Advantages of Spain-Uruguay structuring

This month, two of our Amicorp colleagues featured in a Campden Wealth publication – “Innovative Financial Services Centres – 2015”, which we would like to share with you now.

Advantages of Spain-Uruguay structuring

It is becoming increasingly common to implement corporate structures that provide clients with the maximum tax benefits, including: minimizing the inheritance and succession tax impact; avoiding Controlled Foreign Companies (CFC) rules by using the proper vehicles; reducing the taxation of the intercompany’s group income flow through the application of participation exemption regimes and convenient DTAs; and taking profit of territorial tax regimes in reputational jurisdictions. This article is focused on the needs of clients that carry out business in Latin America. As we shall explain, the combination of a Uruguayan corporate (SAU) and a Spanish holding entity can result in 0% taxation on the dividends flow from many Latin American countries.

BY DORIAN BURZACO AND NICOLÁS ALONSO

Spain as a holding jurisdiction

Spain joined the European Union in 1986 and was in the first-wave countries to adopt the euro on 1 January 1999. It is also a member of the OECD. Spain has entered into a broad array of tax treaties with most of the world’s leading nations (more than 85 tax treaties in force) and with almost all the Latin American countries, namely: Argentina, Bolivia, Brazil, Cuba, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Mexico, Panamá, Peru (not yet in force), Uruguay and Venezuela. Additionally, Spain has signed Protection Investment Treaties with many Latin American countries. These treaties aim to protect the investment of foreign (Spanish) investors (natural persons or entities).

Suggested Structures

Diagram 1 – Spanish/Uruguay Holding Structure

Depending on the domestic tax legislation of the ultimate beneficial owners (UBOs), the patronymic vehicle that hold the shares of the Uruguayan entity may change in either its form (foundation, trust, etc.) or its location (Panama, Curacao, New Zealand, etc.). In this article we focus on the following structure:

One of the key elements considered by private equity firms when investing in Latin America is how to structure their investments efficiently from a legal and fiscal standpoint. Given the favorable tax treatment and legal protections provided by the tax and investment treaties in force, as well as the shared cultural, historical and legal backgrounds, it has been common for private equity firms to invest in Latin America using Spanish entities as a platform for such investments.

Structuring through Spain

Spain is one of the most favorable jurisdictions for holding structures for tax planning. It is important to differentiate between the tax treatment applicable to the inbound dividends (received from the Spanish subsidiaries) and the outbound dividends (dividends paid to the shareholders of the Spanish entity). Inbound dividends and capital gains related to the subsidiary’s participation would be tax exempt under the Spanish participation exemption regime if the following requirements are met:

- Minimum 5% ownership requirement. This requirement can also be met if the acquisition cost is higher than €20 million.
• The Spanish entity must hold the participation for an uninterrupted period of at least 12 months. The exemption also applies to inbound dividends received before the 12 months period if the Spanish entity commits to hold the participation for at least such period.

• Qualifying subsidiaries must be subject to a domestic corporate income tax higher than 10%. If the subsidiary is resident in a country with which Spain has signed a tax treaty (which includes an exchange of information clause), the subject-to-tax requirement is understood to be satisfied.

Outbound dividends distributed by the Spanish entity to its non-resident shareholders will either be taxed at the withholding tax rate provided in the applicable tax treaty (DTA), or will be exempt if they are resident in the EU and the Parent-Subsidiary Directive applies. Otherwise they will be taxed at the standard tax rate of 20% (19% for FY 2016 onwards).

Under the Spain-Uruguay DTA, the outbound dividend will not be subject to taxation in Spain (0% withholding tax) provided that the Uruguayan entity holds directly at least 75% of the capital of the company paying the dividends. This means that if the structure is properly implemented, no taxation will be derived from the different taxable facts raised from dividends received from the Latin American subsidiary and subsequently paid to the Uruguayan entity.

Tax benefits of Uruguayan corporations held by a nonresident

Uruguay has historically defined territoriality as a guiding principle in taxation – only Uruguayan source income is taxable. Uruguayan source income is defined as "income derived from activities performed within Uruguay, assets economically located in Uruguay or rights used in Uruguay, regardless of nationality, domicile or residence of those involved in the operations and venue of the legal business."

If the Uruguayan entity can demonstrate that the service was not rendered in Uruguay (i.e. a representative of the corporation rendered the service in another country) then the service profit, as well as any dividends distributed, will be non-taxable in Uruguay.

If the service was rendered in Uruguay, it will be considered Uruguayan source income and will be taxable under Income Tax on Economic Activities (IRAE) at a rate of 25% and the dividends distribution will be taxable under Income Tax (IRPF) at a rate of 7%.

Trading activities

Trading activities are legally defined in a specific law (Res. 51/997) and are performed when Uruguayan companies buy and sell goods abroad even if the goods are never brought into the country. Resolution number 51/997 of the Uruguayan tax authority – Dirección General Impositiva (DGI) – establishes that 3% of the difference between the buying price and the selling price of the goods (the gross profit) is considered as Uruguayan source income. That 3% is taxed at 25% under IRAE. So in this case IRAE taxes 0.75% on the gross profit of the trading.

The Wealth tax (IP) is an annual tax levied on the assets located in Uruguay. Based on the above, any Uruguayan entity asset located abroad would not be considered for the purposes of IP (i.e. bank account, properties in real estate, shares of corporation, bonds, etc.). The company has a bank account with a Uruguayan financial institution, IP would be applied on the balance of the account at the end of the day of it the fiscal year of the company. The IP rate for companies is 1.5% annually. When dividends are distributed, Uruguayan law applies a withholding tax (WHT) of 7% on taxable income. In trading activities, the company will withhold 7% of the 3% of the gross profit of the distribution. So in this case the tax is 0.21% of the gross profit.

In the above example the Uruguayan entity does not pay tax either on its shares in the holding company or on dividends received or distributed to its shareholders. Provided that the structure is properly implemented, under the territorial basis of taxation, the outbound dividend will not be taxed (subject to WHT) regardless of the residence of the shareholder or its legal form (corporation, natural person, trust or foundation). This allows the UBOs to choose the best vehicle for their domestic tax and patrimonial purposes.

Diagram 2 shows the full tax treatment of the structure:

Diagram 2 – Spanish/Uruguay Holding Structure in practice

- Dividend payment may be subject to WHT but this can be reduced through the application of a favourable DTA.
- Dividends and potential capital gains will be tax exempt in Spain, provided that participation exemption requirements are met.
- As the Uruguayan entity holds more than 75% of the share capital of the Spanish entity, according to the Spain-Uruguay DTA, the dividend will not be taxable in Spain (0% WHT).
- As the source of the income (dividends) was not taxed under the territorial basis, there is no WHT on the outbound dividend.
- The SAU is a very attractive tax vehicle because Uruguay does not tax foreign income, making it tax efficient when allocating foreign earnings.
About the authors

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