14 December 2017

Global Tax Alert

News from Americas Tax Center

Argentine comprehensive tax reform bill sent to Congress

Executive summary

The Argentine Executive Power has sent a draft tax reform bill to Congress. The bill is expected to be enacted before year-end and would be effective 1 January 2018.

A series of Tax Alerts will examine the main proposed changes for the different taxes and topics. This Tax Alert describes some of the main changes to the corporate income tax and cross-border transaction provisions. For more information on the initial announcement of the tax reform, see EY Global Tax Alert, *Argentine Executive Power proposes tax reform*, dated 11 October 2017.

Detailed discussion

Corporate income tax rate and dividend withholding tax

The bill would decrease the corporate income tax rate from 35% to 30% for fiscal years starting 1 January 2018 to 31 December 2019, and to 25% for fiscal years starting 1 January 2020 and onwards. The bill also would establish dividend withholding tax rates of 7% for profits accrued during fiscal years starting 1 January 2018 to 31 December 2019, and 13% for profits accrued in fiscal years starting 1 January 2020 and onwards. The new withholding rates would apply to distributions made to shareholders qualifying as resident individuals or nonresidents.

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With the combination of the corporate rate and dividend withholding rate on after-tax profit, the tax rate for investors would be similar to the current 35% corporate rate. For fiscal years starting in 2018 and 2019, the combined tax rate would be 34.9%; for fiscal years starting in 2020 and onwards, the combined tax rate would be 34.75%.

Additionally, the bill would repeal the current "equalization tax" (i.e., 35% withholding applicable to dividends distributed in excess of the accumulated taxable income) for income accrued from 1 January 2018.

Thin-capitalization rules

The bill would eliminate the current 2:1 debt-to-equity ratio. It also would establish a new limit for the deduction of interest arising from financial loans. The limit would equal 30% of earnings before interest, taxes, depreciation and amortization (EBITDA) or a certain amount to be determined by the Executive Power, whichever is higher.

If all of the interest was not deducted in a certain year, taxpayers could carry the interest forward for three fiscal years. If certain interest was not deductible in a given year due to the application of the thin-capitalization (thin-cap) rules, it could be carried forward for five fiscal years. "Interest" would include foreign exchange differences.

The bill would exempt Argentina banks and financial trusts, as well as other institutions, from the thin-cap rules. The thin-cap rules also would not apply to situations in which it is proved that the ratio of interest to EBITDA of the Argentine borrower is equal to or lower than the same ratio for its economic group – regarding debt with unrelated lenders – for the same fiscal year.

Permanent establishment

The bill would establish a permanent establishment (PE) definition. The definition generally would follow the definition agreed to in many of Argentina's tax treaties, though it would include some provisions that would need to be reviewed on a case-by-case basis. For example, for a dependent agent PE, the bill would establish that the mere performance of a significant role leading to the conclusion of agreements would trigger a PE (in addition to the usual situations in which the agent has and habitually exercises powers to conclude agreements on behalf of the foreign entity). With regard to independent agents, the bill would stipulate that, if the agent acts totally or mainly on behalf of the foreign entity (or related entities), such agent would not be considered independent.

Tax-havens policy

The bill would make changes to the Argentine tax-haven policy, which up to now has only consisted of a list of "cooperating" jurisdictions for tax transparency purposes. Under the bill, the Executive Power would establish a list of "non-cooperating" jurisdictions, which would include jurisdictions that do not have a TIEA (Tax Information Exchange Agreement) or a Convention for the Avoidance of Double Taxation in force with Argentina. The list also would include jurisdictions that have one of the agreements, but do not effectively exchange information with Argentina.

Additionally, the bill would create a category of low- or no-tax jurisdictions, which would be comprised of countries, territories or tax regimes that establish a maximum corporate income tax rate that is lower than 60% of the Argentine corporate income tax rate. For purposes of this calculation, the Argentine corporate tax rate would be 25%, which is the target rate for year 2020 and onwards.

If the bill is enacted, taxpayers participating in transactions with parties located in "non-cooperating" or low- or no-tax jurisdictions may need to analyze the consequences of those transactions from an Argentine transfer pricing standpoint, as well as consider the special deductibility rules, exclusions from capital gains exemptions, among others.

Transfer pricing

The bill would add rules on analyzing transactions involving the import or export of goods with the participation of a foreign intermediary (which is not the actual importer at destination or exporter at origin, respectively), when at least one of the foreign parties involved (i.e., intermediary, importer or exporter) is a related party. In these cases, the bill would require the foreign intermediary to prove that its remuneration is in line with the risks it assumes, the functions it carries out and the assets involved.

In addition, for exports of goods with known prices and with the intervention of an intermediary (either related, or located in "non-cooperating" or low- or no-tax jurisdictions), the bill would require the Argentine exporter to file the agreements supporting the transactions with AFIP (Federal Tax Authorities). If the agreements are not filed, the Argentine-source income from the export would be determined considering the known prices on the date the goods are loaded into the transportation vehicle (with appropriate comparability adjustments, if applicable).

The bill would allow the issuance of additional regulations to establish the minimum thresholds for sales and transaction amounts at which the transfer pricing compliance obligations would apply. Currently, all transactions must be included in the analysis and reporting.

Nonresident's capital gains tax

The bill would generally retain the 15% capital gains tax rate (calculated on the actual net gain or a presumed net gain equal to 90% of the sale price) on the disposal of shares or securities. The bill would establish an exemption for foreign beneficiaries on the sale of shares that are publicly traded in stock exchanges under the supervision of the Argentine Securities and Exchange Commission (CNV). It also would establish an exemption for interest income and capital gains on the sale of public bonds, negotiable obligations (corporate debt bonds) and share certificates issued abroad that represent shares issued by Argentine companies (i.e., ADRs). The exemptions would only apply if the foreign beneficiaries do not reside and the funds do not arise from "non-cooperating" jurisdictions.

In the case of ADRs, the bill would define "source" by the location of the original issuer of the shares. However, the tax would not be due if an exemption described previously applies.

Regarding transactions on non-publicly traded shares, the bill would make the foreign seller, through a representative appointed in Argentina, the responsible party for paying the tax. Currently, the foreign buyer is the responsible party.

For transactions carried out between September 2013 (when taxation on the sale of shares for nonresidents was introduced) and the date of enforcement of this new law, the bill would require the capital gains to be paid. No tax, however, would be due for stock exchange transactions as long as the tax has not yet been paid and the stock exchange agents have not withheld or collected it due to the fact that there are no regulations that require them to withhold the tax at the moment of carrying out the transactions.

Indirect transfers made by nonresidents

The bill would establish a tax on the indirect transfer of assets located in Argentina. In particular, the tax would be triggered on the sale or transfer by nonresidents of shares or other participations in foreign entities when the following two conditions are met: (i) at least 30% of the value of the foreign entity derives from assets located in Argentina; and (ii) the participation being transferred represents (at the moment of the sale or during the 12 prior months) at least 10% of the equity of the foreign entity.

The applicable rate would generally be 15% (calculated on the actual net gain or a presumed net gain equal to 90% of the sale price), of the proportional value that corresponds to the Argentine assets.

Under the bill, the tax on indirect transfers would only apply to participations in foreign entities acquired after the entry into force of the tax reform.

Implications

Companies doing business and different stakeholders investing in Argentina should consider the potential consequences of the proposed changes and evaluate the effect on their current Argentine operations.

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EYG no. 07087-171Gbl

1508-1600216 NY
ED None

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