UAE Corporate Tax
Guide on Taxation of Foreign Source Income released in November 2023

Key Takeaways

November 2023

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Foreign Source Income Taxation Guide

The Federal Tax Authority (FTA) has released a Corporate Tax (CT) Guide on Taxation of Foreign Source Income (FSI). The document includes detailed guidance on who is taxable, which foreign income is taxable, how to calculate the taxable income, how to apply any available exemptions/reliefs, how to apply tax credit etc.

Key highlights

FSI is taxable for the following Taxable Persons:

- Tax resident juridical person as part of worldwide taxable income;
- Tax non-resident juridical person, only if there is a Permanent Establishment (PE) in the UAE and FSI is attributable to the PE;
- Tax resident natural person, only if FSI is related to taxable business activities in the UAE and provided the total turnover exceeds AED 1 million in the calendar year;
- Tax non-resident natural person, only if having a PE in the UAE and FSI is attributable to the PE and provided the total turnover exceeds AED 1 million in the calendar year.

The following are important considerations:

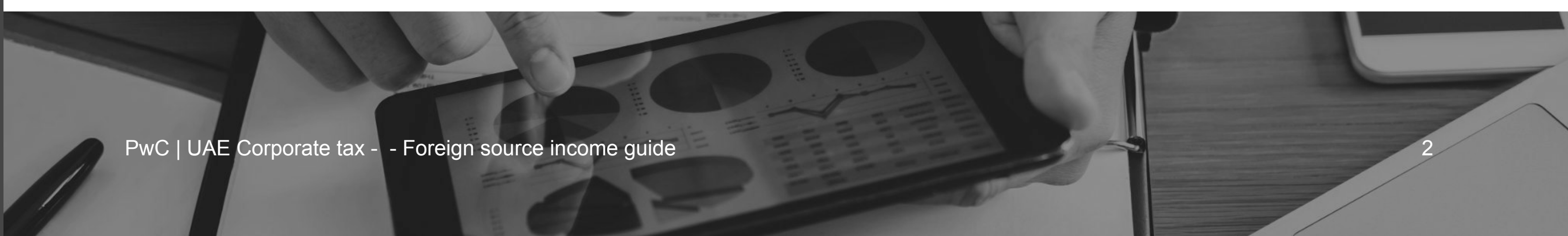
- Taxable Persons may face taxation of FSI, whereby the CT Law provides exemptions such as Participation Exemption or Foreign PE Exemption to prevent or alleviate double taxation.
- In cases where FSI remains taxable, the general rules for determining taxable income apply equally to FSI, including accounting standards, deductible vs non-deductible expenses. Taxable income and deductible expenditure from all sources, whether domestic or foreign, are aggregated for the purposes of calculating taxable income. Thus, tax losses from a foreign source can be offset against income from UAE sources when determining taxable income.
- A potential double taxation can be mitigated or eliminated through a foreign tax credit (FTC), enabling the deduction of taxes paid in a foreign jurisdiction from the UAE CT liability. FTC is allowed for foreign taxes that are similar to CT, contingent upon satisfying specific conditions such as (i) FTC is imposed by and payable to the government; (ii) the payment of foreign tax is compulsory, and (iii) foreign tax is imposed on profit or net income (including WHT).
- FTC is the lower of (a) the actual amount of tax paid on FSI in the foreign jurisdiction or (b) the amount of the CT due on the net FSI (i.e. gross FSI less linked expenditures defined as per UAE CT Law). Thus, FTC is not available in respect of UAE CT exempt income or in case of tax loss. No carry forward of unutilised FTC is allowed.
- The Guide also introduces the income-by-income approach: excess FTC from one FSI cannot be offset against CT due on another FSI for a Taxable Person with multiple income streams.
- FTC applies to tax considered as "paid", which implies the remitted amount or accrued sum committed to the foreign tax authority. The Guide clarifies that the tax shall not be considered as paid if the tax liability in the foreign jurisdiction is contingent or not yet formally accrued, or where the amount of tax paid in a foreign jurisdiction has been refunded or has been confirmed as being refundable.
- A symmetrical approach shall be applied to address any timing mismatch issues - foreign tax paid follows the corresponding FSI on which such tax is paid. FTC will be allowed in the tax period in which the FSI forms part of the taxable income.

Next steps

The Guide provides guidance and clarity on taxation of FSI and the FTC mechanism that taxpayers can use to avoid double taxation. Careful consideration and application of these guidelines are necessary for taxpayers that derive FSI.

It is essential to stay alert and adapt to evolving UAE CT legislation for tax efficiency and tax compliance.

For further assistance, you can reach us by emailing CT.UAE@pwc.com.



Foreign Source Income Guide

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