

# Tax alert

## Circular on Economic Substance Requirements in the Kingdom of Bahrain

13 January 2020

Pursuant to the issuance of the Ministerial Order No. 106 (“MO 106”) on 23 December 2018, the Ministry of Industry, Commerce and Tourism (“MOICT”) has recently issued a circular to all entities registered in Bahrain regarding compliance with the Economic Substance (“ES”) requirements. Entities that carry on one or more “relevant activities” are required to submit an ES Return within 3 months from the end of the fiscal year. Entities that fail to comply will be subject to the sanctions mentioned in MO 106 which include suspension of CR, trader strike off, fines, and referral to Public Prosecution.

In conjunction with the circular, the MOICT has also issued the [ES Guidelines](#) which serve as a preliminary guide to relevant entities on the scope and application of the ES requirements in Bahrain. Some of the key takeaways are summarized as follows:

- A domestic entity, which has no overseas activities, is not a relevant entity for the purpose of the ES requirements, and therefore is not required to satisfy the ES tests. However, it will still be required to notify MOICT (although not mentioned but we believe through Sijilat). A domestic entity has been defined as an entity that is doing business only in Bahrain, is not part of an Multinational Enterprise (“MNE”) group, and/or only transacts with residents / Bahrain customers.
- The MO 106 requires all registered entities who are conducting any of the “relevant activities” to file the ES Return on an annual basis with the MOICT. The Return is submitted through the MOICT’s Sijilat system either by the company itself or its agent, i.e. auditor or professional body. As mentioned above, each relevant entity must report the required information under the substance framework on an annual basis within three months after the last day of the end of each fiscal period.
- It is confirmed that a pure equity holding company (i.e. a holding company that undertakes no relevant activity other than holding equity participations in other entities and earning passive income such as dividends and capital gains) is subject to reduced ES tests.
- An interesting point that significantly distinguishes Bahrain’s ES from the Organization for Economic Cooperation and Development (“OECD”)’s ES framework is the leasing activity. Under the OECD’s recommended ES framework, leasing activity pertains to financial leasing such as hire purchase. The ES Guidelines have defined leasing activity as a rental agreement between two parties – lessor and lessee. This does not appear to only be limited to rental or lease of moveable assets but may also include rental of immovable properties.
- The term “adequate” has not been specifically defined but the ordinary meaning of the term is being referred. The dictionary definition of “adequate” is: “Enough or satisfactory for a particular purpose”. The onus is on the company to ensure that it maintains and retains appropriate records to demonstrate the adequacy of the resources utilized and expenditure incurred.
- The ES Guidelines have also set out a sample format of the ES Return. It is interesting to note that one of the pieces of information to be furnished is details of any MNE Group in respect of which the relevant entity is a Constituent Entity. This could imply that the Country-by-Country (“CbC”) Reporting may be implemented in due time. In fact, it has defined MNE as Groups with a total consolidated revenue of at least EUR750 million which is the OECD’s CbC Reporting threshold.

For more information, please [contact us](#).

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