Kuwait: Update on the proposed Business Profits Tax

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In brief

In light of the declining trend in the oil prices, the State of Kuwait has been considering various fiscal reforms to bridge the budgetary gap between revenues and expenditure. The potential reforms being considered by the State of Kuwait include introducing a business profits tax and a value added tax.

There has been recent media coverage in Kuwait citing possible draft legislation and other coverage concerning the potential introduction of a business profit tax at 10% of profit on local companies and individuals carrying on business, in addition to foreign companies having a permanent establishment in, or earning certain income from, Kuwait.

In this alert we have summarised certain features of the potential profits tax based on our understanding. However there is no certainty that the reforms will be approved and ratified by the parliament in Kuwait and of course the possibility that details will change in the meantime.

In detail

The key highlights of the proposed tax laws are as under:

Tax year

The draft tax law defines the tax year as the period from 1 April to 31 March. In case of Kuwaiti shareholding companies, the tax year is the year of their annual financial statements.

Tax rate and base

The income tax rate is proposed to be 10%. Tax is calculated on the net profit of foreign and local companies. In case of individuals carrying business, the draft law taxes the portion of their net business profit exceeding KD 50,000.

Taxpayers

The proposals include taxing local companies and individuals doing business in Kuwait, in addition to foreign companies having a permanent establishment in Kuwait or earning certain income from Kuwait.

Certain entities may be excluded such as charitable institutions, government authorities and the Central Bank of Kuwait.

Key definitions

Company

The term Company has been widely defined to include local and foreign companies, shareholding companies, limited partnership, joint ventures, trusts, etc.

Resident Company

The term Resident Company is defined as a company established in Kuwait or a company having the place of its effective management in Kuwait.

Permanent Establishment (PE)

The proposals provide for the definition of PE which is not provided in the existing tax law. The term PE is in line with the international definition (i.e. fixed place, agency and service PE).

Imposition of withholding taxes on non-residents

The proposed law provides for withholding tax at the rate of 10% on interests, royalties, technical fees, etc. and 5% on insurance premiums earned by non-residents from sources in Kuwait.

Exempt income

The proposals include exemptions with respect to certain types of income, which primarily include:

- Dividends received by a resident Kuwaiti company (other than financial institutions) from another resident company;
- Dividends received by a resident Kuwaiti company from a non-resident company (except those resident in a low or non-tax jurisdiction[1]) in which it owns at least 10% of the voting shares;
- Capital gains of a resident Kuwaiti company from the disposal of shares in resident and non-resident companies (except those resident in a low or non-tax jurisdiction) in which it owns at least 10% of the voting shares;
- Passive profits and interest income of individuals from securities;
- Interest paid on loans taken by a resident company from international monetary markets;
- Any benefits under relevant tax treaties;
- Any existing tax holidays/benefits in force before the enforcement of the proposed tax law which include the Foreign Direct Investment Law no 116 of 2013.

Carry forward of losses

The proposed tax law proposes the carry forward of tax losses for a period of 5 years (instead of 3 years under the existing tax law).

However, tax losses would not be allowed to be carried forward if:

- The taxpayer ceases its operations and notifies the Ministry of Finance in this respect; or
- The direct or indirect ownership of a company changes by more than 50% unless (i) the company's business activities do not change, and (ii) the company does not undertake any new business or investment with the principal purpose of utilizing the tax losses.

The takeaway

Whilst the proposals are now receiving broader exposure such as in the media, there is no certainty on the timing and content of the final tax law along with its executive regulations.

Further, there could be amendments or revocation of existing levies or contributions applicable to certain local companies including Zakat. Nevertheless, against the backdrop of government funding pressures companies are advised to be ready for the possibility for these or other reforms. We are in discussion with the tax authorities to track the updates and the likely impact on taxpayers.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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[1] A jurisdiction with a tax rate that is lower than the Kuwaiti tax rate.