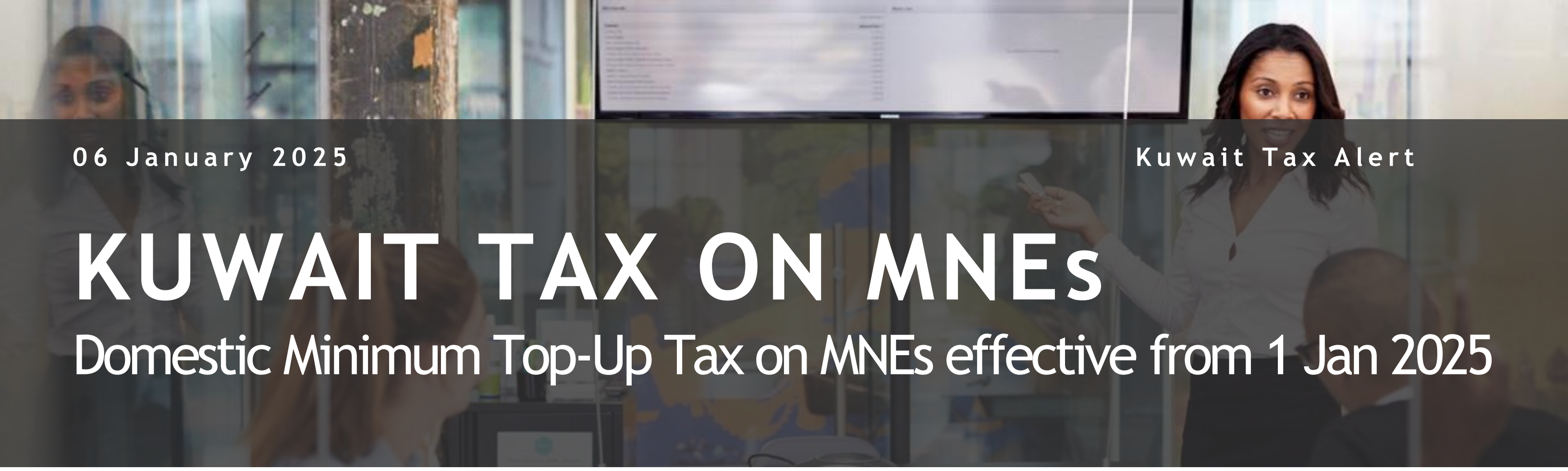


06 January 2025

Kuwait Tax Alert

KUWAIT TAX ON MNEs

Domestic Minimum Top-Up Tax on MNEs effective from 1 Jan 2025

In November 2023, Kuwait joined more than 140 jurisdictions in accepting the international tax reform framework of a two-pillar solution announced by the Organization for Economic Co-operation and Development ("OECD") to tackle base erosion and profit shifting risks arising from the digitalization of the economy (commonly known as "BEPS 2.0"). Pillar Two aims to ensure that multinational enterprises ("MNEs") pay a minimum level of tax wherever they operate.

On 31 December 2024 Kuwait issued Decree No. 157 of 2024 which implements a domestic minimum top-up tax ("DMTT" or "the Law") at an effective rate of 15% that is aligned with OECD Pillar Two Global Anti-Base Erosion Model Rules ("the Globe Rules"). This will help Kuwait collects tax revenue that may otherwise be collected by other jurisdictions trough Income Inclusion Rule ("IIR") or Undertaxed Profit Rule ("UTPR").

- **1 January 2025:** 15% DMTT on MNEs
- **1 January 2025:** Existing tax laws are no longer applicable for MNEs impacted by DMTT
- Tax registration due by 30 September 2025
- No application of IIR or UTPR

Entities subject to DMTT

The Law applies to all entities **in Kuwait** whether as Ultimate Parent Entities ("UPEs") or as Constituent Entities ("CEs") e.g. subsidiaries or permanent establishments ("PEs") of a group that meet **both** of the following criteria:

1) The group is a Multinational Group (i.e. present in more than one jurisdiction through subsidiary, branches, PEs or similar form of presence); **and**
2) The UPE of the group has a consolidated revenue of at least EUR 750 million (approx. KD 240 million) in at least two out of the prior four accounting years.

Broadly, an entity is deemed to be "in Kuwait" if it is a tax resident of Kuwait or in case of a PE in Kuwait. An entity becomes a tax resident in Kuwait if it is incorporated in Kuwait or has its main / effective place of management in Kuwait.

The Law also applies to stateless entities as well as Joint Ventures ("JVs") if owned 50% or more by an in-scope MNE group.

Permanent Establishments (PEs)

The Law provides a PE definition largely aligned with the U.N. Model Tax Treaty. There is a six-month duration test for the creation of a construction/ installation PE as well as the provision of services. A PE is also created if there is a place of business or management, branch, office, workshop, warehouse or an agent in Kuwait. A PE is also created for a non-resident if the entity has a place of business through which the entity does business and the income attributable to such activities is exempt in the jurisdiction of the non-resident.

Applicability

The Law is applicable from financial years beginning on or after 1 January 2025.

Abolishment of existing tax laws for MNEs

Entities in-scope of the DMTT will **not** be subject to the following existing domestic taxes effective from financial years beginning on or after 1 January 2025:

- Zakat
- National Labor Support Tax ("NLST")
- Income Tax under Decree No. 3 of 1955 as amended
- Income Tax on activities in the Neutral Zone of Kuwait – Saudi Arabia

Excluded Entities

The Law excludes certain entities such as government bodies, international organizations, not for profit organizations, pension funds and investment funds/real estate funds that are UPEs. However, the revenue of the Excluded Entities is to be included in the revenue test of the MNE group.

Tax Rate

The tax rate has been prescribed as an effective rate of 15% inline with the Pillar Two Framework. The tax will be collected when the effective tax rate ("ETR") of the taxpayer is below 15% (*see page 4 for further details*).

Safe Harbour

Inline with the OECD guidance, the Law provides for the following welcomed safe harbour provisions aimed at simplifying tax compliances for eligible MNEs:

a) Transitional CbCR Safe Harbour: MNEs that meet certain criteria will be excluded from the Globe rules for a limited period. The qualification criteria are inline with the OECD guidance (De Minimis Test, Simplified ETR Test and Routine Profit Test).

b) Simplified calculation safe harbour: The Law also provides for a simplified calculation for certain MNEs. The conditions will be specified in the executive regulations but expected to be inline with OECD guidance.

c) Exclusion for initial international activities: Tax relief for up to five years is available to MNE groups during the initial phase of international activities subject to meeting certain conditions such as:

- The Group does not have CEs in more than six jurisdictions (including Kuwait);
- Total book value of tangible assets does not exceed EUR 50 million, except for the reference jurisdiction (i.e. the jurisdiction in which the MNE group has the highest total net book value of tangible assets in the financial year in which Pillar Two is first applied to the group); and
- The Kuwait CE is not held by a parent entity located in a jurisdiction that applies the IIR.

Compliances

- Tax registration must be completed within 120 days from the date of becoming taxable under this Law, except for the year 2025 where registration timelines are extended up to 30 September 2025.
- Tax declaration and tax payments are due by the 15th month following the end of the tax year.
- There is no provision for tax installments or advance payments.
- Records must be kept for 10 years.
- Statute of limitations is 10 years.
- Conversion from foreign currencies to Kuwaiti Dinar is to be inline with the rates published by the Central Bank of Kuwait. Further guidance will be provided in the executive regulations.

Penalties

- Late filings will incur a penalty of at least KD 1,000 or 5% - 20% of the final tax due depending on the delay, whichever is higher.
- If the tax assessed exceeds 10% of the declared tax, a 25% penalty on the difference applies. However, the penalty is reduced to 10% for self-corrections.
- Non filings attracts a penalty not less than KD 5,000 or 25% of final tax due, whatever is higher.
- Late payment penalty of 1% of the tax due will be levied for every 30 days delay or part thereof.
- An administrative penalty of KD 3,000 will be imposed in case of delayed tax registration, or failure to timely provide / update information or maintain supporting documents.
- The Law does not provide for transitional penalty relief.

Transfer Pricing (TP)

Article 18 of the Law requires related party transactions to be undertaken based on arm's length principles. The executive regulations will specify criteria of related parties and for transfer pricing methods to be adopted. This brings additional significant tax change in Kuwait (no TP regime in place currently) and is a required provision to address any misallocation of income among entities located in different jurisdictions.

Computing the DMTT

Below is a high-level process for computing the DMTT:

1. Determine the income: The starting point for calculating an entity's income is the Financial Accounting Net Income or Loss ("**FANIL**"), before making consolidation adjustments to eliminate intra-group transactions.

2. Determine the **Globe Income**: Certain tax adjustments are required to be carried out on the income as per FANIL to arrive at the Globe Income. Adjustments include dividends, equity gains or losses, revenue of debt releases and international transportation and shipping income. The executive regulations will specify additional conditions/ clarification.

3. Determine the **Excess Profit** (i.e. the taxable income): The Globe Income is to be reduced by Substance Based Income Exclusion ("SBIE") to arrive at the Excess Profit. SABE is computed at 9.6% - 5% of total payroll cost, and 7.6%-5% of the average book value of the tangible assets. The executive regulations will specify conditions for the implementation of this provision.

4. Compute the **ETR** for Kuwait CEs. ETR = Amount of Adjusted Covered Taxes / GloBE Income

5. If the ETR is below the Minimum Rate, the Top-up Tax Rate for Kuwait must be calculated.
   Top-up Tax Rate = the Minimum Rate of 15% - the ETR as computed under step 4 above.

6. Compute the Top-up Tax due. Top-up Tax = Excess Profit of Kuwait CEs x Top-up Tax Rate

The Law is silent on the possibility of making additional tax payments due to adjustments to covered taxes, changes to ETR due to re-computations of FANIL etc. but maybe provided for in the executive regulations.

Next Step

The Ministry of Finance is expected to issue executive regulations within six months to help clarify certain aspects of the Law including tax registration and tax filing mechanisms. It is our understanding that the Ministry will organize workshops during Q1 of 2025 to elaborate on the mechanics of the Law.

BDO Comments

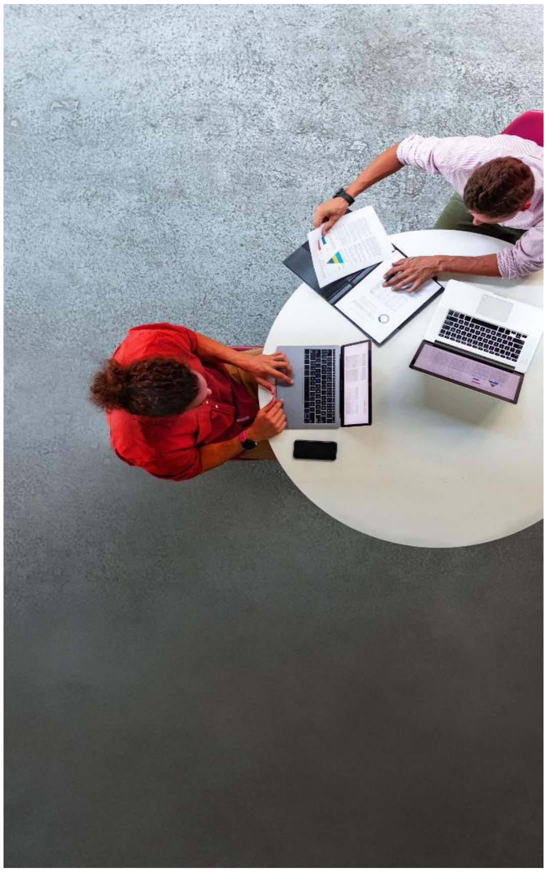
The DMTT Law will help Kuwait raise additional non-oil revenue inline with its Vision 2035 and collect tax revenue that may otherwise get collected by other jurisdictions through IIR and UTPR provisions.

Foreign entities with existing income tax holidays in Kuwait and in-scope for the DMTT will no longer benefit from such tax incentives. Notably, the Law is silent on any potential refundable tax credits to attract investments.

Kuwaiti shareholding companies in-scope of the DMTT will likely continue be required to contribute 1% to Kuwait Foundation for Advancement of Science (KFAS). The Law does not address whether KFAS contributions will be treated as a covered tax, but the expectation is that it may not qualify as one.

The Law states that Income Tax Decree of 1955 as amended will not apply to entities in-scope of the DMTT. It remains to be seen whether the tax retention requirement will no longer apply on such entities.

The new tax rules are complex, will have both short and long-term impacts, and create demands on staff and technology, likely necessitating professional advice. In-scope MNEs should prepare for an increased compliance workload, which will involve complex calculations, identifying any potential gaps, and updating systems and refining existing compliance processes.



HAVE QUESTIONS OR WANT TO LEARN MORE? CONTACT US!

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