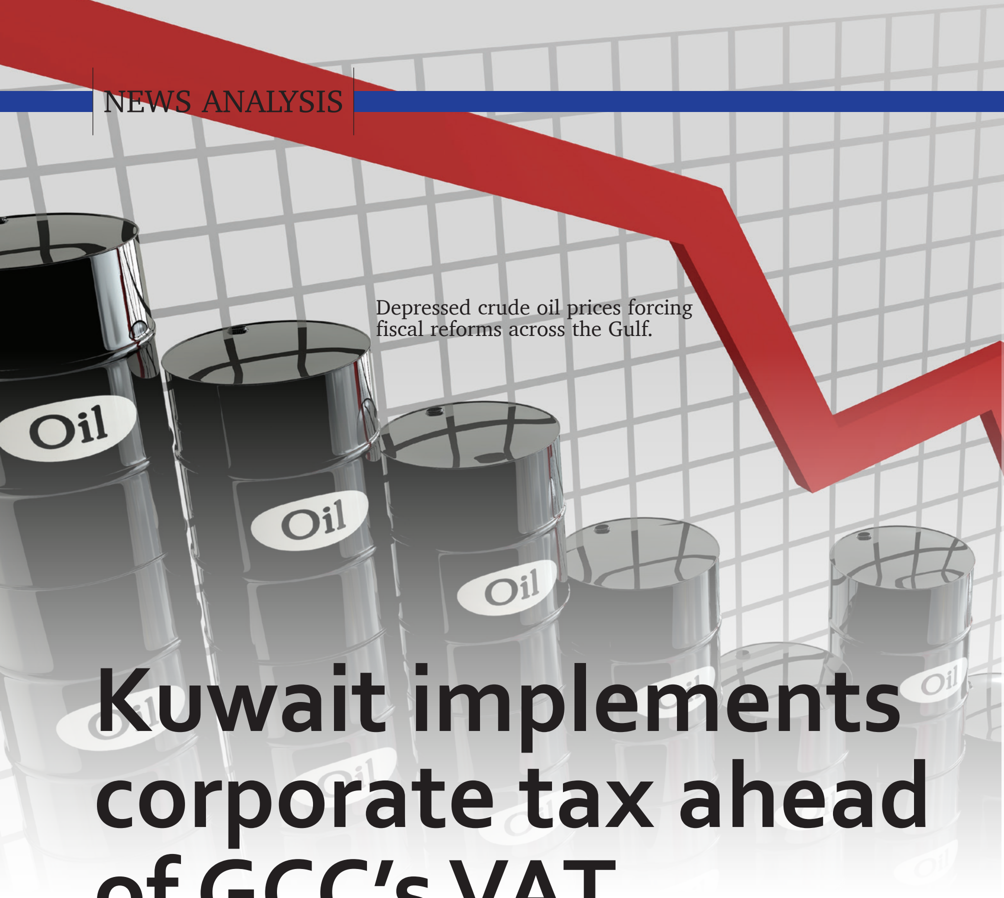

Depressed crude oil prices forcing fiscal reforms across the Gulf.

(Credit: Pavel Chagochkin/Shutterstock.com)

Kuwait implements corporate tax ahead of GCC's VAT

The Middle East looks at ways to plug budget deficits

Following indications made by the Government at the end of last year, the Kuwaiti cabinet approved the implementation of a standardised 10 per cent tax on corporate profits this month, alongside the re-pricing of some commodities and public services. The approvals are part of the Government's fiscal reforms to combat the pressure of depressed oil prices and budget deficits. Corporate taxes were previously imposed at different rates for local and foreign companies.

The IMF forecasted that the oil price plunge was the reason for Kuwait's declining fiscal position in 2014-2015, which tightened to a surplus of 17.3 per cent, compared to a surplus of 34.7 per cent it recorded in 2013-2014. Government revenues reportedly fell by 60 per cent last year due to lower oil prices, as the finance ministry projects a deficit of KWD 12.2 billion in the fiscal year commencing 1 April 2016.

The IMF suggested that the introduction of the tax regime would potentially increase revenues by KWD 500–800 million (1.3 to 2.1 per cent of gross domestic product (GDP)), while Kuwait expects it to generate between KWD 800 million and KWD 1 billion annually. The Government has also been reported to be looking at privatising state-owned assets including airports, ports and the management of schools as well as some facilities of Kuwait Petroleum Company. Nothing has yet been said as to the implementation of income tax for individuals.

In trying times, most hydrocarbon-reliant states across the GCC are considering cutting costs and boosting oil revenues to plug potential deficits. Kuwait has forged ahead with corporate taxation while other Gulf nations look at a different route exploring the introduction of value-added tax (VAT) in their respective economies.

Obaid Humaid Al Tayer, UAE Minister of State for Financial Affairs, in late February officially announced plans for VAT to be developed and implemented over the next two to three years. Al Tayer made the announcement at a press conference with Christine Lagarde, Managing Director of IMF at the Dubai International Finance Centre (DIFC). He said that GCC countries are working in tandem on a framework now, which he expects to be agreed upon and made public in June of this year. Following the framework, member countries will have to implement VAT by 1 January 2019.

"A lot of groundwork needs to be done before implementing VAT," he said, noting that governments would have to move at their own pace. Notably, healthcare and education will be exempt from the UAE's VAT. Lagarde had underlined the need for VAT and potentially corporate tax in the region's 'new economic reality' of low oil prices and decreased government revenues.

"Indirect taxation is generally easier to put in place, and that is typically the case with VAT. Direct taxation is a bit more complicated and we're certainly not recommending to put income tax in place right away, because income tax requires that you have the institutional capacity to actually assess the revenue, organise for that taxation, think about that distributional aspect of it, and decide exactly how you want to design it," she added. Lagarde estimated that even a single-digit VAT rate in Gulf countries could generate revenues in the range of two per cent of GDP.

With previous efforts towards diversification and good capital buffers, the UAE is believed to be well-placed to build a careful tax system. The potential for corporate tax was also discussed. "Tax rates play a part, but are not a dominant factor," she said in response to concerns over whether businesses would divest from the region. Lagarde insisted that it should not drive away business for the UAE.