

ATOZ ALERT

United Arab Emirates introduce a Top-Up Tax in line with the OECD's Pillar Two rules

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The Ministry of Finance of the United Arab Emirates (“UAE”) recently released a [Cabinet Decision No. 142 dated 31 December 2024](#)¹ (the “Decision”) introducing a top-up tax for Multinational Enterprises (“MNE”) in line with the Organisation for Economic Co-operation and Development (“OECD”) framework (the “Top-Up Tax”). The Decision implements Federal Decree-Law No. 47 of 2022 on the Taxation of Corporations and Businesses (the “TCB Law”), as amended [by Federal Decree-Law No. 60 of 2023](#).

In this article, we describe the main provisions of the Decision implementing a Top-Up Tax in the UAE and applicable to fiscal years beginning on or after 1 January 2025.

Background

To ensure that large internationally operating businesses pay a minimum level of tax regardless of where they are headquartered or the jurisdictions they operate in, the Global Anti-Base Erosion (“GloBE”) rules, also called “Pillar Two”, agreed upon by the OECD/G20, introduce a global minimum corporate tax rate set at 15%.

The global minimum corporate tax is levied through a Top-Up Tax using an effective tax rate test calculated on a jurisdictional basis and using a common definition of covered taxes and a tax base determined by reference to financial accounting income (with adjustments for tax policy alignment and timing differences).

On 2 October 2023, Federal Decree-Law No. 60 of 2023 amended the Federal Decree-Law No. 47 of 2022 on the Taxation of Corporations and Businesses (the “TCB Law”) to introduce the Top-Up Tax principle in UAE law.

The Decision now establishes detailed rules for its application, ensuring that **MNE with low-taxed income in the UAE** are subject to a minimum effective tax rate of **15%**.

¹ i.e., 30 Jumada al-Akhir 1446

The UAE's statutory corporate tax rate is currently 9%, below the 15% global minimum tax rate under Pillar Two.

Entities in the scope of the Top-Up Tax

The Top-Up Tax is due, for a fiscal year, by constituent entities located in the UAE that are part of a group that:

- has, in principle, annual revenues of at least EUR 750 million on a consolidated basis (i.e. based on the consolidated financial statement of the ultimate parent entity ("UPE") of the group) in at least two of the four fiscal years preceding the tested fiscal year.
- qualifies as an "MNE Group" because it includes at least one entity or permanent establishment that is not located in the jurisdiction in which the UPE of the group is located.

Constituent entities that are members of a 'Minority-owned Subgroup', 'Joint Ventures' ("JV") and 'JV Subsidiaries' located in the UAE during the relevant fiscal year, as well as 'Stateless Constituent Entities' created in accordance with the laws of the UAE and that are 'Reverse Hybrid Entities' may also be subject to the Top-Up Tax with respect to any of their 'Pillar Two Income or Loss' as allocated and computed in accordance with the Decision.

Excluded Entities

The following entities are not considered as constituent entities and thus are out of the scope of the Decision:

- Government entities, international organisations, non-profit organisations, pension funds and investment funds that are UPEs of an MNE Group ("Excluded Entities").
- Entities owned by at least 95% or 85% by Excluded Entities under certain conditions (primarily targeting certain types of (intermediate) holding companies).

Investment funds and real estate investment vehicles under the Decision, are excluded only when they are UPE, meaning they have to be at the top of the ownership structure. A UPE is defined as an entity that owns, directly or indirectly, a controlling interest in any other entity and that is not owned, directly or indirectly, by another entity with a controlling interest in it. A controlling interest means an ownership interest in an entity whereby the interest holder is required, or would have been required, to consolidate the assets, liabilities, income, expenses and cash flows of the entity on a line-by-line basis, in accordance with an acceptable financial accounting standard.

The Decision also mentions that a constituent entity that is an 'Investment Entity' located in the UAE is itself not subject to the Top-Up Tax (however, this may nevertheless impact other group entities of the same MNE Group, if any).

Effective Tax Rate and Top-Up Tax

According to the Decision, the Top-Up Tax percentage for a fiscal year shall be computed in accordance with the following formula:

$$\text{Top-Up Tax percentage} = \text{minimum tax rate} - \text{effective tax rate}$$

The Decision sets the minimum effective tax rate at 15% and describes how to calculate the effective tax rate ("ETR") of an MNE Group in the UAE.

The ETR is obtained by dividing the adjusted covered taxes of the group (corporate and equivalent taxes) by the net qualifying income earned by the constituent entities of the group in the UAE. The ETR is calculated by fiscal year.

For this purpose, covered taxes include income or profit taxes recorded in the financial accounts, taxes imposed in lieu of a generally applicable corporate income tax, and taxes levied on retained earnings and corporate equity, including a tax on multiple components based on income and equity.

What is the net qualifying income to be taken into account?

The qualifying income or loss of each constituent entity used for the calculation of the ETR and the Top-Up Tax shall be computed by making adjustments to the financial accounting net income or loss of the constituent entities for the fiscal year before any consolidation adjustments for intra-group transactions. The financial accounting net income or loss of the constituent entities shall be determined in accordance with the standalone financial statements prepared in accordance with IFRS.

In summary, adjustments to the financial accounting net income or loss shall notably be made for:

- net tax expenses;
- excluded dividends;
- excluded equity gains or losses;
- included revaluation method gains or losses;
- specific gains or losses from asset and liability disposals;
- asymmetric foreign currency gains or losses;
- policy disallowed expenses;
- prior period errors and accounting principal changes;
- accrued pension expenses and income; and
- excluded insurance reserves expenses.

The Decision also provides for a specific 'International Shipping Income Exclusion' and 'Substance-based Income Exclusion'.

Safe Harbour Provisions

Transitional CbCR Safe Harbour

The Decision provides for a 'Transitional CbCR Safe Harbour' which is a temporary relief based on country-by-country reporting ("**CbC Report**") data, available for the period that covers all of the fiscal years that begin before 1 January 2027 and end before 1 July 2028.

According to this safe harbour, at the election of the filing constituent entity, the Top-Up Tax due for the constituent entities located in the UAE shall be equal to zero for a fiscal year if, for such fiscal year the average qualifying revenue of the constituent entities located in the UAE is less than EUR 10 million and the average qualifying income or loss of that jurisdiction is a loss or is less than EUR 1 million on its 'Qualified CbC Report' for the fiscal year.

The temporary relief will also apply if:

- the simplified ETR of the constituent entity is equal or greater than 16% for the fiscal years beginning in 2025 or 17% for the ones beginning in 2027. The simplified ETR is the ETR calculated by dividing the 'Jurisdiction's Simplified Covered Taxes' (i.e., the income tax expense as reported in the 'MNE Group's Qualified Financial Statements' after any adjustment required by the 'Transitional CbCR Safe Harbour' provisions) by its profit (loss) before income tax as reported on the MNE Group's 'Qualified CbC Report';
- the MNE Group's profit (loss) before income tax in the UAE is equal to or less than the 'Substance-based Income Exclusion' amount for entities reported in the UAE in the CbC Report.

Simplified Calculations Safe Harbour

The Decision also provides for safe harbour provisions to simplify compliance. As a result, at the election of the filing constituent entity, the Top-Up Tax (other than 'Additional Current Top-Up Tax') for the UAE shall be deemed to be zero for a fiscal year provided that the MNE Group meets one of the following tests with respect to its operations in the UAE:

- the Routine Profits Test: if its 'Pillar Two Income' in the UAE is equal or less than the amount that results from computing the 'Substance-based Income Exclusion' for the UAE;
- the De Minimis Test: if the 'Average Pillar Two Revenue' in the UAE is less than EUR 10 million, and the 'Average Pillar Two Income' in the UAE is less than EUR 1 million or has a loss as determined under the 'Simplified Income Calculation'; or
- the Effective Tax Rate Test: if the ETR of the UAE is at least 15%.

For the purpose of determining whether any of the tests are met in the fiscal year, a constituent entity may use a 'Simplified Income Calculation', 'Simplified Revenue Calculation', or a 'Simplified Tax Calculation' provided for in the Decision.

Top-Up Tax return

Each constituent entity, JV, or JV subsidiary in the UAE must file a Top-Up Tax return with Federal Tax Authority within:

- **in principle, 15 months after the last day of the reporting fiscal year, or**
- **18 months after the last day of the reporting fiscal year that is the first Transition Year.**

Transition Year means the first fiscal year that the MNE Group comes within the scope of the Top-Up Tax under this Decision. This means that for the 2025 reporting fiscal year, which should be a Transition Year for UAE constituent entities, the latter shall file their first Top-Up Tax return by the end of June 2027.

The Top-Up Tax return shall require equivalent information and reporting requirements set out in the [Pillar Two Information Return](#) developed at OECD level.

What is next?

The Decision seems to be in line with the **GloBE** rules. However, it remains to be seen whether the OECD grants the UAE the transitional qualified status confirming that the UAE Top-Up Tax is a 'Qualified Domestic Top-Up Tax' ("**QDMTT**") for purposes of the application of GloBE Rules by other jurisdictions. As at today, this qualified status is not yet recognised by the OECD in the latest version available of the [Central record of legislation with transitional qualified status for purposes of the Global Minimum Tax](#) dated 13 January 2025.

Indeed, the effectiveness of the global minimum tax under the GloBE rules results from the combination of three types of provisions that apply in accordance with the following order:

1. The QDMTT which applies first, at the level of source jurisdiction, in respect of any low-taxed profits arising in that jurisdiction.
2. The Qualified Income Inclusion Rule ("**IIR**") which applies in respect of remaining low-taxed profits of non-UAE constituent entities.
 - a. The IIR is applied first at the level of the UPE of the MNE Group and then shifts to the next Intermediate Parent Entity ("**IPE**") in the ownership chain in line with a top-down approach.
3. The Under Taxed Payment Rule ("**UTPR**") which works as a backstop rule and applies at the level of any constituent entity within the MNE Group, to the extent low-taxed profits are not subject to a Qualified IIR.

Recognition of qualified status is thus important for determining the order in which global minimum tax rules apply, i.e. to ensure coordinated outcomes and provide tax certainty for MNE Groups. To achieve this, the GloBE

rules establish a qualification system to ensure that the legislation of jurisdictions implementing the global minimum tax aligns with the GloBE rules.

The recognition of the transitional qualified status to the UAE is thus key to prevent the raising of a top-up tax by other jurisdictions applying the GloBE rules on the basis that the UAE Top-Up Tax would not be a QDMTT.

As the Decision does not introduce an IIR or an UTPR, it does not allow the UAE to levy a top-up tax on the basis that the foreign constituent entities or the foreign UPE of an MNE Group would not be subject to an ETR of at least 15% at this stage. It remains to be seen whether such rules will be introduced in the UAE in the near future.

Finally, the Minister may later specify how additional provisions of **Federal Decree-Law No. 47 of 2022** will apply to this Decision.

MNE Groups having UAE constituent entities should start preparing for the introduction of the Top-Up Tax by the Decision and review their exposure in light of the rules taking effect as from 1 January 2025.

Do you have any questions?



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