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Taxing Remittances: Consequences for Migrant Labour Populations in the GCC Countries

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Abstract: As the world's oil and gas prices decline, taxation of foreign workers' remittances has increasingly become a potentially viable solution to address government budget deficits in the Gulf Cooperation Council (GCC) states. With growing unemployment rates and labour shortages among local populations, the GCC governments have recently proposed legislative and, in some cases already introduced, economic measures to tax foreign workers' remittances. Newly proposed tax measures on remittance outflows are often rationalised as critical stop-gap solutions to mitigate high government budget deficits and share costs in accessing state-subsidized public infrastructure and services. Yet, several GCC governments face a complex policy dilemma between balancing budget deficits and addressing high labour shortages and incentives in local labour markets. Thus, the key policy question is: how can GCC governments manage this emerging policy dilemma within their borders? This policy brief examines not only the recently suggested policy responses of various GCC governments but also their long-term potential implications on national labour markets and migrants and their families both in the destination and origin countries.

Keywords: Bahrain; Kuwait; Oman; Qatar; Saudi Arabia; United Arab Emirates; Foreign Labour; Remittances; Policy; Taxation

Introduction

"If a fee on remittances is imposed, I think it should be relevant to the sum set. It will be cruel to low income workers here [if they face a] 5 percent on their remittances. Most of them have taken huge loans to make it to Kuwait. Why would anyone just give 5 percent to the government?" (A reader quoted in *Arab Times,* June 25, 2015).[1]

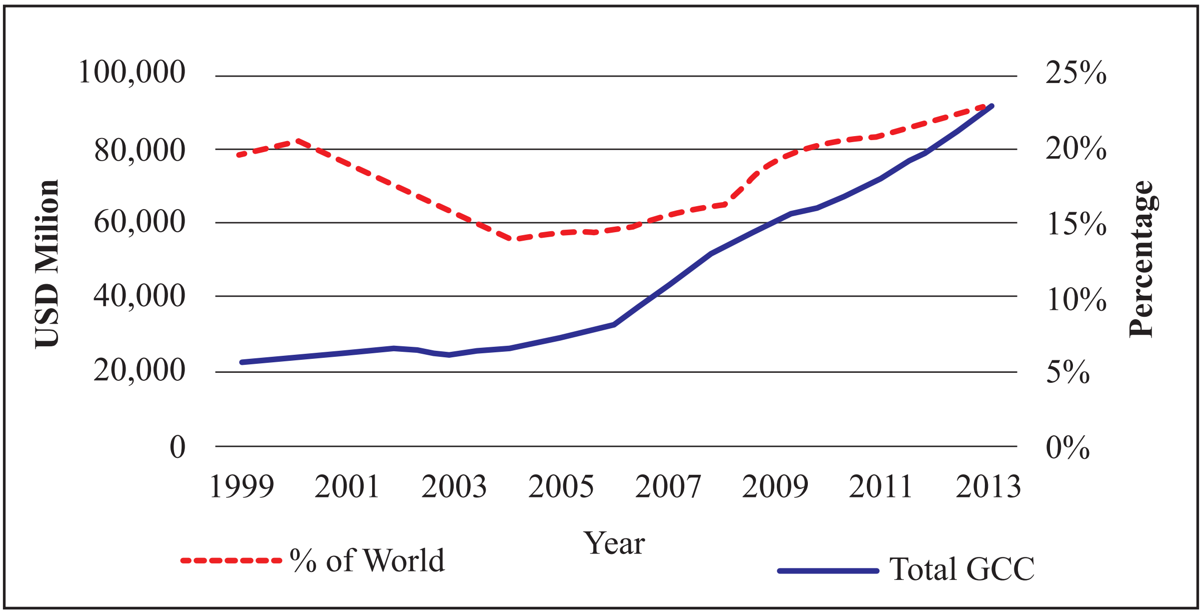
The Gulf Cooperation Council (GCC) countries form one of the world's wealthiest regional blocs both in energy and natural resources such as oil and gas, controlling at least 48.5 per cent of proven oil and gas reserves.[2] With not less than 85 per cent of GCC government revenues derived from oil and gas revenues, the region is heavily dependent on oil economically and has been deeply vulnerable to global oil and gas price fluctuations.[3] The IMF recently warned that GCC government policymakers "need to prepare for sustained period of lower oil prices and reassess their medium-term spending plans accordingly, … while simultaneously address[ing] fiscal vulnerabilities from rapidly eroding buffers and high break-even oil prices… for future generations."[4] Therefore, the GCC countries are not only expected to face short-term economic shocks, but they also need to develop stronger regulatory and governance frameworks, such as taxation systems, to control government budget deficits in the long run.

As labour migration inflows intensified over the past decade, the GCC countries became increasingly concerned about the growing remittance outflows, mostly to the origin countries. In the GCC countries, remittance outflows are seen as leakages of money that could be otherwise circulated and invested in the domestic economy. Therefore, large remittance outflows prompted the GCC governments to seriously consider introducing taxes on money transfers. In fact, only one existing empirical evidence suggests that remittance outflows can actually be beneficial to local economies due to their ability to "exert deflationary pressures on inflation in GCC countries."[5] The lack of a comprehensive assessment of the potential consequences of taxation of remittance outflows from the GCC countries necessitates this policy brief.

This paper examines the GCC governments' recently suggested taxation policies relating to remittances by foreign workers and their potential impact on destination and origin countries' economies. It also briefly examines the size of remittance outflows from the Gulf region and the current situation of budget deficits. Besides, it highlights some of the governments' existing and proposed policies to incorporate remittance tax. The paper also examines policy challenges, the reasoning for the proposed policies and actions, and their implications for foreign workers and origin country governments. The concluding section explores the feasibility of implementing remittance tax policies on foreign workers in the GCC region. The paper, however, will only focus on the potential effects of taxation on the national labour markets, mainly among foreign labour populations, while excluding its unintended consequences on firms' behaviour in the long run.

Remittance outflows from the GCC countries

Figure 1: Remittance outflows from GCC



The GCC countries are critical sources of global remittances, circulating billions of remittances mostly to Asian economies. Approximately 23 percent of the world's $400 billion official remittances in 2013 came from the GCC region, totaling nearly $90 billion and making it the top remitter in the world (see Figure 1).[6] The Kingdom of Saudi Arabia, ranked first in the region with the highest remittance outflows of $34 billion, followed by the United Arab Emirates (UAE) with $18 billion, Kuwait ($15.2 billion), Qatar ($11.3 billion), Oman ($9.1 billion), and Bahrain ($2.2 billion). With the third largest recipient stock of international labour migrants, the GCC countries host at least 18 million migrants (excluding illegal workers), largely from India, Bangladesh, Pakistan, Philippines, Sri Lanka, Egypt, Jordan, and Yemen. Furthermore, temporary labour migrant populations have significantly increased over the past few years due to the massive recruitment needed for the upcoming major events and projects in the region (Dubai Expo 2020; 2022 World Cup in Qatar and the GCC railroad project just to name a few). However, due to recent economic slowdown due low oil prices, it is not unreasonable to expect delays or even cancellations for some of the current and future infrastructure project in the region. That said, temporary labour migration may slow down, but is expected to increase once national economies recover.[7] With a higher number of foreign workers, remittance outflows are also expected to rise. In the UAE alone, for instance, money exchange companies' independent study estimates that at least 80 percent of low-income workers remit most of their monthly income, averaging around Dh1,200 (or $326).[8] This particular case of remittance outflow has not only influenced the UAE and other GCC governments to propose a remittance tax policy, but also triggered them to frame remittance as a form of long-term investment reserve that could contribute to domestic economic growth and development.

GCC Governments' Budget Deficits

With oil and gas prices becoming more volatile in the global market, GCC economies and revenues are slowly feeling the impact, prompting some to propose new taxation legislations, including taxation on remittances and value added taxes, to address serious budget deficits. The Saudi government, for instance, is facing a $38.6 billion budget deficit and has recently withdrawn $70 billion from their sovereign wealth funds' external managers.[9] In Oman, 70 per cent of government revenues mainly originated from oil revenues.[10] In fact, the heavy reliance of Oman on oil, combined with its smaller stock of oil reserves relative to other GCC countries and low non-oil exports, makes it even more vulnerable to oil price shocks. A member of Oman's Majlis Al Shura said, "Let's tighten our belts and prepare together for the coming challenges. The honeymoon is over!" This highlights the recent economic vulnerability of the Omani government and the urgent need to diversify the current source of revenues.[11]

Other GCC countries too have identified possible strategic steps to protect their economies and budgets from the instability of gas and oil prices. For instance, Kuwait recently considered issuing a bond to finance its budget deficit of $7.6 billion this year.[12] The UAE, on the other hand, recently removed its fuel subsidy and linked gasoline and diesel prices to global prices to address budget deficits.[13] In other words, government led-actions imply the vulnerability of the GCC countries to external economic shocks, underlining the pressing need to find other economic avenues, such as value added taxes (VAT) and remittance taxes, to retain and redistribute wealth.[14]

Proposed Remittance Taxation Policies among GCC Governments

To address the growing budget deficits, some of the GCC countries are already considering introducing remittance taxation policies. While there are no specific studies on the potential impact of remittance taxation, it is likely that such economic legislative reforms could positively address government deficit issues, but also generate long-term negative impacts on the local labour market and foreign workers, specifically among the low-skilled categories.

Table 1: Proposed legislative reforms by GCC governments

Country	Proposed tax policy	Remittance tax policy	State concerns	Tax percentage %
Oman[15]	Rejected in December 2014	Economic Committee at State Council rejected the Majlis Al Shura's Proposal to tax remittances (December 2014)	Impact on Investments Inconsistent with Oman's agreements with other countries	2%
UAE[16]	Proposed in June 2015	Proposed a remittance tax policy (create a levy fee system) at the Federal National Council	Reduce labour supply and impact on economy; Declining oil revenues trigger the need to retain wealth within the country	N/A
Saudi Arabia[17]	Imposed tax on the earnings of non-Saudi in 2012[18]	Charged Saudi based private sector companies $52 month for every excess non-Saudi	Aim to address unemployment among local Saudis	$52 per month for every excess non-Saudi employee
Kuwait[19]	Recently discussed by government officials (June 2015)	Tax would reduce "high-subsidised" services provided to foreign workers	Highly-subsidised public services need to be reduced by equally sharing the cost with foreign workers	5%
Qatar	No proposals have been made	-----	-----	-----
Bahrain	No proposals have been made	-----	------	------

While there are clear plans to impose a tax on remittance outflows by most GCC countries, there are still serious concerns among policy makers and government officials in the region. For instance, the economic and financial committee at the State Council of Oman recently rejected the Majlis Al Shura's proposed 2 per cent tax on remittances, contending that although enacting such a tax policy would generate at least $161 million revenues annually, this would also significantly impact current investments.[20]

On the other hand, the UAE government has been discussing the possibility of imposing taxes on foreign workers' remittances since long. A government official proposed a remittance tax in June 2015 to the Federal National Council.[21] The official recommended a levy system be imposed on workers to generate additional government revenues, acknowledging that "the Federal National Council and the Ministry of Finance should produce a package of creative measures to bolster the country's revenues, including a tax on remittance of the billions of dirhams which foreign workers send back to their home countries every year."[22] With the declining oil prices and revenues, combined with the UAE government's proactive introduction of various deregulation measures on petrol prices and potentially a VAT tax, the UAE government may likely consider implementing such a remittance tax policy to further retain wealth within the country.

The Kuwaiti government recently initiated a discussion on the possibility of adding a 5 percent fee on remittances. A tax on remittance would enable the government to collect $659 million in additional government revenue annually. In addition, the growing public discourse among Kuwaiti officials acknowledges that a remittance tax policy is reasonable because highly subsidised services (i.e., water, gas, oil) are equally extended to both citizens and residents benefitting them.[23]

Unlike the aforementioned GCC countries, the Saudi government has already developed an existing remittance tax policy that is also linked to their nationalisation policy. Under the current scheme, any company that hires more foreign workers than local Saudi workers based on the government-mandated localisation requirement (Saudisation) for employers is required to pay $52 per excess foreign employee per month, a policy which aims to discourage the hiring of foreign workers so as to address high unemployment rates among the Saudi populations. However, critics argue that such a policy presents a key economic constraint for employers, as local Saudi labour force tends to avoid various low-skilled jobs, including, for instance, in the construction sector. Therefore, the indirect remittance tax policy poses a critical challenge for employers due to the weak interest in hiring local Saudis over foreign workers, who tend to be more experienced, cheaper, and flexible.

Meanwhile, the governments of Bahrain and Qatar have not yet fully discussed the possibility of imposing taxes on remittances. While there are no policy reforms on remittance taxation currently, the ongoing changes in the labour market and oil/gas prices could certainly influence these countries to rethink their ongoing approaches to remittance outflows.

Policy Challenges in Adopting Remittance Taxation

Adopting remittance taxation is a critical challenge with complex labour market implications for the GCC governments. A major concern is that a remittance tax would reduce labour supply due to the added costs imposed on foreign workers' earnings. This scenario is extremely worrying due to existing high labour shortages in the local labour market, particularly in Kuwait, Qatar, and the UAE where the foreign workers outnumber, by far, the local labour force. On the other hand, the Kingdom of Saudi Arabia and Oman rely relatively less on foreign workers with the share of foreign workers in the labour force being under the 40 percent mark. Furthermore, the GCC region has significantly benefitted from the unlimited supply of labour in the last few decades, which has enabled them to become prime destinations for non-GCC Arab labour, South Asian labour, and, after the 2008 financial crisis, Western labour.[24] The GCC region not only offers job opportunities and a tax-free setting, but also provides world class infrastructure and facilities in a relatively safe environment. Foreign workers, however, are only temporary workers, since they can neither obtain local citizenship nor own property. Therefore, remitting money back to the home countries for a potential return (or future move to another permanent destination) is imperative. However, imposing a tax on money transfers might also influence the initial relocation decision of foreign workers and, therefore, affect labour supply in the long run. While this particular topic is crucial for future migration studies in the GCC, no study has yet empirically examined the effects of a remittance tax on labour supply.

Table 2: Proposed Remittance Tax by GCC Country

Country	Non-Nationals	% of Population	Proposed Tax	Projected Benefits
Bahrain	683,818	52	n/a	
Kuwait	2,877,678	69	5%	$760 million
Oman	1,825,590	44	2%	$182 million
Qatar	1,456,416	86	n/a	--
Saudi Arabia	10,067,839	33	$52 per month for every excess hired non – Saudi employee	n/a
UAE	7,316,073	89	Not known	--

Note: 1. The statistics on the number of GCC non-nationals and their share of the total population cover the period between 2010 and 2015 as follows: Bahrain and Saudi Arabia (2014); Kuwait and Oman (March 2015), Qatar and the UAE (2010). The data are from the Gulf Labour Markets and Migration (GLMM) online database at http://gulfmigration.eu/ 2. The projected benefits information are based on the 2013 remittance outflows for Kuwait (http://www.arabianbusiness.com/kuwaiti-expats-should-pay-5-remittance-tax-says-mp-596348.html) and Oman (http://www.arabianbusiness.com/oman-rejects-proposal-tax-expats-remittances-576864.html#.VcBL7vOqqko).

Our conjecture is that a tax on remittance outflows from the GCC region will ultimately make the region less attractive (particularly among top senders of remittances), but not enough to severely limit the flow of foreign workers to the GCC countries. One change that could be expected is in remitting behaviour of foreign workers. Assuming that the tax on remittance will be collected at money transfer houses, remitters will now more likely resort to unofficial means of sending money to cut costs. These unofficial channels include but are not limited to family members and friends who are travelling abroad. Remitters would also make use of the existing and active hawala system in the region for cost-efficiency purposes.[25] Such undocumented money transfers will not only raise serious security and policy concerns for the GCC countries but also derail efforts by international organizations and local governments to constructively document and examine remittance effects in the long run.

Second, remittance tax has the capacity to create deeper diplomatic divisions with origin countries. In Oman, for example, the government rejected the proposed tax because imposing fees will pose a problem for its existing international agreements with labour exporting countries. The GCC governments not only recognise the potential impact of a remittance tax on diplomatic relations with labour exporting governments, but also see the impact it could have on foreign workers' country of destination for employment. All other things remaining the same, Qatar and Bahrain may likely become more preferable in the long run due to their no-tax policy on remittances. In that sense, the GCC countries also need to weigh in the competitiveness of their labour markets, not only with the outside world but also within the Gulf region itself.

Despite these particular challenges, external economic factors, including declining oil and gas prices, can have a stronger influence on the decision to adopt remittance taxation as part of a larger bundle of state strategies to deal with budget deficit concerns. Therefore, although adopting remittance taxation poses multiple challenges for GCC governments, the large number of foreign workers and the tremendous size of remittance outflows provide a lucrative opportunity to re-direct some of the money back to the local economy.

On the other hand, labour exporting countries have also passed direct or indirect tax regulations on banks and other financial institutions' remittance transactions. In 2014, the Indian government's Central Board of Excise and Customs (CBEC) passed a circular note mandating that all banks and financial institutions must pay a service tax for the fee or commission levied for facilitating money transfers from abroad. Although such regulations specifically target money exchange corporations, the financial cost is directly passed on migrants, an issue which created an international outcry among Indian migrant communities globally.[26] The Philippine government legally exempted overseas Filipino workers from paying taxes and codified their rights under the Republic Act 10002 and Bureau of Internal Revenue (BIR) R.R. 01-2011 citing their contribution to nation-building and development purposes.[27] These government-led actions signify the growing significance of remittance taxation and its contribution to state revenues for both sending and receiving economies.

Potential Effects on Foreign Workers in the GCC

The proposed taxation on remittances can have varying effects on foreign workers in the GCC region, depending on the nationality, skill levels, and industry affiliations of workers. While most foreign workers will likely be impacted by the proposed tax reforms, low-skilled workers in construction, domestic, and other industries will ultimately be severely affected partly due to their low-income status in the local market. In fact, the proposed taxation on remittances, combined with the indirect taxes imposed (rent, visa costs, recruitment fees) significantly decrease purchasing power ability in the GCC region, therefore impacting the total remittances of low-skilled migrant workers. The impact of a tax on remittances will have different effects depending on occupation levels which, in the Gulf region, are often staffed by workers from the same countries or regions. A tax on remittances could therefore be discriminatory, for instance, for construction workers. In the UAE, for example, domestic and construction workers' remittance and consumption behaviour (as well as their financial coping mechanisms) will likely be more impacted by this proposed reform than high skilled expatriates (who mostly come from Western countries). Therefore, the imposition of tax on remittances could have a racial implication too as low-income migrant workers in low-skilled sectors are mostly from Asian backgrounds, thus reinforcing existing discriminatory labour market practices and second class citizenship issues in the GCC region.

In addition, if the proposed tax reforms are implemented in the GCC countries, the region will become even less attractive to migrant workers in the long run due to a rise in the cost of living. For instance, Shah (2012) argues that the increasing work permit visa costs, recruitment costs, and other related services (health service fees and rents) increase the cost of living in the region, significantly deterring foreign workers' long-term residency as well as their ability to save and remit in the long run. These economic factors may affect their decision to stay longer in the GCC region, but would also enable some Gulf governments to reduce and control the share of low-skilled population in their country. Therefore, low-skilled foreign workers will alter their migration and remittance behaviour by staying and remitting less to their countries of origin. This particular situation may also lead others to potentially seek part-time employment, even though Gulf governments have restrictive part-time laws in certain sectors. Thus, low-income workers will not only potentially resort to the informal work sector, but also could face long-term labour market dissatisfaction and unhappiness.

While the proposed tax reforms are likely to influence the overall economic and social well-being of low-income foreign workers, the possible effects on high-skilled workers may not be fully parallel to those of low-skilled. In fact, foreign workers in the banking, finance, retail, and certain government jobs have the ability (by residency laws) to stay longer in the Gulf allowing them, for instance, to weather bad economic times in their countries of origin. However, some high-skilled expatriates may now opt to return to their countries of origin if both the proposed taxation policies and growing indirect costs (rent, visa costs, and food prices) create critical economic pressures to meet their financial targets. Therefore, the proposed taxation reforms' effects on both high and low-skilled workers will also be dependent on indirect economic costs and overall economic well-being in the countries of origin.

Furthermore, the proposed tax on remittances, combined with the growing cost of living in the region, may also impact consumption patterns. In particular, the taxation sanctions could affect local business institutions, as workers reduce domestic consumption in order to still meet their remittance target and balance their financial needs in the long run. It is therefore crucial that governments find acceptable taxation strategies that balance rising costs of living in the GCC region and address growing government deficits. While there is no one-size-fits-all solution, the GCC governments need to ensure that human capital is retained within their national markets as a key ingredient in future and long-term economic development and competitiveness both at the regional and global levels.

To summarise, the effects of taxing remittance outflows depend on how sensitive the demand and supply of labour is to costs of living changes in the Gulf region. A tax on remittances is essentially a higher cost of living for expatriates in the GCC countries. The more inelastic the supply of labour is (in other words, the less the available number of workers that react to rising costs of living) the more the burden of the tax will fall on the worker. At the same time, if the reaction of the supply of labour to changes in the costs of living is strong (elastic), employers in the Gulf will then carry most, if not all, of the burden of the remittances tax (and less of the burden will fall on the worker). Labour supply's sensitivity depends on several factors including the type of labour. One would expect that low-skilled occupations typically do not respond well to changes in costs of living. So in industries such as construction, most of the burden of the tax on remittances is expected to fall on the worker. In high-skilled occupations where talent is difficult to find, the cost of the tax is expected to be absorbed by the employer in the form of higher salary or better benefits to attract and maintain the needed workers.

The demand for labour also influences the effects of a remittance tax. The more elastic (inelastic) the demand for labour, the less (more) cost for the employer and more (less) burden on the worker. Ultimately, the welfare and distribution effects of a tax on remittance outflows will depend on (1) the readiness of the local labour force to replace foreign workers; (2) the type of jobs demanded; and (3) external factors (factors in countries of origins).

Conclusion: Is Remittance Taxation Viable in the Long Run?

Remittance taxation will continue to be one of the most significant policy debates for both destination and origin countries. In the GCC countries' context, the declining prices of oil and gas will not only shape the GCC countries' taxation policy discourses on remittances, but also will pose complex policy dilemmas between addressing government budget deficits and labour market competitiveness. These particular debates will further affect the welfare and conditions of migrant workers, particularly the low-skilled, as also their decisions to remain in the GCC countries in the long run.

GCC countries like the UAE, Oman, and Kuwait are closer than ever to implementing some form of remittance tax policies that would help balance their budget deficits in the long run. Although no official policies have been passed, current discussions suggest that a remittance tax may be imposed in the context of a wider strategy to control budget deficits. Other policies such as removing the gasoline subsidy and imposing a VAT or other types of indirect taxes have already been implemented in the region. The remittance tax, however, imposes a unique dilemma due to its possible ramifications on local labour markets, security, and diplomatic relations in the long run. Therefore, the GCC governments need to consider what would be an acceptable taxation rate if they were to levy a tax on remittances, not only to avoid or minimise distorting the local labour market, but also to maintain market competitiveness and attractiveness of the region.

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Short Reference: F. Malit, Jr. and G. Naufal, "Taxing Remittances: Consequences for Migrant Labour Populations in the GCC Countries," Explanatory Note No. 1/2016, GLMM, http://gulfmigration.eu.

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