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AUDITING & ACCOUNTING

Corporate Tax HANDBOOK

for Free Zone Persons

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Key Concepts and Definitions

Corporate Tax (CT): Tax imposed on business income under the Corporate Tax Law. Applicable to both juridical persons and businesses.

Free Zone Person (FZP): A juridical person incorporated or registered in a Free Zone. This includes businesses set up in Free Zones, enjoying specific regulatory and tax advantages.

Qualifying Free Zone Person (QFZP): A Free Zone Person that meets specific criteria allowing them to benefit from preferential tax treatment. Criteria include maintaining adequate substance in a Free Zone, deriving qualifying income, and complying with transfer pricing and documentation requirements.

Qualifying Income: Income eligible for tax benefits under the Corporate Tax Law, derived from specified activities such as manufacturing, processing, and certain service provisions.

Requirements for Qualifying Free Zone Person (QFZP) Status

Substance in a Free Zone:

- Physical Presence: Must have adequate premises within the Free Zone, demonstrating a genuine business presence.
- Core Activities: Conduct core income-generating activities within the Free Zone. This includes operational and management activities essential to the business.

Qualifying Income:

- Income Sources: Must derive income from specified qualifying activities such as manufacturing, processing, trading, and certain services.
- De Minimis Requirement: Must ensure that non-qualifying revenue does not exceed a specified threshold (e.g., 5% of total revenue).

Requirements for Qualifying Free Zone Person (QFZP) Status

Compliance:

- Transfer Pricing: Adhere to the arm’s length principle for transactions with related parties. This ensures that prices charged in related party transactions are comparable to those charged in independent transactions.
- Documentation: Maintain proper transfer pricing documentation to substantiate the arm’s length nature of related party transactions.
- Audited Financial Statements: Prepare and maintain audited financial statements in compliance with applicable accounting standards.

Election Not to be a QFZP:

- Opting Out: A Free Zone Person can choose to be taxed under the standard corporate tax rules instead of benefiting from QFZP tax incentives. This election must be communicated to the tax authorities and is generally irreversible for a specified period.

Tax Rates

- **QFZP Tax Rate:** Preferential tax rates apply to qualifying income. This can include a reduced corporate tax rate or full exemption, depending on the specific Free Zone regulations and compliance with qualifying criteria.
- **Non-QFZP Tax Rate:** Standard corporate tax rates apply to Free Zone Persons who do not meet the QFZP criteria. This typically involves higher tax rates and fewer exemptions.

Income Classification

Qualifying Income: Includes income from activities such as:

- Manufacturing and processing goods.
- Trading in goods and commodities.
- Holding shares and securities.
- Management and operation of ships.
- Provision of reinsurance and fund management services.
- Offering headquarters, treasury, and financing services to related parties.

Non-Qualifying Income: Income derived from activities not specified as qualifying, such as:

- Certain financial services (e.g., banking, insurance).
- Transactions with natural persons.
- Activities conducted outside the Free Zone without adequate supervision and control.

Maintaining Adequate Substance

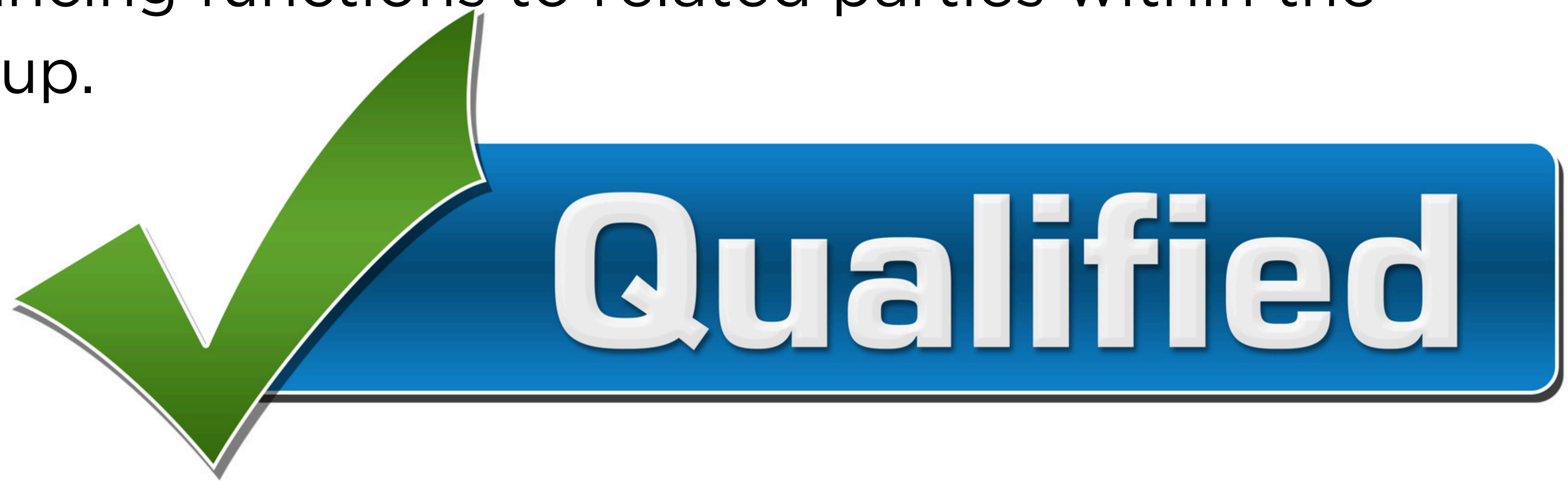
- **Core Activities:** Must be performed within the Free Zone to qualify for tax benefits. This includes administrative functions, management decisions, and day-to-day operations.
- **Outsourcing:** Allowed under certain conditions, but the QFZP must demonstrate adequate supervision and control over outsourced activities. This includes maintaining oversight and ensuring that the activities are conducted as per the arm's length principle.

Immovable Property and Intellectual Property

- **Immovable Property:** Includes real estate properties located within or outside Free Zones. This can encompass commercial properties, warehouses, and industrial facilities.
- **Qualifying IP:** Intellectual Property that meets specific conditions for tax benefits. This typically includes patents, trademarks, and copyrights used in qualifying activities.
- **Tracking Systems:** Required to demonstrate the nexus between the IP and the income derived. This involves maintaining detailed records of IP-related expenditures, revenues, and compliance with local and international IP regulations.

Qualifying Activities - Examples

- **Manufacturing and Processing:** Transformation of raw materials into finished products within the Free Zone.
- **Trading Commodities:** Buying and selling goods, including import and export activities.
- **Holding Shares and Securities:** Investment in and management of shares and securities.
- **Managing and Operating Ships:** Activities related to maritime operations and logistics.
- **Reinsurance and Fund Management Services:** Providing financial services such as reinsurance and managing investment funds.
- **Headquarters, Treasury, and Financing Services:** Offering centralized management, treasury, and financing functions to related parties within the group.



Excluded Activities - Examples

- **Transactions with Natural Persons:** Engaging in business transactions directly with individual consumers.
- **Banking and Insurance:** Activities related to providing banking and insurance services.
- **Specific Financial Services:** Certain financial and investment services not specified as qualifying.
- **Business Activities Outside Free Zone:** Conducting business outside the Free Zone without maintaining adequate supervision and control.

Compliance and Record-Keeping

- **Records:** Maintain accurate and detailed records of all business transactions, income, and expenditures in line with accounting standards specified by Ministerial Decision No. 114 of 2023.
- **Tax Registration:** Free Zone Persons must register for corporate tax with the relevant tax authorities and obtain a tax registration number.
- **Filing and Payment:**

1. Tax Returns: Submit annual corporate tax returns detailing income, expenditures, and tax liability.
2. Tax Payments: Pay the due corporate tax within the specified deadlines to avoid penalties and interest.

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