Doing Business in Iraq 2024

A Tax and Legal Guide

Table of content

Welcome to this guide

Your journey begins

Location | Presence
Objectives | Operations

The Republic of Iraq ("Iraq") is the fourth most populous country in the Middle East and has the world's fifth largest proven oil reserves. Iraq, widely known with its rich heritage as the "Cradle of Civilisation", is predominantly a desert, made fertile by the Euphrates and Tigris rivers. The official languages of Iraq are Arabic and Kurdish

Iraq's economy is dominated by the oil and gas sector, where oil accounted for 43% of the GDP, 92% of the government budget revenues, and 96% of the country's exports in 2019. Iraq holds the world's fifth largest proven crude oil reserves at 145bn barrels, representing 17% of proven reserves in the Middle East and 8% of the global reserves. At the end of 2020, Iraq's proven natural gas reserves were the 12th largest in the world, at approximately ~132tn cubic feet.

This guide is intended to provide an introduction to the taxation and legal aspects of doing business in Iraq, particularly from the perspective of the items an inbound investor will have in mind.

We hope you find the guide useful.

Jochem Rossel – Middle East Tax and Legal Services Leader
Suhaib Asad - Iraq Tax Leader

Introduction

Iraq, a country in Western Asia, is bordered by Jordan to the west, Syria to the northwest, Turkey to the north, Iran to the east, and Kuwait and Saudi Arabia to the south. With Baghdad as its capital, Iraq is divided into 18 governorates. The official languages of Iraq are Arabic and Kurdish, and the currency is the Iraqi dinar (IQD).

Formerly part of the Ottoman Empire, Iraq was occupied by Britain during the course of World War I. In 1920, it was declared a League of Nations mandate under United Kingdom administration. Iraq attained its independence as a Kingdom in 1932, and a 'republic' was proclaimed in 1958. In August 1990, Iraq seized Kuwait but was expelled by United States-led, United Nations coalition forces during the Gulf War of January/February 1991.

In October 2005, Iraqis approved a constitution in a national referendum and, pursuant to this document, elected a 275-member Council of Representatives (CoR) in December 2005. Sustained increases in the standard of living of Iraq still depend on the government passing major policy reforms and developing Iraq's massive oil reserves.

Potential foreign investors now view Iraq with much more interest. As Iraq's economy is dominated by the oil sector, which provides over 90% of government revenue and 80% of foreign exchange earnings, Iraq's recent contracts with major oil companies have the potential to greatly expand oil revenues.

However, Iraq will need to upgrade its refinery and export infrastructure to enable these deals to reach their potential.

PwC has been very active in Iraq since 2006 and has two offices in Erbil, one in Baghdad, and one in Basra.

PwC Iraq provides advisory, audit, and tax services for key government entities, as well as banks, financial institutions, oil and gas companies, industrial companies, and agricultural companies within the Iraqi private sector. We support clients with the local knowledge and skills of our people and with access to a broad range of other professionals across the PwC global network of firms.

Establishing a business in Iraq

As a general rule, any non-Iraqi company which is "carrying on business" in Iraq is required to establish an Iraqi legal presence (e.g. company, branch office).

Legal and regulatory framework

While there is no specific definition of what constitutes "carrying on business" in Iraq, typically an obligation would arise when a company obtains premises (including rented premises) in Iraq, or retains personnel on a more than temporary basis. Penalties may apply in respect of failure to register the enterprise.

There are a number of principal business entities in Iraq, including joint stock company, limited liability company, joint liability company, simple company, sole owner enterprise, representative office and branch office. In practice, the most common form of entities for foreign investors are the limited liability company (LLC) and branch office. As per the amended Companies Law, Iraqi ownership of at least 51% is required to establish a new limited liability or joint stock company in Iraq.

Further to the issue of new foreign branches regulation No.2 of 2017, it is now possible for entities that do not have contracts with the government to register a branch in Iraq. It is difficult to predict the time taken to register a legal entity in Iraq, but a time frame of 6 to 12 months would be typical. It is generally faster and more straightforward to register a branch of a foreign company than an LLC in Iraq.

Permanent Establishment

Iraq's income tax law does not recognise the concept of permanent establishment. However, Iraq broadly takes a territorial approach to taxation. In addition, contracts with on-Iraq residents are also specifically covered by Instructions No. 2 of 2008 (the "Instructions"), which broadly set out tests to define whether the non-resident is "trading with" or "trading in" Iraq. In summary, "trading with" Iraq should not result in an Iraq tax liability, whereas "trading in" Iraq will.

Trading with vs. Trading in Iraq

Broadly, a non-resident would be considered to be "trading in" Iraq when contracts are concluded in Iraq, payments for the services are made into an Iraqi bank account, or services are physically provided in Iraq. Critically, this may also include cases in which services are provided through a business agent or subcontractor in Iraq. A contractor "trading in" Iraq will need to register a legal entity in Iraq, register for tax purposes and submit annual corporate income tax filings. Information on the contract should strictly be sent to the tax office, in order for the tax office to determine whether the contractor is liable for tax, i.e. whether the contract is considered to be "trading in" Iraq, and therefore whether retentions should be made on payments under the contract. As the Instructions are currently drafted, there is no de minimis time limit for provision of services in Iraq – therefore strictly as little as one day spent working in Iraq should be considered to be "trading in" Iraq, and therefore give rise to an exposure to tax in Iraq.

Key Considerations

By way of summary, Potential foreign investors now view Iraq with much more interest. Iraq's economy is dominated by the oil sector, which provides over 90% of government revenue and 80% of foreign exchange earnings. Iraq's recent contracts with major oil companies have the potential to greatly expand oil revenues, but Iraq will need to upgrade its refinery and export infrastructure to enable these deals to reach their potential.

Taxation

Corporate income tax

All income derived from Iraq is subject to tax in Iraq, regardless of the residence of the recipient.

The effective corporate income tax (CIT) system presented in Iraq for juristic persons (except partnerships) is based on a statutory CIT rate of 15% at all income levels, with no progressive tax rate scale.

Moreover, the General Commission for Taxes (GCT) adopts the deemed approach by applying a certain rate on the total reported revenue. Note that the GCT applies the highest of the deemed tax on the reported revenue or the 15% (35% for oil and gas industry, see below) of the reported profit/taxable profit.

Foreign oil company income tax

The income realised in Iraq from contracts concluded with foreign oil companies, their branches or offices, and subcontractors working in Iraq in the oil and gas production sector and related industries is taxed at a rate of 35%.

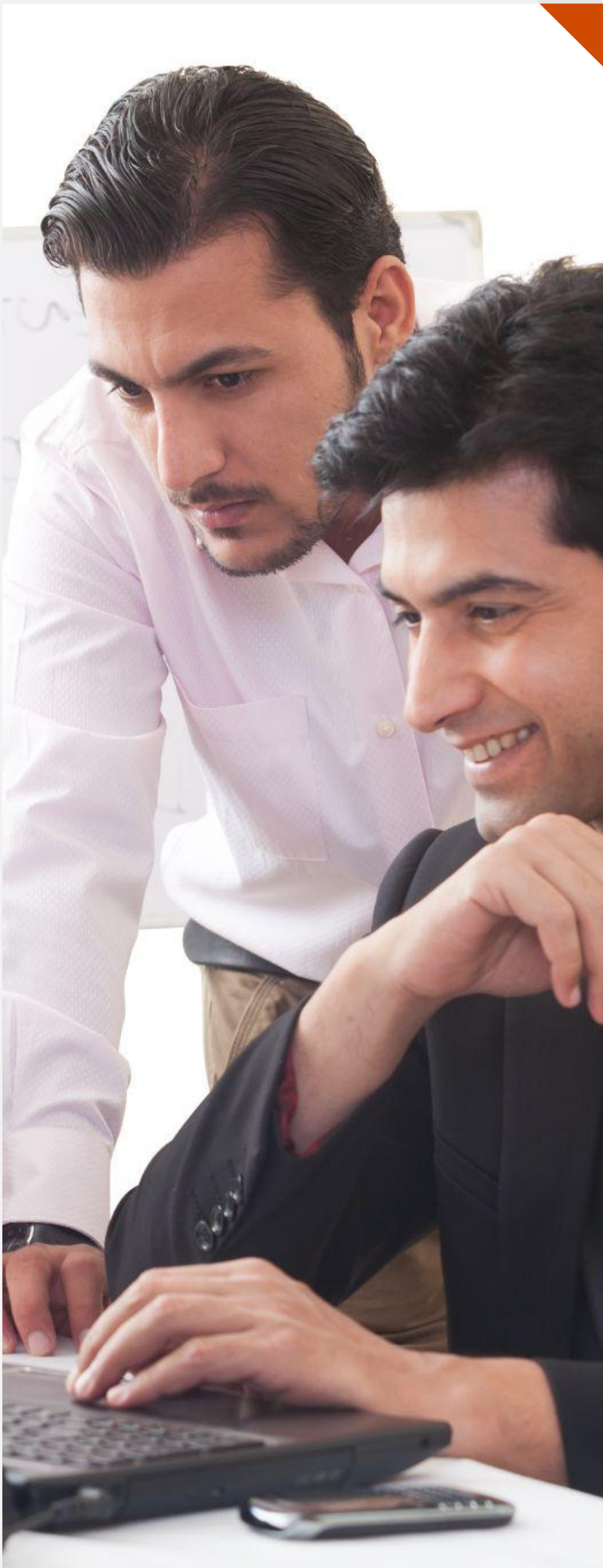
Corporate - Corporate residence

One of the key issues in determining when a company becomes taxable in Iraq is whether the foreign company is considered to be doing business 'in Iraq' or 'with Iraq'. In 2009, with Instructions No. 2/2008, and its amendment instruction #1 of 2014, the Iraqi tax administration provided a clearer distinction between business 'in Iraq' and business 'with Iraq'.

Once the determination has been made that the company is trading 'in Iraq', the company should register with the GCT. A company that is registered with the GCT will be subject to CIT and will be required to file a CIT return.

Permanent establishment (PE)

It is important to note that the current Iraq income tax law does not clearly define a PE; consequently, it is important to monitor commercial activity being performed in the country to ensure compliance with the registration requirements and tax law. The company should consult with their internal tax department and external advisers if they have signed a contract to provide any type of services inside Iraq to determine if the company should have a legal registration and begin to file CIT returns.



Sales tax

A sales tax of 300% is imposed on alcohol and tobacco (cigarettes), 15% on travel tickets, 15% on cars, and 20% on mobile recharge cards and internet. This is in addition to services rendered by deluxe and first class restaurants and hotels, which are subject to a 10% sales tax.

Customs duties

The customs duty rates are specified in the customs tariff and the agriculture agenda that are annexed to the Customs Duty Law.

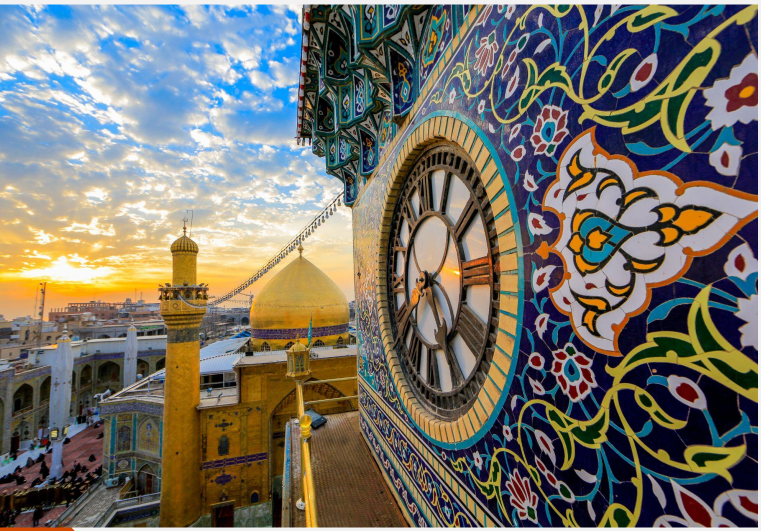
Payroll taxes

The payroll tax system in Iraq is similar to a pay-as-you-earn (PAYE) system, whereby the employer is obligated to withhold tax from salaries and wages paid to its employees and remit same to the tax authorities. Failure to do so will result in the employer being subject to penalties and late payment interest.

Social security contributions

With respect to contribution to the social security fund in Iraq, employers are divided into a number of categories, which is the driver for determining the contribution percentage. The categories include employers that are categorised as prime contribute at the upper rate (25% from the employer and 5% from the employee), whereas other categories contribute at the lower rate (12% from the employer and 5% from the employee).

Determining to which category the employer relates is subject to the social security department discretion. The criteria for this determination is not crystallised in the law; however, in practice, the social security authorities make their determination based on the business sector the employer is involved in (e.g. those in the oil and gas related industries are expected to attract the upper rate).



Withholding Tax

Under the tax law, the amount due from any residing taxpayers to a non-resident, whether the payment is made in cash or credited to the account, is subject to withholding tax (WHT) at the rate of 15% if such amounts are related to interest on debentures, mortgages, loans, deposits and advances, as well as annual allowances, pension salaries, or other yearly payments.

The WHT rate in cases where a resident is making a payment for interest to resident is 1.8% to 10%.

Dividends are not subject to WHT since dividends paid out of profits that have been subject to tax are not taxed again in the hands of the shareholder.

Additionally, industries/activities (non-upstream) contracted with oil and gas companies are subject to WHT on all payments at a rate of 3.3% or 7%.

Ministry of Finance in Kurdistan has issued instruction number (7) regarding WHT implementation in Kurdistan region on 11 April 2022 as follows:

The non resident entity in Iraq will be subject to WHT at a rate of 15% from the deemed profit determined by the Ministry of Finance.

Capital Gain

Capital gains on sales of depreciable assets are taxed at the normal CIT rate. To the best of our knowledge and legal practice, gains derived from the sale of shares and bonds not in the course of a trading activity may be exempted from tax. Capital gains derived from the sale of shares and bonds in the course of a trading activity are taxable at the normal CIT rate.

Excise Tax

There is no tax provision in the Iraqi tax law addressing excise taxes.

Transfer Pricing

The precise meaning of transfer pricing under the effective Iraqi tax system is rather unclear from a tax and legal perspective.

We note that while having no specific transfer pricing legislation, Iraq does have a 'third party' arm's-length provision contained within its tax legislation; whereby, if a non-resident taxpayer is engaged in business with a resident and it appears to the tax authority that due to the connection existing between the resident and the non-resident, and the substantial control of one over the other, that the business relationship is arranged in a manner that leaves no profits to the resident, or the profits left are much less than what is normally earned, the tax shall be assessed on the actual profits of the non-resident and charged to the resident as if the resident is the business agent for the non-resident.

Stamp Duty

Contracts are subject to stamp fees at rates that range between 0.1% and 3% of the contract value.

Taxable period

The taxable year in Iraq is the calendar year.

Tax returns

The statutory timeline for filing tax returns is 31 May of the year of assessment. If the self-assessment of tax is not accepted by the tax authorities, tax is assessed on the income of the taxpayer based on the information available to the tax authorities.

Failure to file a tax return may lead to an estimate of income and assessment of tax by the tax authorities; however, such an assessment does not relieve the taxpayer from responsibility for non-submission of the return within the statutory timeline stipulated by law.

Payroll taxes

Payment of the tax liability has to occur within three days from the assessment date by the tax authority. There is no requirement of quarterly payments during the taxable year.

Tax audit process

Tax inspection is mandatory in Iraq, as the tax authority will scrutinise the financial statements of the taxpayer to determine the tax liability and, accordingly, issue a tax clearance.

Statute of limitations

The statute of limitations is five years. However, the tax authority has the right to go back beyond five years in certain instances.

Topics of focus for tax authority

Obtaining a tax clearance from a tax audit/inspection is becoming increasingly important for importation and government bidding purposes, as well as for other areas that affect the continuation of operations.

Iraqi GAAP

The Iraqi tax law requires all taxpayers to maintain books and records in accordance with Iraq's local unified accounting system (Iraqi GAAP).

These books shall constitute tax books/accounts. This accounting treatment will determine when income is accrued and costs are incurred for computing taxable profits.

Pillar Two

Background

On 1 July 2021 and 8 October 2021, the Organisation for Economic Cooperation and Development (OECD) Inclusive Framework (IF) issued a 'Statement' focused on addressing the remaining key challenges of base erosion and profit shifting (BEPS) arising from the digitalization of the global economy.

The Statement proposed a 'Two Pillar' Solution, comprised of (i) Pillar One which aims to ensure a fairer distribution of taxing rights is established with respect to the profits of large multinational enterprises (MNEs); and (ii) Pillar Two which implements a new global minimum Effective Tax Rate (ETR) of 15% for MNEs.

Pillar Two

Pillar Two aims to ensure an appropriate level of tax is paid by MNEs through a series of measures aimed at modernising the international tax system for modern businesses. The Subject to Tax Rule (STTR) and the Global Anti-Base Erosion (GloBE) are the two components of Pillar Two.

STTR

The STTR is a treaty based rule that applicable to intra-group payments from source countries that are subject to low nominal tax rates in the country of the payee. The STTR focuses on where a source country has given up taxing rights on certain outbound intra-group payments, and it should be able to recover some of those rights where the income in question is taxed in the state of the payee at a nominal rate below 9%. The STTR applies to interest, royalties and a defined set of other payments made between 'connected persons', including services.

The OECD IF members have committed to adopt the STTR when requested by other IF members that are developing countries, as well as developed countries. In October 2023, the OECD IF issued a multilateral instrument ("MLI") that brings into effect the STTR by allowing for multiple bilateral tax treaties to be amended at the same time. Signature of the MLI is underway and applicability of the STTR expected to be commence in the near future.

GloBE

The GloBE Rules are designed to ensure that in-scope MNE Groups are subject to a minimum level of tax on the income arising in each jurisdiction where they operate.

Over 140 countries have committed to implementing the GloBE measures, and for the rules to have effect, individual jurisdictions must implement them into domestic law.

The GloBE Rules require implementation into domestic law by individual countries before they become effective. The rules came into effect on 1 January 2024, and over 30 countries have introduced tax rules that put into force a 15% effective tax rate on in scope entities, as well as over 100 being expected to also introduce rules that will come into effect in 2024 or 2025.

In brief, the GloBE Rules have been designed with an objective of accommodating a diverse range of tax systems, including different tax consolidation rules, income allocation and entity classification rules, as well as rules for specific business structures such as joint ventures and minority interests.

The GloBE Rules contemplate three different mechanisms for assessing tax on a MNE's income, and MNEs will have to comply with the filing requirements for each applicable rule. The first opportunity to collect the top up tax is the so called Qualified Domestic Minimum Top-up Tax (QDMTT) which gives the choice for the low tax jurisdiction itself to collect the tax (relating to this country). Second in line is the so called Income Inclusion Rule (IIR), which generally imposes tax on the parent entities within the MNE group to the extent that the foreign subsidiaries of the Group are taxed at a rate less than 15% (after the application of the QDMTT in their respective countries, if any).

These two mechanisms are accompanied by a 'backstop' rule, known as the Undertaxed Profits Rule (UTPR) which permits the collection of any remaining Top-up Tax (after QDMTT and IIR are applied) globally by any country where the MNE is active, meaning where there are people and/or tangible assets on the ground. Under certain conditions, the QDMTT could be elevated to a safe harbour that switches off the IIR and UTPR in other jurisdictions.

Status of Pillar Two in Iraq

Iraq is not a member of the OECD Inclusive Framework and has not made any announcement on the implementation of Pillar Two. Developments should be monitored.

What to expect?

Even if the rules will not be implemented in Iraq, MNEs headquartered in Iraq with consolidated subsidiaries in at least one implementing jurisdiction, may still be required to undertake the GloBE calculations for all the jurisdictions and may have specific compliance requirements. Further guidance is expected from the OECD with respect to filing obligations / location of submission of the GloBE Information Return (GIR), in cases where the ultimate parent entity jurisdiction such as Iraq does not implement the rules in 2024.

As per the existing Pillar Two administrative guidance, where a MNE is headquartered in a location that has not implemented the rules, GIR filing would be made in a different location, i.e. the location of a 'designated filing entity', where the MNE has operations and the respective location has implemented the rules earlier than the MNE's headquarter location.

Payroll income tax, social security and other taxes

Employment tax in Mainland Iraq

Employees are not usually required to file individual tax returns in Iraq and the tax due is withheld by the employer from the salaries and wages, and paid to the tax authorities. Accordingly, it is the responsibility of the registered employer to deduct the payroll taxes on the salaries and benefits of the employees and remit them to the tax authority on a monthly basis no later than the 15th of the following month.

A monthly statement has to be filed at the Direct Deduction Division of the General Commission of Taxes. The statement states the names of the employees along with the gross salaries, as well as details of deductible allowances and the amount of monthly income tax due, which needs to be settled by the employer.

The following progressive tax rates, after granting the resident the legal allowances are applicable to individual income taxation in Iraq:

- Up to IQD 250,000 …. 3%
- From IQD 250,000 up to IQD 500,000 …. 5%
- From IQD 500,000 up to IQD 1,000,000 …. 10%
- Over IQD 1,000,000 …. 15%

Penalties and interest in relation to PIT:

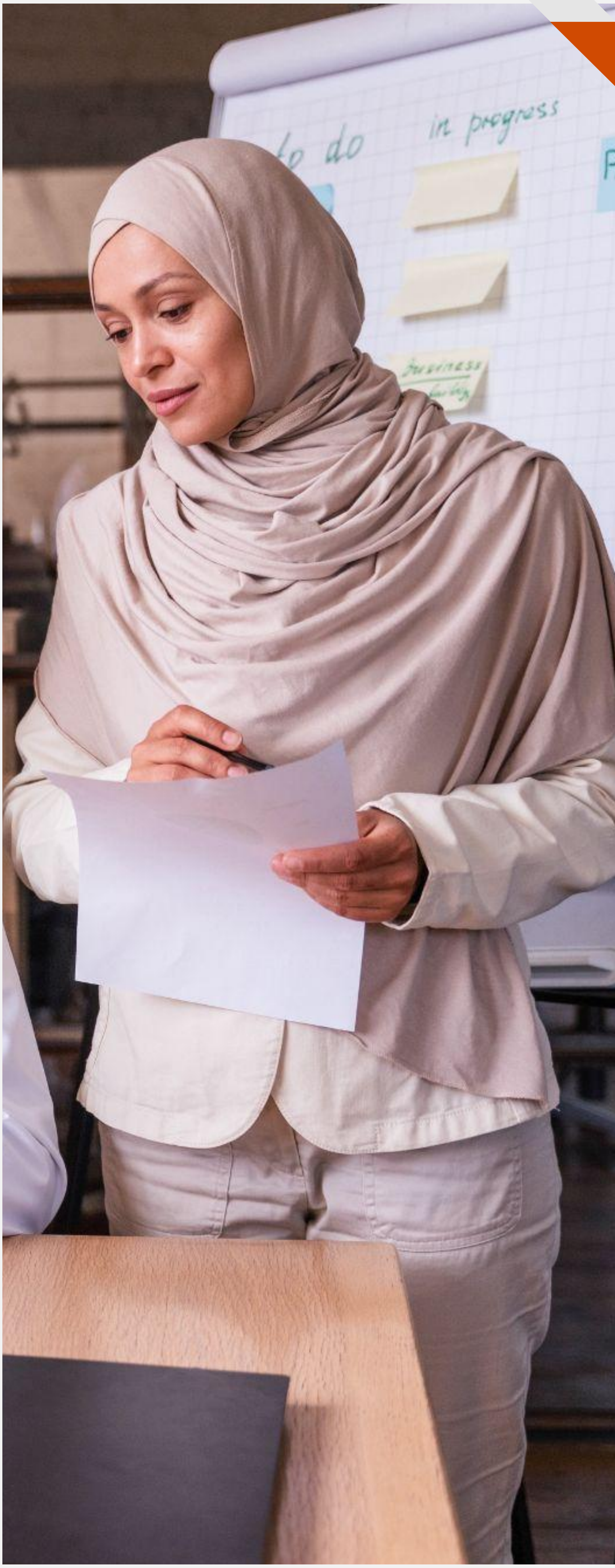
- Late filing penalty: IQD 500,000 (one time penalty)
- Late payments Penalties: 10%
- Late payment interest: 11% per annum.

Payroll Tax Inspection

As part of the employment tax audit process, the tax inspector reviews the audited financial statements to reconcile the salaries and wages expense in the financial statements with the total income reported in the yearly payroll schedules.

- To the extent that the amount declared in the financial statements is higher than the amount declared for employment tax purposes, the tax authority would seek to assess additional employment taxes of 10% on the difference.

- In practice, The tax assessor applies 1% - 2% of the total revenue as deemed PIT liability on the taxpayer and will be considered as a final liability if it is higher than the monthly PIT declarations for the concerned year.



Payroll income tax, social security and other taxes (Cont'd)

Employment tax in Kurdistan

- Employees are usually not required to file individual tax returns in Kurdistan and the tax due is withheld by the employer from the salaries and wages, and paid to the tax authorities. Accordingly, it is the responsibility of the registered employer, to deduct the payroll taxes on the salaries and benefits of the employees and remit them to the tax authority on a quarterly basis by no later than 21st of the next month of the ending quarter.
- A quarterly declaration in Kurdistan needs to be submitted along with the payment, the declaration compromises of a breakdown of the wages and salaries and concluding to the tax payable, the declaration needs to be signed and stamped by the branch manager and an original copy needs to be submitted to the tax authority in Erbil.
- The tax rate in Kurdistan is a fixed percentage of 5% of the taxable income.
- Penalties and interest in relation to PIT:
  - Late filing penalty: IQD 75,000 (one time penalty)
  - Late payments Penalties: First 21 days 5%, then its increased to 10%
  - Late payment interest: 1.5% accumulating per month on the total amount (principal and penalties)

Payroll Tax Inspection

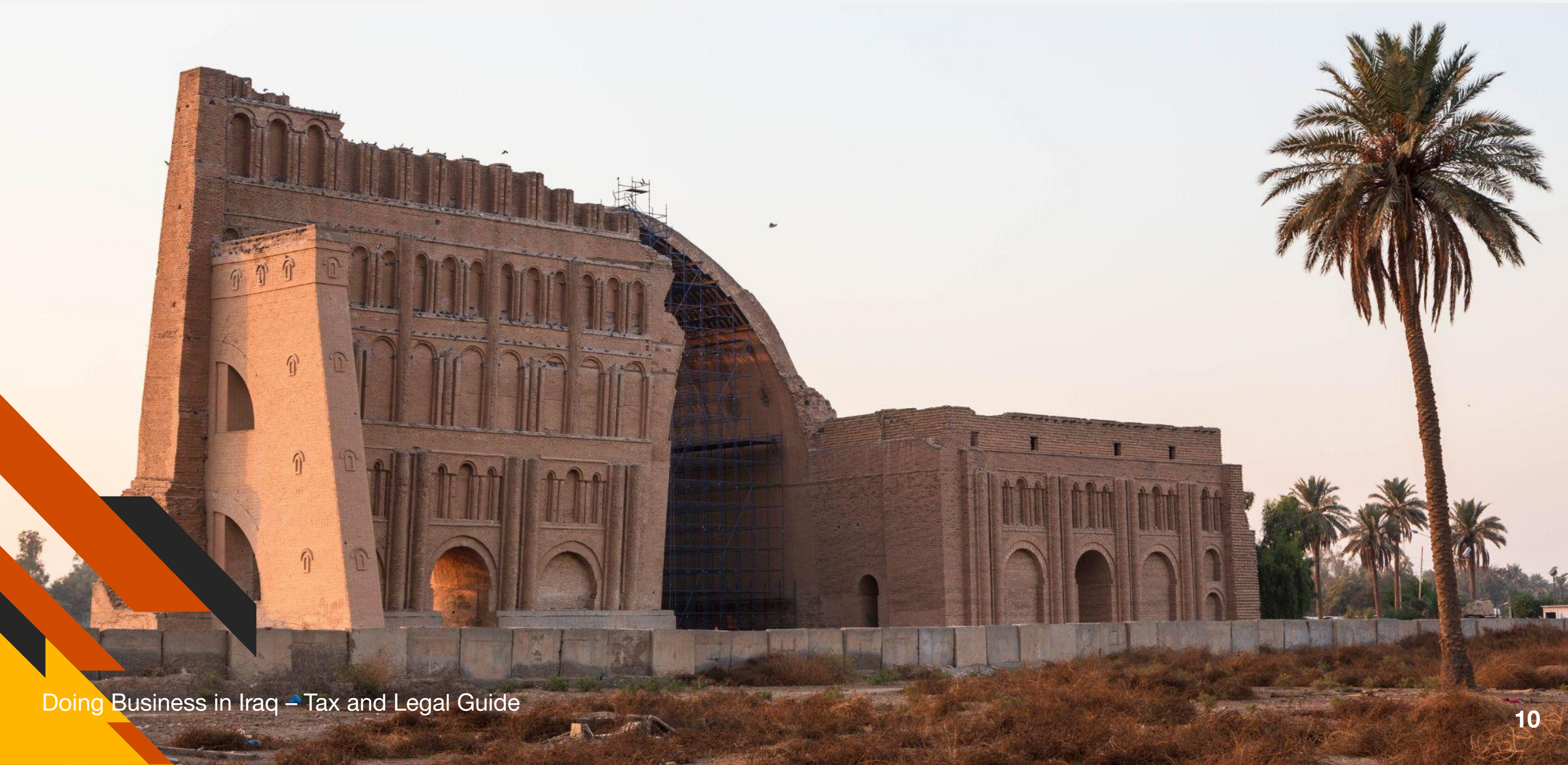
- Yearly declaration consisting of all paid salaries and wages including its breakdown needs to be submitted, the amounts of the yearly declaration need to be aligned with the quarterly declarations submitted. If a difference occurs between the yearly and quarterly, the tax authorities imposes a penalty between 5% and 15% on the difference.

Social Security in Mainland Iraq and Kurdistan

- Generally, the employee's social security contribution is 5% of the salary, and the employer's contribution is 12% of the salary. It is the employer's responsibility to deduct the social security contributions of both the employer and employees, and remit them to the Social Security Department before the end of the following month;
- For non-Iraqi nationals, who are capable of demonstrating that they are covered under a state social security system in their country of origin while working in Iraq, the requirement for social security can be waived provided that this is demonstrated by way of an official letter (certified by the Iraqi embassy) from the country of origin;
- Social security contribution late payment interest fees: 2% a month for each month the payment is late;

Key Considerations

The payroll tax system in Iraq is similar to a pay-as-you-earn (PAYE) system, whereby the employer is obligated to withhold tax from salaries and wages paid to its employees and remit same to the tax authorities. Failure to do so will result in the employer being subject to penalties and late payment interest.



Key Tax Indicators in Iraq

Tax Indicators	Resident	Non-Resident *
Fiscal year end	Calendar year. However a special year end can be used provided permission is granted in advance by the Lebanese Tax Authorities	Not applicable
Companies		
Income Tax	GCT applies the highest of the deemed tax on the reported revenue or the 15% (35% for oil and gas industry) of the reported profit/taxable profit.	Under the tax law, the amount due from any residing taxpayers to a non-resident, whether the payment is made in cash or credited to the account, is subject to withholding tax (WHT) at the rate of 15% if such amounts are related to interest on debentures, mortgages, loans, deposits and advances, as well as annual allowances, pension salaries, or other yearly payments.
Tax on Capital Gains	Capital gains on sales of depreciable assets are taxed at the normal CIT rate. To the best of our knowledge and legal practice, gains derived from the sale of shares and bonds not in the course of a trading activity may be exempted from tax. Capital gains derived from the sale of shares and bonds in the course of a trading activity are taxable at the normal CIT rate.	Not Applicable
General Sales Tax	A sales tax of 300% is imposed on alcohol and tobacco (cigarettes), 15% on travel tickets, 15% on cars, and 20% on mobile recharge cards and internet. This is in addition to services rendered by deluxe and first class restaurants and hotels, which are subject to a 10% sales tax.	Not applicable
Value Added Tax	Not applicable	Not applicable
Individuals		
Individual Marginal Tax Rate (Max)	Progressive rates up to: (i) 15% for salaries and wages in Iraq Mainland and (ii) 5% for salaries and wages in Kurdistan	
Basis of Taxation	Salary paid from Iraq or abroad or other Iraqi source income	Iraqi source income
Withholding Tax - Iraq Mainland		
Dividends	Not applicable	Not applicable
Interest	1.8% to 10%	15%
Royalties	Not applicable	15%
Management Service Fees	Not applicable	15%
Customs	The customs duty rates are specified in the customs tariff and the agriculture agenda that are annexed to the Customs Duty Law.	
Exchange Controls	NA	
Thin Capitalisation	No clear or detailed thin capitalisation rules.	
Transfer Pricing	The precise meaning of transfer pricing under the effective Iraqi tax system is rather unclear from a tax and legal perspective.	
Double Tax Treaties in Force	NA	
Treaties Awaiting Conclusion or Ratification	Canada, Cuba, Gabon, Sudan, KSA.	

About PwC Middle East

We are one of the fastest growing PwC member firms globally and the largest professional services firm in the Middle East.Our tailored solutions help clients meet the challenges and opportunities of doing business in the Middle East and beyond.

We've experience in diverse industries, including government, energy, financial services, retail, construction, manufacturing, telecoms and more.Our clients in the Middle East include leading public and private companies, governments, banks and more. More than 50 employees from our worldwide network are on secondment to the Middle East firm, bringing global perspectives and support to our clients in the region.

Established in the region more than 40 years, PwC has more than 10,000 people in 12 countries across the region: Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Libya, Oman, the Palestinian territories, Qatar, Saudi Arabia and the United Arab Emirates.

10,800+ people

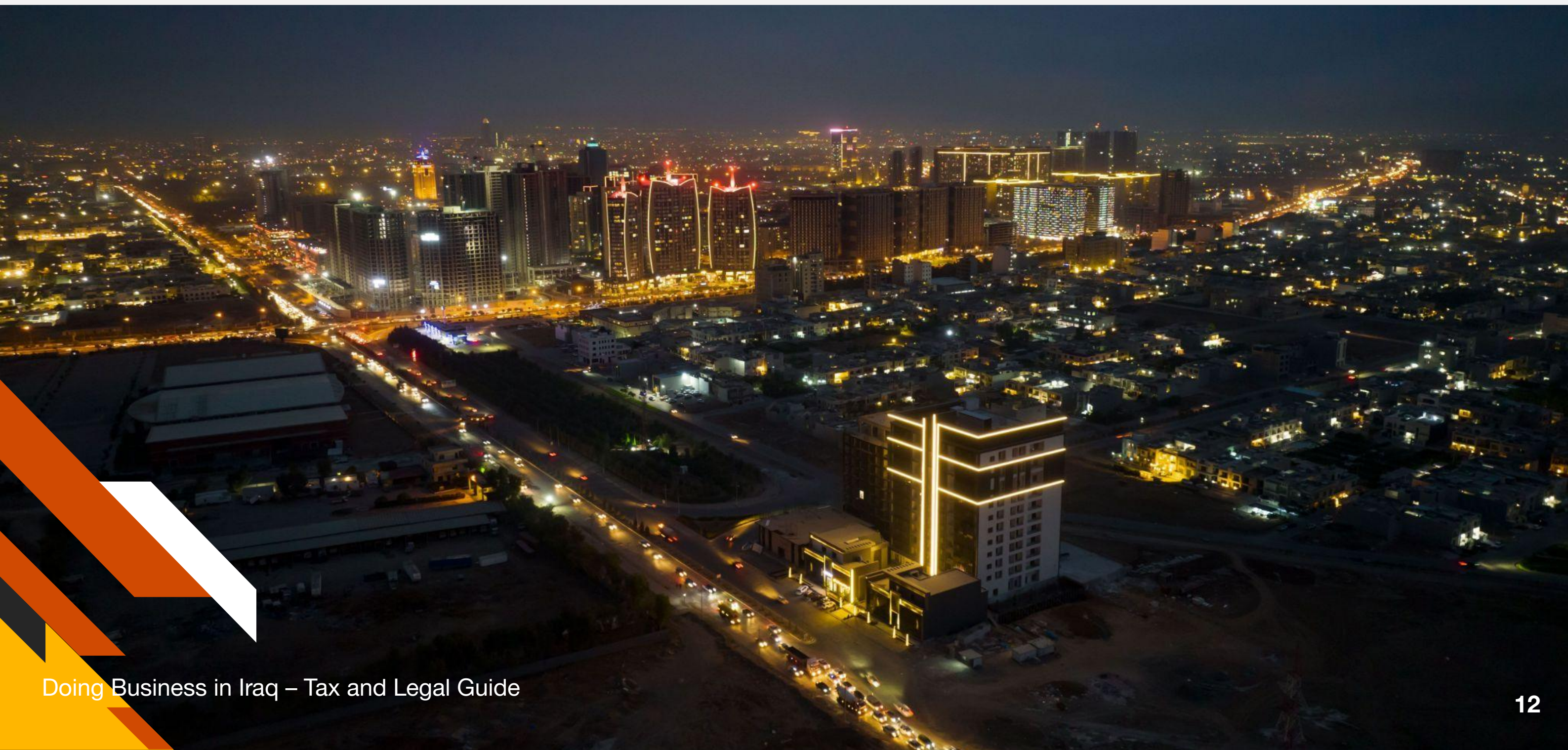
including **450** partners, in **12** countries

The largest professional services firm in the

Middle East

Supporting clients in the region for

over 40 years

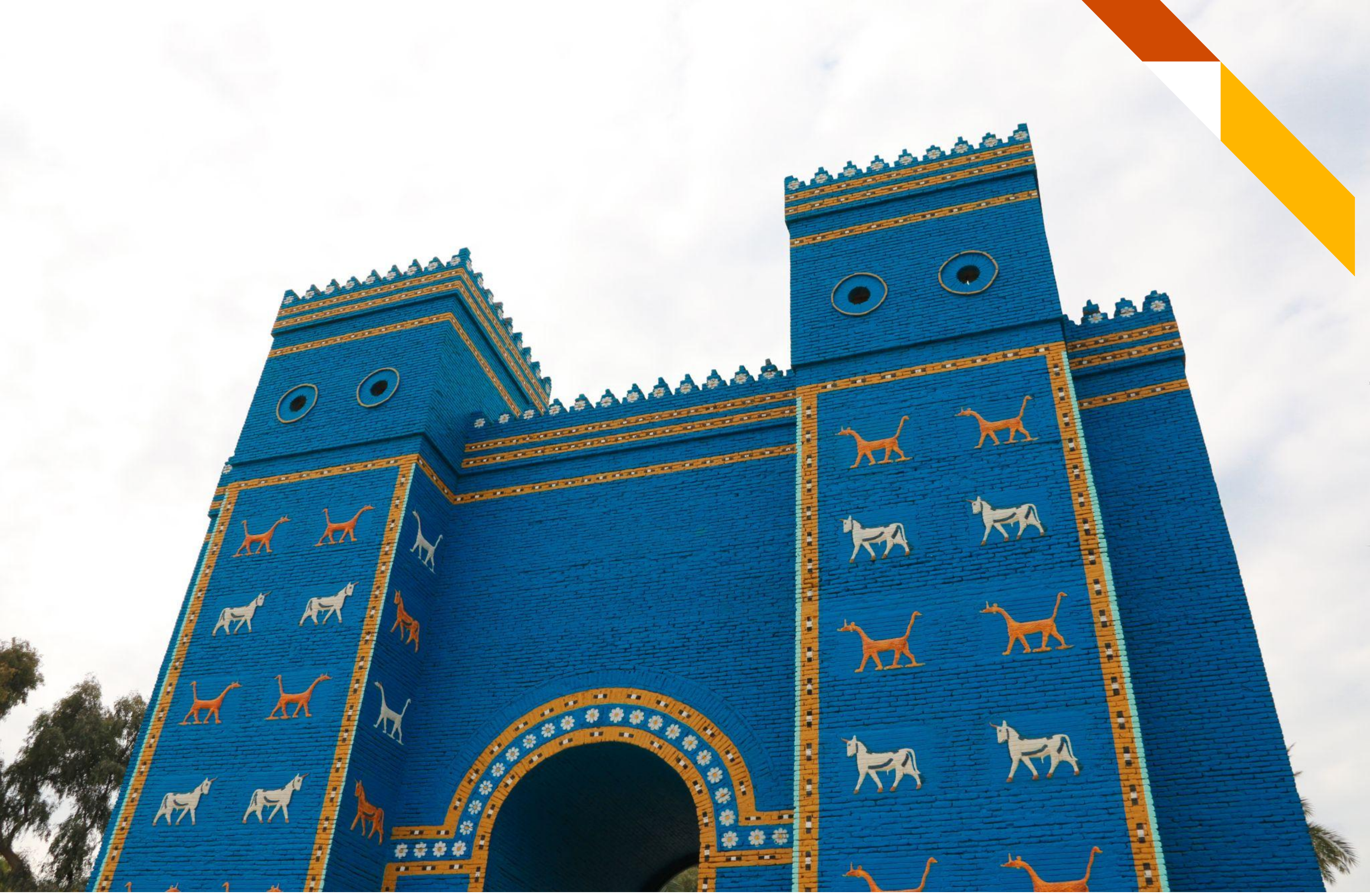


Contacts

Jochem Rossel
Middle East Tax & Legal Services Leader
Email: jochem.rossel@pwc.com

Suhaib Asad
Partner
suhaib.asad@pwc.com

Taking this **#journeywithyou**



Disclaimer

This publication has been prepared for general guidance on matters of interest only, and does not constitute professional advice. You should not act or refrain from acting upon the information contained in this publication without obtaining specific professional advice. No representation or warranty (express or implied) is given as to the accuracy or completeness of the information contained in this publication, and, to the extent permitted by law, PricewaterhouseCoopers [PwC Middle East network of firms], its members, employees and agents do not accept or assume any liability, responsibility or duty of care for any consequences that you or anyone else acting, or refraining to act, in reliance on the information contained in this publication or for any decision based on it.

How we are structured - Click here