UNITED ARAB EMIRATES

Dubai: a return to normalcy

by Adriaan Struijk

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"Return to normalcy," the slogan with which Warren Harding won the US presidential election after World War I, perhaps best describes Dubai today. Property and rental prices are reasonable now (you can find a four-bedroom villa centrally located for €2000 a month), the taxis are plentiful, and the traffic jams are largely gone. Gone too is the hype. Major infrastructural works are in the final stages of completion: five bridges now cross the Creek, with the sixth and seventh set to be completed in 2012; the Dubai metro, probably the cleanest in the world, went into operation last year, with the last few stations still to be completed; Internet access used to be substandard, but now, a 40 Mbps fibreoptics connection costs as much as an average-speed ADSL connection cost last year. Dubai is now a more pleasant, cosmopolitan city then ever before.

In others ways, though, Dubai is anything but normal; and it is doing justice to its century long history as a trading hub. Dubai is a city where one can conduct business with a minimum of government interference, with access to the world's workforce, and no direct taxation and VAT. The financial crisis last year probably helped draw attention to what makes Dubai unique. Hence, the aspirations to implement VAT seem to be off the table for the time being.

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Operating a business in the UAE

Under UAE federal law, foreign businesses have three main forms to choose from to conduct business in the United Arab Emirates: as a local limited liability company; as a branch of a foreign company; or as a representative office of a foreign company. Alternatively, six out of seven Emirates (the exception being Abu Dhabi) offer the possibility to conduct business out of a free zone. And two emirates – Dubai and Ras al Khaimah – offer an International Business Company regime.

Free zones

If there is no need to sell goods directly to the local market, setting up in a free zone is often more attractive than setting up a local company, which requires 51% local ownership. This allows the provision of services through a free-zone entity to the local market as long as a significant proportion of the turnover is realised abroad. The main advantages of setting up in a free zone in the UAE are:

- 100% foreign ownership allowed;
- a guarantee for 15 to 50 years against the future imposition of corporation tax (it is not clear whether the guarantee covers an imposition of VAT as well);
- the import of goods duty free provided the goods are not supplied to the local market;
- streamlined procedures (all formalities are typically dealt with through the free zone authorities instead of the various government departments);
- no restrictions on hiring expatriates.

The free zones each have their own profit-making free zone authority. Their main source of income is from renting office space, collecting licence fees, and providing services to companies operating in the free zone. All share the features above but differ along the following lines.

- Many free zones focus on attracting businesses from a particular sector, though there is flexibility.
- Office rents outside Dubai are significantly lower.
- Minimum office space required to be rented varies.
- Support facilities.
- Annual trade licence fees.
- Paperwork in forming the business.
- Capital requirement.
- Number of visas allocated per square metre of office space.

In all free zones financial statements need to be submitted to the free zone authorities annually.

It was a requirement to rent office space until a few years ago, but some free zones outside Dubai have introduced a flexi-desk concept: a room is shared or a desk is rented for a number of hours a month. This translates into a much lower annual cost. Among others, the Ajman Free Zone, RAKIA Free Zone, RAK Free Trade Zone, and the VirtuZone in Fujairah offer this option.

The free zones also compete with each other on the speed of set up. Ajman Free Zone companies, for instance, can be set up in 1 day after the required documents have been submitted.

Finally, the capital requirement has been falling in all free zones. AED500,000 used to be the absolute minimum capitalisation requirement in the free zones located in Dubai; now several do not require any capitalisation (the RAKIA free trade zone, for example) and others have lowered it significantly (such as Silicon Oasis, a free zone aimed at technological companies in Dubai, which dropped the requirement to AED100,000).

International Business Companies

Dubai, through its Jebel Ali Free Zone, and Ras al Khaimah, through the RAKIA free zone and the RAK Free Trade Zone, offer an IBC regime. These companies are ideal for holding investments such as shares in local or free zone companies, UAE real estate, or for trading activities outside the UAE. IBCs cannot rent office space or apply for staff visas, and they are not allowed to trade with parties inside the UAE.

Navigating international waters

Although the UAE is a zero-tax jurisdiction, it has managed to navigate the international efforts aimed at cracking down on "offshore" quite well. It is on the Organisation for Economic Co-operation and Development (OECD) Financial Action Task Force's "white list" of cooperative jurisdictions, it is not castigated as one of the secrecy jurisdictions in proposed US legislation, and it has managed to stay out of the European Savings Directive Zone. It has concluded approximately 50 tax treaties, many of them with OECD countries. In its tax treaties, the UAE has consistently refused to include a clause requiring it to assist in the collection of taxes on behalf of the other contracting state. An exchange of information article, however, is normally included. Most of the tax treaties are not very attractive due to "limitations of benefits" clauses, the inclusion of liable-to-tax clauses and uncertainty as to whether UAE residents are considered to be liable to tax in the context of the treaty. Some restrict the benefits for individuals to UAE nationals, and some can only be accessed by government entities. However, several, such as the treaties with India, New Zealand, Austria and the Netherlands, have a liable-to-tax requirement. The treaty with the Netherlands was ratified in June 2010 and its most important effect for outward investment is that it limits the dividend withholding tax rate to 5%. The Netherlands is a particularly attractive country for inward investment into the UAE now because for most items of income the Netherlands will exempt UAE income even though it has not been subject to tax. Gains and dividends derived from a UAE subsidiary are exempt under domestic legislation in the Netherlands (subject to conditions).

Summary

All in all, Dubai offers something that to many will sound too good to be true: an unrivalled lifestyle in a business-friendly, no-tax environment, with a strategic location and an international reputation. ■