submit a Notification: AED 20k

Failure to submit an Economic Substance Report: ● Penalty of AED 50k; and ● Deemed failure to demonstrate economic substance in the UAE

Failure to provide accurate or complete information: ● Penalty of AED 10k to 50k; and ● Deemed failure to demonstrate economic substance in the UAE

Failure to demonstrate sufficient economic substance in the UAE for the relevant Financial Year:

First failure ● Penalty of AED 50k; and ● Information exchange with foreign competent authority of: (1) parent company, (2) ultimate parent company, and (3) ultimate beneficial owner

Second consecutive instance of failure ● Information exchange with foreign competent authority of: (1) parent company, (2) ultimate parent company, and (3) ultimate beneficial owner; and ● Penalty of AED 400k; and ● the company could be: suspended, struck-off or not renewed

What should a Licensee consider before the end of a financial period?

The following is meant as a non-exhaustive list of matters a Licensee should consider (and action, where relevant) before the end of a financial period:

- Assess what (if any) Relevant Activities it has performed during the financial period (applying a “substance over form” approach);
- Assess the amount and type of income earned (if any) from the Relevant Activity during the financial period;
- Hold board meetings with a quorum of directors physically present in the UAE;
- Ensure board meeting minutes are signed and maintained in the UAE;
- Identify the amount and type of expenses and UAE based assets (incl. premises) in respect of the Relevant Activity, and ensure access to assets (incl. premises) can be demonstrated (through agreements and financial records)
- Identify the number of UAE based full-time employees or other personnel (and their qualifications) responsible for carrying on the Licensee’s Relevant Activity; and

- Ensure control and supervision over any outsourcing arrangements can be demonstrated, e.g. through contractual agreements. Additional actions may be required to ensure a Licensee can demonstrate sufficient economic substance in the UAE for a relevant financial period, and the considerations above may differ where a Licensee has either a Holding Company or a High Risk IP Business.

ESR Contact Information

For ESR enquiries please email esr@rakicc.com

USEFUL LINKS AND RESOURCES

United Arab Emirates Economic Substance Regime

<https://www.mof.gov.ae/en/StrategicPartnerships/Pages/ESR.aspx>

The website includes:



[New Cabinet Resolution No 57 of 2020 revoking Cabinet Resolution No 31 of 2019](#)



[Ministerial Decision 100 of 2020 ESR Guidance and Relevant Activities Guide Issued 19 August 2020](#)



[Economic Substance UAE Economic Substance Flowchart](#)



[Relevant Activities Summary](#)



[Notice of COVID-19](#)