

an overview of the

Maldives-UAE DTA



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Introduction

The Double Tax Avoidance Agreement (“DTA”) between the Maldives and United Arab Emirates (“UAE”) (“Maldives-UAE DTA”) holds a distinctive position in the history of Maldives’ international trade relations, as it marks the first-ever agreement of its kind between the Maldives and its bilateral trade partner.

The purpose of a DTA entered between any two jurisdiction is to prevent double taxation of income and capital and to attain a more balanced allocation of taxing rights than is achieved by domestic law alone. A DTA also makes clear of the taxing rights between contracting states on the different types of income arising from cross-border economic activities and reduces the overall tax burden falling on residents of the contracting states by way of a reduction or exemption of tax on certain types of income.

Signed on 17 October 2017, the Maldives-UAE DTA lays down the rules and procedures for determining the tax liability of individuals and entities operating in both countries. It covers various types of income, including dividends, interest, royalties, and capital gains, ensuring that taxpayers are not subjected to excessive taxation in either jurisdiction. The treaty applies from 1 January 2017.

This overview provides a brief analysis of the Maldives-UAE DTA. The key provisions of the DTA will be looked at, including the implications it has on enterprises attempting to make use of the treaty.

1. Scope of the DTA

The general position is that the DTA applies to a **person** who is resident of either states, meaning that if a person does not satisfy either the criteria of residence of one or both of the contracting states, they cannot access the benefits afforded under the DTA.

“Person” includes an individual, a company and any other body of persons.

Article 5 defines the concept of residence for the purpose of DTA. This is one of the most fundamental conditions for the application of DTA as the DTA benefits such as the allocation rules and relief from double taxation flow from this. A mechanism (often referred to as **tiebreaker rules**) is provided in Article 5(2) and (3) whereby a person can ensure they are only treated as being a resident of one of the two states.

A resident of Maldives is considered as any person who, under Maldives law, is a resident for tax purposes whereas a person can qualify as a resident of UAE if he/she is a UAE national. Since each country has its own distinctive definition of residency, a person may qualify as a resident in more than one country. As the scheme of the DTA only works if a person is resident in one of the states, the DTA provides the following tiebreaker rules for individuals to determine residency in one of the states:

1. Permanent home available to the resident
2. Personal and economic relations
3. Habitual abode
4. National
5. Mutual agreement

Where an individual is considered as tax resident of both contracting states, for treaty purposes, the individual is deemed to be resident of the state in which he or she maintains their permanent home. Where permanent home test does not suffice, i.e., if he or she has a permanent home in both states or in neither, the residency status will be determined taking into account the individuals personal and economic relations (centre of vital interests). In case, the centre of vital interests cannot be determined, the next test is to examine the habitual abode. In case where the habitual abode cannot be determined, the next test is to examine the state of which the person is a national. Where all of these tests fail to break the tie, the countries are required to determine the residency via mutual agreement.

If a company or any other person other than an individual is considered as tax residents of both Maldives and UAE by application of the residency definitions of the respective states, for treaty purposes, the person is deemed to be a resident only of the state in which they have their place of effective management.

2. Relief from double taxation

DTA applies to persons who are residents of one of the contracting states to the DTA and the function of the DTA is to allocate the various types of income, between the relevant contracting states. In some cases, there is a relatively clear allocation of income to the resident state (e.g., Article 11 dividends) or the source state (e.g., Article 8 business profits of a PE that are attributable to that PE). In other circumstances the right to tax the income is shared between the resident and source state (e.g., Article 13 where the source state may tax up to a certain percentage of royalty).

Article 23 provides the mechanism for granting relief from double taxation where a resident of a contracting state is required to pay taxes in the other contracting state. The Article follows **ordinary credit method** whereby the resident state allows as a deduction from its own tax on the income of its resident, an amount equal to the tax paid in the source state on the income derived from the source state. This deduction is restricted to the appropriate proportion of its own tax.

For example ...

A Maldives tax resident may derive income from UAE according to the provisions of the Maldives-UAE DTA and pay taxes in UAE. If that is the case, Maldives will allow a deduction on taxes of an amount equal to the taxes paid in UAE or the taxes that income must have suffered in the Maldives, whichever is lower.

As Maldives also provides unilateral foreign tax credit under the Income Tax Act, generally, there is no difference between the relief that a taxpayer could claim under domestic law and the relief that could be claimed under a DTA. However, the existence of the treaty provision guarantees that the relief continues to be available even if the residence state repeals the relief in its domestic law.

3. Business Profits & Permanent Establishments

The business profits of a resident of one contracting state are exempt from taxation by the other contracting state unless those profits are attributable to a **Permanent Establishment** (“PE”) located within that state. Meaning, the business profits of a UAE resident cannot be taxed in the Maldives, unless the UAE resident has a PE in the Maldives, and the business profits are attributable to the PE and vice versa.

Article 6 of the Maldives-UAE DTA defines a PE as a fixed place of business through which the business of an enterprise is wholly or partly carried on.

This includes the following:

1. a place of management;
2. a branch;
3. an office;
4. a factory;
5. a workshop;
6. a mine, an oil or gas well, a quarry, or other place of extraction of natural resources.

In addition to the above, a building site or construction or installation project is deemed to constitute a PE if it lasts more than 12 months. Similarly, furnishing of services including consultancy services through employee or other personnel are considered to establish a deemed PE, if such activities continue for a period aggregating more than 6 months in any 12-month period.

Article 6(6) lists a number of business activities, that if carried out by an enterprise resident in the other contracting state will not constitute a PE in that other state. The excluded activities will not constitute a PE even where they are carried out through a fixed place of business, and they can be described as being 'preparatory or auxiliary' in nature. These include storage facilities held for certain purposes, such as storage of goods for the purpose of display or delivery, maintenance of a fixed place solely for the purpose of carrying on activities that are of a preparatory or auxiliary character, etc.

4. Taxation of different types of income

Income from immovable properties

Article 7 of the DTA allocates the primary right to tax income derived from immovable property to **situs state** (that is the state in which the immovable property is situated).

What constitutes an immovable property is contingent upon the domestic law of the country in which the property is situated. Regardless, it includes property accessory to immovable property, livestock and equipment used in agriculture, forestry, rights to which the provisions of general law respecting landed property apply, usufruct of immovable property and rights to variable or fixed payments as consideration for working of, or the right of work, mineral deposits, sources and other natural resources – ships boats and aircrafts are not included.

Dividend

Dividends paid by a company that is a resident of one contracting state to a resident of the other contracting state is only taxed in that other state. Meaning, under the Maldives-UAE DTA, dividends are only taxable in the recipient's state of residence and that there are **no source state taxation** applied.

For example ...

Where a UAE-resident shareholders derives dividends from a Maldives-resident company, the dividends are not taxable in the Maldives regardless of the fact that the domestic law provides that dividends payable to non-residents by resident companies are considered as sourced from the Maldives and subject to taxation

Resident State: UAE



Treaty allocates taxing rights only to UAE

Source State: Maldives



Domestic Law: Withholding tax at 10%

Treaty: No tax allowed.



Interest

Similar to that of dividend income, under Article 12 of the DTA, interest arising in a contracting state and paid to a resident of the other contracting state is **only subject to taxation in the recipient state**. Article 12(1) provides that a resident in State A who derives interest from a source in State B will be taxable only in State A.

Hence, even in the case of interest income, where a UAE-resident lender earns interest income from a loan advanced to a Maldives-resident company, the interest income arising from the Maldives is not taxable in the Maldives.

Shipping and air transport

Profits derived by an enterprise of a contracting state from the operation of ships and aircraft in international traffic (determined **based on effective management** of the enterprise) shall be taxable only in that contracting state.

The provision applies to the share of the income from the operation of ships or aircraft derived by an enterprise of a contracting state through participation in a pool, a joint business or an international operating agency and selling of tickets on behalf of another enterprises.

Students and trainees

Students and trainees who were residents of a contracting state immediately before visiting the other contracting state, for the purpose of training or education and are temporarily present in the other contracting state solely for the purpose of education or training, shall be exempt from tax in the other state.

Royalties

Royalty income arising in a contracting state and paid to a resident of the other contracting state may be subject to taxation in the recipient state. However, royalties may also be taxed in the source state at a reduced rate of 7% of the gross amount of the royalties.

While this may result in a full levy of tax in the residence state plus a partial levy in the source state, residence states in this situation would grant double tax relief and the overall result would be that double taxation is avoided.

For example ...

Where a Maldives resident company pays royalty to a UAE-resident, the royalty being sourced from the Maldives, will be subject to tax in the Maldives at the reduced rate of 7%. However, this does not take away the right to tax royalty from UAE.

Resident State: UAE

Source State: Maldives



Royalty



UAE may tax the royalty income. Double taxation relief (credit will be applicable)

Domestic Law: Withholding tax at 10%

Treaty: May tax at the reduced rate of 7%

The Maldives-UAE DTA **definition of royalties** is limited to payments of any kind received as consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films and works on films, tapes or other means of reproduction for use in connection with television or radio broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use information (know-how) concerning industrial, commercial or scientific experience. It does not include payments received for use or right to use any industrial, commercial, or scientific equipment.

Snapshot

Type of Income	Treaty Provision
Income from immovable property	Taxed in the state in which the immovable property is situated.
Dividend	Only taxable in the recipient's state.
Interest	Only taxable in the recipient's state.
Shipping and air transport	Only taxable in the state of residence in which the place of effective management of the enterprise is situated.
Students and trainees	Exempt from tax in the visiting state.
Royalty	Taxed at a rate of 7% in the state in which the royalty income arises (i.e., source state). May be taxed in recipient state as well.

Note that the above provisions relating to dividend, interest and royalty income **do not apply if the recipient has a PE** in the state in which the income arises and, (1) in case of dividends; the holding in respect of which the dividends are paid, (2) in case of interest; the debt claim in respect of which the interest is paid, (3) in case of royalty; the right or property in respect of which the royalties are paid, are effectively connected with the PE of fixed base. In such case, Article 8 of the Maldives-UAE DTA will be applicable, and the specific type of income will be treated as business profits of the PE and will be taxed accordingly.

5. Taxation of Capital Gains

Article 14 of Maldives-UAE DTA covers the taxation of capital gains. The key rules prescribed in relation to disposal of different types of properties are as follows:

Immovable property

Gains derived by a resident of one contracting state from the disposal of immovable property that is situated in the other contracting state may be taxed in that other state. Meaning, gains arising from the alienation of an immovable property can be taxed in the state where the respective immovable property that is being disposed of is situated.

Movable property of a PE

Article 14(2) deals with movable property that forms part of the business property of a PE. Under the Article, capital gains on property falling within the definition of movable property that forms part of the property of a PE will only be taxed in the resident state.

Ships and aircrafts and boats

Gains from the alienation of ships or aircraft operated in international traffic or boats engaged in inland waterways transport, or movable property pertaining to the operation of such ships or aircraft or boats are taxable in the state of residence in which the place of **effective management** of the enterprise is situated.

Shares

Article 13(4) applies to gains realised from the sale of shares deriving more than **50 per cent of their value** directly or indirectly from immovable property.

Gains realised from the sale of shares deriving more than 50 per cent of their value directly or indirectly from immovable property may be taxed in the state in which the property is located, unless it is listed in a recognised stock market.

For example ...

If more than 50% of the value of a UAE holding company is directly or indirectly related to the property situated in the Maldives, then the disposal of the shares of the UAE holding company would be subject to capital gains tax in the Maldives and would be captured through domestic **'offshore-indirect transfer'** withholding tax rules as well as general capital gains tax rules.

Gains arising from the alienation of any other property other than those explained above will be taxable only in the recipient's state of residence.

6. Employment Income and Director's Fee

The general rule under Article 15 of the DTA with respect to salaries, wages, and other similar remuneration in respect of employment is that it will be subject to tax in the state in which the employment is exercised. In other words, in the contracting state where the employee is physically present when performing the activities for which the employment income is earned.

Article 15 also prevents the remuneration from short term assignments being taxed in the state in which the assignment is carried out. To qualify for this exception, the following three conditions must all be met.

- The recipient is present in the other state for a period of not exceeding in the aggregate 183 days in a 12-month period commencing or ending in the fiscal year concerned.
- The remuneration is paid by, or on behalf of, an employer who is not a resident of the country in which the employment is exercised.
- The remuneration is not borne by a PE that the employer has in the state in which the employment is exercised.

The purpose of the above exception is to facilitate the international movement of personnel and the operations of enterprises engaged in international trade. It ensures that employees are not subject to withholding tax where neither the employee nor the employer has a sufficient nexus with the source state.

Under the Maldives-UAE DTA, directors' fees or other similar payments received by the resident of one contracting state in his or her capacity as a director of a company that is resident in the other contracting state is only taxable in the contracting state. Therefore, even if a UAE resident director is paid a directors' fees from a Maldives-resident company, the same is not taxable in the Maldives.

Contact us

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About us

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We are ranked in the 2022 edition of Chambers Global Guide, and as a Recommended Firm by Asia Law Profiles in the area of General Business Law.

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