
Argentine Congress passes comprehensive tax reform

January 31, 2018

In brief

The Argentine Congress passed the proposed tax reform on December 27, 2017 and it became effective on January 1, 2018. Some changes are significant, including an immediate transitional reduction in the corporate income tax (CIT) rate from 35% to 30% for the two taxable years beginning on or after January 1, 2018. For taxable years beginning on or after January 1, 2020, the CIT rate will decrease again, to 25%. The reform also includes a one-time tax on an asset revaluation for tax purposes.

Passage of the legislation reflects the Congress's commitment to modernizing the tax system and addressing the fiscal deficit.

In detail

Tax reform

Corporate income tax rate reduction

The two-step corporate tax rate reduction is offset by a new withholding tax on dividend distributions and branch profit remittances at 7% rate (while the applicable corporate income tax rate is at 30%) and 13% (when the corporate rate lowers to 25%). The withholding tax on dividends and branch profits can be reduced by tax treaties. Thus, in the absence of a tax treaty, the combined effective rate on dividend and profit distributions initially is set at 34.9%. It will decrease to 34.75% when the 25% corporate income tax rate is in place.

The tax reform also has abolished the so-called equalization tax for profits generated in taxable years starting on or after January 1, 2018. The equalization tax was a withholding tax levied at a 35% rate on dividend distributions in excess of tax earnings. However, the equalization tax still applies to dividend and branch profit distributions made out of earnings accumulated prior to January 1, 2018 that exceeded tax earnings as of the year-end prior to the relevant distribution.

Transfers of Argentine shares

Tax reform confirmed that the transfer of Argentine securities that occurred after September 23, 2013, including transfers of

Argentine shares made between non-residents, is subject to tax. The tax, however, does not apply to the sale of shares and American Depositary Receipts (ADRs) made by non-residents through stock exchanges, whether local or foreign.

Prior to the tax reform, the rules required the buyer to withhold tax on the capital gain. However, in practice, taxes were not withheld on sales between non-residents because there was no legal mechanism to do so. In July 2017, the Argentine tax authorities issued Resolution No. 4094-E, establishing the mechanism for paying the capital gains tax due by non-residents. It applies retroactively for transactions that occurred on or after

September 23, 2013. Because of the turmoil this Resolution caused, the tax authorities later published Resolution No. 4095-E, suspending the prior Resolution for 180 days. On January 11, 2018, after the enactment of the tax reform, the tax authorities again issued Resolution No. 4190-E, which repealed Resolutions Nos. 4094-E and 4095-E.

Tax reform now provides that the seller, and not the buyer, should be the party responsible for withholding the tax. As such, Resolution No. 4190-E provides that the tax authorities will issue a new mechanism regulating how non-resident sellers should pay the tax on the capital gain for transactions that take place on or after January 1, 2018.

Since, under the previous rules the buyer was responsible for the withholding tax, the tax authorities also are expected to issue a resolution regulating how non-resident buyers should comply with their withholding tax obligations with respect to taxable transactions (such as, transactions conducted outside of a stock exchange) that occurred between September 23, 2013 and December 31, 2017.

Non-residents are now exempt from tax on capital gains realized from the sale of shares in publicly-traded companies, but only to the extent that the shares are sold through the local Stock Exchange. Furthermore, non-residents continue to be exempt from tax on capital gains from the sale of sovereign bonds and corporate bonds issued in an IPO. The yields from those bonds also are exempt from Argentine tax. In all cases, the exemption is conditioned on the foreign seller being a resident in a jurisdiction that has an exchange of information agreement with Argentina and that the funds come from these jurisdictions. Only yields and capital gains derived from specific securities issued by the Argentine

Central Bank (LEBACs) do not benefit from this exemption. In these cases, both the income and the capital gain are subject to a 5% tax. If the tax cost cannot be determined in the case of a sale, the tax is levied at a rate of 4.5% over the sales proceeds.

Indirect transfers of Argentine assets (including shares) are now taxable under tax reform, provided that (i) the value of the Argentine assets exceed 30% of the transaction's overall value and (ii) the equity interest sold in the foreign entity exceeds 10%. The tax is due if any of these thresholds were met during the 12-month period prior to the sale. The indirect transfer of Argentine assets, however, is only subject to tax to the extent those assets are acquired on or after January 1, 2018. Furthermore, indirect transfers of Argentine assets within the same economic group do not trigger taxation provided the requirements (which will be set by regulations) are met.

Other income tax changes

In line with the OECD Model Tax Convention on Income and Capital guidelines, the tax reform limits the concept of 'ancillary or preparatory' in order to limit the type of activities that are not deemed to constitute a permanent establishment.

Tax reform replaced the 2:1 debt-to-equity thin capitalization rule with the BEPS-based rule. The deduction on interest expense and foreign exchange losses with local and foreign related parties now is limited to 30% of the taxpayer's taxable income before interest, foreign exchange losses, and depreciation. The taxpayer is entitled to carry forward excess non-deductible interest for five years and unutilized deduction capacity for three years.

Amendments have been introduced to relax the so-called sixth method for transfer pricing analysis in cases

involving commodity transactions with foreign intermediaries.

Tax reform has amended the Argentine CFC rules. Thus, an Argentine taxpayer is immediately taxed on the passive income generated by a CFC that is directly or indirectly held by the Argentine taxpayer to the extent that more than 50% of that CFC's income is passive and is effectively subject to a tax that is lower than 75% of the applicable Argentine income tax rate.

Tax reform subjects individuals to tax on both the sale and yields of sovereign bonds and corporate bonds issued in an IPO. The tax, however, is levied at a 5% rate if the bonds are issued in Argentine currency and 15% if they are issued in foreign currency. Before tax reform, individuals were exempt from tax on this type of income.

Tax reform also confirms that ADRs generate Argentine-sourced income. However, a non-resident is exempt from the current 15% capital gains tax on the sale of ADRs if they reside in a jurisdiction that has an exchange of information agreement with Argentina.

Other tax changes

The tax reform includes a new 10% excise tax on drinks with caffeine and taurine. The excise tax rate on certain automobiles has been reduced. The tax reform also increased the tax on financial transactions that is creditable against the income tax liability.

With respect to VAT, tax reform provides for an expedient recovery mechanism for VAT credit balances on certain infrastructure and investments in capital goods, to the extent that companies have not been able to recover the VAT within six months. VAT legislation has also been amended to include 'digital

transactions (such as, digital services, hosting, on-line technical support, software services, and internet services) as a taxable event. As a result, this type of services is now subject to VAT at a 21% rate if they are supplied by a non-resident entity to an Argentine customer, provided that that the services are effectively used in Argentina.

The tax reform also updates the minimum thresholds to characterize a tax omission as tax fraud and introduces other amendments to the Tax Procedure Act.

Argentine employers are also exempt to pay social security contributions for the first 12,000 Argentine Pesos per month per employee. The change will be implemented gradually over a five-year period (from ARG2,400 in 2018 to ARG12,000 in 2022 and thereafter).

Negotiations with the provinces are expected to reduce provincial taxes, such as the turnover tax and the stamp tax.

Tax on asset revaluations

As part of the reform package, the Argentine Congress also approved a one-time tax aimed at offsetting the absence of inflation adjustment rules with an optional revaluation of assets for companies and individual entrepreneurs.

Under this revaluation tax, taxpayers are entitled to adjust their tax basis in fixed and movable assets (except automobiles), shares in Argentine companies, and intangible assets. Assets that have been fully depreciated are excluded. The revaluation must be computed based on certain factors. An external appraisal instead of those factors can be used for real estate that is not treated as inventory as well as for movable assets, provided that the revaluation does not exceed 1.5 times the revaluation had those factors been applied.

The tax is levied on the amount of the adjustment at a rate of 8% in the case of real estate (15% if it is considered inventory), 5% for shares if held by individuals, and 10% for other assets. The taxpayer can select which class of assets to adjust, but once the category has been selected, all of the assets included in that category have to be adjusted.

The basis adjustment is depreciable over the remaining useful life with a minimum of five years, except for basis adjustments in real estate and intangibles, where the depreciation must be made over the longer of either 10 years or 50% of the remaining useful life. Going forward, for newly acquired assets as well as those whose bases have been adjusted, taxpayers are entitled to recover their lost value by adjusting the tax basis for inflation, because inflation adjustments have been reinstated for those assets.

Taxpayers opting to revalue their assets must withdraw judicial or administrative proceedings that claim inflation adjustments for past or future taxable years.

The takeaway

Given the wide scope, nature and relevance of these changes, the Argentine Tax Reform legislation may significantly affect the way MNEs operate and organize their businesses in Argentina.

Therefore, MNEs may need to revisit their holding structures for their Argentine investments as well as for existing financing and cash repatriation structures.

See also: [Tax reform in Argentina: Transfer pricing implications](#)

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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