

# argentina .

## DATELINE

### ARGENTINE TAX REFORM INCLUDES NEW MINIMUM TAX ON ASSETS

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**A**rgentina's tax reform, which was implemented as of January 1, 1999, is intended to reduce tax-payment avoidance and discourage corporations from taking on excessive debt. In addition, the reform authorizes and encourages the Executive Power (i.e., the Executive branch of the government) to reduce employers' contributions on their employees' retirement regime, therefore anticipating an expansion of the general employment rate. With the implementation of this reform, there will be an estimated fiscal collection of 2.1 billion Argentine pesos, which is equivalent to the expected reductions in employer contributions to the labor system.

The reform has essentially modified some aspects of the VAT (*Impuesto al Valor Agregado* or IVA) and the income tax (*Impuesto a las Ganancias*), and has created new taxes such as the minimum presumed profit tax (*Impuesto a la Ganancia Mínima Presunta*) and the tax on interest paid and financial costs of business indebtedness (*Impuesto a los Intereses Pagados y al Costo Financiero del Endeudamiento Empresarial*). The discussion below provides a general overview of the reforms.



## VAT

The VAT, currently levied at 21%, has been extended to the following:

- Imports of movable goods.
- Telecommunication services rendered by radio stations.
- Insurance services, except for private pension and retirement funds, any kind of life insurance, and affiliation contracts entered with Labor Risk Insurance Companies

vetoed it, but without giving any further explanation. Therefore, the situation remains confusing and could be interpreted as supporting two different positions. On one hand, the prepaid medicine care companies, having already started to apply this tax, contend that the Executive Power veto intended to apply the general rate of 21%. On the other hand, the position supported by Congress is that medical

**Derivatives.** Rights and obligations arising from derivative transactions have become subject to tax. In this regard, rights and obligations arising from derivative instruments or contracts are considered Argentine-source income when the risk assumed is located in Argentina (i.e., if any of the parties are residents of Argentina). However, when the parties have not expressed their eco-

**The new minimum presumed profit tax based on combined assets is intended to prevent the preparation of negative balance sheets for tax-avoidance purposes**

(*Aseguradoras de Riesgo del Trabajo* or ART).

Passenger and cargo commercial airplanes remain exempt, as well as ships and their components, but in the latter situation only when the buyer is the federal government or its centralized or non-centralized organizations.

A 27% rate will be levied on the sale of gas, electric power, and water services that are measured by meters, at locations not exclusively devoted to permanent, recreational or summer homes, and the buyer or user could be categorized as a "registered liable person" (*responsable inscripto*) or "non-registered liable person" (*responsable no inscripto*),<sup>4</sup> or has opted for the simplified regime for smaller contributors.

- A reduced rate of 10.5% will apply to:
- Cable television service.
  - Fruits, vegetables, and bovine meats that are not "elaborated products" (i.e., not manufactured), as well as to bovine living animals.
  - Interest and fees of loans granted by entities that are financial entities under Law 21,526 (Financial Entities Law).
  - Labor, sowings and crops, agrochemical or fertilizer application, and other preparation of land.
  - Works or repairs directly made to real property for lodging purposes.

With regard to prepaid medicine care, which was formerly exempt, Congress originally passed the law applying the half-rate of 10.5% mentioned above. The Executive Power

care should remain exempt. The issue still awaits the pronouncement of the Supreme Court of Argentina. If the court's pronouncement is against collection of the tax, the amounts that prepaid medicine care companies have already collected should be credited or refunded to their affiliates.

## Income Tax

Highlights of the income tax reform include an increase in the individual and corporate tax rates.

**Rate increase.** The individual and corporate maximum income rate has been increased from 33% to 35%. This rate will apply to:

- Stock companies and joint-stock associations, the latter only with regard to partners that have limited liability.
  - Limited liability companies, limited partnerships, foundations, and civil associations not specifically subject to a different tax treatment.
  - Trust funds, except those in which the trustee is also the beneficiary, and financial trusts with certificates of participation placed through public offerings.
  - Mutual funds and individuals with an annual income of over 200,000 Argentine pesos.<sup>5</sup>
- The same rate will apply to commercial, industrial, agricultural, mining and any other type of entities doing business in Argentina regularly, but under the name of corporations or individuals residing abroad.

economic intention, the source will be determined by principles applicable to the source of production, in accordance with economic reality.

**Interest on credit obtained abroad.** For interest paid on any kind of credit obtained abroad, regardless of its source or kind, a net effective withholding tax rate of 15.05% (the law assumes in this instance that 43% of the payment is net income; 43% times 35% = 15.05%) will be applied in any of the following circumstances:

- The borrower of the credit is a financial entity subject to Financial Entities Law 21,526 (e.g., banks, insurance companies).
- Financial operations of imports of movable goods that can be depreciated (except automobiles).
- The borrower is a capital corporation (the equivalent of a U.S. Subchapter C corporation or limited liability company or limited liability partnership), individual, or estate, and the lender is a bank established in a country where the Central Bank or its equivalent has adopted the International Standards of Banking Supervision ruled by the Basel Banking Committee<sup>6</sup> (an effective withholding rate of 35% will apply when such adoption has not occurred).
- Debt bonds issued by countries with which Argentina has a Reciprocal Agreement on Investment Protection.

- Interest paid on savings accounts, special savings accounts, and time deposits (these deposits should have been made in financial entities ruled by Law 21,526).

**Foreign beneficiary.** Net profits of any kind paid to beneficiaries abroad, except dividends, are subject to a 35% rate. For this purpose, the law presumes as net profit 43% of the interest originated by the following deposits: saving accounts, special savings accounts, time deposits, and deposits by third parties or other forms of obtaining public funds, in accordance with Argentine Central Bank regulations. As the applicable rate is 35% over the presumed net profit of 43%, the final result will be a net applicable rate of 15.05% on the interest originated by such deposits.

**Dividends, foreign profits, imports/exports.** Corporations will be subject to income tax on the distribution of dividends exceeding their taxable profit. Also, foreign profits of individuals and Argentine corporations will be subject to tax. In this regard, it can be interpreted that the principle of worldwide income is added to the principle of entailment (territorial source), but only for residents of the country.

Income derived from exports of goods that were produced, manufactured, or bought into the coun-

try will be deemed Argentine source. The income earned by foreign exporters from the introduction of goods in the Argentine Republic will be deemed foreign source. However, when the sale price of such imported goods to the public in Argentina is higher than the wholesalers' price in the country of origin, including the cost of transportation and insurance, the difference between both prices will be considered Argentine-source income. In both situations, the Federal Administration of Public Revenues (*Administración Federal de Ingresos Públicos* or AFIP) may establish the value of the products involved.

**"Resident" defined.** In defining "resident" for tax purposes, the law provides several examples. When a corporation's owners or partners are Argentine residents, the entire corporation will be considered an Argentine "resident." Also considered Argentine residents are foreign individuals who, with or without an Argentine permit of residence, are allowed to do business within the Argentine territory for more than 12 months.

#### Tax on Interest Paid and Financial Costs of Business Indebtedness

This tax has been established for a period of ten years as of the enactment of the law, to discourage corporations from taking loans. It will be applied on the interest of credit operations obtained from financial entities, loans granted by individuals or estates, and negotiable bonds. The new law considers the borrowers of the loans and the issuers of the negotiable bonds as taxpayers. The tax applies at the moment that the interest is paid, at the following rates:

- 15% for interest on loans obtained from financial institutions and on negotiable bonds, when the bearers are individuals, estates, or foreign beneficiaries. Foreign beneficiaries include physical persons or corporations that receive payments (1) abroad; (2) through a power of attorney, agent, or representative in Argentina; or (3)

within the country but are not permanent residents.

- 35% on loans granted to individuals or estates domiciled or residing in Argentina.

#### Minimum Presumed Profit Tax

This new tax will be applied during the ten fiscal periods following enactment. It is levied on the assets of corporations, civil associations, financial entities, individuals, mutual funds established in the country, trusts (other than financial trusts), and commercial, industrial, and any other entities established in Argentina, when the aggregate value of assets is at least 200,000 Argentine pesos. The law establishes methods for valuing the assets. The tax is imposed at 1% on the total value of the assets and any payments will be credited against income tax.

**Example.** Taxpayer has assets with a value of 250,000 pesos. The minimum presumed profit tax would be 2,500 pesos (1% of 250,000). The taxpayer's balance sheet shows positive net income of 100,000 pesos. The income tax would be 35,000 pesos (35% of 100,000). The taxpayer is permitted to credit the 2,500 against the 35,000, for a net income tax of 32,500 pesos.

The aim of the tax is to prevent corporations from preparing negative balance sheets for tax-avoidance purposes. In this regard, as payment of this tax will be deducted from income tax, if the entity's income balance is positive, there will be compensation between both taxes. However, if the balance sheet is negative, only minimum presumed profit tax at 1% will be paid. In this sense, there will be a tax credit if a positive balance sheet is disclosed in the following fiscal period.

The following assets will be exempt from the tax: assets located in the province of Tierra del Fuego and in the islands of the South Atlantic; assets of individuals within the scope of the investment regime for mining activities; securities and other forms of capital participation of entities subject to this tax; the quota participation of mutual funds; and the assets of government companies and corporations in which the government has a participation. ●

<sup>1</sup> Under the VAT law, there are three types of tax contributors in Argentina divided into two categories: (1) the final consumer (the person who buys the goods or pays for the service that he or his direct relatives use or consume); (2) the responsible provider, who is either the seller of the goods (also known as trader) or the renderer of the services (professionals included), both are liable for VAT purposes, but they may register or not depending on the amount of their annual invoicing. Accordingly, within this second category are (a) registered liable persons, who face more exposure to control by the Tax Bureau (*Dirección General Impositiva*, or DGI), but also receive the benefit of deducting the amount that they have paid for VAT and using it as a fiscal credit against other taxes; and (b) non-registered liable persons, whose annual invoicing does not reach the minimum established by the VAT law for registration. However, they are free to register and usually do so because of the benefits mentioned above.

<sup>2</sup> Pursuant to Convertibility Law 23,928, one Argentine peso is equivalent to one U.S. dollar.

<sup>3</sup> The Basel Committee is the leading body for international banking regulation, with members from all G-10 countries.