

Benefits of Double Taxation Avoidance Agreements for foreign investors in the UAE

I. Purpose of Double Taxation Avoidance Agreements (DTAAs)

International tax treaties originated from the Fiscal Committee of the League of Nations (later known as the United Nations) which after World War I commenced work on the development of model tax conventions. This work culminated in Model Conventions in 1943 (the Mexico draft) and 1946 (the London draft) for treaty negotiations at that time. These Models were not unanimously accepted, and the work of creating an acceptable model treaty was taken over by Organisation for Economic Co-operation and Development (OECD) and, a few years later, the United Nations.

Tax treaties currently represent an important aspect of the international tax rules of many countries with over 3,000 bilateral income tax treaties in effect, and the number is growing. The majority of these treaties is based in large part on the OECD and UN Models Double Taxation Conventions.

The main difference between the two model conventions is that source countries have greater taxing rights under the UN Model Convention compared to the OECD Model Convention. For example, unlike Article 12 (Royalties) of the OECD Model Convention, Article 12 of the UN Model Convention does not prevent the source country from imposing tax on royalties paid by a resident of the source country to a resident of the other country. The UN Model Convention also gives the source country increased taxing rights over the business income of non-residents compared to the OECD Model Convention. For example, the time threshold for a construction site Permanent Establishment under the UN Model Convention is only 6 months, compared to 12 months under the OECD Model Convention.

The aim of introducing bilateral tax treaties was traditionally to promote international trade between nations and strengthen international cooperation by addressing issues of double taxation.

The UAE has signed tax treaties with around 142 countries so far, some of which are yet to enter into force. The UAE is also a member of the Global Forum on Tax Transparency for exchanging cross border tax information.

With global evolution, the purpose of DTAAs has been refined to avoid treaty shopping arrangements which usually lead to double non-taxation or reduced taxation through tax evasion or tax avoidance. This is further underpinned by the Multilateral Instrument

(MLI) enforced by the UAE in 2019 to comply with the minimum standards set forth by the OECD. The DTAAAs with the UAE have included two minimum standards as follows:

- The **Preamble Statement (Article 6 of the MLI)** which refers to the desire to further develop economic relationship with other Contracting Jurisdictions and enhance cooperation in tax matters. Such preamble clarifies that tax treaties are not intended to create opportunities for non-taxation or reduced taxation through tax evasion or avoidance including through treaty-shopping arrangements.
- The **Principle Purpose Test (PPT) (Article 7 of the MLI)** is the main anti-abuse provision to counter treaty abuse. The PPT will apply to deny treaty benefits when it is reasonable to conclude, having regard to the relevant facts and circumstances, that obtaining tax benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit. The PPT would not however apply where it is established that granting of tax benefits in relevant circumstances will be in accordance with the object and purpose of the relevant provisions of the DTAAAs.

The key benefits of entering into DTAAAs can be summarized as follows:

- To eliminate double taxation;
- To prevent tax evasion;
- To prevent tax avoidance.

These benefits contribute, inter alia, to:

- Encourage foreign investments and stimulate international trade and cooperation;
- Allocate taxing rights fairly for cross-border transactions;
- Reduce source-country taxation (such as withholding taxes);
- Allow recourse to dispute resolution mechanisms when required;
- Encourage taxpayers to pay their fair share of tax.

It is noteworthy that provisions of tax treaties will in most cases prevail over domestic laws. Tax treaties provide certainty to investors on their tax exposure which would have otherwise been highly uncertain and somehow impinged by constant amendments in the domestic tax legislations.

II. Access to DTAAAs

All taxpayers who are resident in the UAE for tax purposes may benefit from the provisions of the tax treaties on the following conditions:

- The taxpayers must hold a valid Tax Residence Certificate to certify their tax residency status in the UAE;
- Taxpayers with dual residency should follow the provisions of the DTAAs on residency to establish their country of tax residence;
- The taxpayers should be subject to the UAE corporate tax obligations;
- The purpose of the arrangements should be genuine and not solely to benefit from treaty provisions as dictated by the Principle Purpose Test;
- Any arrangements should demonstrate real economic substance in order to satisfy beneficial ownership tests and qualify for the treaty benefits. In other words, the entities should not be merely conduit ones with narrow powers over decision-making processes;
- The substance of any arrangements is crucial for the purposes of DTAAs as opposed to their legal form;
- Companies conducting activities abroad and construed as having permanent establishments there are guided by the provisions of the DTAAs;
- Companies entering into intra-group transactions are subject to treaty provisions to determine the taxing rights of the relevant jurisdictions;
- Owners of immovable properties , inasmuch as treaty provisions are applicable;
- Other forms of activities, remunerations and income stream, as enunciated amongst the treaty provisions.

III. Reduced Withholding Taxes (WHT) between UAE and some African countries

Type of Income	Senegal	Ivory Coast	Mozambique	Morocco	Zimbabwe
<i>Treaty rates</i>		<i>Under ratification</i>			
Dividends	5%	10%	0%	0%/5%/10%	5%
Interests	5%	10%	0%	0%/10%	0%
Royalties	5%	10%	0%/5%	0%/10%	9%
Technical fees	*	10%	*	*	*
<i>Non-Treaty rates</i>					
Dividends	10%	15%	20%	15%	15%
Interests	8%/13%/16%	18%	20%	10%	15%
Royalties	20%	20%	20%	10%	15%
Technical fees	20%	20%	20%	10%	15%

(source: tax highlights published online)

*In the absence of any provisions for technical fees in certain tax treaties, no withholding taxes should be levied by the source countries despite withholding taxes are applicable as per the domestic laws of the latter, unless a permanent establishment exists. This is the norm of the treaty provisions.

As per the above table, it is clear that the tax treaties which the UAE has concluded with the listed countries are indeed attractive in terms of reduced withholding tax rates when dealing with these countries.

Other overwhelming benefits of the DTAs with some of these countries are in terms of their Article on Associated Enterprises and Mutual Agreement Procedure.

Associated Enterprises

The provisions on Associated Enterprises allow taxpayers to make corresponding adjustments to the amount of tax charged in the second country in cases where their profits have been adjusted in the first country, provided that such profits would have accrued on comparable arrangements between independent parties.

In determining such adjustments, due consideration should be given to other provisions of the DTAs together with any requisite consultation between the Competent Authorities.

The corresponding adjustments can be viewed as a safeguard to mitigate double tax imposition.

Mutual Agreement Procedure (MAP)

MAP is an important instrument to allow taxpayers to resolve international tax disputes arising out of the application of the treaty provisions. The Competent Authorities of the concerned jurisdictions are encouraged to interact and cooperate mutually to sort out the tax disputes.

The provisions on Mutual Agreement Procedure (MAP) grant taxpayers the possibility to present their case to the Competent Authority of either country within three years from the first notification of the action resulting in taxation which is not in accordance with the provisions of the DTAs.

MAP acts as a guarantee to taxpayers and eliminates double taxation as the taxing rights of the relevant jurisdictions are established.

Action 14 of the OECD BEPS Projects have enhanced the MAP mechanism by introducing mandatory binding provisions. The UAE has not adopted the binding provisions.

Concluding remarks

DTAs shed light on the tax exposure of companies operating cross-borders and facilitate global outreach to Competent Authorities. In addition to the principal objectives of tax treaties

as outlined above, there are several ancillary objectives. One such ancillary objective is the elimination of discrimination against foreign nationals and non-residents. The tax treaty ensures that the residents of a contracting state who carry on business in the other contracting state are given the same tax treatment as the residents of that other state who carry on similar activities. A second ancillary objective is to facilitate administrative cooperation between contracting states, for example, in areas such as exchange of information and assistance in collection of taxes.

The UAE has a large network of tax treaties with promising and encouraging countries to explore avenues for international expansion.

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