RSM Kuwait Tax Newsletter

Breaking New Ground: Kuwait – UAE Tax Treaty Synopsis

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Introduction

As the economic landscapes of Middle Eastern countries evolve, the concept of "tax-free countries" is rapidly becoming outdated. On July 14, 2024, Kuwait issued Decree No. 7 of 2024, approving the Double Taxation Avoidance Agreement (DTAA) with the United Arab Emirates (UAE). This Treaty, signed in Dubai on February 11, 2024, aims to enhance economic relations and foster cooperation on tax matters between the two nations. It focuses on avoiding double taxation on income and capital taxes, as well as combating tax evasion and avoidance.

Summary of Key Provisions of the Tax Treaty

Type of Taxes covered in the Tax Treaty

Taxed covered (Article 2)	
Kuwait	1. Income Tax Decree no. 3 of 1955 amended by Law No. 2 of 2008. 2. National Labor Support Tax (Law No. 19 of 2000). 3. Income Tax Law concerning Neutral Zone and Specified Area (Law No. 23 of 1961)
UAE	1. Income Tax 2. Corporate Tax

Note: The Treaty excludes Kuwait's Zakat and contributions to the Kuwait Foundation for the Advancement of Sciences (KFAS) from the list of covered taxes under Article 2. However, any new or similar taxes introduced after the signing of the Treaty will also be considered covered taxes as per Article 2.

Permanent Establishment ("PE")

Article 5 on PE follows common international rules for PE establishment. Types of PEs defined in Article 5 include:

Fixed Place PE	If an enterprise has fixed place of business in source state, it creates a fixed place PE.
Construction PE	If the activities on site of construction, assembly or installation continues for more than 6 months.
Service PE and Equipment PE	If the activities are continued for more than 3 months in any 12-month period.

Applicability of Residency Rule (Article 4)

	Definition of "Resident" covers	Definition of "Resident" does not cover
Kuwait	1. Any corporate entity incorporated in Kuwait 2. Kuwaiti nationals who are domiciled in Kuwait	1. Non-Kuwaiti resident individuals in Kuwait
UAE	1. Any company or entity incorporated in UAE 2. UAE citizens 3. Individuals who are resident in UAE or have habitual abode or vital interests in UAE	

Note: In cases of dual residency for individuals and corporates, factors such as permanent home and place of effective management are considered for taxation.

Business profits

Business profits earned by a PE of one state in the source state will be taxable in the source state to the extent such profits are attributable to the activities of PE in the source state. This attribution rule also applies to the expenses incurred in the source state, hence, any expense incurred to the extent it is attributable to the PE shall be allowed as deduction for the purpose of determining profits of the PE.

Dividend and Interest

Article 10 and 11 on taxation of dividend and interest respectively provides that right to tax dividend and interest income lies only with the residence state and not source state, subject to meeting certain conditions .

> For instance– if a UAE citizen or entity earns dividend income from shares invested in Kuwait and the entity does not have a PE in Kuwait, **such dividend income will be taxable in UAE and not Kuwait.**

Royalties and Fees for Technical services

Article 12 and 12a on Royalties and Fees for Technical services respectively provides the right to tax such income to resident country but the source country may also have the right to **tax such income at the maximum rate of 10% of royalties or fees for technical services**, subject to certain conditions.

Capital gains

Capital gains arising from the sale of immovable property may be taxed in the source state. Capital gains arising from the sale of unlisted shares shall be taxed in the residence state unless such shares, at any time during the **365 days preceding the transfer of ownership, derive more than 50% of their value from immovable property situated in the source state.** Capital gains arising on sale of listed shares may be taxed only in the residence state. Special rules relate to capital gains on other assets.

Tax credit mechanism

The Tax Treaty provides a provision under Article 24 whereby credit is available against the tax paid in Kuwait and UAE on income or capital gains.

> For instance – if a UAE company (with 100% foreign ownership) has a **PE in Kuwait and paid tax amount of KD 1,000 in Kuwait. Such KD 1,000 could be available to this UAE company** as tax credit while calculating tax liability under the UAE tax laws.

Open ended question

Although the DTAA provides clarity on almost every aspect of taxation between the UAE and Kuwait, **a prominent question remains regarding the taxability of a 100% UAE nationals– owned company in Kuwait.** Historically, as per the mutual agreement between GCC countries, a company wholly owned by UAE nationals has been exempt from taxation in Kuwait. However, with the introduction of new tax laws in the UAE, a Kuwaiti company having a PE in the UAE is now subject to taxation. Given the implementation of the DTAA, **the question arises whether such 100% UAE– owned companies will continue to be exempt from taxation in Kuwait, or if they will become liable for taxation.** In other words, if there is a conflict between the provisions of domestic law and the DTAA, which law would prevail? It remains unclear at the moment that what practice will be adopted by Kuwait tax department, **however RSM Kuwait will keep a close track with the tax department on this issue for any further update.**

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RSM Albazie & Co. has qualified personnel with bilingual skills, and experience and knowledge of local and international taxation.

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