

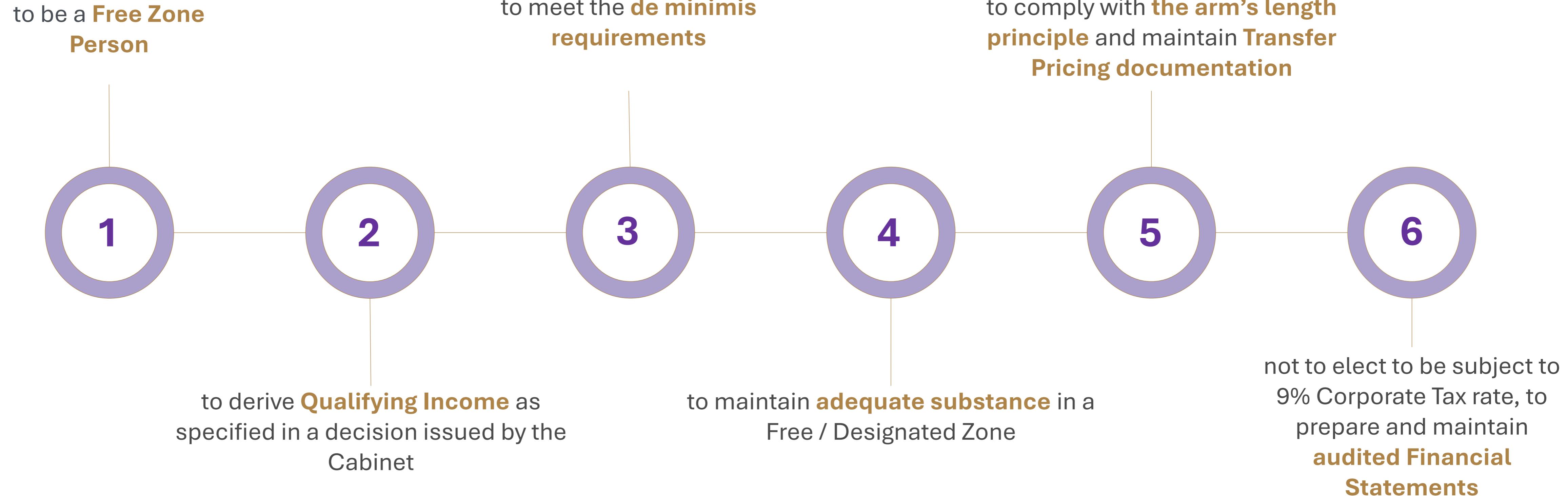
The Fragile Status of Free Zone Tax Benefits

**A Closer Look at Conditions, Common Errors, and
Implementation Challenges**

2025



Conditions to apply 0% Corporate Tax Rate



Is the Taxable Person making an election to be subject to Corporate Tax under the standard Corporate Tax regime? i

Yes No

Does the Taxable Person meet the requirements to be considered a Qualifying Free Zone Person?

Yes No

Common challenges and missteps

Incorrect selection of a Free Zone

Failure to control revenue streams

Lack of adequate substance

Non-compliance with TP rules



Failure to meet **any** requirement triggers a 5-year disqualification from the QFZP regime



The same consequences apply if a Free Zone Person elects to be subject to the 9% Corporate Tax rate.

01

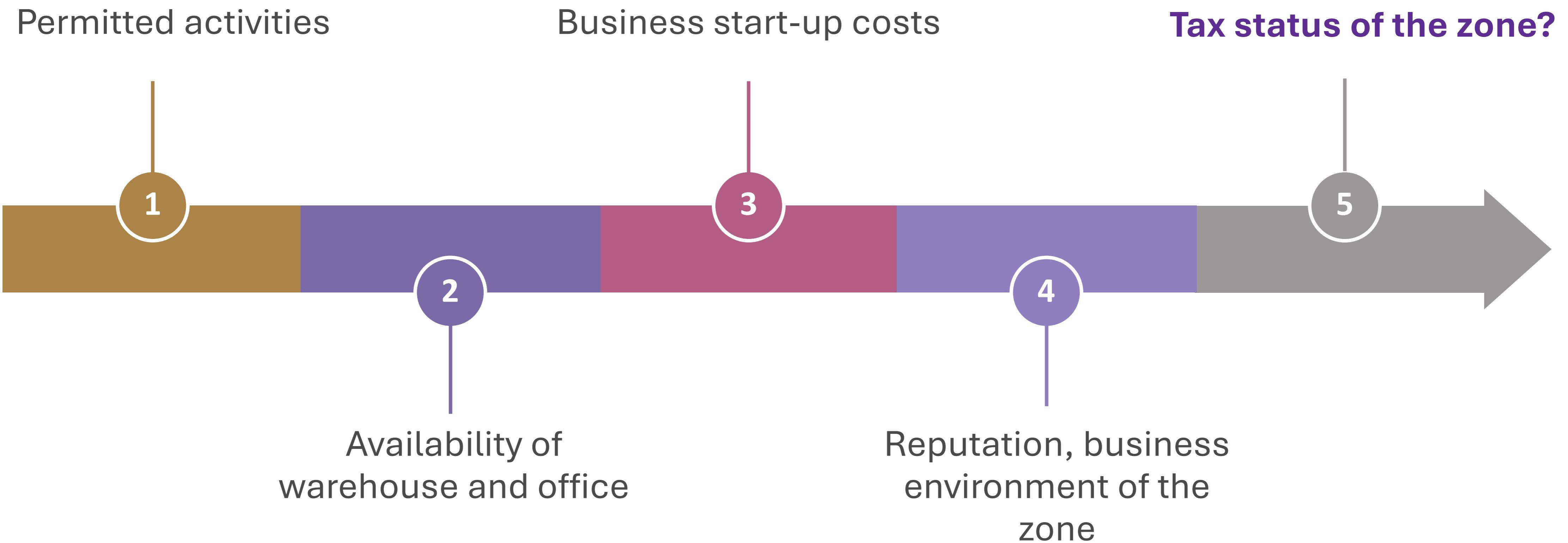
Incorrect selection of a Free Zone

Factors to consider when choosing a Free Zone

An overview of Free Zones

Case study – Distribution of goods

Factors to consider when choosing a Free Zone

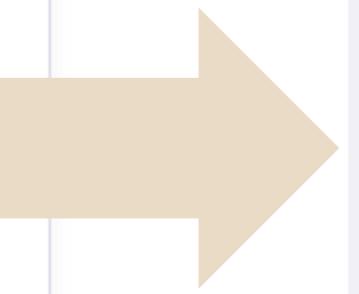




Free Zone

«A designated and defined geographic area within the UAE that is specified in a decision issued by the Cabinet at the suggestion of the Minister»

There is [Cabinet Decision No. 54 of 30 May 2023](#), but there is no list of free zone



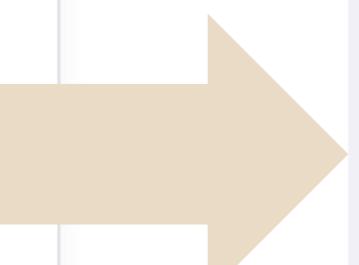
«All taxpayers should check with their respective Free Zone Authority to confirm if they operate in a Free Zone or Designated Zone for Corporate Tax purposes»



Designated zone

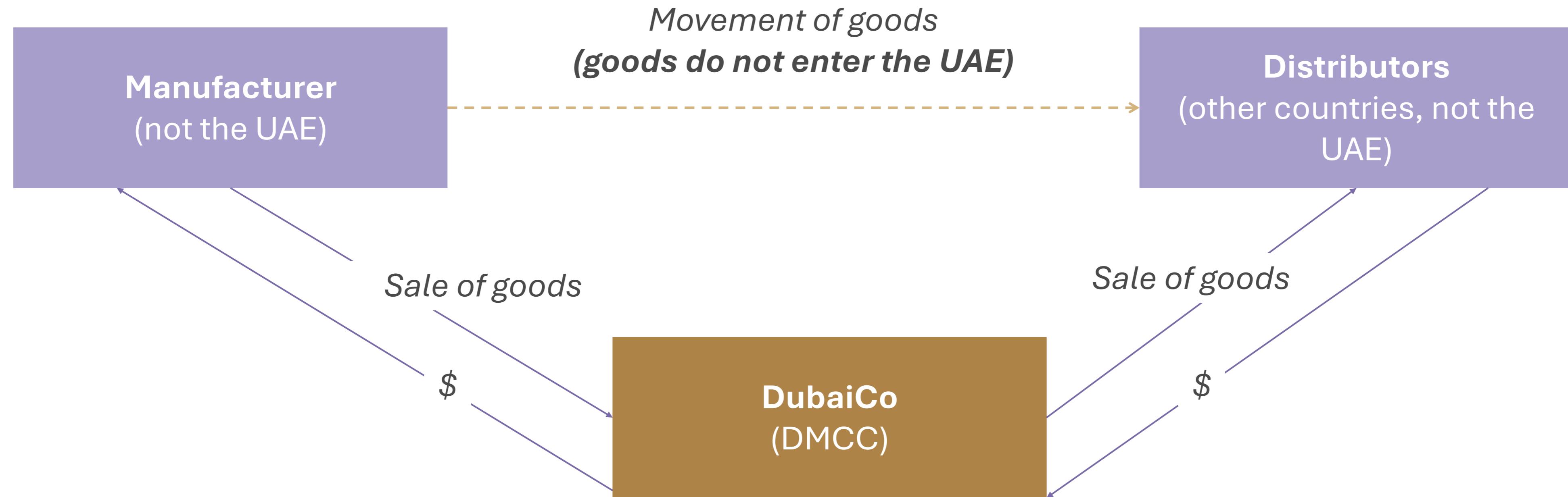
«A designated zone according to what is stated in Federal Decree Law No. 8 of 2017 ([reference](#)), and which has been included as a Free Zone in accordance with the Corporate Tax Law»

This is crucial for the 0% Corporate Tax rate for income derived from the distribution activities



[Corporate Tax Guide | Free Zone Persons | CTGFZP1](#)

Case study – Distribution of goods



*Goods are not Qualifying Commodities
DMCC is not a Designated zone*

No possibility to apply the 0% Corporate Tax rate in relation to income derived from the distribution of goods

02

Failure to control revenue sources

De minimis requirements

Case study – Holding of shares and securities

The **de minimis** requirements are deemed to be met if:

The non-qualifying Revenue in a Tax Period



5% of the total Revenue or AED 5,000,000 (whichever is lower)

Non-qualifying Revenue includes:

- (1) Revenue from Excluded activities
- (2) Revenue from non-qualifying activities, if the other party to the transaction is not a Free Zone person
- (3) Revenue from a FZP, where such FZP is not the Beneficial Recipient

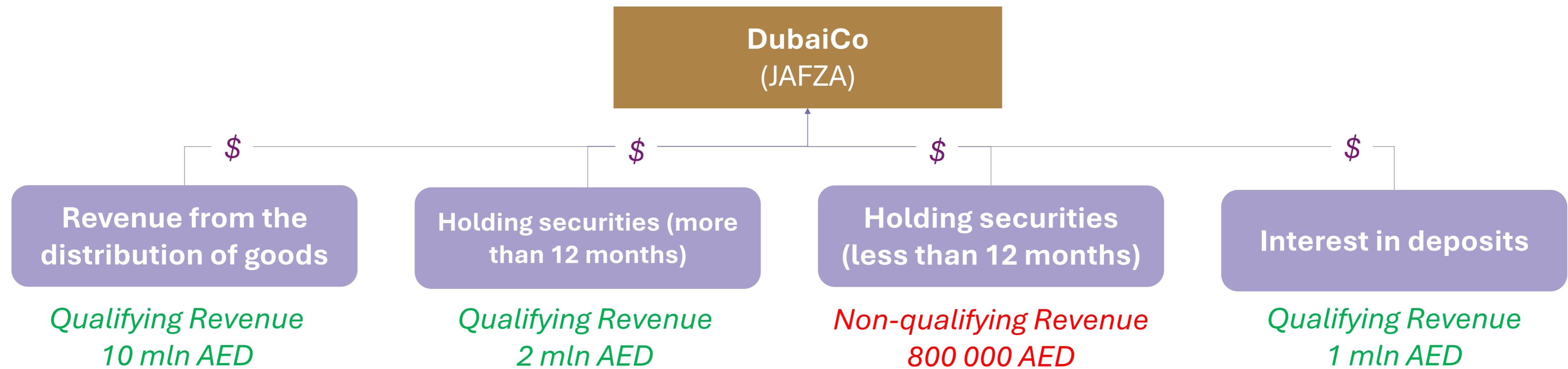
Total Revenue includes:

all Revenue received by a qualifying Free Zone person during the tax period



Income from immovable property, from a foreign or domestic permanent establishment and IP income (except for qualifying income), income of an Exempt person are EXCLUDED from the calculation

Case study – Holding of shares and securities



Total revenue – 14,5 mln AED

Non-qualifying revenue – 800 000 AED (less than 5 mln AED, but exceeds 5% of the total revenue)

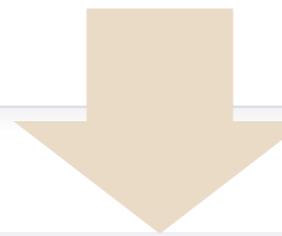


De minimis requirements are not met – the taxpayer is deprived of the 0% Corporate Tax rate in this tax period and 4 subsequent tax periods



Investment nature

«shares and other securities are deemed to be held for investment purposes when held for an uninterrupted period of at least (12) twelve months»



But what if the intention was to hold the securities for at least 12 months, but due to market changes the taxpayer was forced to sell them earlier (e.g., to avoid losses)?



A private clarification from the FTA (addressed individually, not applicable to all taxpayers)

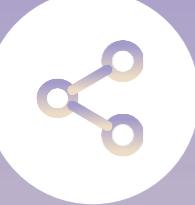
It may be possible to substantiate the investment nature of the acquisition if there is evidence of the initial intention to hold the securities for more than a year, along with justification for the early sale

03

Lack of adequate substance

The requirement to meet adequate substance

Case study on adequate substance test



Core Income Generating Activities (CIGAs)

All CIGAs related to the qualified activity must be carried out in the Free (Designated) Zone

CIGAs depend on the nature of the business

Personnel performing CIGAs must be located in the Free (Designated) Zone

Assets and operating expenses related to CIGAs must also be situated in the Free (Designated) Zone

Support functions (such as accounting, legal support, IT support, contract execution, and logistics) may be carried out either on the mainland or abroad



How is substance measured?

There are no specific figures or standard requirements regarding the level of presence

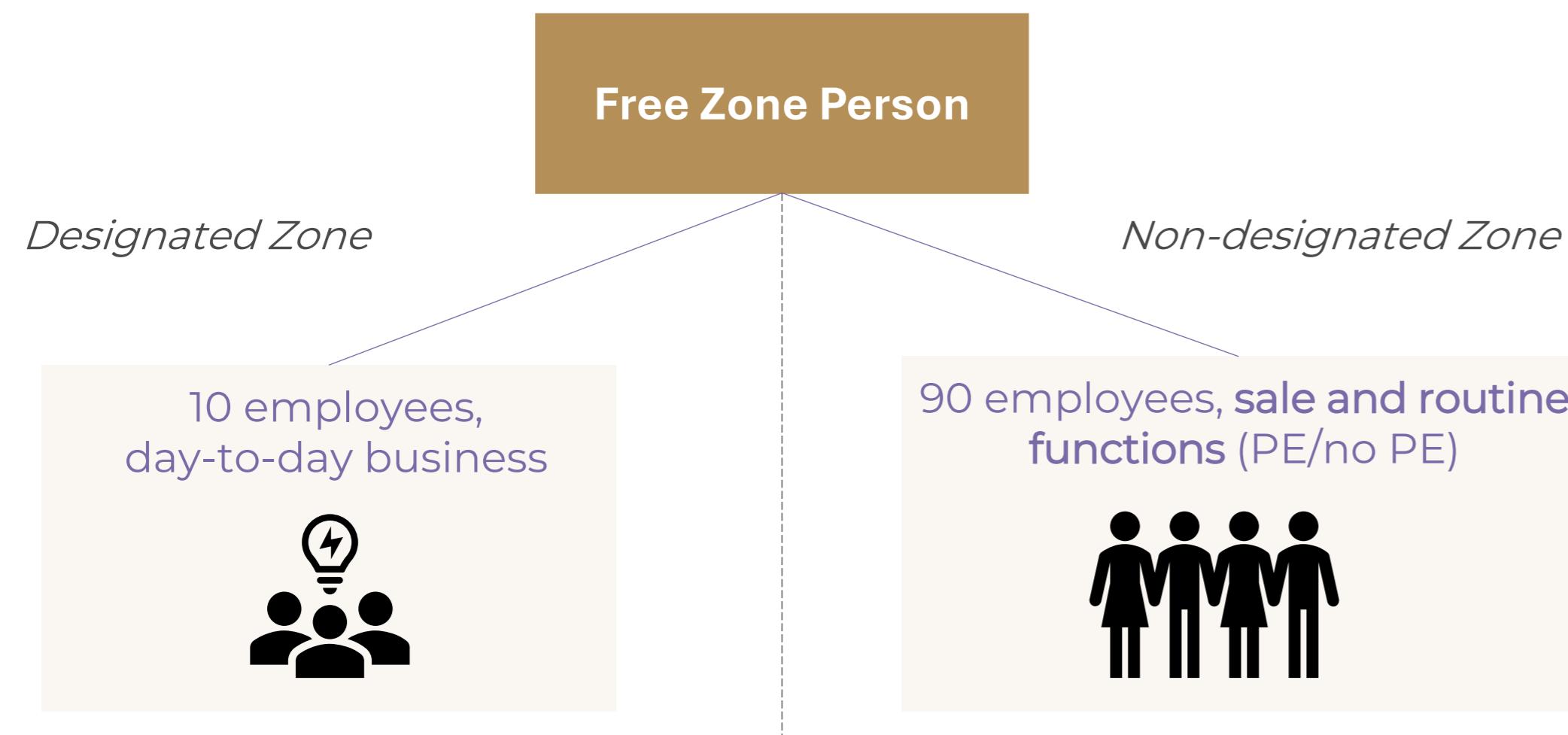
Neither the number of employees, nor the team composition, nor the quantity of tangible assets, nor the amount of expenses or their ratio to income are set out in numerical terms

«This would need to be determined on a case-by-case basis»

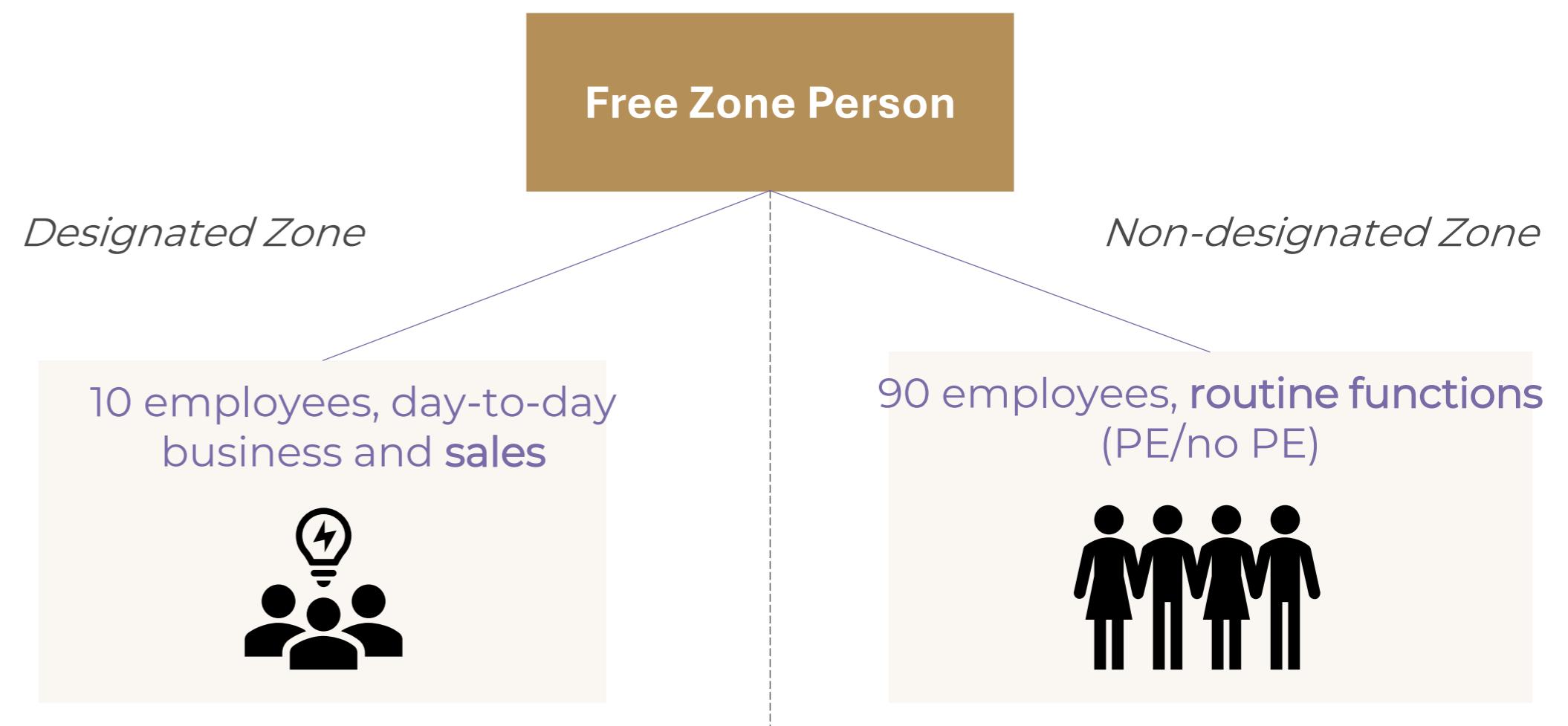
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Adequate Substance case study

Adequate substance examples for distribution business



vs.



 **Adequate substance test is failed, since CIGAs (sales) are not in the Designated Zone**

 **Adequate substance test is met, since CIGAs (sales) are in the Designated Zone**

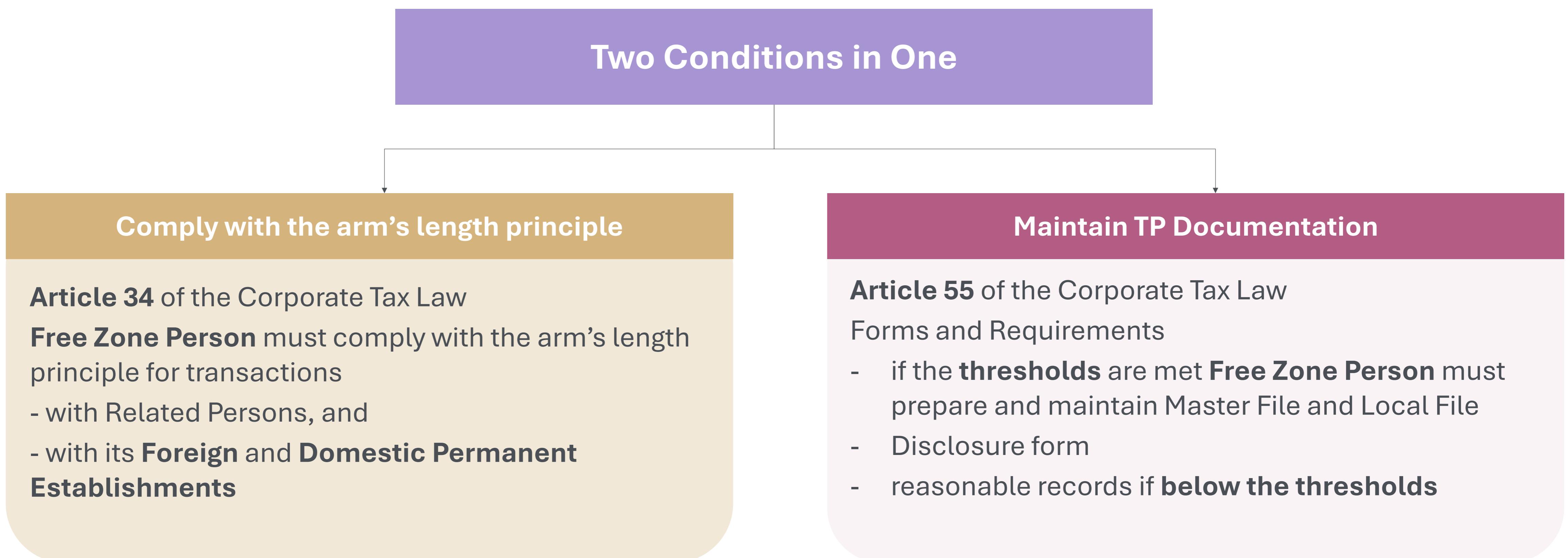
04

Non-compliance with TP rules

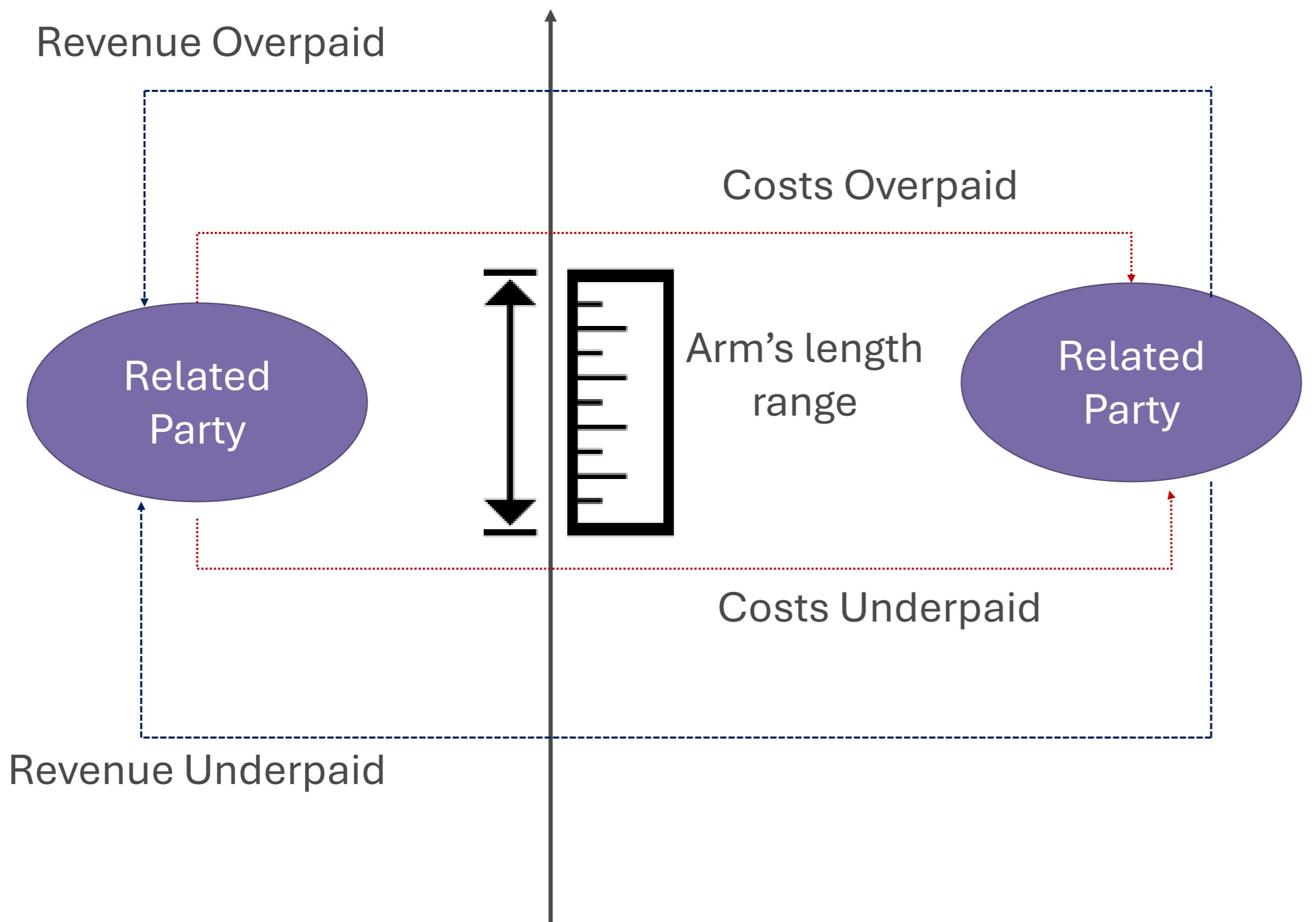
TP condition in details

Scope for the arm's length offences

True-up adjustment may fix non-arms length pricing?



Scope for the arm's length offences



Function and assets are scattered between multiple related parties





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