

UAE Business Tax news

Investment Funds and Investment Fund Managers Guide

13 June 2024

On 06 May 2024, the Federal Tax Authority (FTA) in the United Arab Emirates (UAE) published the Corporate Tax Guide on “Investment Funds and Investment Managers” (the Guide) thereby providing general guidance on the UAE Corporate Tax treatment for investment funds and investment managers under the UAE Corporate Tax Law (UAE CT Law).

Investment Fund

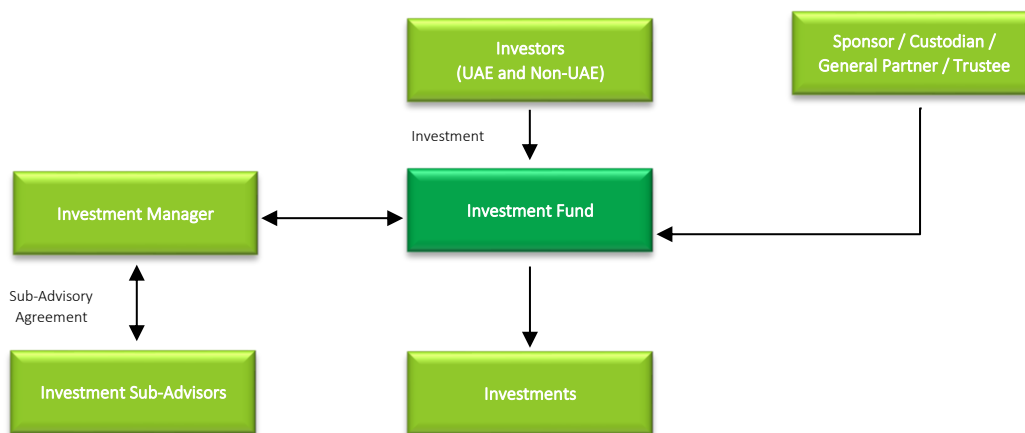
An Investment Fund invests funds received from investors on a collective basis in accordance with a defined investment policy, and the investors share in the profits of the investment fund. It can consist of one or several entities and use different types of corporate entities, as well as unincorporated partnerships or investment trusts or entities incorporated outside the UAE. An investment fund can include different types of public/private funds including real estate funds and the investors can range from natural persons, foundations, other funds, or corporate entity structures.

Investment Manager

To manage the investment fund, it may appoint an Investment Manager (IM) who will make investment decisions on behalf of the investment fund, in line with a pre-agreed investment policy and applicable investment procedures.

Fund Structure

A typical investment fund structure is depicted below:



Guidance provided in the Investment Funds and Investment Fund Managers Guide

The UAE CT Law seeks to ensure neutrality such that investors of an investment fund are in similar Corporate Tax positions as if they had invested directly in the underlying assets of the fund. In view of this policy objective, CT Law contained various related tax provisions. However, there were a few areas relating to Qualified Investment Fund and Investment Manager which required more clarity. The aforesaid guide now provides valuable guidance on related key aspects such as:

- inclusion of a fund’s net income in the income of investors;
- allocation of income between Exempt income, Interest income, income from immovable property and other income;
- treatment of distributions;
- conditions of being a Qualified Investment Fund in terms of eligibility, investment business, diversity of ownership, etc;

- compliance requirements; and
- elaborate guidance on IM exemption related conditions.

The key points elaborated in the guide are summarized as follows:

(A) The Corporate Tax treatment for various categories of Qualifying Investment Funds - QIF (entity/partnership structure), Investment Managers and Investors:

Sr. #	Categories	Corporate Tax Treatment
1	Investment Fund that is a Resident Entity	<ul style="list-style-type: none"> • Investment Fund which is a resident person [incorporated in the UAE (including a free zone entity) or is effectively managed and controlled in the UAE]] will be subject to tax unless the relevant conditions for QIF are met and an application for <u>exempt status is approved by the FTA after obtaining registration as a taxable person</u> for the purpose of UAE CT Law.
2	Investment Fund is an Unincorporated Partnership	<ul style="list-style-type: none"> • Investment Fund which is an Unincorporated Partnership (fiscally transparent) is not considered a taxable person in its own right and instead the investors (partners) will be taxable in respect of the income derived by such a partnership. • Where the investors (partners) apply to the FTA for the fiscally transparent unincorporated partnership to be treated as fiscally opaque (taxable in its own right), such a partnership can avail the exempt status of QIF subject to meeting the relevant conditions. • The QIF, being a fiscally opaque unincorporated partnership is required to notify the FTA within 20 business days of any investor/partner joining or leaving the said partnership.
3	Investment Fund is a Non-Resident Entity	<ul style="list-style-type: none"> • Investment Fund which is incorporated outside the UAE and is not effectively managed and controlled in the UAE will be subject to tax in respect of: <ul style="list-style-type: none"> (a) income attributable to a permanent establishment (may not exist if Investment Manager exemption conditions are met); (b) state sourced income not attributable to a permanent establishment (subject to 0% tax withholding); or (c) nexus in the UAE (earns income from immovable property).
4	Investment Manager	<ul style="list-style-type: none"> • Resident Person - Fees for brokerage or investment management services from QIF are taxable. IM may be able to benefit from the preferential 0% tax rate if the eligibility conditions under the Qualifying Free Zone Regime are fulfilled. • Non-Resident Person - Taxable in respect of fees attributable to a permanent establishment in the UAE or earning the fees as state sourced income not attributable to a permanent establishment (subject to 0% tax withholding).
5	Investors in a QIF	<ul style="list-style-type: none"> • Resident Juridical Person - Proportionate share of net income available for distribution by QIF (that is not exempt income) is taxable. • Resident Natural Person - Proportional share of net income available for distribution by QIF (that is not exempt income) is taxable in the hands of a natural person if ownership interest in QIF is held as part of business or a business activity. If such interest is held in a QIF as a personal investment, the net income of QIF is not taxable in the hands of the natural person.

Sr. #	Categories	Corporate Tax Treatment
		<ul style="list-style-type: none"> • Non-Resident Person - Proportionate share of net income (that is not exempt income) from ownership interest in QIF which is attributable to the permanent establishment is taxable. Likewise, UAE sourced income (not attributable to a permanent establishment) derived from ownership interest in QIF is taxable in the hands of investor but subject to 0% tax withholding. • Ownership interest in QIF which is earning income from Immovable Property in the UAE will be treated as if the non-resident juridical person has nexus in the UAE. The proportionate part of net income from Immovable Property of QIF will be taxable in the hands of such an investor. • Exempt Person - Net income from ownership interest in QIF is not subject to tax in the hands of exempt persons. Where certain categories of exempt persons for instance Government Entity, are treated as taxable persons due to conducting business or business activity, the proportional share of net income (that is not exempt income) from ownership interest in QIF will be taxable to the extent that such interest is held as part of taxable business or business activity.

(B) Other related pertinent points discussed in the Guide:

Sr. #	Particulars	Description
1	Allocation of Income at QIF Level	<ul style="list-style-type: none"> • The QIF shall allocate the amount reflected as net income available for distribution in its financial statements into four categories: <ul style="list-style-type: none"> i. Exempt Income - includes dividend from resident juridical persons (excluding dividend received from exempt persons), dividend from foreign participation interest and capital gains etc., in relation to participation interest 'subject to meeting participation exemption' condition to be assessed at the QIF level. ii. Interest income. iii. Income from Immovable Property in the UAE. iv. Other income - Any net income available for distribution that is not categorized as Exempt Income, Interest income or income from Immovable Property in the UAE, should be allocated to other income. • The requirement to allocate net income equally applies to QIF which is a Real Estate Investment Trust (REIT).
2	Allocation of QIF Income at Investor Level	<ul style="list-style-type: none"> • Any investor being a taxable person shall include in their income the proportional share of the amount reflected as net income available for distribution in the financial statements of the QIF. • If the net income relates to exempt income, it is treated as exempt income for the investor. • Any proportional net interest income of QIF is treated as interest income of investor, which would reduce the net interest expenditure of the investor. • The net income from Immovable Property in the UAE can create a nexus for a non-resident investor who is a juridical person. • All other income shall be included in the taxable income of the investor where relevant. • If the investor disposes of its investment stake in the QIF, it can claim exemption if the QIF meets all the conditions for participation exemption (a participation in

Sr. #	Particulars	Description
		<p>a QIF is considered to meet the subject to corporate tax condition under Article 23(2)(b) of the UAE CT Law).</p>
3	Time Apportionment of Income	<ul style="list-style-type: none"> • The net income for a particular financial year is the amount reflected in the financial statements of the QIF as <u>at its year end</u>. • In case the investor follows a different tax period (corresponds to the financial year followed), the investor is to include net income available for distribution by the QIF in the tax period in which the year-end of QIF occurs. • If the investor held stake for only part of the financial year of the QIF, the net income is also required to be apportioned by the QIF. The investor is thus required to include the net income from the QIF that was earned in a tax period when it no longer holds the investment in the QIF.
4	Treatment of Distributions	<ul style="list-style-type: none"> • Any distributions made by a QIF should not be included in the income of the investor to the extent that net income available for distribution was previously included in the income of the investor, the determination of which should be done on a combined basis for all tax periods up to and including the tax period in which the distribution is made. • The net income previously included by an investor includes net exempt Income, net interest income, net income from immovable property in the UAE and other net income. If a QIF realizes exempt income, investors that are taxable persons would also consider such income for the purpose of Article 4(2) of Cabinet Decision No. 81 of 2023.
5	Application of Other Corporate Tax Provisions	<ul style="list-style-type: none"> • A QIF is not subject to tax being an exempt person and therefore, the net income of QIF that is available for distribution should not be adjusted under the provisions of the Corporate Tax Law as such the adjustments only apply in respect of the taxable persons.
6	Treatment of Exempt Persons held by QIF	<ul style="list-style-type: none"> • A juridical person <u>incorporated in the UAE</u> that is wholly owned and controlled (legally and beneficially owns all the shares and holds all the voting rights continuously throughout the applicable tax period) by a QIF can also apply for exempt status (following the same procedures and time limits for QIF), if certain conditions (mentioned in Article 4(1)(h) of the UAE CT Law) are met. • The net income available for distribution by QIF should also include the net income of such exempt persons wholly owned by the QIF. This can be achieved if the QIF prepares consolidated financial statements, which can be used by the investors for determining the net income available for distribution to be included in their own income. If consolidated financial statements are not available, the net income available for distribution by the QIF and that by the wholly owned exempt persons is to be aggregated in a manner similar to consolidation, eliminating dividends paid by the exempt persons and any other transactions with the QIF.
7	Impact of Ceasing to be part of a Qualifying Group	<ul style="list-style-type: none"> • If the investment fund was part of a Qualifying Group for the purpose of Article 26 of the UAE CT Law in respect of tax neutral transfer of assets or liabilities, upon obtaining the QIF status it will cease to be part of the said group, and this would trigger a claw back of the relief if the status is changed within 2 years of the transfer.
8	Impact of leaving a Tax Group or causing a Tax Group to cease to exist	<ul style="list-style-type: none"> • An investment fund that is part of a tax group is automatically ousted from the beginning of the tax period in which it attains the QIF status. • If the investment fund was a parent company for tax grouping purposes, the tax group ceases to exist from the beginning of the tax period in which it attains the QIF status unless another parent company replaces it.

Sr. #	Particulars	Description
		<ul style="list-style-type: none"> If the investment fund was part of the tax group and an asset or liability was transferred to or from it and the QIF status is obtained within 2 years of the transfer, then the associated gain or loss is to be considered by the relevant transferor or the transferee as the case may be.
9	Impact on relief for Tax Losses	<ul style="list-style-type: none"> Any existing tax losses or unutilized net interest expenditure prior to obtaining the exempt status cannot be utilized while the QIF has exempt status. If the exempt status is changed to taxable in later tax period, only the tax losses or unutilized net interest expenditure from that tax period onwards can be utilized.

(C) Conditions for being a Qualifying Investment Fund:

The Guide discusses the conditions that are required to be met for the purpose of QIF exemption and also the additional conditions for investment funds and REITs as further prescribed in the relevant Cabinet Decision. All the prescribed conditions must be met continuously during the relevant tax period by the QIF or the REIT for the exempt status during the relevant tax period.

If the conditions as prescribed are not met in certain cases (for instance the failure to meet is of temporary nature and the situation can be rectified), this may not disentitle a QIF to lose the exempt status.

Sr. #	Conditions	Description
	In addition to the conditions of regulatory oversight, fund ownership etc., following guidance is provided in the guide on certain related key aspects:	
1.	Prescribed Additional Conditions under Cabinet Decision No. 80 of 2023 for Investment Funds (excluding REITS)	
1	Investment Business	<ul style="list-style-type: none"> This condition requires that the main business or business activities conducted by the investment fund are investment business activities, and any other business or business activities conducted by the investment fund are ancillary or incidental (revenue from these activities does not exceed 5% of the total revenue in the same financial year). In case of feeder fund (pools capital commitments of investors) that feed capital into master fund which directs and oversees all investments held in the investment fund, such feeder fund can have the exempt status if all conditions are met including investment business condition to be assessed at the level of feeder fund entity itself.
2	Diversity of ownership	<ul style="list-style-type: none"> The diversity of ownership condition requires ownership interest of 30% / 50% in specific cases, and it is clarified that the number of investors is determined by reference to an investment fund's direct investors after looking through any investor that is either (a) a Qualifying Investment Fund, or (b) tax transparent for Corporate Tax purposes (for example, an Unincorporated Partnership or a Foreign Partnership). Related parties are counted as a single investor. The requirement of more than 30% or 50% ownership interest is to be seen in aggregate including direct and indirect (through related parties).

Sr. #	Conditions	Description
3	Investment Manager	<ul style="list-style-type: none"> This condition requires that the investment manager that is managing or advising the investment fund must have a minimum of three investment professionals who need not necessarily be full-time employees and can also be independent contractors (in the business of managing or advising investment funds on investment related matters).
4	Independence	<ul style="list-style-type: none"> The guide states that investors should not have control over the day-to-day management of the investment fund. However, merely having a right to be consulted or to give directions does not result in an investor having day-to-day control of the investment fund. If an investment manager holds an ownership interest in the investment fund it manages, this would not prevent the investment fund meeting the independence condition.
2. Prescribed Additional Conditions under Cabinet Decision No. 80 of 2023 for REITs		
1	Minimum Real Estate Asset Value	<ul style="list-style-type: none"> REIT real estate asset's minimum value excluding land is more than AED 100 million based on the carrying value in the financial statements. The management and ownership of real estate assets can be said to be under the RIET even if it does not have legal title but manages such assets itself or through wholly owned companies including Special Purpose Vehicles.
2	REIT Real Estate Percentage	<ul style="list-style-type: none"> The REIT real estate percentage condition requires that the REIT has an average Real Estate Asset Percentage (REAP) of at least 70% (based on carrying value in the financial statements) during the relevant twelve-month period. REAP represent the portion of the Real Estate Income (from renting of land or real estate excluding gains on disposal of such assets) generating assets as a percentage of the total value of the assets of the REIT; and is to be computed taking the average position throughout the year, based on the average of the quarterly closing balances. For computing REAP, real estate assets and non-real estate assets held by wholly owned companies/SPVs that have exempt status are also taken into consideration.

Guidance on Compliance Requirements for Qualifying Investment Fund

Particulars	Description
Application for Exempt Status	<ul style="list-style-type: none"> Application for exemption can be made to the FTA if the Investment Fund has obtained Corporate Tax Registration Number and all the conditions for exemption are met for the tax period specified in the application. FTA may apply a different starting date for the Qualifying Investment Fund status: <ol style="list-style-type: none"> from the correct date, if the tax period specified in the corporate tax registration form is not correct. from the date all conditions are met by an applicant (acquired during a tax period by a Qualifying Investment Fund) who applies under Article 4(1)(h) of the Decree Law. from the date the conditions are met in later tax periods if FTA receives sufficient supporting evidence to that effect and the tax period mentioned in the application is not correct. If the conditions for exemption are not met and the non-fulfilment of conditions is not of temporary nature, a QIF will cease to be considered as an exempt person

Particulars	Description
	<p>including its wholly owned and controlled entities from the start of the relevant tax period.</p> <ul style="list-style-type: none"> • In case of liquidation/termination, FTA must be notified within 20 business days from the date of the beginning of the liquidation or termination; and the QIF shall cease to be an exempt person on the following day of the completion of the liquidation or termination procedure. • In case of non-fulfilment of conditions is due to an event of a temporary nature which is promptly rectifiable, the QIF will not lose the exempt status if the event/situation is beyond control (not reasonably predicted or prevented); and an application has been made within 20 business days of such failure to meet conditions. The FTA will review and notify its decision within 20 business day or other review time period as notified. It is reasonably expected to rectify the failure to meet the conditions within 20 business days from the submission of such application, extendable upon request for another 20 business days subject to the FTA's approval.
Submission of Annual Declaration	<ul style="list-style-type: none"> • An annual declaration is required to be filed no later than nine months from the end of the relevant tax period, confirming compliance with the exemption conditions.
Retention of Records	<ul style="list-style-type: none"> • All records for ascertainment of Qualifying Investment Fund are required to be retained for 7 years following the tax period to which they relate.

It is clarified in the Guide that if a QIF is approved by the FTA to be considered as Exempt from corporate tax (subject to meeting the prescribed conditions) then the following relief/benefit under the UAE CT Law will not be available to QIF:

- (a) Qualifying Group Relief.
- (b) Business Restructuring Relief
- (c) Transfer of Tax Loss
- (d) Tax Grouping

Investment Manager Exemption

Under the Decree Law, the Investment Manager Exemption is provided so that activities conducted in the normal course of their business in the UAE may not be considered as giving rise to permanent establishment implications for non-resident persons (investors).

An Investment Manager is considered an independent agent acting in the ordinary course of its business on behalf of the non-resident persons subject to the fulfilment of relevant conditions prescribed in the CT Law. The Investment Manager would be seen as acting in its independent capacity, where the non-resident person (whether or not a related party or services are exclusively provided to such person) relies on the special skills and knowledge of the Investment Manager and is not subject to detailed instructions or control as to the performance of services.

Transfer Pricing (TP) Considerations for Investment Manager Exemption

With the evolving TP landscape in the UAE, the Guide provides details and emphasizes the importance of considering the arm's length principle set forth in the UAE TP regime when determining the appropriate compensation for intercompany transactions, such as investment management or brokerage transactions, between Investment Managers and their related parties.

Furthermore, the Guide reinforces that it is mandatory, in order for the Investment Manager exemption to apply that all the intercompany investment services between the Investment Manager and non-resident persons are performed on an arm's length basis.

The Guide provides further examples of the application of the arm's length principle, namely:

- Any Investment Manager or brokerage fees should be conducted at arm's length basis. This should be considered on a case-by-case basis, taking into consideration the specific facts and circumstances of each transaction, to ensure that the appropriate TP support is in place.
- The Guide provides clarity in relation to the application of retroactive TP adjustments to Taxable Income (i.e., "true-up") to comply with the arm's length standard; therefore, this approach should be considered consistent with the arm's length principle. Please note that any TP adjustment mechanisms should be considered in detail and reviewed on a regular basis to ensure they reflect the economic reality of the transaction and maintain compliance with the UAE TP regulations.
- Furthermore, the Guide outlines that if the Investment Manager fee results from a third-party arrangement and is subject to arm's length commercial negotiations, then it would be considered that the arm's length principle is met.
- The Guide provides details in relation to the compensation of the Investment Manager when the fund structure includes several entities or if it has agreed to offer certain co-investment opportunities on the basis that all the transactions are conducted on an arm's length basis. It is also important to ensure that the allocation of fees among the entities is consistent with their respective functional profile and value creation. Furthermore, any services sub-contracted by the Investment Manager to other related parties should also be conducted at arm's length and the necessary support should exist.

From a wider UAE TP perspective, the Guide further underlines the importance of the adherence to the UAE TP rules to ensure that all related party transactions with residents and non-resident persons are conducted in line with the arm's length principle. On that basis, it is crucial to regularly review and update the TP policies and documentation to reflect any changes in business operations.

Finally, it is essential that robust support exists to demonstrate adherence to the arm's length principle and compliance with the UAE TP regime. This should be in the form of supporting TP Documentation (i.e., Local File) and intercompany agreements. The TP documentation should be prepared on a contemporaneous basis providing a comprehensive analysis of the TP method applied and the arm's length considerations.

Key Takeaways

The Guide states that it is not a legally binding document but is intended to provide assistance in understanding the principles and rules that govern the application of the QIF and IM exemption under the UAE CT Law.

The comments in this guide summarize and provide valuable guidance on the important aspects of QIF along with the Investment Manager and the compliance requirements including procedural aspects relating to the filing of an application and the annual declaration for exempt status.

The Guide talks about allocation of the net income at the QIF level into various streams of income available for distribution, however, no detailed guidance is provided on the apportionment of common expenses. QIF should therefore ensure they keep track of such expenses and apportion the same on reasonable basis.

For non-resident juridical investors, taxable as a result of nexus in the UAE, where the QIF derives income from immovable property, the requirement to register becomes applicable on the non-resident person. The non-resident

juridical investor may evaluate other alternatives in such scenarios for example whether to invest in the QIF through a UAE domestic entity.

Further, the Investment Manager exemption is to be evaluated at based on specific facts surrounding the relationship with the non-resident person for the purpose of determining the permanent establishment considerations in the UAE.

It is crucial now that all the impacted Funds, Investors and Investment Managers should immediately evaluate their structures and procedures to ensure that they are aligned with the required conditions to take advantage of the simplified and neutral UAE CT taxation.

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You can also contact us and submit all your queries on this email cituae@deloitte.com.

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