Peru: New rules issued on indirect transfers of shares

Peru’s Ministry of Economy and Finance published a decree on 6 November 2013 that includes long-awaited regulations to enable the tax authorities to better monitor indirect sales of shares of (or participating interests in) Peruvian companies. The guidance also should help taxpayers with their compliance obligations. Unless otherwise specified, the new rules apply as from 7 November 2013.

Background

Under rules introduced on 15 February 2011 (Law No. 29663), capital gains derived from certain indirect transfers of the shares of a Peruvian legal entity fall within the scope of Peruvian tax (generally taxed at a rate of 30%, although a lower rate of 5% may apply in certain cases). Law No. 29663 indicated that the Ministry of Economy and Finance would be issuing guidance to facilitate compliance with the new rules; however, no regulations were issued, which led to practical implementation issues and uncertainty for both taxpayers and the tax authorities.

On 21 July 2011, the Peruvian government enacted another law (Law No. 29757) that introduced measures to facilitate compliance by taxpayers and to enable the tax authorities to appropriately monitor relevant transactions and collect tax due. The regulations to be issued by the Ministry of Economy and Finance were then intended to provide guidance based on these updated capital gains tax (CGT) provisions.

On 26 June 2013, the government enacted the Securities Market Promotion Act (Law No. 30050), which contains rules for withholding CGT on indirect transfers that Peruvian Clearing and Settlement Institutions (ICVLs) must apply when they participate in cash settlements of relevant securities transactions. The withholding obligation will apply as from 1 January 2014.

Even with the subsequent provisions complementing the February 2011 law, the revised CGT rules have continued to give rise to practical implementation issues and, for this reason, additional regulations were needed to ensure compliance. The Ministry finally has issued these regulations.

Identifying an indirect transfer

Capital gains derived from an indirect transfer of the shares of a Peruvian legal entity currently fall within the scope of the Peruvian tax net if the following conditions are satisfied:

1. When the shares of a nonresident entity that owns, directly or indirectly, shares of a Peruvian company are transferred and either:
   a. The market value of the shares of the Peruvian company owned directly or indirectly by the nonresident entity is equal to 50% or more of the market value of all of the shares representing the equity capital of the nonresident entity (“50% market value rule”) for the 12-month period before the transfer, and there has been a transfer (or transfers) of shares representing 10% or more of the equity capital of the nonresident entity within the relevant 12-month period (in the event of an audit, the tax authorities have the burden of demonstrating that these conditions are satisfied); or
   b. The nonresident entity is resident in a tax haven or low tax jurisdiction, unless it can be demonstrated that the conditions in the previous bullet are not satisfied (in the event of an audit, the taxpayer has the burden of demonstrating that these conditions are not satisfied).

2. When the nonresident entity directly or indirectly issues new shares as a result of a capital increase (generated by a new capital contribution, the capitalization of credits or a reorganization), and allocates the shares a value below their market value. This deeming provision will apply only if at least one of the circumstances described in 1) is present. Under this CGT anti-avoidance measure, the nonresident entity will be deemed to have transferred the shares issued as a result of the capital increase.

There also is a deemed foreign distribution provision (with tax withheld at a rate of 30%) when a capital reduction is made by a nonresident entity that owns, directly or indirectly, shares of a Peruvian entity. This residual anti-abuse provision is triggered when the conditions provided by the CGT anti-avoidance measure are not fulfilled. In addition to the conditions for the more-than-50% market value rule being satisfied within a 12-month period before a capital increase, the application of the deemed dividend rule requires the occurrence of two events: (i) a capital reduction within a 12-month period after
the capital increase, and (ii) a payment in excess of the par value of the shares that are cancelled as a result of the capital reduction.

The pre-regulations rules did not explain how to determine the market value of the shares or the extent of a participation when there are different tiers of entities in the ownership structure. Even when the general provisions were used in practice to close the loopholes, it was unclear which approach would prevail in the event of an audit. The new regulations provide the market value rules that should be used to calculate the 50% market value (depending on whether there is a quoted price, audited financial statements or an appraisal value; any value expressed in foreign currency must be converted into local currency using specified guidelines), as well as the procedure for identifying the percentage participation of a nonresident in a Peruvian company when there are different tiers of entities. The regulations offer more certainty for determining whether a transaction falls within the scope of the reporting obligation, and allow taxpayers to anticipate which transactions are more likely to be scrutinized by the tax authorities and what documentation should be available.

**Capital gains determination**

Under the pre-regulations rules, the taxable base for purposes of the CGT on indirect transfers is determined by taking into account the market value of the shares in the nonresident legal entity that are transferred, multiplied by a percentage identified when applying the 50% market value rule. The regulations clarify that, once an indirect transfer has been identified, the taxable base will be determined as follows:

- By taking into account all transfers of shares representing the equity capital of the nonresident entity that took place within the 12-month period before the indirect transfer; and
- By taking into account the market value of the shares transferred:
  - Applying the highest of (i) the value agreed by the parties, (ii) the exchange valuation (if applicable) or (iii) the equity value at the time of each transfer. (For purposes of identifying the equity value, the most recent annual balance sheet issued by the foreign company before the transfer of its shares cannot be older than 12 months. If such a balance sheet is not available, the equity value of the shares will be their appraised value.)
  - Transfers between related parties or from, through or to a tax haven would be subject to Peru’s transfer pricing rules.

The tax basis of the shares in the nonresident legal entity transferred would be the value obtained by applying the percentage determined when applying the 50% market value rule to the total tax basis available under Peruvian provisions. The tax basis available must be supported by documents issued abroad according to the tax rules of the relevant jurisdiction or by any other documents that would accurately support the amount claimed as tax basis.

On the other hand, for purposes of the CGT anti-avoidance measure when a nonresident is deemed to have transferred the shares issued as a result of a capital increase, the taxable amount would be the difference between the market value of the shares issued and the value allocated to them. Under the pre-regulations rules, no further guidelines on how to calculate the market value for this purpose were available. The regulations provide rules that define the market value the nonresident should take into account for purposes of quantifying the deemed taxable amount under the CGT anti-avoidance provision.

**Withholding tax on certain indirect transfers**

ICVLs currently are treated as withholding agents for CGT purposes when they participate in cash settlements of direct and indirect transfers of shares representing the equity capital of a Peruvian company (where the reduced rate of 5% applies).

Reporting obligations and rules facilitating the information-gathering process in connection with indirect transfers recently were provided by Law No. 30050, which from 1 January 2014 requires that CGT withholding on an indirect transfer of shares representing the equity capital of a Peruvian company by a nonresident entity is to be made at the time of the settlement and remittance of funds, if the taxpayer or an authorized third party notifies the ICVL of the indirect transfer and the amount subject to reporting and provides supporting documentation.

The regulations clarify that ICVLs must report the percentage determined when applying the 50% market value rule, as well as the tax basis and market value of the shares involved. The regulations also provide that an authorized third party for purposes of the reporting obligation includes a broker or any other ICVL participant.
Joint and several liability of the issuer company

Under the CGT rules, a Peruvian company is jointly and severally liable with a nonresident transferor for the payment of any CGT that may arise from a transfer of its shares if the Peruvian company and the nonresident transferor were economically related within the 12-month period before the transfer. These rules do not apply to indirect transfers where the transferee is a Peruvian resident, but will continue to apply when an ICVL is acting as a withholding agent.

The regulations set out instances in which a nonresident transferor would be deemed to be economically related to the Peruvian issuer company. Until the regulations were issued, taxpayers had resorted to the general transfer pricing rule to determine whether an economic relationship existed. That rule requires a more-than-30% direct or indirect participation of one entity in the equity capital of another entity; the regulations set the threshold at 10%.

The new regulations should be examined closely when estimating the risk of a possible assessment by the tax authorities at the Peruvian level in connection with any potential CGT due by nonresident shareholders at the upper tiers of the economic group.

Reporting obligations

The CGT rules require the Peruvian issuer company to notify the tax authorities when its shares are indirectly transferred. General information on how to comply with this reporting obligation can be found on the website of the Peruvian tax authorities. However, where a Peruvian legal entity is not jointly and severally liable with a nonresident transferor for CGT due on an indirect transfer, tracking and gathering all the required information connected with all indirect transfers would be a substantial administrative burden. The regulations, therefore, exempt the Peruvian issuer company from this reporting obligation when there is no economic relationship with the nonresident transferor.

Comments

The new regulations complement Peru’s CGT rules by introducing guidelines that should help taxpayers with their compliance obligations with respect to indirect transfers of shares of a Peruvian company, and should enable the tax authorities to better monitor such transactions. The Peruvian tax authorities will likely conduct audits to verify compliance with the CGT rules governing the direct or indirect transfer of shares. Potentially affected taxpayers should evaluate the risk of an information request and start designing a plan for appropriate compliance.

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