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Doing business guide  
Understanding Iraq's  
tax position

العراق



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East since

1926



# Market overview

## Country overview

- The economy of Iraq is hugely dependent on its energy sector. 'Oil and Gas Journal' estimates that on January 1, 2015, Iraq held around 144 billion barrels of proved crude oil reserves which represents 18% of the proved reserves in the Middle East.
- Iraqi government aims to increase crude oil production to nine million barrels per day by 2020, as per the Energy Intelligence Group estimates. Currently, the government of Iraq is negotiating the field production targets with international oil companies.
- Economic policy-making in the country is expected to remain a low priority due to the Islamic State (IS) incursion. The main aim of the government will be to continue expanding the oil sector.
- Diversification from oil is expected to be slow due to insecurity and infrastructure challenges in the country.
- On September 8, 2014, a new government was formed in Iraq, following the parliamentary election in April. Fuad Masum was elected as president of the country. He is the second non-Arab president of Iraq, succeeding Jalal Talabani.
- In December 2014, Iraq's central government and the Kurdistan Regional Government (KRG) entered into an agreement to end their dispute over oil exports and budget payments. The deal is expected to allow the Iraqi government to increase its oil exports (Kurds committed to hand over 550,000 bpd of regional oil), and will provide the Kurdish government 17% of Iraq's national budget. Later in January 2015, the deal was incorporated into the National Budget Law of Iraq for 2015.
- Currently, the Iraqi central government has paid only a fraction of the committed budget share to KRG, as the oil exports were not meeting the target level of 550,000 bpd as agreed in the deal (KRG oil exports reached an average of 350,000 bpd in the first week of March). KRG officials are attributing the outages in Turkey and other technical issues at the oilfields for the shortfall.

## Government

<b>Government type</b>	Parliamentary democracy
<b>Chief of state</b>	Fuad Masum – President
<b>Head of government</b>	Haydar al-Abadi – Prime Minister
<b>Legal system</b>	Mixed legal system of civil and Islamic law
<b>Administrative divisions</b>	18 governorates (muhafazat, singular - muhafazah (Arabic); Parezgakan, singular - Parezga (Kurdish) and one region*; Al Anbar; Al Basrah; Al Muthanna; Al Qadisiyah (Ad Diwaniyah); An Najaf; Arbil (Erbil) (Arabic), Hewler (Kurdish); As Sulaymaniyah (Arabic), Slemani (Kurdish); Babil; Baghdad; Dahuk (Arabic), Dihok (Kurdish); Dhi Qar; Diyala; Karbala'; Kirkuk; KRG*; Maysan; Ninawa; Salah ad Din; Wasit)

Source: Central Intelligence Agency Fact book, The Economist Intelligence Unit

## Economy overview

- Iraq is highly dependent on the oil sector. The main oil-producing region in the south is expected to remain secure from insurgents. Economist Intelligence Unit (EIU) forecasts remain relatively conservative, at 5.2m bpd by 2019 due to political instability and inefficient bureaucracy in the country.
- According to the International Monetary Fund (IMF), the Gross Domestic Product (GDP) of the country is expected to contract by 0.5% in 2014 due to the economic effects and IS insurgency. The World Bank forecasts an annual GDP growth of 0.9% in 2015.

\* As a semi-autonomous region in Northern Iraq, the Kurdistan Region has introduced certain laws and practices which differ from the position in Federal Iraq. Throughout this guide, we have provided our comments with respect to Federal Iraq, unless otherwise noted. Where the position in Kurdistan Region differs materially from that in Federal Iraq, we have noted this.

# Industries of opportunity

## Industry overview – Oil and natural gas

According to the U.S. Energy Information Administration (EIA), Iraq has the fifth largest proven crude oil reserves in the world. The energy sector of the country is heavily based on oil. More than 90% (2010 estimate) of the country's needs are met by petroleum. The rest is supplied by natural gas and hydrocarbons.

## Oil

- Despite having large proven oil reserves, Iraq is lagging behind in its production targets. This is mainly due to the country's limited infrastructure (both refining and export capacity) and political disputes.
- According to Iraq's deputy prime minister for energy, capital expenditures of US\$30 billion per year in the country's energy infrastructure are required to meet Iraq's production targets.
- The majority of the oil produced in Iraq comes from Kirkuk, the North Rumaila field in southern Iraq, and the South Rumaila field. Southern fields of the country produce around 75% of the country's crude oil.
- The Ministry of Oil oversees the production and development activities through its operating entities – the North Oil Company (NOC) and the Midland Oil Company (MDOC) in the north and central regions, and the South Oil Company (SOC) and the Missan Oil Company (MOC) in southern regions.
- Production of oil and gas in the northern region is controlled by the KRG.

## Planned new refineries in Iraq

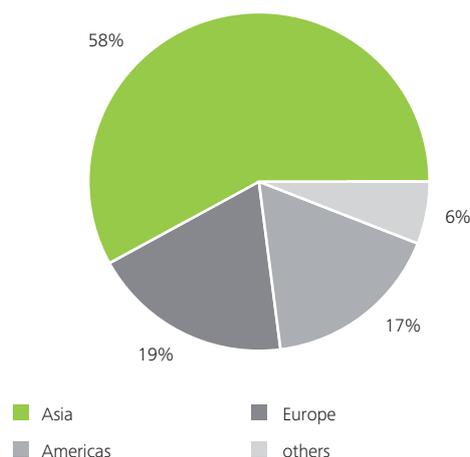
Refinery	Nameplate capacity (bbl/d)	Investment (US\$ billion)	Front end engineering contract
Nassiriya	300,000	9	Foster Wheeler
Kirkuk	150,000	5.5	Shaw Group
Missan	150,000	5	Shaw Group
Karbala	140,000	5	Technip

Total **740,000 bbl/d**

Source: Middle East Economic Survey, FACTS Global Energy

- Iraq exported 2.6 million bbl/d of crude oil in 2014, around 0.2 million bbl/d higher over 2013.
- The majority of Iraq's oil exports goes to Asia, followed by Europe and the Americas.

## Iraq's crude oil exports, 2014



Source: Lloyd's Intelligence List (APEX tanker data)

## Natural gas

- As of January 2015, Iraq had total proved natural gas reserves of around 112 trillion cubic feet, 12<sup>th</sup> largest proven natural gas reserves in the world (Oil & Gas Journal).
- Around 75% of the country's natural gas resources are associated with oil, located in southern Iraq. Most of the non-associated reserves of the country are concentrated in various fields in the north which includes Ajil, Bai Hassan, Jambur, Chemchemal, Kor Mor, Khashem al-Ahmar, and al-Mansuriyah.
- Iraq reported a gross natural gas production of 724 billion cubic feet (Bcf) in 2012, out of which around 58% of the gas produced was vented and flared.
- While some portion of the natural gas is used as fuel for power generation and for reinjection to increase oil recovery, the majority of Iraqi natural gas production is flared.
- To reduce flaring, South Gas Company (state-owned entity) signed an agreement with Royal Dutch Shell and Mitsubishi and began operations in May 2013 under a limited liability company named Basrah Gas Company which is a consortium of the three entities (South Gas Company 51%, Shell 44% and Mitsubishi 5%). The 25-year agreement is estimated to cost around US\$17 billion which includes upgrading current facilities and establishing new facilities to expand gas processing capacity.

## Doing business in Iraq

### Iraq's ranking on doing business parameters in 2015



Source: Doing business report Iraq, 2015, World Bank group

Note: A total of 189 economies were considered in the study for rankings

### Indicators for starting a business in Iraq

Indicators	Iraq	MENA	OECD
Procedures (number)	10	8	4.8
Time (days)	29	18.9	9.2
Cost (% of income per capita)	38.2	28.1	3.4
Paid-in minimum capital (% of income per capita)	12.8	45.6	8.8

Source: Doing business report Iraq, 2015, World Bank group

### Procedures for starting a business in Iraq

Number	Procedure	Time to complete (in days)	Associated cost (IQD)
1	Reserve a unique company name at the Baghdad Chamber of Commerce and the Federation of Chambers of Commerce	2	500,000
2	Hire a lawyer to draft articles of association	1	About 1,500,000
3	Deposit the initial capital at a commercial bank and obtain proof thereof	2	5,000–25,000
4*	Obtain the shareholders' tax clearance certificates from the General Commission of Taxation	1 (simultaneous with previous procedure)	1,000 per tax clearance certificate
5	Apply for registration at the Companies Registry	14	250,000–350,000
6	Obtain the registration certificate	1	Included in procedure 4
7	Make a company seal	2	20,000
8	Register for taxes at the General Commission of Taxation	2	450,000
9	Legalize accounting books	2	175,000
10	Register employees for social security	3	20,000

\* Takes place simultaneously with another procedure

Source: Doing business report Iraq 2015, World Bank group

# Entering the market

## Types of legal entity

As a general rule, any non-Iraqi company which is 'carrying on business' in Iraq is required to establish an Iraqi legal presence (e.g. company, branch office). While there is no specific definition of what constitutes 'carrying on business' in Iraq, typically an obligation would arise when the company obtains premises (including rented premises) in Iraq, or retains personnel on a more than temporary basis. Penalties may apply in respect of failure to register the enterprise.

There are a number of forms of business entities in Iraq, however the most common forms of entity for foreign investors are the Limited Liability Company (LLC), and branch of a foreign company. There are currently no restrictions on foreign ownership of an Iraqi LLC. Therefore, a foreign investor can hold 100% of the share capital of an Iraqi LLC under Iraqi Company Law.

It is difficult to predict the time taken to register a legal entity in Iraq, but based on our experience, a time frame of 6 to 12 months would be typical. It is generally faster and more straightforward to register a branch of a foreign company than an LLC in Iraq.

## Permanent establishment

Iraq's Income Tax Law does not recognize the concept of permanent establishment. However, Iraq broadly takes a territorial approach to taxation. In addition, contracts with non-Iraqi residents are also specifically covered by Instructions no.2 of 2008, which broadly set out tests to define whether the non-resident is trading 'with' or trading 'in' Iraq. In summary, trading 'with' Iraq should not result in an Iraq tax liability, whereas trading 'in' Iraq will.

## Trading 'with' versus trading 'in' Iraq

Broadly, a non-resident would be considered to be trading 'in' Iraq when contracts are concluded in Iraq, payments for the services are made into an Iraqi bank account, or services are physically provided in Iraq.

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Critically this may also include cases in which services are provided through a business agent in Iraq, however, there is no clear definition of what the term 'services' includes.

Specifically, it is mentioned in the Instructions that complementary or supplementary works (including erection, supervision, maintenance, engineering duties and other works that are to be implemented in Iraq) whether agreed upon by virtue of a single contract, concluded through several contracts, or included in supply contracts, are treated as trading 'in' Iraq.

A contractor trading 'in' Iraq will need to register a legal entity in Iraq, and also register for tax purposes and obtain a tax clearance from the Iraqi authorities. Information on the contract should be sent to the tax office, in order for the tax office to determine whether the contractor is liable for tax, i.e. whether retention should be made on payments under the contract.

As the Instructions are currently drafted, there is no de minimis time limit for provision of services in Iraq – therefore strictly as little as one day spent working in Iraq should be considered to be trading 'in' Iraq, and therefore give rise to an exposure to tax in Iraq.

# Taxation in Iraq

## Tax administration

The main source of tax law in Iraq is the Federal Income Tax law, Law no. 113 of November 22, 1982, as amended in 2003 (the Federal Income Tax Law). There are no state level or municipal taxes imposed in Iraq.

The tax authority in Federal Iraq is the General Commission for Taxes (GCT). The tax authority in the Kurdistan Region is the Income Tax Directorate (ITD).

The tax year in Iraq is the calendar year. Entities registered in Iraq are required to prepare and submit audited financial statements, which are prepared in Arabic, and in accordance with Iraq Uniform Accounting Standards (UAS), and audited by an Iraqi statutory auditor. The audited UAS financial statements should be submitted to the GCT, together with the corporate income tax return, by May 31 following the year end.

## Taxable income

Taxable income is broadly total income less allowed deductions. Taxable income generally includes all income from whatever source. The Federal Income Tax Law provides that expenses incurred in generating taxable income during a period should be deductible in calculating taxable income.

In practice, it is common for the tax authority to seek to assess an entity for tax on a 'deemed profits' basis when they consider that there is insufficient documentation to support expenses disclosed in the financial statements.

Article 2 of the Federal Income Tax Law broadly defines types of income which are subject to tax in Iraq. According to Article 2, the following types of income are included as taxable:

- Profits from commercial activity or from activity having a commercial nature, vocations and professions, including contracts, undertakings and compensation for non-fulfilment thereof if not for making good a loss sustained by the taxpayer
- Interest, commissions, discounts and profit arising from trading in bonds and securities
- Any other source not exempted by law and not liable to any tax in Iraq

Article 5 provides that "tax shall be imposed on income of the resident Iraqi person which arises inside or outside Iraq, regardless of the place of receipt." 'Person' in this context refers to both natural persons and legal persons (i.e. companies, branches of foreign companies, etc).

Tax is also imposed on the income of a non-resident which arises in Iraq, even if it is not received in Iraq.

## Withholding tax

Iraq has a complex legislative framework with respect to withholding tax and tax retentions. In practice, there are few final withholding taxes, however, specific focus should be given to contracts which fall within the scope of Instructions no. 2 of 2008, concerning contracts with foreign parties, and Instructions no. 5 of 2011, for upstream oil and gas contracts.

## Dividends

In practice, there is no withholding tax on dividends.

## Interest

A tax of 15% applies to payments of interest from an Iraqi LLC or branch to a non-Iraq resident (e.g. the foreign parent company or non-resident bank).

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It is common for the tax authority to seek to assess an entity for tax on a 'deemed profits' basis when they consider that there is insufficient documentation to support expenses disclosed in the financial statements

## Rents and royalties

There is no specific legislation that addresses withholding tax on payments for royalties. However, there are provisions in the tax law which the tax authority could use to argue that such payments should be taxable in Iraq, i.e. if the income is considered to be 'income arising in Iraq.'

To the extent that payments for management fees, technical services, rent, etc. are made by the Iraqi entity to a foreign entity, there is a risk that the tax authorities could argue that such payments are subject to tax in Iraq, on the basis that they relate to 'income arising in Iraq.'

In practice, the tax authorities generally defer to the legislation regarding tax retentions and we note our comments below in this respect.

## Tax retentions

### Instructions no. 2 of 2008 – Contracts between Iraqi and foreign contracting parties

The main provisions regarding tax retentions are set out in Instructions no. 2 of 2008 which require that information relating to contracts with foreign suppliers should be disclosed to the GCT in order for the tax office to determine whether the contractor is liable for tax and to confirm the rate of retention.

Retentions of tax on payments for certain contracts must be made by the payer, at various rates up to a maximum of 10% of the gross payments, depending on the nature of the contract/services performed, plus the whole of the final payment installment.

Tax retentions under Instructions no. 2 of 2008 are not intended to be a 'final' withholding tax. Amounts retained on installment payments should be transferred to the tax authority (although no specific time frame is defined within which retentions on installment payments should be paid over to the tax authority). In addition, according to Instructions no. 2 of 2008, the whole of the final installment payment should be retained from the contractor, unless the contractor is able to obtain written approval, or a tax clearance, from

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## Subcontractors to whom the Oil and Gas Tax Law applies should be subject to retentions of tax on their contract payments at a rate of 7% of the gross amounts for petroleum contracts and at a rate of 3.3% for non-petroleum contracts

the tax authority. Tax clearance can strictly only be awarded once the supplier has completed their tax filing obligations and settled any due taxes in Iraq. If no tax clearance is obtained within 90 or 180 days from the end of the contract (depending on the type of contract), then the amounts retained should strictly be transferred to the tax authority, in accordance with the Instructions.

### Instructions no. 5 of 2011 – Oil and gas contracts

Instructions no. 5 of 2011 provide that subcontractors to whom the Oil and Gas Tax Law applies should be subject to retentions of tax on their contract payments at a rate of 7% of the gross amounts for petroleum contracts and at a rate of 3.3% for non-petroleum contracts.

The Instructions provide that the entity making the payment should remit the retained amounts to the tax authority within 30 days of making the payment, with the amounts to be held by the tax authority to be reconciled with the contractor's final tax calculation. In addition, the whole of the final installment payment should be withheld from the contractor until the contractor has completed the corporate tax filing and has obtained a tax clearance.

### Free zones/neutral zones

The General Authority for Free Zones (GAFZ) was established to manage the free zones in Iraq, and this authority sits within the Ministry of Finance.

Decree no. 170 for year 1998 was issued on October 19, 1998, to exempt investment projects which are conducted within the free zones, and the capital invested in the free zones, from income tax and stamp duty. According to the Decree:

- Investment projects in the free zones and the capital invested in them along with the profits and annual interest will be exempted from income tax and stamp duty or other duties including the national tax payment.
- Import and export activities for the free zones area are exempted from import and export restrictions, in addition to what is exported from these areas for Iraqi internal use.
- Non Iraqi employees' income in the free zone is exempt from income tax.
- 50% of the Iraqi employees' income in the free zone is exempt from income tax.

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## Following registration of the LLC or branch of a foreign company in Iraq, the entity is required to register with the GCT in Federal Iraq for corporate tax purposes

### Tax treaties

Iraq has not entered into any material tax treaties with other jurisdictions. There is a treaty of the Arab Economic Union Council, of which Iraq is a signatory; however we do not see this applied widely in practice.

### Corporate taxation

#### Registration

Following registration of the LLC or branch of a foreign company in Iraq, the entity is required to register with the GCT in Federal Iraq for corporate tax purposes.

For the Kurdistan Region, registration is typically completed for corporate tax at the time of making the first corporate tax filing. i.e. the Kurdish entity will be required to make its first filing for corporate taxes by June 30 following the year end and it is typical to complete the registration with the tax authority (for all taxes) at that time.

#### Filing and payment

The tax year in Iraq is the calendar year. The corporate tax return must be filed by May 31 following the end of the year, with payment due following the tax authority's assessment of the tax return.

The filing deadline for corporate income taxes in the Kurdistan Region is May 31, however a one month extension to June 30 is granted to all taxpayers.

#### Rates

Under the Federal Income Tax Law, the headline corporate income tax rate is a flat rate of 15%.

A separate tax law was passed in March 2010, Law no. 19 of 2010 (the Oil and Gas Tax Law), which applies to upstream oil and gas companies and supporting industries, operating in Federal Iraq. The Oil and Gas Tax Law provides for an increased corporate income tax rate of 35% on contracts concluded with foreign oil companies and their subcontractors operating in Iraq in the field of oil and gas production and associated industries.

At the time of writing, it is not expected that the Oil and Gas Tax Law will be enforced in the Kurdistan Region of Iraq, however this position should be monitored closely.

#### Personal taxation

In Federal Iraq, personal income tax applies on employees' salaries at the following rates:

- Up to IQD250,000: 3%
- IQD250,001–500,000: 5%
- IQD500,001–1,000,000: 10%
- More than IQD1,000,000: 15%

Personal income tax is applicable for both Iraqi tax residents, and non-Iraqi tax residents who have Iraq-sourced income. Personal income tax is broadly levied on all employees' income, including basic salary and allowances which are paid in addition to basic salary. Iraq's tax legislation sets out certain exemptions/ deductions which are available in calculating taxable income.

The Kurdistan Region tax authority has issued a circular which provides that all employees should be subject to a personal income tax at a rate of 5% on any income which exceeds IQD1 million. The Kurdistan tax authority generally levies income taxes on basic salary only. Allowances paid in addition to the basic salary are not typically subject to tax.

Social security applies to employees' salaries at the rates of 5% for the employee contribution, and 12 or 25% for the employer contribution. It is possible to apply for a formal exemption from social security for expatriate individuals who are working in Iraq.

#### Visas/Work permits/Labor laws

Foreign individuals working in Iraq are required to obtain a visa and work permit. The visa requirements in Iraq are subject to change and therefore it is recommended to obtain specific legal/immigration advice in this respect.

#### Indirect taxes (Customs and excise, VAT, environmental taxes, etc.)

##### Value added tax

Iraq levies sales taxes on certain consumer products, including 5 star hotels, phone cards, tobacco and alcoholic beverages.

##### Stamp duty

Stamp Duty Law no. 71 of 2012 provides that the signing of contracts should be subject to stamp duty at a rate of 0.2%.

In practice, the payment of stamp duty is not common for contracts between private parties, where the contract is not intended to be presented to a court or

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## In practice, the payment of stamp duty is not common for contracts between private parties, where the contract is not intended to be presented to a court or official office

official office. In such instances, the parties will not pay the stamp duty at the time of signing the contract, but only if it becomes necessary at a later date to either present the document to a court or an official office.

Conversely, for contracts to which a government is a party, stamp duty will typically be paid at signing unless an exemption is relevant.

#### Customs duty

The customs regime in Iraq can be challenging, and at the time of writing, has been undergoing a degree of transformation.

#### Background

After the regime change in Iraq in 2003, the Coalition Provisional Authority was set up. This authority suspended the operation of the Iraqi customs tariff, which was replaced with a flat rate import duty known as the Reconstruction Levy (RL), at a rate of 5%, with limited exemptions.

Even after the handover of power to the Iraqi government, the RL remained in place, although several attempts were made in the last few years to replace it with a conventional customs tariff. Initially, these attempts were not successful.

#### A difficult transition period

Eventually, on January 2, 2014, the new tariff was implemented, but not in its entirety. The lack of



widespread notification of the introduction, the fact that previously announced introductions had not materialized, and an absence of clear guidance to businesses and to customs and port officials, resulted in increased delays in customs clearance in some of the Iraqi ports of entry.

The situation was made increasingly difficult by two other aspects:

1. The implementation of the new tariff was on a phased basis (over 100 tariff codes became subject to the new customs tariff upon implementation on January 2, with the remainder still subject to the 5% flat rate until the next phase is implemented).
2. The initial reticence of the autonomous Kurdistan Region to follow the federal government's lead

meant that imports to the Kurdistan Region of Iraq were initially subject to only the 5% RL, which naturally posed something of an anomaly.

It is understood that phase one of the new customs tariff was eventually implemented in the Kurdistan Region, just over a month behind schedule on February 6, 2014.

Accordingly, phase one of the new Iraqi customs tariff should be implemented across Iraq at this time, but the timescales for further phases of implementation are not clear.

#### Other taxes

None, other than those noted above.

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DME launched an International Tax Services Center for Excellence in Dubai in 2009. The Center offers clients and investors in the region services which include structuring groups with inbound and outbound investments within the Middle East and North Africa. The Center leads some of our largest global tax engagements.

DME's practice has been awarded a Tier One ranking in tax services for five consecutive years by the International Tax Review's World Tax Awards. Top tier rankings are provided to firms that have "an international network and leading reputation" which is "reflected in the size and quality of transactions" in the relevant jurisdiction. (International Tax Review)

Deloitte has legal entities registered in Baghdad, Federal Iraq and Erbil, and Kurdistan Region, with dedicated resources on the ground, available to meet with clients locally and to liaise with regulatory and tax authority personnel as required. Our tax practice is centrally headquartered in Dubai, with dedicated tax professionals available to travel as required to meet with clients in Iraq and the wider Middle East region.

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## DME's practice has been awarded a Tier One ranking in tax services for five consecutive years by the International Tax Review's World Tax Awards

### Using our expertise to add value and reduce risk

We understand the risks and challenges that your business faces in Iraq and our team possesses the experience that you require. We have a deep understanding of the Iraqi accounting and tax compliance process and we manage accounting and audit, corporate income tax, withholding tax, employment tax and social security compliance for some of the world's largest companies operating in Iraq.

### Knowledge and value

Statistically, Iraq ranks as one of the most difficult countries in which to complete tax filings. Due to the lack of developed systems and infrastructure in Iraq (including online filing and payment), the tax compliance process in Iraq is inherently more challenging than in many of the other jurisdictions in which we operate. Our team has extensive working knowledge of the Iraqi investment and regulatory climate, and accordingly will be well placed to provide support with regards to corporate income tax, employment tax and social security filing obligations, and to create lasting value as your business develops its operations in Iraq.

**Want to do business in Iraq?**

**We are here to help.**

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We welcome the opportunity to discuss your needs further and provide you with a better understanding of the issues discussed in this material. Please do not hesitate to contact one of our specialists.

The 'Doing business guide' series are supplemented by the [Middle East Tax Handbook](#), which provides a summary of basic tax information on a country-by-country snapshot.



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Deloitte is among the region's leading professional services firms, providing audit, tax, consulting, and financial advisory services through 26 offices in 15 countries with around 3,000 partners, directors and staff. It is a Tier 1 Tax advisor in the GCC region since 2010 (according to the International Tax Review World Tax Rankings). It has received numerous awards in the last few years which include Best Employer in the Middle East, best consulting firm, and the Middle East Training & Development Excellence Award by the Institute of Chartered Accountants in England and Wales (ICAEW).