

Understanding Participation Interest Exemption

What is Participation Interest?

A Participating Interest means, either a 5% (five percent) or greater ownership interest or the acquisition cost of that ownership interest equal to or exceeds AED 4,000,000 (four million dirhams) in the shares or capital of a juridical person.

Exemption Criteria

Holding test: Held or intention to hold, the participation interest for an uninterrupted period of 12 months.

Subject to tax test: The participation except in a qualifying freezone or an exempt person is liable to corporate tax, or any other tax with a minimum rate of 9%, as mandated by the relevant laws of the country or territory where the juridical person is Resident. The principal objective and activity of the Participation is the acquisition and holding of shares or equitable interests and the income of the Participation derived during the relevant Tax Period or Tax Periods substantially consists of income from Participating Interests.

Ownership test: The Taxable Person is entitled to a minimum share of 5% of the profits allocated for distribution by the Participation and a minimum of 5% of the proceeds from the liquidation upon the termination of the Participation.

Asset test: Not more than 50% (fifty percent) of the direct and indirect assets of the

Participation consist of ownership interests or entitlements that would not have qualified for an exemption from Corporate Tax, if held directly by the Taxable Person, and should be satisfied throughout the Tax Period and should determine the satisfaction of the criteria basis of either of the following:

The consolidated balance sheet of the Participation and the accounting assets values reflected therein.

A Market Value valuation of the direct and indirect ownership interests and other assets of the Participation.

Ownership Interest includes the following:

- a. Ordinary Shares.
- b. Preferred Shares.
- c. Redeemable Shares.
- d. Membership and Partner Interests.
- e. Other types of securities, capital contributions and rights that entitle the owner to receive profits and liquidation proceeds.

An ownership interest shall only be treated as such if it is classified as equity interest under the Accounting Standards as applied by the Taxable Person holding the ownership interest.

Aggregation of Ownership Interests

Different types of ownership interests as specified above in the same juridical person as well as held by members of a Qualifying Group as per Clause (2) of Article (26) of the Corporate Tax Law in which the Taxable Person is a member shall be aggregated.

Treatment of Income derived from foreign participations as well as resident participations.

SI No	Income derived from a participation	From a foreign participation that is not a resident person	From a resident person
1	Dividend income/ other profit distributions not deductible for participation	Exempt	Exempt
2	Gain/loss on transfer, sales, or other disposition after 2 years from the acquisition of participation interest and subject to tax test	Exempt	Exempt
3	Foreign exchange gains or losses in participation interest	Exempt	Exempt
4	Impairment gains or losses in relation to participation interest	Exempt	Exempt
5	Deductible impairment loss in respect of loan receivable from a participation	Not exempt	Not exempt

The exemption under Article 23 of the corporate tax law does not apply to a loss realised on the liquidation of a Participation.

Liquidation loss = the acquisition cost of the Participating Interest (proportionate adjusted for any part disposals) Less the fair value of the liquidation proceeds received Less Liquidation cost.

The liquidation loss shall be adjusted for the following in the relevant Tax Period and the preceding Tax Period, as applicable:

- a. Tax Losses transferred by the Participation to the Taxable Person.
- b. Exempt Dividends or other profit distributions received by the Taxable Person from the Participation.
- c. Income or gains on the transfer of assets or liabilities between the Taxable Person and the Participation not taken into account under the provisions of transfers within the qualifying group or business restructuring relief of the Corporate Tax Law.

1. The value of the equity interest or capital contribution made, or consideration paid in cash or in kind for ownership interests in the Participation by the Taxable Person.
2. The value of any subsequent equity interest and capital contributions made to the Participation less the value of any equity interest or capital repayments made by the Participation to the Taxable Person.
3. Expenditure incurred by the Taxable Person in relation to the acquisition or transfer of ownership interests in the Participation that shall be **capitalised** as part of the acquisition cost of the ownership interest in the Participation. For example, professional fees, due diligence fees, litigation cost, appraisal and valuation cost etc.

Interest expenditure incurred in relation to the acquisition and subsequent holding of a Participating Interest shall be deductible subject to General Deduction Rule.

Computation of minimum acquisition cost

