Exceptional Taxation: UAE Supreme Court Rules on Domestic and Foreign Related Companies' Tax Liabilities

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The recent judgment delivered by the Federal Supreme Court regarding the application of tax liabilities to related companies, even those situated outside the state, in exceptional circumstances where the tax event occurs within the state, is of paramount importance. It not only delineates the legal boundaries of tax obligations among interconnected corporate entities but also sets a precedent for how tax laws are interpreted and applied in cross-border corporate scenarios. This judgment underscores the necessity of a nuanced understanding of the legal and fiscal framework governing such entities, thereby providing a robust foundation for tax planning and compliance, especially in an increasingly globalized business environment.

Tax events amongst related entities

The Federal Supreme Court's analysis concerning a tax event and the separation of liabilities among multi-entity enterprises is a nuanced examination of the legal and fiscal responsibilities that these entities bear. The court's reasoning on the matter sheds light on the intricate fabric of corporate law and tax obligations, particularly in the context of parent and subsidiary companies or branches.

The court underscores the distinct legal persona of a subsidiary company, which is conceived through the collaboration of another company, yet operates independently from its parent company. This independence is manifested in its legal and moral personality, enabling it to acquire rights and bear obligations. The subsidiary, with its unique name and domicile, operates as a separate legal entity, its nationality remaining unblended with that of its partners or parent company.

On the other hand, the tax event, as delineated by the court, is a pivotal circumstance that triggers tax liability. The court adopts a clear standard in identifying the tax event, which is fundamentally the supply of goods within the state. This standard is instrumental in determining the tax liability, which is incumbent upon the entity where the tax event is realized.

The separation of liabilities among multi-entity enterprises is a complex domain, necessitating a meticulous examination of the legal and fiscal dynamics that govern the relationships between parent companies, subsidiaries, and branches. The court's analysis provides a robust framework for understanding these dynamics and the legal parameters that define tax liability in the context of multi-entity enterprises and multinational companies.

The Supreme Court says in this regard:

"The subsidiary company is the company that is co-founded by another company and is independent. Originally, from a legal standpoint, it is independent of the parent company, and its legal and moral personality is established, which qualifies it to acquire rights and bear obligations. It is considered a separate legal entity from the partners and the parent company. The subsidiary company has an independent name and domicile, which is the place where its main administration is located. Also, its nationality does not mix with the nationality of the partners. The person liable for tax is the one in whom the event established by law is available. The

legislator adopted a clear standard in determining the event that creates the tax liability.”

Tax liabilities for out-of-state entities

The Federal Supreme Court’s analysis on the application of tax liabilities to related companies, even those situated outside the state, in exceptional circumstances where the tax event occurs within the state, unveils a nuanced understanding of the legal and fiscal framework governing such scenarios. The Court emphasizes the sanctity of the distinct legal persona of each company, underscoring the principle that the tax liabilities of one cannot be arbitrarily imputed to the other. However, it carves out an exception to this rule in extraordinary circumstances, thereby introducing a layer of complexity to the tax liability discourse.

The Court’s stance is rooted in a logical necessity that once the tax event is realized, the tax assessment becomes anchored in the legal truth. This notion of a tax event is pivotal as it triggers the tax liability, and its occurrence within the state’s jurisdiction is a critical factor in determining the tax obligations of related companies. The Court highlights that the tax liability is not merely a function of the corporate structure or the domicile of the companies but is intricately tied to the locus of the tax event.

This analysis brings to the fore the concept of exceptional circumstances as a determinant of tax liability. The Court posits that in such rare scenarios, the veil of separate legal persona of related companies may be pierced, allowing for the tax liabilities to be assessed in a manner that transcends the conventional boundaries of corporate separateness. This is a significant departure from the traditional understanding of tax liability as being confined to the entity where the tax event is realized.

Furthermore, the Court’s discourse illuminates the legal rationale underpinning this exception. It underscores the imperative of a rational and equitable assessment of tax liability, particularly in scenarios where the strict adherence to corporate separateness may lead to an unjust enrichment or evasion of tax obligations. The Court’s analysis is grounded in a pragmatic understanding of the fiscal realities, recognizing the potential for cross-border corporate structures to be employed in circumventing tax liabilities.

The Court’s exposition also hints at a broader legal and fiscal paradigm wherein the principles of equity and justice are harmonized with the tenets of corporate law and tax policy. It invites a reevaluation of the legal doctrines governing the assessment of tax liability, particularly in the context of multi-company enterprises with cross-border operations.

Moreover, the Court’s narrative underscores the imperative for a meticulous examination of the circumstances surrounding the tax event, advocating for a judicious approach in the assessment of tax liabilities. This nuanced understanding of tax liability, as expounded by the Court, provides a robust framework for navigating the complex terrain of tax law, particularly in scenarios involving related companies with cross-border operations.

The Supreme Court says in this regard:

“It was decided, according to the judgment of this court, that the legal personality of both companies must be respected, and it is not permissible to penetrate it or decide the liability of one for the tax debts of the other, except in exceptional cases… As by logical necessity, as long as the tax event has occurred, the tax assessment becomes based on the correct law.”

Takeaway

In light of this judgment, tax planners should meticulously evaluate the legal and fiscal landscape governing the operations of related companies, especially those with cross-border operations. The clear distinction between the legal personas of related companies, as emphasized by the court, necessitates a thorough examination of the tax implications arising from the activities of each entity. Moreover, the exceptional circumstances clause introduced by the court warrants a careful analysis to ensure that tax planning strategies are robust enough to withstand legal scrutiny, particularly when the tax event occurs within the state's jurisdiction.

Furthermore, tax planners should consider adopting a holistic approach that takes into account not only the legal stipulations but also the ethical and reputational considerations associated with tax liabilities. The judgment serves as a reminder of the intricate interplay between corporate law, tax policy, and the overarching principles of justice and equity. By fostering a comprehensive understanding of the legal doctrines and fiscal realities underscored in the judgment, tax planners can better navigate the complex terrain of tax law, ensuring that the tax strategies devised are in compliance with the legal stipulations, and are resilient in the face of evolving legal and fiscal landscapes.

Additionally, in structuring contractual commitments and arrangements, it becomes imperative to meticulously consider the position articulated by the Federal Supreme Court. The judgment accentuates the significance of clearly delineating the legal and fiscal responsibilities of each entity involved, especially in scenarios where related companies engage in transactions that could trigger tax events within the state. Contractual arrangements should be crafted with a keen eye towards the legal nuances that could potentially impact tax liabilities, ensuring that the terms and conditions encapsulated within the contracts are in alignment with the legal framework elucidated by the court. This entails a thorough review and, if necessary, a revision of existing contractual commitments to ensure they are robust and resilient against the backdrop of the court's stance. By proactively addressing the implications of this judgment in contractual agreements, companies can mitigate risks, ensure compliance with prevailing tax laws, and foster a conducive environment for transparent and equitable business transactions.

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UAE Judgment on Creditors Claiming Tax Penalties from Debtors

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Wasel & Wasel has represented clients in over two hundred tax dispute procedures in the United Arab Emirates, gaining valuable experience in protecting taxpayers from tax penalties.

The tax consequences arising out of deficient payments by debtors in commercial transactions has consistently grown more important as more taxpayers face tax penalties. A recent Dubai judgment introduces a novel perspective to this dynamic. This judgment, which potentially empowers creditors to claim tax penalties from their debtors, represents a significant shift in the commercial and tax law landscape. This development is particularly noteworthy given the evolving tax regime in the UAE, underscoring its potential implications for future commercial interactions.

Liquidity Shortfall and Tax Penalties: The Age-Old Dilemma

When creditors issue invoices, they anticipate timely payment. However, delays in these payments can lead to a liquidity shortfall, preventing the creditor from meeting their tax obligations. This can result in penalties from the Federal Tax Authority (FTA). These penalties, often substantial, further strain the creditor’s finances, essentially penalizing them for the debtor’s delay.

The New Test Established by the Judgment

The recent judgment has introduced a potentially groundbreaking test for creditors. The creditor was subject to tax penalties imposed by the FTA and claimed those tax penalties from the debtor. The three-member tribunal addressed the claim over the tax penalties as follows:

“Regarding the request for the value added tax penalty, the plaintiff demands that the defendant be obligated to pay the VAT penalty…and whatever accrues until the date of paying the VAT. Given that the plaintiff did not provide evidence of paying the value of this penalty to the Federal Tax Authority, he cannot claim its payment from the defendant.”

This implies that if a creditor can provide evidence of having paid the respective tax penalty, they might be able to claim it from the debtor. This test, while seemingly straightforward, could have profound implications for commercial transactions, especially when considering the broader context of the UAE’s evolving tax landscape.

Understanding the Scope of Damages

The Civil Transactions Law recognizes both direct and indirect damages. If a particular head of damage encompasses both direct and indirect elements, the direct aspect takes precedence. Nevertheless, this does not preclude the possibility of claiming other heads of damages that are indirect alongside those that are direct.

The distinction between direct and indirect damages is further clarified in Articles 283 and 284 of the Civil Transactions Law. Direct damages necessitate a guarantee without any conditions. In contrast, indirect damages require an offence, intent, or an action that leads to harm. If both direct and indirect causes coexist, the ruling leans towards the direct cause.

Given this legal framework, it is evident that creditors have a viable avenue to claim tax penalties from their debtors. If a debtor’s delay in payment (the act) leads to a creditor facing tax penalties (the damage), and there is a clear causal relationship between the delay and the penalties, the debtor could be held responsible.

UAE Federal Decree-Law No. 47 of 2022: Implications for Companies and Their Debtors

The introduction of the UAE Federal Decree-Law No. 47 of 2022 on the taxation of corporations and businesses marks a significant shift in the UAE’s tax regime. With corporations now having to pay taxes on their profits, the financial landscape for businesses has undeniably changed.

In this new environment, the judgment’s potential to allow creditors to claim tax penalties from their debtors becomes even more relevant. Companies, now burdened with tax obligations on their profits, might face penalties due to liquidity issues arising from delayed payments by debtors. This judgment provides them with a potential avenue to recoup these penalties.

In essence, companies can utilize this legal avenue to ensure that they are not doubly penalized – first by the delay in payments from debtors and subsequently by the tax penalties arising from the new corporate income tax law. This development not only provides a safety net for businesses navigating the new tax regime but also serves as a deterrent for debtors, emphasizing the importance of timely payments in the broader context of the country's tax obligations.

Flexibility of Courts and Evidence Consideration

The judgment's statement, " Given that the plaintiff did not provide evidence of paying the value of this penalty to the Federal Tax Authority, he cannot claim its payment from the defendant," opens the door to a broader discussion on evidence. While evidence of payment is a clear route to claiming penalties, the courts' flexibility in considering other forms of evidence is crucial.

For instance, would enforcement actions by the FTA, despite the liquidity of the creditor, be sufficient evidence? This could be particularly relevant in cases where the creditor has made arrangements with the FTA or is contesting the penalty. Other forms of evidence might include communication with the FTA regarding the penalty, documentation of the liquidity shortfall directly resulting from the debtor's delay, or even evidence of the debtor acknowledging their role in the creditor's financial strain.

Such flexibility would be in line with the pragmatic approach by the UAE courts, focusing on the real-world implications and fairness of the law, rather than a rigid adherence to form.

Pragmatic Implications and the Way Forward

From a pragmatic standpoint, this judgment, especially when viewed in the context of the UAE's new tax law, could be transformative for creditors. It offers a potential remedy against the financial strain of delayed payments and the new tax obligations. Moreover, the potential flexibility of the courts in considering varying evidence further strengthens the creditor's position.

However, this potential remedy is not without challenges. Debtors could contest the validity of claims, and the exact nature and type of evidence accepted will likely be refined over time through subsequent judgments.

Conclusion

This judgment represents a significant development in the commercial and tax law landscape of the UAE. As the country's tax regime evolves, this judgment offers a potential safety net for businesses, ensuring they are not unduly penalized due to the actions of their debtors. The road ahead will undoubtedly see further clarifications and refinements, but for now, creditors have a new avenue to explore when faced with tax penalties..

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Disputes on Delayed Approvals in Construction: An Analysis of Dubai Court Judgments

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In the intricate tapestry of construction law within the United Arab Emirates (UAE), delays related to approvals have emerged as a recurring theme in disputes. The courts' approach to these matters is both nuanced and pragmatic, reflecting a deep understanding of the complex realities of construction projects. This article will dissect three key judgments from the Dubai Courts, each shedding light on the stance of the judiciary on delays arising from construction-related approvals.

Judgment 1: Case No. 673 of 2021, Court of Cassation (Dubai)

The case involves a maritime construction project. The developer's failure to obtain necessary approvals, licenses, and permits led to significant delays, resulting in the purchaser's request for contract termination.

Court's Findings and Reasoning

Contractual Obligations and Delayed Approvals: The court found that the developer's delay in obtaining necessary approvals was not excusable. The developer was expected to study the project's requirements and obtain all necessary approvals before commencing the project. The delay of over three years was deemed a breach of contractual obligations.

Rejection of Force Majeure: The court rejected the developer's claim of force majeure, reasoning that the delay in obtaining approvals did not constitute an unforeseeable event. The court emphasized that the delay was within the developer's control and did not render performance impossible.

Expert Evidence and Site Inspection: The court relied on an expert committee's report and site inspection, which revealed that the construction was incomplete and did not meet the agreed specifications. The court found this evidence sufficient to form its belief in the developer's failure to perform.

Interest Rate Adjustment: The court reduced the interest rate from 9% to 5%, balancing the developer's breach and the purchaser's legitimate expectations.

Relation to Disputes Arising from Approval Delays

The judgment offers significant insights into how courts may approach disputes arising from approval delays in construction projects:

Pre-Contractual Planning: The judgment emphasizes the importance of thorough planning and understanding of regulatory requirements before entering into a contract.

Clear Contractual Terms: The case underscores the need for clear contractual terms addressing potential delays and unforeseen challenges, including approval delays.

Judicial Discretion and Evidence Evaluation: The judgment illustrates the court's discretion in evaluating evidence and understanding the factual matrix, particularly concerning delayed approvals.

Judgment 2: Case No. 105 of 2013, Court of Cassation (Dubai)

The dispute at hand revolves around a construction project that suffered significant delays. The developer (the appellant) alleged that the delays were caused by factors beyond its control, including changes made by the principal developer and governmental inaction. The buyer (the respondent), on the other hand, contended that the developer's negligence and failure to meet its fundamental obligations led to the delays.

The Court's Reasoning

The Developer's Obligations: The court embarked on a detailed analysis of the developer's obligations under the contract and the relevant statutory provisions. It emphasized that the developer’s commitment was not confined to the explicit terms of the contract but extended to all that was necessary for the proper execution of the project, including obtaining necessary approvals and ensuring the readiness of the land.

The Developer’s Conduct: The court scrutinized the developer’s conduct, finding no credible evidence to support the claim that the delays were beyond its control. The absence of documents proving governmental interference or changes by the principal developer led the court to conclude that the developer was either negligent or in default of its obligations.

The Buyer’s Rights: The court also considered the buyer’s rights under the law, recognizing that the buyer was entitled to withhold payment if the developer failed to fulfill its corresponding obligations. The court’s reasoning was grounded in the principles of good faith and reciprocity that underpin contract law.

Analysis and Implications

The Importance of Documentation: This judgment underscores the critical importance of proper documentation in construction disputes. The developer’s failure to provide evidence of external factors leading to delays proved fatal to its case. Parties must be diligent in maintaining records that can substantiate their claims, particularly when alleging circumstances beyond their control.

The Interplay between Contractual and Statutory Obligations: The court’s interpretation of the developer’s obligations illustrates the complex interplay between contractual terms and statutory provisions. It serves as a reminder that parties must be mindful of not only the express terms of their agreements but also the broader legal framework within which they operate.

The Broader Context of Construction Disputes: The judgment also sheds light on the broader context of construction disputes arising from approval delays. It highlights the multifaceted nature of such disputes, encompassing not only legal and contractual issues but also practical considerations such as project readiness, governmental actions, and the conduct of various stakeholders.

Judgment 3: Case No. 161 of 2011, Court of Cassation (Dubai)

The dispute arose between a contractor and a property owner. The contractor, having completed a significant portion of the construction, alleged breaches due to delayed approvals, which they claimed led to increased costs and project delays. The owner, on the other hand, attributed the project's delays to the contractor's actions, particularly their cessation of work pending increased prices.

Delayed Approvals: The Heart of the Dispute

Cancellation of Annex and Modified License: The court's analysis delved deep into the impact of delayed approvals. Specifically, it examined the contractor's claim that the cancellation of parts of the work, such as a service annex, required a halt in work pending a modified license. The court found that such cancellations did not necessarily warrant a work stoppage.

Impact on Timelines: The court juxtaposed the actual project delays against the contractual timelines. It underscored the contractor's refusal to continue work without price hikes as a breach of contract. Yet, it also acknowledged the role of delayed approvals in extending the project's duration.

Increased Costs: The court recognized that delayed approvals, combined with the contractor's cessation of work, led to escalated costs for completing the remaining work. Damages were awarded, reflecting the multifaceted repercussions of delayed approvals.

The Court’s Reasoning

The court’s approach was marked by a meticulous examination of the contractual obligations, the parties’ conduct, and the overarching role of delayed approvals.

Contractual Obligations: The judgment emphasized the importance of clear contractual terms. In this case, the absence of provisions allowing the contractor to demand price increases due to delays became a pivotal point.

Expert Testimony: The court leaned heavily on expert testimony to decipher the cause of delays and the resultant damages. This reliance underscores the significance of expert analysis in disputes pivoting on delayed approvals.

The disposition of the court in this vein was as follows:

“And the cancellation of the annex and the issuance of a modified license does not cause a delay because the contractor does not stop work pending the issuance of the modified license, and there are no instructions from the municipality to stop the work until the issuance of the modified license, except in the works that include the execution of additions or additions to the building. As for the cancellation of parts of an issued license, as is the case in this lawsuit, the cancellation of a part of the licensed works, such as a service annex, does not require the contractor to stop until the issuance of the modified license. Also, the cancellation of the annex reduces the agreed-upon work that must be executed, and therefore reduces the time needed to execute what is agreed upon, and does not cause a delay.”

Implications for Construction Disputes

This judgment offers a lens into the handling of delayed approvals in construction disputes.

Understanding Different Types of Delays: The court’s nuanced differentiation between various types of delays provides a roadmap for future disputes, offering clarity on the distinct impacts of each delay type.

The Importance of Contractual Clarity: The case accentuates the need for lucid contractual terms, especially when navigating the murky waters of delayed approvals.

Assessment of Damages: The court's methodical assessment of damages resulting from delayed approvals sets a precedent for gauging the multifaceted impact of such delays..

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UAE judgments and tax committee decisions on FTA reconsideration procedures

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Wasel & Wasel has represented clients in over two hundred tax dispute procedures in the United Arab Emirates, gaining valuable experience in protecting taxpayers from significant losses over small procedural errors.

From the start of a dispute at the reconsideration stage to the final trial at the Federal Supreme Court, the issues extend beyond taxes and penalties. They fundamentally focus on whether procedures have been followed correctly.

This focus has been clear in numerous Federal court judgments and tax dispute resolution committee decisions since 2018. As a tax dispute moves through the court system, procedural integrity becomes increasingly scrutinized.

The Federal Tax Authority’s litigation team is held as one of the UAE’s most skilled government litigation departments. Therefore, it is crucial to have counsel who are experts in the specific challenges of litigating Federal Tax Authority decisions.

This article outlines key procedural judgments from the Federal courts and committees, providing insights for taxpayers on risk assessments and mitigation of taxes and penalties.

Part I: Evidencing the Reconsideration Procedure

Procedural Requirement

The reconsideration procedure necessitates the submission of evidence to establish that the objector has filed a request for reconsideration in accordance with the law.

Position of the Courts or Committees

The Dubai Tax Dispute Resolution Committee no. 100/2021 emphasized the importance of evidence in the reconsideration procedure:

“The evidence was devoid of anything that benefits establishing that the objector had filed a request for reconsideration, in accordance with the procedure set by law until the objection is considered by this committee, which makes the objection request submitted to the committee non-compliant procedurally.”

Legislative Impact

The Federal Decree-Law No. 28 of 2022 sets the legal framework for the reconsideration procedure, outlining the specific requirements for submitting evidence.

Takeaway/Guidance

The importance of evidence in the reconsideration procedure cannot be overstated. Taxpayers must ensure that all necessary documentation is included in the reconsideration request to establish compliance with the law.

Part II: Scope of the Tax Dispute

Procedural Requirement

The scope of the tax dispute must be clearly defined and confined to the specific issues at hand.

Position of the Courts or Committees

The Supreme Federal Court, in cases no. 327/2021, 220/2021, and 181/2021, provided guidance on the scope of the tax dispute:

“What the appellant raised regarding the legality of the tax imposition’s origin does not detract from that, as the scope of the relevant lawsuit does not relate to the extent of the legality of the tax imposition basically but its scope is limited to challenging the committee’s decision to cancel the delay penalty in payment, which does not allow exceeding that to reasons that were not a place for the relevant dispute from the beginning.”

Legislative Impact

The Federal Decree-Law No. 28 of 2022 does not explicitly define the scope of the tax dispute, leaving it to the courts to interpret and apply the law in this regard.

Takeaway/Guidance

Understanding the specific nature of the dispute and aligning legal arguments accordingly is essential. The scope of the dispute must be confined to the original issues, and overreaching must be avoided. In contrast, before a reconsideration request is filed, the taxpayer must ensure that the underlying decision obtained from the FTA encompasses all the items the taxpayer wishes to dispute.

Part III: Discretion in Accepting Late Reconsideration Requests

Procedural Requirement

The reconsideration procedure allows for the possibility of accepting late requests, provided there are valid reasons for the delay.

Position of the Courts or Committees

The Emirati judiciary, in Federal Primary Court case no. 424/2019 and 438/2019, considered the discretion in accepting late reconsideration requests:

“It is settled that the deadlines for appealing administrative decisions before the general appeal committees are characterized as regulatory deadlines intended for reconsideration of the administrative decision within specific deadlines without keeping them open without a controller for the stability of situations and legal positions. It means that the matter is left to the discretion of the administration in estimating the reasons for the excuse submitted for non-compliance with the deadline or the period specified by law, so if the applicant for reconsideration exceeds this specified period with an excuse accepted by the body, it has to override its will for these dates and address the reconsideration request. Saying otherwise makes the deadline set by the law non-existent, and the deadlines become open without a controller, which leads to instability of situations and legal positions that require the nature of tax laws and legislations due to the financial and economic effects on both parties, the state, and the tax funder. And the appellant company did not provide any reasons for not submitting its reconsideration request to the Federal Tax Authority within the specified period as stipulated in Article 27 of Law No. 7 on Taxes, and therefore the Authority rejected the request or did not accept it, its decision coincides with the correct law and what the tax legislator wanted."

Legislative Impact

The Tax Procedures Law No. 7/2017, before being replaced with Decree-Law No. 28/2022, provided the legal basis for this discretion, allowing the administrative body to assess the reasons for non-compliance with stipulated deadlines.

Takeaway/Guidance

The discretion in accepting late reconsideration requests emphasizes the importance of providing valid reasons for any delay. Taxpayers must be aware of this flexibility but should not rely on it without substantial justification.

Part IV: Issuance of a Reconsideration Decision After the Absence Thereof

Procedural Requirement

In the absence of a decision on a reconsideration request within the stipulated period, the administrative authority may still issue a decision, triggering a new period for recourse to the Tax Disputes Resolution Committee.

Position of the Courts or Committees

The Federal Supreme Court, in case no. 568/2022, provided guidance on this matter:

"As long as this deadline is among the regulatory deadlines, if a person submitted a reconsideration request and the request was not decided within the stipulated period, and he did not resort to the Tax Disputes Resolution Committee after the period specified to decide on his request had passed, and the administrative body – hypothetically – decided on the request a year after its submission, then the decision on the request opens a new period for resorting to the tax disputes resolution committee."

Legislative Impact

The Federal Decree-Law No. 28 of 2022 does not explicitly address this scenario, leaving it to the courts to interpret and apply the law in this unique situation.

Takeaway/Guidance

The lack of a reconsideration decision may be considered an implicit rejection that would grant the taxpayer right to proceed with the dispute before the competent Tax Dispute Resolution Committee, but if the FTA issues a decision on the reconsideration request down the line, the time-bar restarts for the taxpayer to challenge the decision. Practitioners must be aware of the possibility of a late decision on the reconsideration request and be prepared to respond accordingly.

Conclusion

The federal courts and tax dispute resolution committees in the UAE have provided clear guidance on the reconsideration procedures in tax disputes. By understanding their positions and the legal framework set by Federal Decree-Law No. 28 of 2022, taxpayers can navigate the complex landscape of tax disputes efficiently.

The insights provided by the federal courts and committees, coupled with the comprehensive framework set by the Federal Decree-Law No. 28 of 2022, offer a robust foundation for tax advisors, taxpayers, and stakeholders to approach tax disputes with confidence and clarity.

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Dubai Judgments on Extension of Time Claims: Repair and Additional Works, Concurrent Delay, and Contractual Wording

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In the construction and engineering sector, extension of time claims (EoTs) are ubiquitous, often representing complex contractual and legal implications. Amid the evolving international perspectives on these claims, the United Arab Emirates (UAE) has carved out its distinct path, driven by a pragmatic and robust legal framework. A deep dive into the UAE's legal ethos towards EoT claims reveals rich insights, hinged on a series of landmark court judgments. To capture this perspective, we turn to three pivotal rulings:

- Dubai Cassation Court case no. 389/2022 issued on 19 September 2022.
- Dubai Cassation Court case no. 161/2021 issued on 11 April 2021.

- Dubai Cassation Court case no. 348/2015 issued on 22 May 2016.

1. EoT in Repair Works: Dubai Cassation Court case no. 389/2022

In this case, the appellant claimed that the defendant had failed to adhere to the agreed upon project timeline, leading to significant delays. Further, the appellant alleged that the work done was flawed, requiring deconstruction and reassembly. The case turned on the question of whether the delays were permissible under the contract, and whether the repairs could be considered a breach of the same.

Crucially, the expert's report, addressing the appellant's objections, concluded that modifications made to the architectural and structural works, boundary wall modifications, general modifications, and sanitary drainage modifications—totaling eight core works—required additional time beyond the original project timeline for completion. In other words, the delay was necessary, and not a result of any failure on the part of the contractor.

One must observe that time extension claims often arise from the unforeseen complexities that are integral to any construction project. Contractors can be confronted with a variety of challenges beyond their control. Here, the nature and magnitude of the required modifications justified the delay.

The consultant agreed to extend the project deadline based on a letter issued in response to the plaintiff's request. Consequently, any delay could not be blamed on the contractor. The contractor rectified the flawed works, and the repairs were approved by the consultant. Therefore, as per the court, the appeal lacked a solid basis and was therefore dismissed.

The Dubai Cassation Court's ruling in case no. 389/2022 highlights the complex nature of time extension claims in construction contracts. It underscores the importance of considering project-specific circumstances, the necessity of repairs, and agreed-upon contract terms while dealing with such issues. Through this lens, the court's ruling offers a logical, well-argued, and reasoned response to such claims, proving instrumental for arbitration in similar cases in the future.

2. EoT in Additional Works and Concurrent Delay: Dubai Cassation Court case no. 161/2021

In the Dubai Cassation Court case No. 161/2021, the Court made a seminal ruling on EoT claims, throwing into sharp relief the fine line between the rights and obligations of contractual parties.

The Court's ruling navigates the muddled waters of concurrent delay and additional work – both being principal triggers of EoT claims. Essentially, it ruled that a contractor could claim an EoT in instances of concurrent delay, provided the owner's delay activities are simultaneous with those of the contractor. Simultaneity here denotes that the owner's actions (or inaction) must be within the same period as the contractor's delay-causing activities. Moreover, the ruling underscores the essentiality of establishing causation – the delay must directly spring from the owner's actions.

The Court also delineated on the question of additional work causing delay. It observed that when additional work requiring extra time is commissioned, it becomes imperative to grant an EoT to the contractor. This not only maintains the contractual balance but also upholds the fundamental principle of fairness. The judgement makes it clear that an owner cannot take refuge in the delay penalties clause if the contractor's delay in execution arises from causes attributable to the owner.

The critical aspect of this case, though, lies in the unfurling of the connection between EoT claims and performance bonds. The Court postulated that a contractor's entitlement to return of performance bonds is intricately linked to its adherence to contract completion timescales – extended or not. In situations where the contractor has dutifully executed its obligations and delays are not its sole fault, it is entitled to the return of the bonds, as they have fulfilled their purpose.

Moreover, the Court also shed light on the role of a project consultant, highlighting that the certificates issued by the consultant, attesting the progress of work, are consequential for the contractor's payment claims. In this context, it was emphasized that allegations of collusion between the consultant and the contractor must be substantially proven.

The ruling elucidates that in the adjudication of EoT claims, every aspect of the case is scrutinized – from the causation of delays to the extent of their impact on the project timeline. It reiterates the importance of thorough examination and comprehensive understanding of the project specifics, as well as the nuances of the EoT claim itself.

The Court's decision in case No. 161/2021 indeed serves as a comprehensive guide for stakeholders in construction contracts. It lucidly explicates the concept and ramifications of EoT claims, helping parties navigate this intricate facet of contract law. This case, thus, is a welcome addition to the compendium of legal guidance available for understanding EoT claims, a complex, yet pivotal element of construction contract disputes.

3. Elucidating Contractual Clarity: Dubai Cassation Court case no. 348/2015

The contractor sought compensation for additional costs arising from an extended period of project execution. The employer argued that the contract contained no provision allowing the contractor to claim any costs related to the EoT.

The case turned upon the interpretation of Articles 199 and 207 of the UAE Civil Transactions Law, which emphasize the significance of a valid cause and subject matter for a contractual obligation to be legally enforceable. The Court, applying these provisions, found that the contractor’s claim for additional costs lacked a legitimate contractual or legal basis since there was no provision in the contract allowing such a claim. The EoT claim was purely for additional time and not for additional costs.

This judgment showcases how the courts can, and will, enforce the strict letter of the contract, highlighting the importance of precise contractual wording. The contractor could not claim additional costs because the contract did not explicitly provide for such a claim in the event of an EoT. This indicates that, in EOT claims, courts are unlikely to imply terms or interpret contracts generously.

It should be noted that the Court also reinforced the employer’s obligation to compensate the contractor for the contracted works upon their completion. This reciprocal obligation mirrors the contractor’s commitment to finish the work in the agreed-upon time, further reinforcing the symmetrical nature of construction contracts.

Interestingly, the court rejected the notion that the extension of the contract duration would equate to a contractual amendment leading to additional obligations. The contractor’s claim for additional expenses arising from the extension period was deemed invalid, emphasizing that the performance of contractual obligations during an extended period does not grant the right to additional remuneration unless explicitly agreed in the contract.

In conclusion, this judgment from the Dubai Cassation Court reaffirms the criticality of meticulous contractual drafting and provides a cautionary tale for contractors entering into EOT claims. It reinforces the need to ensure that provisions allowing for additional costs during an EoT are included in the contract. Moreover, it reiterates the importance of careful contract management to ensure contractual obligations are met and rights are adequately protected during the project lifecycle.

The decision underscores the need for parties to consider all possible scenarios and articulate their mutual obligations comprehensively. Ultimately, it serves as a reminder that the law does not provide a safety net for those who fail to take the necessary precautions in their contracts. The burden lies with the parties to negotiate and agree on all material terms, including those related to EoT claims.

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UAE Supreme Court: Fraud and deception in construction quantity schedules

September 22, 2023

Introduction

The United Arab Emirates Federal Supreme Court has offered an important perspective on the implications of fraud and deception in the context of construction contracts, based on a ruling that delved into these concepts. The ruling gives critical insights into how the court views contractual procedures, quantity schedules, and the necessary evidence to establish fraud and deception.

Construction Contract Procedures

In the contract in dispute, a critical element was the inclusion of all specifications and descriptions related to the beautification work, which was the responsibility of the contractor. The contract details served as a roadmap for the contractor, defining their responsibilities and obligations in executing the project.

Quantity Schedules

Integral to the contract is the quantity schedule, a document detailing the types and quantities of work to be completed as part of the project. It acts as a guiding tool that helps eliminate disagreements over the project's scope. The court ruling stressed that any variance from this quantity schedule or any modifications in the design would be viewed as a change, signifying the owner's awareness of the contractor's prices and work items.

However, the court also noted that the owner had the opportunity to seek better price offers than what had been agreed upon, implying a level of responsibility on the owner's part in terms of due diligence before entering into the contract.

Legislative Provisions and Interpretations

The court based its decisions on relevant legislative provisions, namely Article 94 of the Civil Procedures Law and Article 21 of the Commercial Companies Law No. 2 of 2015.

Article 94 of the Civil Procedures Law primarily addresses issues related to lawsuits and legal procedures. In the context of this case employed to analyze the eligibility of parties involved in the lawsuit, eventually leading to the determination that directing requests to the three individuals along with the contracting company was litigation against an ineligible party.

On the other hand, Article 21 of the Commercial Companies Law No. 2 of 2015 offers guidance on the responsibilities and liabilities of shareholders in a company used to examine the roles and potential liabilities of the three defendants who were partners in the company initially sued.

Court Requirements to Evidence Fraud and Deception

When it comes to proving fraud and deception, the court requires solid evidence to establish such allegations. In this case, the court found no compelling evidence of the three defendants' role in the contract under litigation, undermining the strength of the claim of fraud.

The court reasoned that the owner failed to establish that the contractor used means to mask falsehood as truth and create a deceptive appearance, accompanied by physical manifestations that would affirm the deception. Simply being partners in the contractor company initially sued does not, in itself, provide sufficient proof of deception.

Similarly, claims of overreaching in the contract, while possibly significant, were dismissed by the court.

Variations to Quantity Schedule: Fraud and Deception?

In the context of construction contracts, variations or changes to the quantity schedule can become potential points of contention. The quantity schedule, as part of the construction contract, specifies the type and quantity of work to be undertaken. It serves as a guiding document that assists in preventing disagreements over the scope of the project. The courts are likely to consider deviations from this agreed schedule as a substantial change, provided these deviations are not mutually agreed upon by the parties.

In the ruling at hand, the court took a pragmatic view of such variations. It asserted that any divergence from the quantity schedule or modifications in the design constituted a change. However, this alone does not equate to fraud or deception. The court maintained that the property owner’s awareness of the prices, work items, and overall understanding of the contract terms plays a crucial role in deciding whether any changes amount to fraudulent activity.

The fact that the owner had the possibility to seek more favorable price quotes than what had been agreed upon in the contract signaled that they were aware of the pricing dynamics. This indirectly implies that even if the contract resulted in less favorable terms for the owner, it cannot be directly classified as fraud or deception unless the contractor employed fraudulent means to mislead or deceive.

If any changes to the quantity schedule are made with the intention to deceive, mislead, or defraud the other party, it can be classified as fraudulent behavior. This could include actions like the contractor artificially inflating quantities or the owner knowingly accepting lower quantities than required, with the intent to later claim additional costs. However, changes made in good faith, or with full transparency and mutual agreement, are generally considered legitimate variations to the contract.

In the absence of strong evidence of fraudulent means, as in this case, variations to the quantity schedule are not typically regarded as fraud or deception. This highlights the importance of clear, honest communication, and comprehensive documentation in construction contracts, particularly when dealing with changes to the project’s scope as outlined in the quantity schedule.

As a takeaway, both parties should be fully aware of their obligations and rights, exercise due diligence before entering the contract, and maintain transparency and clear communication throughout the project to avoid misunderstandings that could be construed as deception or fraud.

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Dubai Court finds Canadian company and its owner liable in USD 7M cryptocurrency dispute

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Background

The plaintiff, a Canadian businessman, filed a suit before the Dubai Primary Court against the first defendant, an individual who owned the second defendant, a company established according to the laws of British Columbia, Canada. The company operated in the cryptocurrency market, facilitating the buying and selling of various currencies using fiat currencies such as Canadian and US dollars.

In early 2018, the first defendant traveled from Canada to the

United Arab Emirates and met the plaintiff at a hotel in Dubai. Following their discussion, an agreement was reached wherein the company owned by the plaintiff, would use the services of the Canadian company (second defendant) to facilitate electronic transfer payments. It was agreed that the second defendant would act as a third-party payment processor for both the plaintiff personally and his company for payments and wire transfers.

As a part of the agreement, the plaintiff opened a trading account with the second defendant. The plaintiff would transfer Bitcoin or any other currency to the second defendant using his personal account. The terms and conditions allowed the plaintiff to cancel the account and withdraw all his balances at any time.

By the end of 2018, the second defendant delayed several transfers and claimed to have sent electronic transfer confirmation forms to the plaintiff, but the plaintiff received none of these transfers. In early 2019, the plaintiff emailed the first defendant, pointing out the pending transfers that lacked tracking codes. He asked the first defendant to provide the tracking numbers for these transfers. The first defendant promised to send them to the plaintiff, but the plaintiff received neither the tracking numbers nor the transfers that the first defendant claimed to have sent.

In mid-2019, the plaintiff attempted to withdraw his cryptocurrency assets from his account with the second defendant. However, the first and second defendants refused to hand over the cryptocurrency assets and wrongfully retained them. The value of the cryptocurrencies in the account of the plaintiff with the second defendant amounted to USD 6,782,459.96, representing the average price of the cryptocurrencies in said account during the period from February 2021 to March 2021 according to details in an expert report submitted by the plaintiff.

Procedures

The court deliberated the submissions and issued an interim order to appoint a financial expert to report on the technical submissions of the plaintiff.

The court-appointed expert relied on details of the digital currency wallet of the plaintiff, extracted from the website of the Canadian company (the second defendant). The details contained the balance of the digital currencies and their value at the dates of transfer and claim proceedings. The total value of the digital currency balance as of the date of transfer to the second defendant was found to be USD 2,711,570.98 and as of the date of the preliminary court-appointed expert report was USD 7,460,838.38.

Analysis

The court found a definite relationship between the parties, evidenced by the email correspondence exchanged between the plaintiff and the first defendant. Furthermore, the cryptocurrency wallet details, obtained from the website of the Canadian company (second defendant), including the cryptocurrency balance and its value, played a crucial role in the proceedings.

The court accepted the values of USD 2,711,570.98 and USD 7,460,838.38 as points for formulating the quantum of the amount claimed.

The plaintiff had snapshots of his trading account with the second defendant, which confirmed the balance demanded in the lawsuit. As pointed out by the court-appointed expert in his report, this balance was owed to the plaintiff by both defendants, based on an email sent by the first defendant to the plaintiff in early 2019. This correspondence acknowledged the outstanding balance in the account of the plaintiff, including the existence of cryptocurrencies in the crypto wallet.

Moreover, the plaintiff presented extracts from the accounting software used by both defendants, showing the balances of the crypto wallet belonging to the plaintiff and the deposited cryptocurrencies. The court found that this electronic correspondence and documents pointed to the liability of the first and second defendants for the crypto wallet belonging to the plaintiff.

Disposition

Based on these findings, the court deduced that the first defendant, as the owner of the second defendant, controlled the tracking numbers of the transfers and the cryptocurrencies in the crypto wallet of the plaintiff.

The court found the first and second defendants jointly liable to pay the plaintiff an amount of USD 6,782,459.96 or its equivalent in Emirati Dirham, along with legal interest at an annual rate of 5% from the date of judgment until the full payment.

Takeaway

This recent judgment by the Dubai Primary Court marked a significant precedent, displaying the ability of the Dubai Courts to pierce the corporate veil of foreign companies, in this case, a Canadian company, holding its owner personally liable. This judgment highlights the universal reach of Dubai Courts, effectively adjudicating multi-jurisdictional disputes, irrespective of the place of incorporation or domicile of the entities involved.

In this case, the decision by the Dubai Primary Court to hold the owner of the Canadian company personally responsible signifies a significant expansion of Court authority over international entities in cryptocurrency disputes, demonstrating the commitment by the Dubai Courts to ensuring justice and enforcing liability.

This decision also highlights the acceptance of the Dubai Courts of sophisticated evidence regarding crypto transactions and crypto wallets. This development can be regarded as progressive in the rapidly evolving digital world of today.

The reliance by the Court on digital currency balances, the examination of email correspondences, and data from accounting software indicate a keen understanding and acceptance of digital and cryptographic evidence.

As the world continues to grapple with the legal implications and complications of cryptocurrencies, the judgment by the Dubai Courts represents a significant step towards developing an effective judicial framework that can handle cases involving international crypto transactions. The ruling sends a clear message that the Dubai Courts are capable of providing justice in cases involving cryptocurrencies, despite their inherent complexity and the international jurisdictional issues involved.

The progressive stance and competent handling of such complex cases by the Dubai Courts are likely to attract more international crypto-related cases, thereby further establishing Dubai as a global hub for resolving disputes in the realm of digital currencies, and reaffirming the commitment by Dubai to innovation, technological advancement, and its position as a pioneering legal jurisdiction in the age of digital finance.

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Abu Dhabi Court upholds out-of-scope award and indirect arbitration claims

September 22, 2023

A recent case from the Abu Dhabi Cassation Court serves as an exemplary canvas on which several key arbitration concepts were explored, particularly concerning the validity and enforceability of an arbitration award that delves beyond the scope of its underlying arbitration agreement and the role of indirect claims in arbitration under the UAE Civil Transactions Law.

Case

The case revolved around a dispute arising from a contractual relationship involving the appellant – a contractor – and three respondents. The first respondent, on behalf of the other two, had previously filed a lawsuit against the appellant to enforce its rights per the UAE Civil Transactions Law's Articles 392 and 393. These articles form a cornerstone of the UAE's law regulating civil and commercial matters.

Articles 392 and 393 of the Civil Transactions Law permit a creditor, even if their right is not due for performance, to exercise all the rights of the debtor, unless those rights are intimately linked to the debtor's personality or non-attachable. A creditor is thus deemed to be representing their debtor in exercising these rights, and any benefit derived from such an exercise enters the debtor's assets and becomes a guarantee for all the debtor's debts.

Decision

The case’s focal point centered on the enforceability and validity of the arbitral award rendered in the ensuing arbitration proceedings. The appellant sought to nullify the arbitral award, primarily on the grounds that the arbitral tribunal had decided on matters not encompassed within the arbitration agreement. However, the Abu Dhabi Cassation Court dismissed these arguments, standing by the arbitral tribunal’s decision.

Importantly, the Court upheld the arbitral award’s validity, noting that even if the award delved into issues not covered by the arbitration agreement, it would not be void if the award’s portions subject to arbitration could be separated from those that were not. The court further held that based on Article 393 of the UAE Civil Transactions Law, the first respondent was entitled to indirectly claim the last two respondents’ rights from the appellant, including resorting to arbitration under the construction contract between the appellant and the last two respondents.

Thus, the arbitration award was affirmed, obliging the appellant to pay the first respondent the sum adjudged in the award, considering the first respondent as a representative of the second and third respondents.

Reasoning

The Court’s judgment was rooted in a number of principles. First, it relied on the fundamental notion that an arbitration agreement’s ambit defines the arbitrators’ jurisdiction. However, the Court applied a pragmatic approach in recognizing that an award may still be valid, even if it touches upon matters outside the arbitration agreement, provided those portions can be segregated without impacting the decision’s overall integrity.

The Court’s decision also involved a careful interpretation of Articles 392 and 393 of the UAE Civil Transactions Law. The

Court acknowledged that these provisions enabled a creditor to exercise all the rights of the debtor, even those not due for performance, subject to certain limitations. These provisions thereby authorized the first respondent to act on behalf of the other two respondents in claiming their rights from the appellant.

This interpretation gave rise to an intriguing legal scenario, one where the first respondent was allowed to resort to arbitration based on the construction contract between the appellant and the last two respondents. Consequently, this reasoning empowered the first respondent to indirectly claim the last two respondents' rights from the appellant through arbitration proceedings despite the lack of an arbitration agreement between the appellant and the first respondent.

Significance

The Court's decision in this case sets several significant precedents and offers a profound avenue for future indirect claims, particularly for subcontractors in the construction sector in the UAE, such as in cases where a subcontractor attempts to pursue the employer on behalf of the main contractor via arbitration.

1. **Arbitration Agreement and Scope**: The judgment underscores the arbitration agreement's significance in delineating the arbitrators' jurisdiction. However, it advances a nuanced interpretation, asserting that an arbitration award can still retain its validity even if it ventures beyond the agreement's scope, as long as the portions relating to the arbitration agreement can be segregated from the rest.
2. **Role of Indirect Claims**: Perhaps the most remarkable facet of this judgment is its interpretation and application of the provisions of the UAE Civil Transactions Law concerning indirect claims. By endorsing the first respondent's capacity to act on

behalf of the last two respondents in claiming their rights from the appellant, the Court offers a crucial precedent for the applicability of Articles 392 and 393.

3. **Arbitration and Indirect Claims**: The judgment also establishes an essential principle regarding arbitration's place within the domain of indirect claims. It affirms that a party representing another's rights, under the context of Articles 392 and 393, may resort to arbitration under the original contract between the debtor and the creditor.
4. **Enforceability and Validity of Arbitral Awards**: The ruling further adds to the ongoing dialogue concerning the enforceability and validity of arbitral awards. By upholding the award despite the appellant's objections, the Court reinforces the UAE's pro-arbitration stance and offers reassurance about the robustness and reliability of its arbitration regime.

The decision's legal implications are broad and far-reaching. It augments the body of legal precedents that will undoubtedly influence future disputes involving similar arbitration issues. It offers important guidance on interpreting the UAE Civil Transactions Law towards indirect arbitration claims under Articles 392 and 393 and provides valuable insights into the UAE's arbitration landscape.

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Shariah rules and crypto disputes: UAE court judgment and official Fatwa invalidate cryptocurrency transaction

September 22, 2023

Brief

"Bitcoin is a digital currency that does not meet the legal and Sharia criteria that make it a currency subject to the rulings of dealing with official legal currencies recognized internationally. It also lacks the Sharia controls that make it a commodity capable of being exchanged for other commodities."

In a dispute over OneCoin cryptocurrency, a UAE court (Ras Al-Khaimah Primary Court) ordered the invalidation and rescindment of a cryptocurrency sale contract on the basis that the cryptocurrency transacted (OneCoin) was not a recognized currency or commodity in violation of Shariah rules and the Civil Transactions Law.

Reference to Fatwa No. 89043

The Court referenced Fatwa No. 89043 issued by the General Authority for Islamic Affairs and Endowments in 2018 which addressed Bitcoin and cryptocurrencies in general. The Fatwa addressed the status of Bitcoin in that it did not possess the necessary specifications to make it a tradable currency, like the approved currencies that are traded worldwide. And that it also lacks the necessary legal requirements to be considered a commodity for exchange with other commodities. The following is the Fatwa content quoted by the Court in its reasoning:

“Firstly, defining Bitcoin: Those who call Bitcoin a currency describe it as a virtual, intangible electronic currency with no physical existence. These currencies, with their varying types, methods of access, and acquisition, have been widespread and known for several years. Among the most famous are Ethereum, Dash, Ripple, Litecoin, and Ethereum Classic, all of which are digital currencies, each with its characteristics, features, and ways of processing and generation. The purpose of resorting to such currencies is that they are decentralized, allowing individuals to control them, providing them with a high degree of privacy and confidentiality, and they cannot be tracked because they do not rely on official institutions and intermediary financial entities like banks. As they are not linked to any financial institution, they have no real assets or balances, are not protected by any financial regulations or laws, and are not subject to any regulatory authority. This has been one of the reasons for their exposure to massive increases or sharp declines, and in addition to all this: the unawareness of who is behind the promotion of this virtual currency makes it susceptible to damage and loss of value in the face of any sudden changes. For this reason, no country in the world, including the United Arab Emirates, has recognized Bitcoin as legal tender.

Secondly, the Sharia criteria considered in currencies: In the previous paragraph, we provided a description that clarifies the reality of this currency in its current state. In this paragraph, we mention the most important Sharia requirement for considering anything as currency, which is: state adoption, meaning that it should be issued by the state. This is what the scholars express as minting or striking coins. This is explained as follows: The adoption of monetary currencies is considered a special function of the state in Sharia. The state alone has the right to issue coins, according to the adopted laws and regulations. This is explicitly stated in the texts of scholars, whether for metallic money – like gold dinars or silver dirhams – which have intrinsic value and were prevalent in the past, or for credit currencies that rely on the power of the law and do not have intrinsic value, such as paper currencies, which have become prevalent worldwide.

In conclusion, Bitcoin is a digital currency that does not meet the legal and Sharia criteria that make it a currency subject to the rulings of dealing with official legal currencies recognized internationally. It also lacks the Sharia controls that make it a commodity capable of being exchanged for other commodities. Therefore, it is not permissible to deal with Bitcoin or other electronic currencies that do not meet the recognized Sharia and legal criteria, as dealing with them leads to unsound consequences, whether for the individuals involved, the financial markets, or the entire community, and whether we consider it cash or a commodity, the ruling encompasses both cases."

(United Arab Emirates – General Authority for Islamic Affairs and Endowments, Fatwa No. 89043 dated 30/1/2018)

Invalidity of a cryptocurrency contract

In its reasoning in Primary Court case no. 87/2020 (Ras Al-Khaimah), the Court applied the statutes, case law, and legislative commentary, that govern the validity of contracts under the Civil Transactions Law. The following are extracts from the respective judgment.

"According to the provisions of Articles 125, 129, and 141 of the Civil Transactions Law, a contract is the binding commitment issued by one of the parties by accepting the other party's offer and their mutual agreement in a way that establishes its effect on the subject matter and results in the obligation of each party to fulfill what is required of them to the other party. For a contract to be concluded, both parties must agree on the essential elements of the obligation and on the other legitimate conditions that indicate their essentiality, and <u>the subject matter of the contract must be something possible, specific, or determinable and permissible to deal with</u>. (Federal Supreme Court – Civil and Commercial Judgments – Appeal No. 226 of the year 25 Judicial – Civil and Commercial Circuit – dated 2006-03-14 Technical Office 28 Part 1 Page 525)

Article 202 of the Civil Transactions Law stipulates the possibility of having a future thing as the subject matter for counterbalances if the uncertainty is eliminated. The explanatory memorandum clarified the meaning of uncertainty as the inability to deliver, based on the statements of Ibn Al-Qayyim, which can be summarized in that there is nothing in the Book of Allah or the Sunnah of His Messenger (peace be upon him) that indicates that a contract on something non-existent is not permissible, and to what is mentioned in the Sunnah of the prohibition of selling some non-existent things as in his saying (peace be upon him) “Do not sell what you do not have”. The reason is not non-existence, but uncertainty due to the inability to deliver. (Emirate of Abu Dhabi – Court of Cassation – Civil and Commercial Judgments – Appeal No. 286 of the year 2014 Judicial – Commercial Circuit – dated 2014-06-03 Technical Office 8 Part 3 Page 942)

In accordance with Article 210 of the Civil Transactions Law, an invalid contract is one that is not legitimate in its essence and is described as having a defect in its pillar, subject matter, purpose, or the purpose imposed by law for its conclusion, and it has no effect and is not subject to ratification, and anyone with an interest may invoke its invalidity. The court may rule on it by itself, as the invalid contract has no legal existence, like a contract. (Federal Supreme Court – Civil and Commercial Judgments – Appeal No. 284 of the year 25 Judicial – Sharia – dated 2004-01-27

Technical Office 26 Part 1 Page 240)”

Court finding

The Court ultimately found that:

“The sale of the cryptocurrency is not real and therefore not valid for trading. It does not meet the necessary criteria to be considered a tradable currency, particularly the requirement of being recognized by the state. Moreover, it cannot be considered a tradable commodity due to its lack of essential conditions, such as its existence and eligibility for trading. It is something that has not been proven to have actual existence or real value, and its ownership cannot be transferred, its value cannot be determined, nor can it be traded in any legitimate form.

As a result, the sales contract lacks the necessary legal conditions that must be present in any contract, such as the subject matter of the contract being possible, specific, or identifiable, and permissible for trading. In the case of a sales contract, specifically, the item sold must exist, be specific or identifiable, and eligible for trading. Furthermore, the cryptocurrency lacks the legitimate conditions that make it suitable for trading, as it is neither a tradable currency nor a commodity that can be exchanged, given that the state has not recognized it as a currency. It is also tainted with uncertainty due to the inability to deliver it.

Consequently, the contract that forms the basis of the claim is flawed, and is considered illegitimate in its essence and description. It has no effect, and the court has the authority to rule its invalidity on its own, in accordance with Article 210 of the Civil Transactions Law.”

When are crypto transactions legal?

Notwithstanding the quotation of the Fatwa used by the Court, the complete text of Fatwa No. 89043 ultimately concludes as follows:

“It should be noted that this ruling applies specifically to these currencies that are the subject of the question at this time and are still beyond the control of responsible authorities. However, if a decision is made to regulate and adopt them and place them under a supervisory umbrella by those authorities, so that they meet the criteria that make them a legal currency, used in transactions between countries, then the ruling on dealing with them would take the same ruling as dealing with officially recognized currencies.”

The Fatwa, which states that dealing with cryptocurrencies such as Bitcoin is not permissible unless they meet the Shariah and legal criteria and are regulated by responsible authorities, can be considered compliant with manifest the Dubai Financial Services Authority (DFSA)’s recognition of certain cryptocurrencies.

The DFSA is the independent regulatory authority responsible for overseeing and regulating financial and ancillary services conducted in or from the Dubai International Financial Centre (DIFC).

The DFSA recognizes financial services and activities involving Crypto Tokens in two ways: (1) if the Crypto Token is included in the initial list published by the DFSA (Bitcoin, Ethereum, and Litecoin), or (2) if an application for recognition of a specific Crypto Token is submitted and approved by the DFSA. As per the DFSA’s notice of November 2022, Bitcoin (BTC), Ethereum (ETH), and Litecoin (LTC) are recognized Crypto Tokens.

The jurisdiction of the DFSA is within the DIFC, which is a special economic zone within Dubai. As a result, the DFSA’s recognition of specific cryptocurrencies and its regulation of related financial services may be considered to only apply within the DIFC. This creates potential risks and uncertainties for cryptocurrency transactions conducted in other Emirates or outside the DIFC in Dubai.

In another example on a Federal level, the Central Bank of the UAE took the position in December 2020 that it is presently “not recognizing crypto assets as legal tender in the UAE, such assets are not recognized by the Central Bank as a means of payment and can only be used as assets for investment with a potential high risk”.

Takeaway

The Central Bank, the Securities and Commodities Authority, the Financial Services Regulatory Authority and the Abu Dhabi Global Market, the Dubai Financial Services Authority and the Dubai International Financial Centre, the Virtual Asset Regulatory Authority, and even prosecutive authorities via anti-money laundering regulations have identified and defined cryptocurrencies and virtual assets in one way or another.

Notwithstanding, if a transaction turns contentious, there is an onus (on whichever party) to evidence that the cryptocurrency (or virtual asset) subject of the transaction fulfills legal and – potentially – Sharia criteria.

The laws and provisions are essentially static, until they are tested before the courts, and their application becomes dynamic, granting clarity over their actual application.

If a cryptocurrency is not recognized by the overseeing UAE authorities, transactions involving such cryptocurrencies may be deemed invalid pursuant to Fatwa No. 89043 and the Civil Transactions Law.

And this would apply to consideration or perception of the disputed cryptocurrency as either currency or commodity.

It is essential for individuals and businesses to be aware of the legal status of the cryptocurrencies they are dealing with in light of the position of the UAE courts and consider the potential risks before engaging in transactions involving unrecognized cryptocurrencies.

And in caution against giving in to the escapism of crypto craze without adequate due diligence:

“There is a wisdom that is woe; but there is a woe that is madness. And there is a Catskill eagle in some souls that can alike dive down into the blackest gorges, and soar out of them again and become invisible in the sunny spaces. And even if he forever flies within the gorge, that gorge is in the mountains; so that even in his lowest swoop the mountain eagle is still higher than other birds upon the plain, even though they soar.” (Herman Melville, Moby Dick)

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UAE Federal Court rules no penalties on voluntary disclosures related to unintentional tax errors

September 22, 2023

Overview

The taxpayer filed its tax return with incorrect amounts by mistakenly calculating the tax rate at a different value than the standard rate of 5%, resulting in an incorrect tax amount.

The taxpayer submitted a voluntary disclosure to correct the error, and the Federal Tax Authority imposed a penalty for the difference between the incorrect and correct tax amounts.

The Federal Primary Court, adjudicating the dispute, ruled that what the taxpayer did in the original form of submitting the voluntary disclosure subject to the contested tax is nothing more than a correction of the error it made when calculating the tax imposed on it for its activity at a different rate instead of the standard rate of 5%, and it is not a voluntary disclosure of errors in the value of the tax return or tax assessment, for which the penalties prescribed in Cabinet Resolution No. 40/2017 and its amendments are due, and therefore the imposition of penalties loses its legal basis.

The Court reasoned that the voluntary disclosure subject of this dispute, is merely a correction of an “unintentional error in calculating the tax”. Instead of using a 5% rate, the company mistakenly applied a different rate in the tax return.

The judgment confirms that this voluntary disclosure is not a “disclosure of errors in the tax return or assessment”, which would warrant penalties as per Cabinet Decision No. 40/2017 and its amendments.

As a result, the Federal Primary Court found that the imposition of penalties lacks a valid legal basis.

Significance

This judgment comes as a relief to taxpayers in the UAE because it provides a more lenient interpretation of the tax regulations and reduces the likelihood of penalties for honest mistakes. By differentiating between an “unintentional error in calculating the tax” and “a voluntary disclosure of errors in the tax return or assessment” the Court ruling essentially provides taxpayers with a more forgiving approach to correcting their tax filings.

In the given ruling, the Federal Primary Court treats the voluntary disclosure submitted by the taxpayer as a correction of an unintentional error rather than a voluntary disclosure of errors in the tax return or assessment. This interpretation has significant implications for taxpayers in terms of reduced penalties.

According to Cabinet Decision No. 40/2017 and its amendments, penalties can be imposed on taxpayers for errors in tax returns or assessments. By treating certain voluntary disclosures as a correction of an unintentional error, the court effectively eliminates the legal basis for imposing such penalties.

Overall, the judgment is a relief to UAE taxpayers because it offers a more favorable interpretation of the tax regulations, reduces the likelihood of penalties for unintentional errors, and encourages voluntary disclosure and correction of such errors.

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