



ABU DHABI GLOBAL MARKET
سوق أبوظبي العالمي

UAE ECONOMIC SUBSTANCE REGIME ADGM OUTREACH SESSION

3 February 2020



Session Outline



Agenda

- 1. Welcome Remarks**
- 2. Background**
- 3. Overview of the UAE Economic Substance Regime**
- 4. The Economic Substance Test**
- 5. ADGM Requirements**
- 6. Consequences of Non-Compliance**
- 7. Next Steps**
- 8. Q&A**



Global Standards

- European Union Code of Conduct Group (Business Taxation) – Criteria 2.2
- OECD Global Standard on Base Erosion and Profit Shifting (BEPS) – Action 5

The UAE Regulatory Response

Federal Economic Substance Regime, comprising:

- *Cabinet Resolution No. 31 of 2019 concerning Economic Substance Regulations, as amended by Cabinet Resolution No. 7 of 2020 (Regulations)*
- *Ministerial Decision No. 215 of 2019 (Guidance)*
- *Cabinet Decision No. 58/2019 on the Determination of Regulatory Competencies*

Overview of the Economic Substance Regime



Description

1

Licensee

A natural or a legal person licensed by a Competent Licensing Authority in the UAE, including FZs and FFZs, to carry out a 'Relevant Activity'

Note: 'Licensee' in the following slides is as per above

2

Application in ADGM

Licensees can be companies, partnerships, foundations, non-profit organisations, branches of foreign companies that:

- ✓ are located in ADGM
- ✓ earn income from one or more Relevant Activities
- ✓ for Financial Years commencing on or after 1 January 2019

3

Exempt Licensee

A Licensee directly or indirectly owned **51% or more** by the UAE Government

The onus is on Licensees to provide evidence to support their exempt status

Overview of the Economic Substance Regime



What are Relevant Activities?



What are the Requirements?

All Licensees (including Exempt Licensees)

- ✓ Notify the Regulatory Authority of whether or not undertaking one or more Relevant Activity(s)



Non-Exempt Licensees deriving income from the Relevant Activity

- ✓ Meet the Economic Substance Test; and
- ✓ File Economic Substance Return

Economic Substance Test – General



All three (3) requirements below must be met

- 1. Core Income Generating Activities (CIGAs) Undertaken in UAE**
- 2. Directed and Managed in the UAE**
- 3. Adequate employees, physical assets and expenditure in the UAE**

Requirements 1 and 3 are subject to 'Permitted Outsourcing Arrangements'



Core Income Generating Activities (CIGAs) Undertaken in UAE

'CIGAs':

- ✓ core/primary functions that underpin the Relevant Activity
- ✓ must be undertaken in the UAE
- ✓ see the non-exhaustive list in Article 5 of the Regulations
- ✓ may be outsourced in some cases

Economic Substance Test – General (2/3)



Directed and Managed in the UAE

Relevant Activity must be ‘directed and managed’ in the UAE, demonstrated by:

- ✓ number of board meetings held in the UAE
- ✓ minutes of board meetings recorded, signed and kept in the UAE
- ✓ quorum of directors present in the UAE
- ✓ directors’ knowledge/expertise to discharge their duties
- ✓ for Representative Offices/branches: the Principal Representative/SEO being in the UAE when making key decisions

Economic Substance Test – General (3/3)



Adequate employees, physical assets and expenditure in the UAE

No definition of 'adequate' - not a 'one size fits all' requirement.

ADGM will apply a pragmatic, risk based approach having regard to the level of Relevant Activities being carried out.

Consider:

- ✓ number of employees (employed by Licensee/another entity) present in the UAE
- ✓ the level of operating expenditure in the UAE
- ✓ physical premises and assets in the UAE

Adequacy requirements are subject to 'Permitted Outsourcing Arrangements'

Permitted Outsourcing Arrangements



What can be outsourced?

- ✓ Core Income Generating Activities (CIGAs) or parts of CIGAs
- ✓ Adequate employees, operating expenditure, physical assets
- X NOT the requirement to be 'directed and managed in the UAE'

To whom?

Adequately resourced Third Party Service Provider or related companies in the UAE

What are the conditions for outsourcing?

The Licensee must demonstrate:

- ✓ Adequate supervision of the outsourced activity by the Licensee
 - ✓ All parts of outsourced CIGAs must be undertaken in the UAE
 - ✓ Third Party Service Provider must be adequately resourced
 - ✓ No 'double counting' where the services are provided to more than one Licensee
- Licensees should have agreements evidencing appropriate oversight

Note: Outsourcing must not be used to circumvent the Economic Substance Test

Economic Substance Test Variations: Holding Company Business



What is a Holding Company Business?

A business whose primary function is the acquisition and holding of equity interests (e.g. shares) in other entities, which:

- ✓ derives income from dividends and capital gains; and
- ✓ does not carry out any other commercial activity.

Reduced Economic Substance Test

Requires:

- ✓ Compliance with existing ADGM reporting/compliance requirements by submitting necessary documents, records or information to the Regulatory Authority
- ✓ Adequate number of employees and physical assets (e.g. premises):
 - may be satisfied through a Corporate Service Provider or related company
 - directors can be counted as ‘equivalent full-time employees’
 - registered offices or flexi-desks can be counted as ‘premises’

Does not require:

- ✓ being ‘directed and managed’ in the UAE (*subject to ADGM regulatory /policy framework*)
- ✓ ‘adequate expenditure’ being incurred in the UAE

Economic Substance Test Variations: High Risk IP Business (1/2)



What is a High Risk IP Business?

Condition A or B must be met to be considered a High Risk IP Business

Condition A (cumulative – all of the following must be met)

The Licensee:

- did not create the IP asset which it holds for the purposes of its business
- acquired the IP asset either from:
 - a Connected Person; or
 - in consideration for funding research and development (R&D) by another person situated outside the UAE
- licenses the IP asset to a Connected Person(s) or otherwise generates income from the asset in consequence of activities performed by Foreign Connected Person(s).

Condition B

The Licensee does not carry out R&D, or branding, marketing and distribution as part of its CIGAs in the UAE.

Economic Substance Test Variations: High Risk IP Business (2/2)



Consequences of being a High Risk IP business?

1. Increased Economic Substance Requirements

Rebuttable Presumption: the Licensee is presumed to not meet the Economic Substance Test, unless the Licensee meets the increased substance requirements.

How: the Licensee must demonstrate and provide evidence that:

- ✓ it does, and historically has, exercised a high degree of control over developing IP
- ✓ it has an adequate number of full time employees, with the necessary qualifications, that permanently reside and perform their activities in the UAE
- ✓ it has a business plan, showing the reasons for holding the IP in the UAE
- ✓ its decision-making takes place in the UAE.

2. Reporting Requirements for Regulatory Authorities

Regulatory Authorities must provide all information provided by a High Risk IP Business to the Competent Authority, irrespective of the Economic Substance Test Determination.

3. Exchange of Information by the Competent Authority

The Competent Authority will provide the information received in relation to a High Risk IP Business to the relevant Foreign Competent Authority.

Requirements for Licensees (1/3)



Annual Notification Requirement

All Licensees are required to notify the Registration Authority of the following annually (regardless of being **exempt** or not earning income), i.e. the “Annual Notification Requirement”:

1. Whether or not the Licensee is carrying on a Relevant Activity;
2. If the Licensee is carrying on a Relevant Activity, whether or not all or any part of the Licensee’s gross income in relation to the Relevant Activity is subject to tax in a jurisdiction outside the UAE; and
3. The date of the end of the Licensee’s Financial Year (Accounting Reference Period).

Requirements for Licensees (2/3)



Annual Notification Filing

Licensees are required to provide a first **Annual Notification** to the Registration Authority by **31 March 2020**.

Information to be provided includes:

- Reportable period for substance purposes,
- Relevant Activities (type, whether income was earned and subject to tax), and
- Confirmation of whether the Licensee is exempt.

Note: the notification template will be available soon

Method: the Annual Notification should be filed electronically via the Online Registry Solution, using the 'Lodge a General Document' service (www.registration.adgm.com).

Requirements for ADGM Licensees (3/3)



The Economic Substance Return

Licensees that are **not exempt** and undertake a **Relevant Activity** from which they earn income during a relevant Financial Year, are required to:

1. Meet economic substance requirements; and
2. File an Economic Substance Return.

The *Economic Substance Return* is due **within 12 months** of the end of the Licensees' Financial Year (Accounting Reference Period).

Therefore the first Economic Substance Returns will be due by **31 December 2020**.

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 Economic Substance Return.

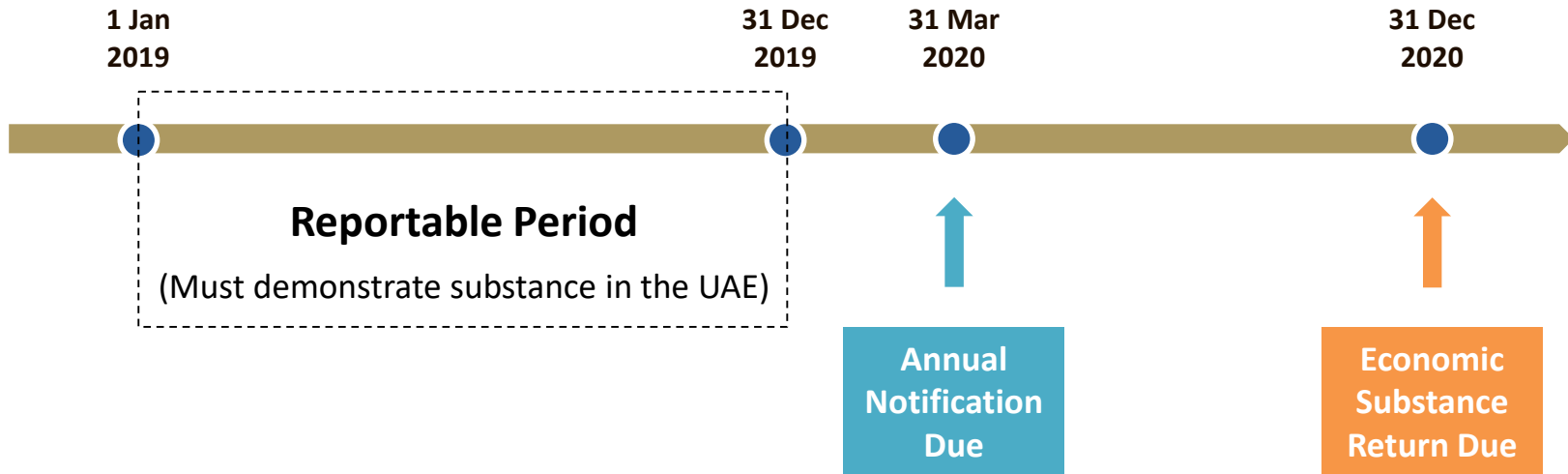
Timeline For An Existing Licensee - Example #1



Timeline for Annual Notification, Reportable Period and Return Filing

Example #1:

Existing Licensee with a 1 January to 31 December financial year (accounting reference period).



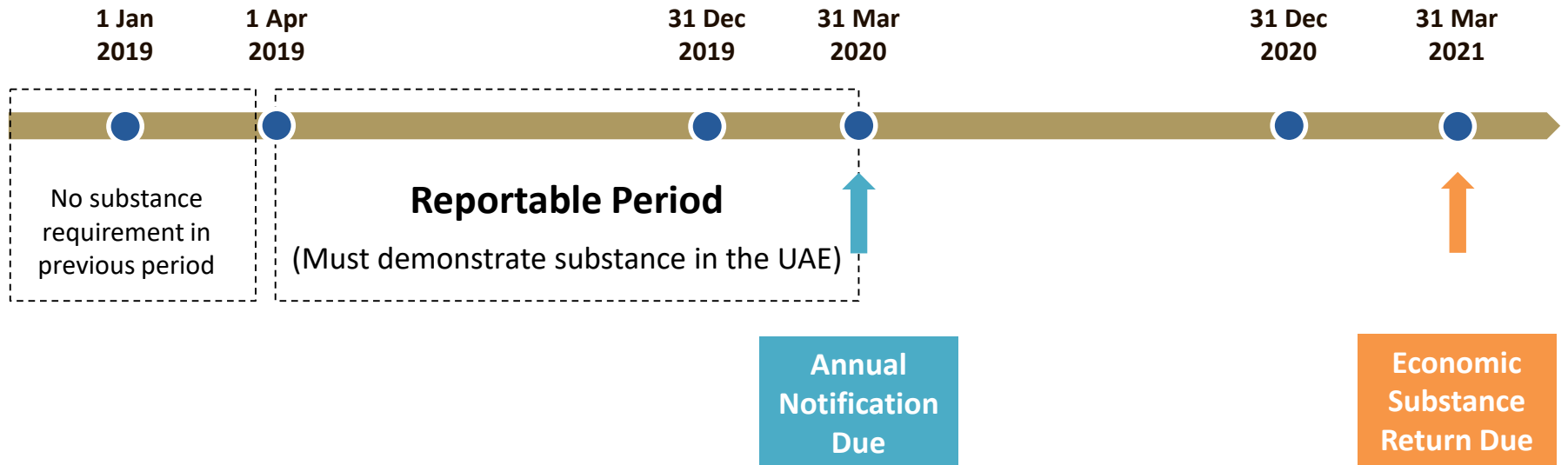
Timeline For An Existing Licensee - Example #2



Timeline for Annual Notification, Reportable Period and Return Filing

Example #2:

Existing Licensee with a 1 April to 31 March financial year (accounting reference period).



Consequences for Non-Compliance



Failure to:

1 Provide information

Financial Penalty:
AED 10,000 to 50,000
AND

Deemed **failure to demonstrate economic substance** in the UAE

2 Provide accurate or complete information

Financial Penalty:
AED 10,000 to 50,000
AND

Deemed **failure to demonstrate economic substance** in the UAE

3 Demonstrate sufficient economic substance in the UAE for the relevant Financial Year

First year of failure:

- Financial penalty of **AED 10,000 to 50,000**; and
- **Information exchange** with foreign competent authority of parent, ultimate parent & UBO.

Second consecutive year of failure:

- Financial penalty of **AED 100,000 to 300,000**;
- **Information exchange** with foreign competent authority of parent, ultimate parent & UBO; and
- Possible **commercial license suspension / withdrawal**.

Next Steps



Consider the following...

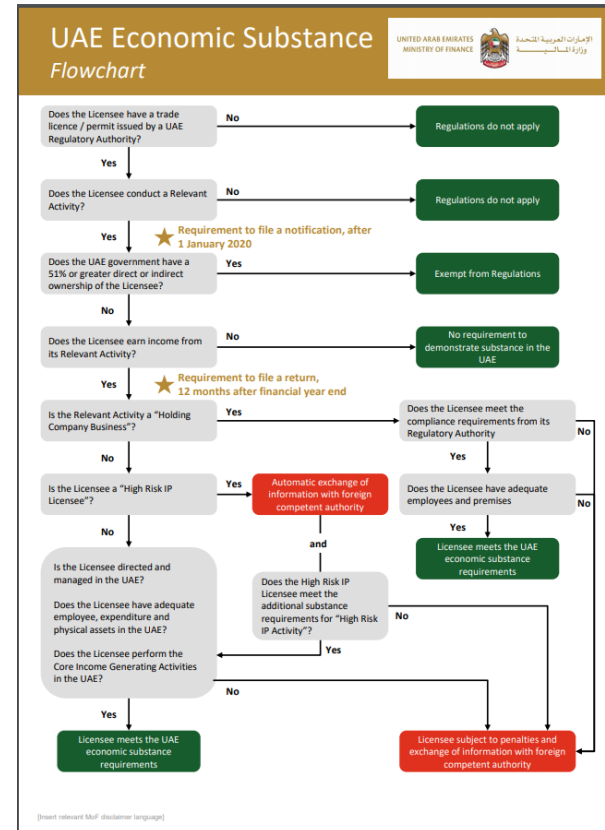
1. Is your business a Licensee?
2. Is your business an exempt Licensee?

ADGM Registration Authority

- Will publish Annual Notification Template soon, along with reporting guidance.
- For enquiries email: economicsubstance@adgm.com

Additional Resources

- UAE Ministry of Finance:
 - Economic Substance [FAQs](#)
 - Economic Substance [Flowchart](#)



Source: UAE Ministry of Finance, www.mof.ae



Q&A