Introduction of Corporate Income Tax ("CIT") in Kuwait

October 2024
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Background

A potential two phased approach on the introduction of CIT is expected in Kuwait[1]. The first phase would target multinational companies with revenues over EUR 750 Million (approx. KD 250 Million) and the second phase will be applicable to all Kuwaiti companies. The expectation is that this will include a wide range of operating structures, including corporate entities, partnerships, and other businesses with separate legal existence. However, individuals and small and medium-sized entities are initially expected to be exempt from the tax law.

Kuwait currently has a 15% CIT regime applicable to the foreign (non-GCC) corporate entities. However, with the changes in the region, we would expect that the local legislation will be updated to the standard being followed across other GCC countries.

What would CIT in Kuwait look like?

It is likely that Kuwait will implement a standard Corporate Income Tax (CIT) regime similar to other jurisdictions. Based on the United Arab Emirates (UAE) CIT legislation, we have set out below some key features that one may expect to see in the Kuwait CIT law:

- CIT is likely to apply to all commercial activities. Entities engaged in the exploration, production or refining of hydrocarbons may be excluded as they are strategic to the country. Small business relief may be available to businesses with revenues below a certain threshold. Further, individuals earning employment income or passive investment income are expected to be excluded from CIT.
- We expect the CIT rate to be flat 15% in line with the Global Minimum Tax for the businesses which would be subject to tax under the CIT regime in Kuwait.
- Capital gains from disposal of assets are likely to be taxed. There may be a capital gains exemption available subject to meeting certain conditions (for example, for entity reorganizations).
- A participation exemption may apply to dividends or capital gains received from qualifying foreign or local subsidiaries on the basis that this income has already been taxed.

[1]A news article published in Al-Rai newspaper on 24 October 2023.

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What would CIT in Kuwait look like? (continued)

- Withholding tax (WHT) on payments (such as dividends, interest, royalties, management fees) to non-residents may be introduced to capture tax on income earned by non-residents.

  This would be major shift from the current tax retention regulations and allow non-residents to be taxed at source rather than requiring non-residents to register with Kuwait tax authority and file a tax return, thereby streamlining the tax process for non-residents.

  The UAE prescribes a WHT rate of 0% but Saudi Arabia and other GCC countries impose WHTs ranging from 5% to 20% depending on the nature of payment.
- Tax depreciation rates generally differ from depreciation rates used for accounting purposes. As a result, the tax base and book value of capital assets may differ.
- Carry forward of tax losses may be available to offset taxable income of future tax periods or against taxable income in other group entities, subject to meeting conditions.
- Personal/recreational expenses and/or payments to related persons would typically be disallowable from a tax perspective.
- Specific transfer pricing rules are expected to apply to ensure that domestic and cross border transactions between related parties are carried out at arm's length (at market value) to prevent any manipulation of taxable income.
- Any tax (including WHT) paid in foreign jurisdiction may be available as a foreign tax credit for offsetting against the CIT liability in Kuwait. This will be subject to conditions prescribed in Double Taxation Avoidance Agreements (DTAAs) between Kuwait and the relevant foreign jurisdiction.
- The Kuwait CIT regime may allow group entities to form a tax consolidated group (different from accounting consolidation) and be treated as a single taxable person. Whilst certain jurisdictions including the UAE, Australia and certain EU countries allow tax grouping for CIT purposes, many other jurisdictions including KSA and Oman in the region do not allow tax grouping.
- Taxpayers may be expected to prepare and maintain stand alone financial statements.

What are some of the key impact areas under a CIT?

Related party transactions must reflect the taxable income that would have arisen if the transactions had been carried out at arm's length (with a third party). Related party transactions between entities within a group that have different tax profiles (such as loss-making entities or entities subject to different effective tax rates) may attract more scrutiny from the tax authority as there could be a motive to shift profits to other group entities that are subject to a lower tax rate.

A CIT regime introduces several compliance concepts (transfer pricing, consolidation rules, interest deductibility limitations) so businesses will need to ensure that their current systems will be able to handle these requirements.

Existing structures may or may not be tax effective. Even before a CIT is introduced, businesses can evaluate their existing operations and structures to see if they would be tax effective and consider any optimization opportunities well before any transitional rules or restrictions are announced along with the introduction of a CIT.

Income and expenses may be recognized in different periods for tax and accounting purposes and specific income and/or expenses may not be recognized for tax purposes but recognized for accounting purposes, or vice versa.

The treatment of capital gains and losses will vary for the purposes of CIT and accounting. Tax losses in a particular year may be available to offset the taxable income in later years. This will also result in differences between accounting profit and taxable income (or the carry forward tax loss).

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What should Kuwait businesses be doing now?

Kuwait businesses have historically been operating under a no domestic CIT regime and the introduction of a CIT regime will be a significant disruption to the status quo with far reaching financial and commercial implications. Businesses should focus on the following main areas:

- Impact a CIT will have on business profits and therefore return to shareholders.
- The current role of the tax function in the organization.
- Legal structure, business model, and capital structure rationalization.
- Adequacy of resources and capabilities within the finance function.
- Systems and technology infrastructure used by finance and whether it can be leveraged for tax and consider any updates if required.
- Polices and controls for governance, strategy and reporting.

We strongly recommend that Kuwait businesses conduct at least a preliminary analysis of the impact the introduction of a CIT will have.

Update on other local taxes

Based on media reports, **Kuwait** has formally joined the **Union of Tax Authorities in Islamic Countries** to facilitate the improvement of tax administration and strengthen the imposition of taxes in accordance with Islamic law, with special reference to Zakat in Islamic countries.

At this stage it is not clear if the current **Zakat regulations** in Kuwait will be updated to accommodate for the change towards a Shariah based Zakat and the **impact** on the current Zakat legislation based on the expected introduction of CIT.

Reach out to us

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