ATB & PARTNERS LAW FIRM

Foreign Investment Insight

KUWAIT INVESTMENT & JOINT VENTURE FORUM
29-10-2014

Introduction

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- Strategic Factors of the Kuwaiti Market
- Recent regulatory reform to liberalize the market
- KDIPA & Law no 116/2013
- Market entry considerations and concerns
- Appendix 1 :Forms of Foreign Partnerships

This brief will be addressing the initiatives that have been taken by the Kuwaiti government recently to liberalize the Kuwaiti market to foreign investors and increase its competitiveness, In addition it will cover the Key challenges and concerns a foreign investor should take into consideration prior to initial market penetration.

A key element that plays a role in the success of Foreign Kuwaiti partnership is the historical entrepreneurial nature of Kuwaitis. Kuwait is home to some of the leading businesses in the region in sectors such as telecom, retail, logistics, financial services, aviation, construction designing, animation, art etc, demonstrating the strong business acumen and commercial mindset of Kuwaiti businessmen in establishing and growing scalable businesses.

This has resulted in the creation of deep-rooted relationships between foreign and local entities spanning for several decades and making these local partners a pivotal part of this larger foreign business entity. This is fairly evident in commercial agencies which are the most common form of foreign partnerships in Kuwait.

Main factors that play a role in making the Kuwaiti Market an attractive market to foreign investors

- The Substantial government resources and record high surpluses in government budget from oil exports.
- Significant infrastructure development as Kuwait is promoting unprecedented levels of infrastructure development activity aimed at realizing its long term vision of diversifying the economy and transforming Kuwait into one of the leading hubs for financial trade and logistics in the region.
- Kuwait is cost competitive in terms of power, water, land and labour. Power tariffs are subsidized by up to 86% by the Government.
- It has one of the highest GDP with a diverse community.
- ranked as the world’s 6th most attractive tax regime with benefits including no personal income tax, low corporate tax for foreign companies (15%), limited restrictions on imports and exports, unrestricted movement of funds, including repatriation, a strong and stable currency supported by an independent monetary policy.
- Increasing the involvement of the private sector has been a key priority for the Government under its diversification program. The Government’s initiatives such as the PPP program, privatization law and opening of 14 key sectors for 100% foreign investment are aimed at increasing the share of private sector in GDP

Regulatory reforms aimed at liberalizing the Market

In the last few years, government has stepped up efforts to liberalize the economy and attract foreign investments. Robust policies and regulatory reforms have been enacted to boost the competitiveness of the Kuwaiti Market.

- **Privatization**: Law 37 of 2010, defines a broad framework for the privatisation of public enterprises. Projects need to be first selected by the Supreme Council for Privatization (SCP), after which an approval needs to be sought from the Council of Ministers prior to proceeding with the privatisation. Private sector participation may also include foreign investors who, once approved by the SCP, may bid for shares in the project company being established to own the privatized entities.
- **PPP** is now regulated by Law No. 7 of 2008 regarding (BOT) Operations and Similar Operations which amends parts of Law 105/1980 and is aimed at encouraging approved foreign as well as local investors to invest in the growth and infrastructural development of the State through partnership projects with the public sector.
- **Labour Law:** Reforms have also included the private sector labour law on the enactment of Labour law No. 6/2010 easing up the transformation of the work sponsorship for foreign workers from an employee to another , promoting gender equality and providing better work condition to the employees.
- **Taxation:** Kuwait Taxation law was amended to boost foreign direct investment in the country in 2008, prior to which a tax rate of up to 55% has been amended to a flat tax rate of 15% on net income. The flat tax rate resulted in significant decrease of tax liability of foreign entities.
- **Protection of Competition:** The adoption of Law No. 10 of 2007 (as amended by law No. 2/2012) regulating The protection of competition "Anti Trust" aimed to regulate unfair and illegal competition and tackle monopolies in commercial transactions and trades. The law has appointed an Independent Protection of Competition Authority under the Council of Ministries to regulate competition and oversee the market for any harmful activities to competition; the law has further adopted criminal penalties for unlawful acts impairing competition.

The establishment of Kuwait Direct Investment Promotion Authority (KDIPA) and law no 116/2013

- The most important reform that expresses the government commitment towards its long-term goal of liberalizing the market and increasing its competitiveness is the adoption of regulations that allow for a 100% foreign ownership in local business.

- Major initiatives have been taken by Kuwait government in the past to promote foreign Investments and it has been taken through stages. previous to 2001 The basic laws regulating conducting business in Kuwait did not allow non-Kuwaitis to engage in commercial activities without a Kuwaiti partner whose equity holding should not be less than 51 per cent or through a local agent or distributor.
- Later on an exception came to this general rule by the issuance of law No 8/2001 which has permitted foreign investors to establish Kuwaiti companies holding stakes in them reaching up to 100% foreign equity.
- But this law did not serve in achieving the goal that was required and very limited licenses have been actually granted to allowing over 50% foreign ownership. Most of these licenses were to foreign bank branches HSBC, BNP Paribas.
- This lead the government to adopt act no. 116 /2013 regarding the promotion of foreign direct investment, Following are the highlighted key points of the Law:
  - The law established a new **independent public authority (KDIPA)** directed on promoting direct investment by both foreign and local investors by streamlining the investment environment to improve Kuwait position in competitiveness and doing business in international indices, licensing direct investment with set criteria, promoting investments into Kuwait and raising awareness.
  - The **adoption of the NEGATIVE LIST** APPROACH the Council of ministries under the new law are required to determine the list of direct investments excluded from the scope of the New Law in light of its developmental and economic plans and the State's general policy.
  - **Forms of foreign investment** subject to the act, may be:
    - A Kuwaiti company under the new law with up to 100% foreign ownership.
    - A licenced branch of the foreign company.
    - A representative office to exclusively conduct marketing studies without engaging in commercial activities.
  - **Shorten duration for licensing procedures** a decision on the merit of the application shall be rendered within a maximum duration of 30 days.
  - **Incentive by the law for investors**, include:
    - **Tax holidays** for up to 10 years on income tax and custom exemption for the importation of machinery.

    - Allowing the **employment of foreign labour** in according with established principles and restriction.
    - The **allocation of land and real-estate** for the investor.
    - Benefiting from all **international convention** in force related to investment and avoiding double taxation.
- **The law further provides investors with guarantees which include:**
    - Investment protected against nationalization or expropriation unless for public interest and in return of a fair and timely compensation.
    - Freedom to transfer capital and earnings abroad.
    - Right to transfer or merge ownership of the project to local or foreign buyers
    - The right to confidentiality in respect of technical, economic, and financial information relevant to the project and imposed imprisonment penalties reaching up to a year for officials that disclose such information.
- **The new law introduces a list of criteria upon which the value, type and duration of the incentive and exemption granted will be determined when considering applications**
    - The extent of transfer and settlement of technology and modern management methods, advanced technical and marketing experience into the state of Kuwait.
    - The amount and quality of the products and service offered.
    - The need of the local and gulf market to this investment and its contribution to economic diversifications.
    - Increase in National Export.
    - Creation of Job opportunities for and training of the national workforce.
    - Contribution to the development of areas that lack similar projects.
    - Positive environmental impact.
    - The extent of Community service and benefit the investor has to offer outside the framework of its financial project.
    - Use of national products.
    - Use of national technical, professional and consulting services.

- **Dispute Resolution**: The law further provides a very solid guarantee allowing foreign investors to request that all disputes arising be settled through arbitration.

No licenses have been issued yet under KADIPA law. The complete implementation of the Law is subject to the issuance of the Executive bylaws which are expected to be issued soon.

Market entry and start up Considerations

Prior to market initial penetration foreign investors shall take into account the following consideration:

1. Mode of entrance:

Choosing the right mode of Entry is crucial to the success of the partnership. Depending on the nature of the project the foreign investor shall decide on whatever form best suites the investment.

The general rule regulating conducting business in Kuwait states that non-Kuwaitis cannot engage in commercial activities without a Kuwaiti partner whose equity holding should not be less than 51 per cent. An exception to this under Law No 116/2013 has been enacted permitting foreign entities to establish Kuwaiti companies with stakes up to 100% foreign equity participation.

The following ways define how a foreign individual or entity may enter the market and carry out business in Kuwait:

1. Establishing a **regular Kuwaiti company** or signing a **joint venture** agreement with foreign ownership of up 49%. Easy to setup and straightforward process.
2. Appointing a Kuwaiti **commercial representative, agent, franchisee or distributor**, this widely used in the F&B sector, sales of consumer goods and services .
3. **Sponsorship and agencies** which are widely used in government infrastructure projects.
4. Applying for license **under Foreign Direct Investment law no. 116 /2013** to establish a foreign fully owned company, branch or representative office.
5. Setting up a **Free Trade Zone** company with up to 100% foreign equity.

Kindly see the chart in appendix 1 for more information on the forms of partnerships and foreign equity

2. Finding the right local partner:

Make no mistakes in finding the right partner. It can be a hard work, however finding the right partner can reduce the time and costs in terms of getting products in to the market.

- A good starting point for identifying potential business partners is Kuwait Chamber of Commerce. It is a vital resource, although companies must be precise about their requirements.

- Conduct due diligence on prospective Kuwaiti associates, as “break up” is often is costly and messy.
- If commercially feasible, start with a short term, nonexclusive agreement with a narrow scope.
- Avoid committing to a “master” or “regional” agreements if you have doubts.
- Secure letters of credit when appropriate

3. TAX:

Kuwait tax rates are among the lowest worldwide. Personal income taxes do not apply on salaries or investment in stock activities.
Foreign investors shall pay 15% income tax on net revenue, a 4% custom tax is payable on imports.

4. Following Regulatory Government Rules:

Foreign investors must pay attention to different government rules related to the business particularly these so called minor rules of the municipality, Ministry of Commerce or Ministry of Labor and Social Affairs, as they might have a significant impact on the business and may cause delays that will result in extra costs. in addition, to the existence of legal restriction in certain fields imposed by the law (such as the ban on scrap metal export or use of asbestos pipes).

Example of minor rules with great impact is that employing staff whom do not hold valid health card may result in hefty penalties and a court order to temporarily suspend the business.

Further, Kuwaiti law does not recognize any unregistered agency agreements. This advice holds good for the foreign business community in Kuwait as well.

5. Labor challenges:

Kuwait is currently trying to balance the need for foreign labor with interests of its local population, and companies are strongly encouraged to hire local nationals wherever possible.

Business in Kuwait must be in compliance with the minimum ratios for employment of Kuwaiti nationals as designated by the Council of Ministers in decree no. 1028 / 2014, which varies depending on the sector (banking 64% , petrochemical and refineries 30%, telecommunication 60%, insurance 18% , Monetary exchange 13% …) .

Kuwait has a stringent visa regime and most work permits require a local sponsor. Visa requirements for citizens of 34 nations, including the United States, were relaxed in 2004 allowing for application for a visa at the airport upon arrival.

Employers are required to contribute towards a health insurance scheme for all its expatriates resident in Kuwait and their dependents also required to make payments to the Public Institution for Social Security on behalf of all its Kuwaiti employees. This scheme is contributory with the employer liable to pay 11% of the employee's monthly salary.

6. General business etiquettes:

Paying attention to general and business Etiquettes leads to a more successful relationship.

In Kuwait, doing business is dependent on building up a lot of trust and developing personal relationships. Therefore, never try to rush business matters, but wait until an atmosphere of trust and friendship has been established.

Also, it may seem that your Kuwaiti counterparts rarely are in any rush. Decisions are often reached slowly, and negotiations require patience. One of the most disrespectful things to do during a business meeting – or any other social event – is to appear to be in a hurry.

7. Dispute Resolution:

Adopting an effective dispute resolution method eases up the breakup and reduces the costs associated, might save both the local and foreign party a great deal of delay and extra costs.

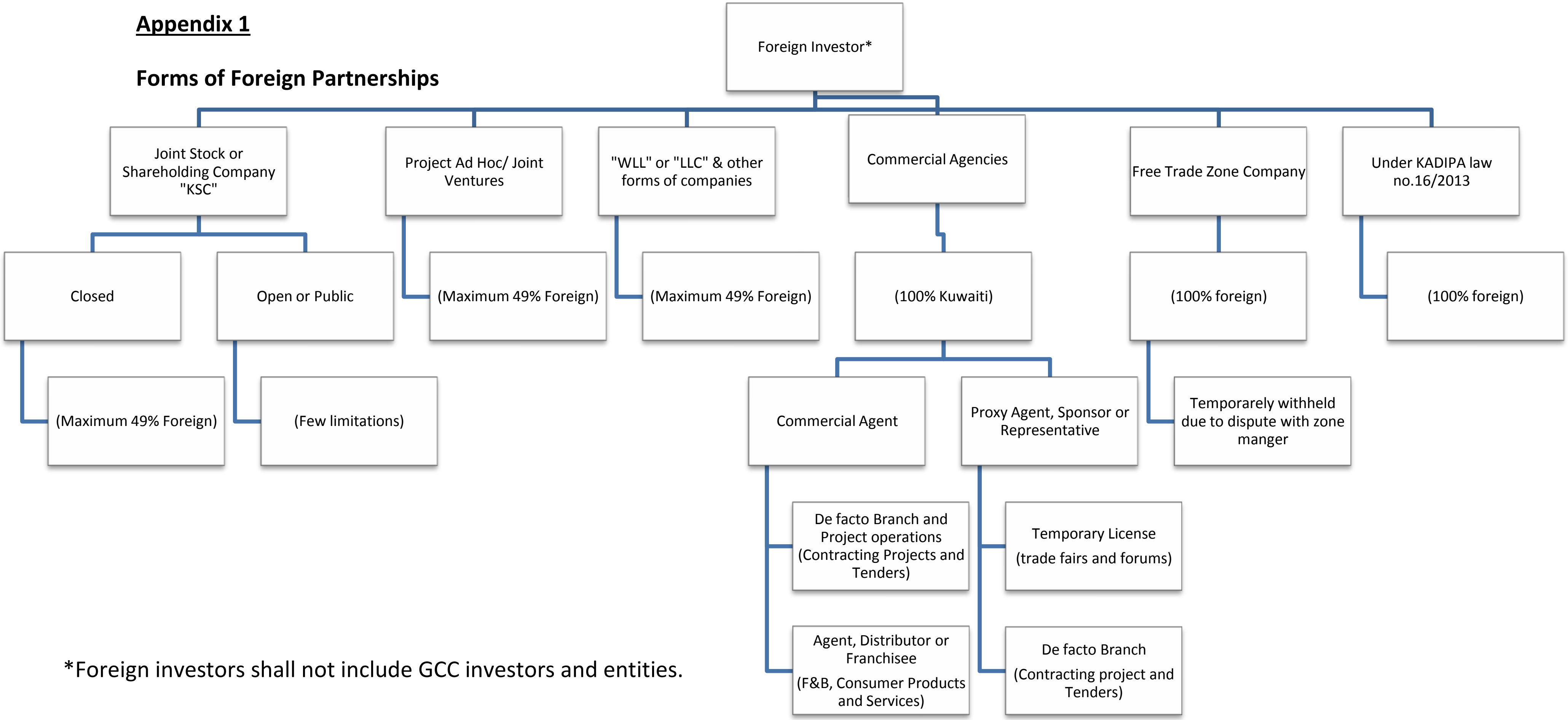
Although Kuwait has a solid and effective legal system this system may be costly and time lengthy at times.

Moreover, the law comes to provide guarantees to the local distributor that may not be favorable to the interest of the foreign entity (such as compensation is due for termination without cause even in case of Agreement expiry).

Hence, Arbitration is always advised in similar methods of partnerships.

Appendix 1

Forms of Foreign Partnerships



*Foreign investors shall not include GCC investors and entities.

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