

New Tax Rules: Are they valid and how will they affect Kuwaiti companies?

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The Kuwaiti tax laws have granted the Minister of Finance inherent powers to issue a set of executive rules and instructions to facilitate the implementation and enforcement of the legal provisions provided in the said tax laws. However, what would be the legal and practical effect when an “executive rule” seemingly exceeds its objective and purpose or contradicts with its source of legislation in all tax matters?

General

Income-tax in Kuwait is regulated by the Decree No.3 of 1955 (“Decree”) and Law No.2 of 2008 amending certain provisions of the Decree (“Amendment”) and the Ministerial Resolution No. 29 of 2008 concerning the issue of executive by-laws (“Implementing Regulations”), (collectively referred to as “Tax Laws”).

The Tax Laws enable the Minister of Finance, Kuwait or a representative /delegate/ authorized person of the Ministry of Finance, Kuwait to issue executive rules containing prescribed forms and procedures to facilitate the implementation and enforcement of the legal provisions provided in the Tax Laws. Such executive rules address procedural issues relating to tax cards, correspondence, submission of declarations, approval of fiscal year, exemptions and other procedures related to the administration of tax.

New Executive Rules

In January 2011, the Ministry of Finance has issued a new set of executive rules (“Executive Rules”). The Executive Rules are intended to regulate the proper execution of the provisions of the Tax Laws which constitute the source of legislation in that matter.

Executive Rule 20 versus Article 46 of the Implementing Regulations

- Executive Rule 20 (“ER 20”) prescribes certain forms and procedures with respect to the implementation of Article 46 of the Implementing Regulations.
- Article 46 of the Implementing Regulations prescribes a withholding tax requirement applicable to ‘investment and portfolio managers, fund managers and custodians’ distributing dividends. Such entities are required to withhold and pay the prescribed tax to the tax authorities within thirty days from the date of distribution. Now, ER 20 appears to include an addition namely “incorporated entities/bodies” to the aforesaid entities stated under Article 46.

A Questionable Change in the Tax Landscape?

One could argue that there has been an improper widening of the scope of ER 20 now requiring each Kuwaiti shareholding company (beyond the scope of its capacity as investment and portfolio manager, fund manager or custodian) to withhold/ pay tax whereas Article 46 is silent on such reference.

Such widening of the scope of ER 20 is currently under scrutiny from a legal and financial perspective, particularly due to the uncertainty and lack of clarity on the issues pertaining to the date of issuance of the Executive Rules, their date of applicability and their binding effect vis-à-vis the earlier set of executive rules of 2008.

This ambiguity begs two key questions – (i) whether the Executive Rules should have been published in the Official Gazette of Kuwait (Kuwait Alyoum), and (ii) whether ER 20 improperly widens the scope of Article 46 of the Implementing Regulations. Each of these has been discussed below.

Do the Executive Rules need to be published in the Official Gazette of Kuwait (“Official Gazette”) in order to be valid?

- The Constitution of Kuwait provides that for laws to take effect and to become enforceable in Kuwait, their publication in the Official Gazette is mandatory. All laws must be ratified by Kuwait’s National Assembly and ultimately signed by the Amir of Kuwait.
- Secondary and subordinate legislation must be issued in accordance with the procedures laid down in the relevant piece of primary legislation. Secondary legislation usually takes the form of ministerial decisions or executive orders over their areas of responsibility. Secondary legislation must also be published in the Official Gazette in order to come into force, but is not required to be ratified by the National Assembly or signed off by the Amir.
- The Implementing Regulations provide that any matter not specifically provided in the Implementing Regulations shall be governed by the executive rules and instructions issued by the Minister of Finance or his representative, pursuant to the provisions of the Tax Law.
- One may therefore argue that where there is a specific enabling provision in the Tax Laws pertaining to the issuance of the Executive Rules, and where the Implementing Regulations have been published in the Official Gazette, it appears that the Executive Rules need not be separately published in the Official Gazette for them to be effective and applicable, given that the Minister of Finance has inherent powers to issue the Executive Rules as explained above.

Does ER 20 improperly widen the scope of Article 46 of the Implementing Regulations?

- One can argue that ER 20 does expand the scope of the entities required to withhold/ pay tax given that ER 20 now includes ‘incorporated entities/bodies’ within its purview. As a result, each shareholding company (beyond the scope of its capacity as investment and portfolio manager, fund manager or custodian) declaring dividends is now required to withhold/ pay the prescribed tax.
- Having understood the general objective of issuing the Executive Rules as explained above, where any particular executive rule exceeds its objective and purpose, one could argue that such excess would require a proper amendment to the relevant legislation in order for it to have full legal and binding effect. Such issue could be subject to proper assessment and analysis by an appropriate forum, being either the Tax Challenges Committee (“Committee”) at the Department of Income-Tax (“DIT”) or the competent court, as the case may be.
- A bonafide argument may be made before the relevant forum to the effect that there has been an improper widening of the scope of the ER 20. However, given that there is no precedent on this issue so far, it is difficult to determine the interpretation that may be adopted by the Committee or the court whether in relation to the supposed widening of the scope of Article 46 or in relation to the proper mechanism for issuance/ dissemination of the Executive Rules.

Conclusion

We believe that the intended implementation of ER 20 by all incorporated entities/bodies (which would include Kuwaiti shareholding companies as well) would be a tedious exercise and any of these entities may be inclined to challenge ER 20 before an appropriate forum or may elect not to adopt such implementation. Given that there is no legal precedent on this issue so far, it is difficult to anticipate the outcome of such challenge proceedings.