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TAX & LEGAL

EXECUTIVE COMPENSATION AND BONUSES:

transfer pricing valuation challenges in the UAE

Why this topic has come to the forefront

Our recent work on clients' Corporate Tax returns highlighted a recurring challenge: management roles and responsibilities are often insufficiently defined or documented, making it difficult to apply the FTA's criteria for directors and officers.

The preparation process can reveal that an individual's actual authority and functions differ from what their job title or company documents suggest. Remuneration is often not clearly broken down by role or type of payment, and bonus policies may be missing or fail to reflect how bonuses are actually determined and paid.

Preparing the return brings these gaps into focus: how should the payment be classified, valued and supported?

Under Article 36 of the Corporate Tax Law, payments to a company's director or officer are deductible from the taxable base only within market value. As directors and officers are expressly named as Connected Persons, such payments are also subject to disclosure when exceeding the prescribed thresholds (AED 500,000 per Connected Person, together with their Related Parties, for the relevant Tax Period).

CTP010 also clarifies that a person who is both a Related Party and a Connected Person is treated only as a Related Party. This includes individual owners holding 50% or more, directly or indirectly, alone or with their Related Parties (Article 35). Subject to the relevant disclosure thresholds, their remuneration belongs in the Related Party transaction Schedule, which requires identification of the TP method, the Connected Persons Schedule does not request it (CTGTXR1, sections 16.1 and 16.2).

This issue takes on particular significance for free zone companies. For a Qualifying Free Zone Person, compliance with TP documentation requirements is a direct condition for retaining the preferential tax status (CTGFZP1). And since job descriptions and the actual functions performed by directors and officers also serve as evidence of having "qualified full-time employees" for the core income-generating activity, correctly classifying these individuals and substantiating their remuneration becomes significant on two fronts at once.



Benchmarking executive remuneration

As a general rule, to determine the market value of controlled transactions, the Law refers to the transfer pricing rules. However, neither the FTA's TP Guide (CTGTP1) nor the OECD Guidelines provide a methodology tailored to directors' and officers' remuneration. The recognised methods and standard corporate databases were developed principally for transactions between enterprises, not individual employment packages. Applying them to salaries and bonuses is therefore a complex exercise: corporate financial data do not capture employment terms, while TNMM and cost plus do not readily value an individual's services.

In our practice, the main approaches we consider are:

- the comparable uncontrolled price method (CUP), where reliable data on comparable uncontrolled remuneration arrangements are available, including suitable internal comparables. A salary survey may support CUP only if its underlying data and comparability can be substantiated;
- another method under Article 34(4) of the Law, where none of the five recognised methods can reasonably be applied, with the choice and economic rationale documented (CTGTP1, section 5.2.1.10).

Salary surveys are one of the most accessible and frequently used sources of information for substantiating the market level of directors' remuneration and the bonuses tied to it. They may offer useful market ranges by industry, location, company size and seniority, but the source, reference period and remuneration components must be checked before those ranges are used.

At the same time, from a comparability standpoint, such surveys have significant limitations. First, some draw on employer-reported pay, employees' current remuneration or completed recruitment assignments; others include advertised salaries, candidates' expectations, forecasts or recruiters' estimates. Actual remuneration data may be closer to transactional evidence, subject to reliability and independence checks. Expectations and estimates are indicative market information, not proof of remuneration actually agreed. The sample and data-collection methodology therefore matter.

Second, the quality of job matching varies: some surveys use structured job evaluation, while others rely on titles or general descriptions. This is particularly critical at director level, where the scope of authority, responsibilities and actual influence on the business can differ substantially under a formally identical title.

Third, published ranges or percentiles may conceal the underlying observations and restrict comparability checks and adjustments. OECD paragraph 3.37 recognises the potential usefulness of aggregated third-party data, but does not make every salary range a reliable comparable.

Finally, a survey's commercial origin or non-tax purpose is not itself disqualifying; its underlying data and detail must support the chosen method (OECD paragraphs 3.30–3.34). A useful analogy appears in paragraphs 10.107–10.108: bank opinions on hypothetical rates generally do not evidence arm's length terms because they are not based on actual transactions. This distinction is relevant to advertised salaries, candidates' expectations, forecasts or recruiters' estimates.

A separate problem arises with respect to the variable part of remuneration – **bonuses**. Target bonus opportunities must be distinguished from actual payments. Comparability may depend on the formula, KPIs and their weighting, the share of variable pay, and payment conditions such as deferral and clawback. A broad percentage of salary, without this context, is unlikely to substantiate a particular bonus on its own.



Executive roles and supporting documentation

Since the scope for testing against open data is objectively limited, documenting the actual authority and functions of a given individual is essential to selecting and interpreting comparables. It does not, by itself, establish that the remuneration is at market value.

The FTA's public clarification CTP010 states directly that the job title alone does not settle the question: the word "director" in a position's title does not make a person a director within the meaning of Article 36(2)(b) of the Law, just as the title "head of department" does not exclude someone from being an "officer."

A director is a member of the board of directors or an equivalent governing body under the applicable law and the company's constitutional documents. The determining factor for the "officer" is the actual scope of authority. An "officer" is a person who has the authority and responsibility for planning, directing and controlling the company's activities, or the authority to make strategic decisions, or the right to enter into agreements or approve actions that legally bind the company; someone who does not have final strategic or binding authority is not an officer. Actual conduct takes priority over formal status: a person without a C-suite title who in fact performs the relevant functions will be treated as an officer – and vice versa. The examples given in CTP010 illustrate well the logic the FTA will apply when reviewing a case.

The same logic underlies the TP guidance on functional analysis: the individual's actual functions, responsibilities, conduct and remuneration structure should be documented, with job descriptions providing supporting evidence (CTGTP1, section 5.1.1.4). This is fully consistent with the OECD approach: if the actual characteristics of a transaction or function diverge from the contractual wording, the analysis must be based on the parties' actual conduct rather than the letter of the document ("substance over form").

Accordingly, three categories of documents help establish the relevant functions and support the remuneration analysis:

1. **Job descriptions**: authority is recorded precisely, without overly broad formulations such as "general management" or "strategic decisions."
2. **Delegation of authority matrix**: who makes the final decision, and who merely prepares materials or implements what has been approved. Powers of attorney, the trade license and board resolutions must be consistent with it.
3. **Bonus policies**: the formula, KPIs, approving bodies, link to functions, reference to the benchmark source, and explanation of how its data support the selected TP method.

Where documents are drawn up clearly and reflect actual practice, this can reasonably narrow the pool of individuals treated as officers. However, once the documents are put in order, the company's practice must then match them.



What we recommend doing in the off-season

Since the correct classification of directors and officers rests on the substance of their authority rather than their job title, it makes sense to carry out this work in advance, outside the peak period of tax return preparation:

1. Compile a register of all individuals potentially falling within the “director” or “officer” categories, assessing each against the functional criteria set out in CTP010, rather than by formal job title. First check whether ownership or control already makes the individual a Related Party.

2. Align job descriptions, the authority matrix, powers of attorney and board resolutions with one another, so that the scope of authority actually granted does not diverge from what is recorded on paper.

3. Approve bonus policies with a clear calculation formula, a set of KPIs and an approval procedure for payments. Separately document the rationale for the chosen remuneration level.

4. Compile and retain the internal documents supporting the remuneration arrangements, together with evidence of the functions actually performed and the basis for calculating fixed and variable pay. These materials provide the factual foundation for assessing the market value of the remuneration.

5. Check the applicable disclosure thresholds for Related Parties and Connected Persons, the correct tax return schedule and, where required, the TP method to be reported

We help companies develop and document a remuneration position that reflects how their business actually operates. Our work covers the individual’s tax classification, the choice and justification of the valuation approach, and the preparation or revision of job descriptions, authority matrices and bonus policies.

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Best regards,

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