



The ripple effect of BEPS in Latin America

How local jurisdictions are embracing and developing the
OECD guidelines

—

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Welcome and introduction



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Topics for discussion

Agenda



Welcome and introduction

Digital tax

Multilateral Instrument — MLI

Interest deductions

Hybrid mechanisms

Low tax jurisdiction

Q&A

Administration

Polling questions

- Polling questions will appear as we proceed through the presentation.
- As mentioned, in order to receive the certificate of attendance, we require participants to take part in at least four of the five polling questions.
- If you qualify for the certificate of attendance, it will be sent to you following the webcast.



Attendee questions

- You may submit questions in the *Ask a question* button on the left. We will answer as many questions as we can during Q&A. If we are unable to answer your question during the webcast, someone from KPMG may reply via phone or email following the webcast.
- For technical issues, please use the *Question Mark* button in the upper-right hand corner of the media player.



Your feedback

- When the webcast is over, the webcast player will automatically refresh to display an exit survey. Feel free to complete the survey, as your comments are very valuable to us.





Digital tax



Ricardo Ruiz
International Tax Partner
KPMG in Colombia



BEPS Action 1 report

Tax challenges arising from digitalization

BEPS Evolution on digital taxation

BEPS 2015 report

- The [2015 Action 1 Report](#) identified a number of broader tax challenges raised by digitalization which it identified as “nexus, data and characterization”, and that relate to the question of how taxing rights on income generated from cross-border activities in the digital age should be allocated among countries. While some options to address these concerns were discussed, no consensus emerged and decision was made to continue working in this area. This context explains the growing focus of OECD in the VAT area.



VAT Recommendations

- The OECD issued the 2016 [“International VAT Guidelines”](#) complemented by the 2017 report on [“Mechanisms for the effective collection of VAT/GST where the supplier is not located in the jurisdiction of taxation”](#) and the 2019 report on [“The role of digital platforms in the collection of VAT/GST on online sales”](#) providing technical guidance that has been influential in different tax reforms. As of today, over 50 jurisdictions have adopted rules for the application of VAT to B2C supplies of services and intangibles by foreign vendors.



Income tax recommendations

- No consensus has been reached but the OECD is committed to deliver a final report in 2020 aimed at providing a long-term solution. The current proposals target the profit allocation and nexus rules, with a view to allocate more taxing rights to the country where the customers and/or users are located (Pillar 1), and a Pillar 2 focused on a global anti-base erosion mechanism by which a jurisdiction would “tax back” where other jurisdictions have not exercised their primary taxing rights or the payment is otherwise subject to low levels of effective taxation.



Taxation on digital services (MEX/ARG/COL/CL/PE/CR)

1 VAT/Cross border services

- Destination Principle (user tax residence)
- VAT Digital Services Regime: COL (2016), ARG y CR (2018), CL and MEX (2020),
- General VAT rate
- PE does not have a VAT Digital Services regime, so B2C services are untaxed

2 VAT Compliance features

- Reverse Charge mechanism for B2B — customer is a local VAT taxpayer — (MEX: N/A)
- Non Resident as VAT taxpayer: Simplified system for B2C transactions
- Optional Withholding at source by financial entities upon electronic payments (still in implementation COL, CR) (MEX: limited to intermediation)

3 Income Tax Withholding features

- Technical services, technical assistance and royalties have been traditionally covered
- PE has a digital services WTH, based on a broad notion of economic use by Corporate Taxpayer
- DTT's might exempt them through the "business profits" clause, save for explicit coverage of "royalties" clause



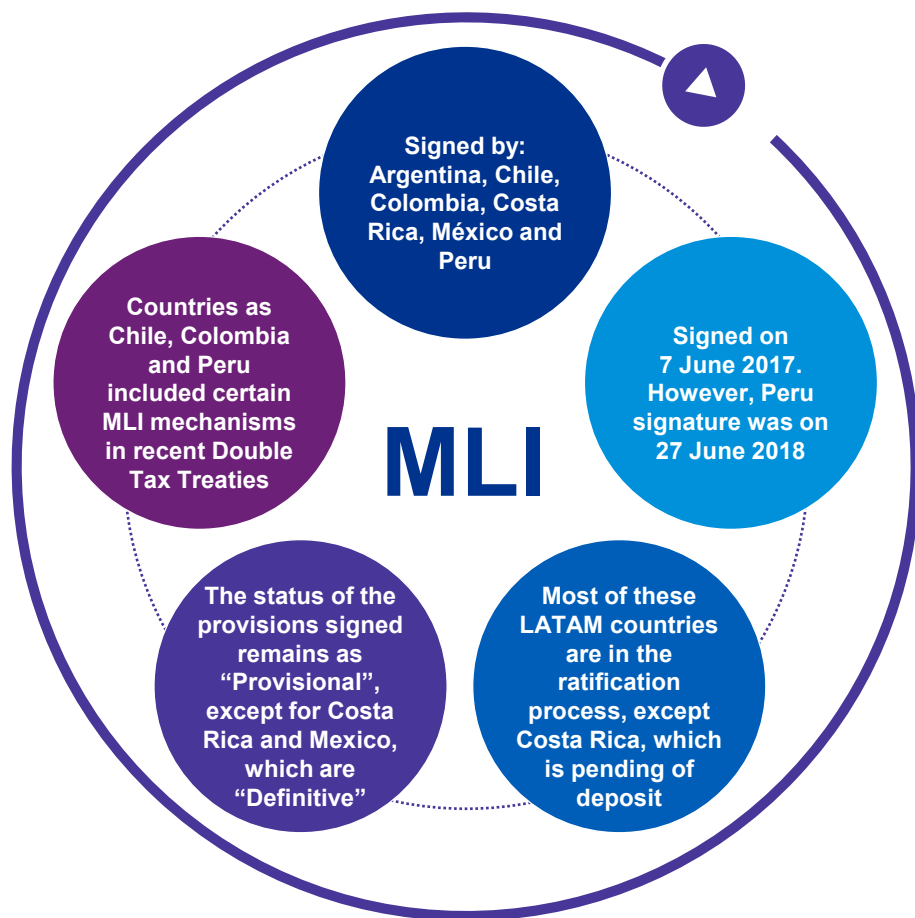
BEPS Action 15 Report

Multilateral Instrument — MLI



Armando Lara Yaffar
Head of International Tax
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Multilateral Instrument — “MLI”



No match between jurisdictions as “Covered treaties”:

- **Colombia** — Switzerland
- **Costa Rica** — Germany
- **Mexico** — Indonesia and United States
- **Peru** — The Andean Community Treaty



Argentina reservations

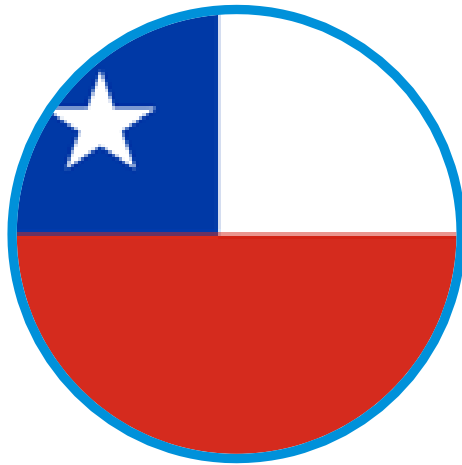
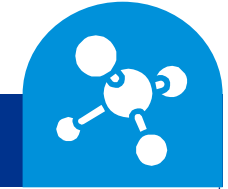
Multilateral Instrument



- **Art. 6 Preamble** — Pursuant to Article 6(4), reserves the right for Article 6(1) not to apply to its Covered Tax Agreements that already contain preamble language.
- **Art. 7 PPT/S-LOB** — Pursuant to Article 7(15)(b), reserves the right for Article 7(1) not to apply to its Covered Tax Agreements that already contain provisions that deny all of the benefits that would otherwise be provided under the Covered Tax Agreement where the principal purpose or one of the principal purposes of any arrangement or transaction, or of any person concerned with an arrangement or transaction, was to obtain those benefits. Pursuant to Article 7(15)(c), reserves the right for the provisions contained in Article 7(8) through (13) not to apply to its Covered Tax Agreements that already contain the provisions described in Article 7(14).
- **Art. 10 PE in 3rd** — Pursuant to Article 10(5)(b), reserves the right for the entirety of Article 10 not to apply to its Covered Tax Agreements that already contain the provisions described in Article 10(4).
- **Art. 13 PE** — Pursuant to Article 13(6)(b) reserves the right for Article 13(2) not to apply to its Covered Tax Agreements that explicitly state that a list of specific activities shall be deemed not to constitute a permanent establishment only if each of the activities is of a preparatory or auxiliary character.

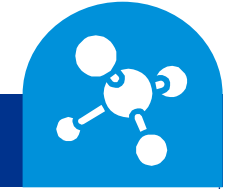
Chile reservations

Multilateral Instrument

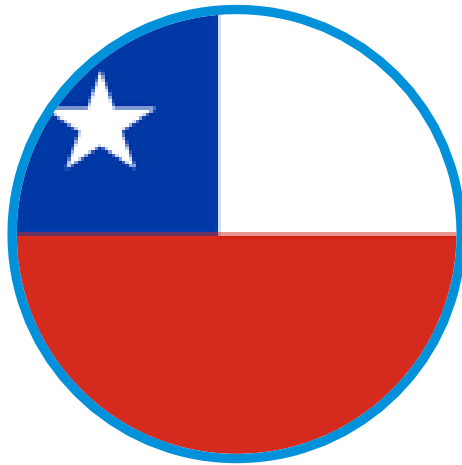


- **Art. 3 Transparent Entities** — Pursuant to Article 3(5)(b), reserves the right for paragraph 1 not to apply to its Covered Tax Agreements that already contain a provision described in Article 3(4)
- **Art. 4 Dual Resident Entities** — Pursuant to Article 4(3)(a), reserves the right for the entirety of Article 4 not to apply to its Covered Tax Agreements.
- **Art. 6 Preamble** — Pursuant to Article 6(4), reserves the right for Article 6(1) not to apply to its Covered Tax Agreements that already contain preamble language.
- **Art. 7 PPT/S-LOB** — Pursuant to Article 7(15)(b), reserves the right for Article 7(1) not to apply to its Covered Tax Agreements that already contain provisions that deny all of the benefits that would otherwise be provided under the Covered Tax Agreement where the principal purpose or one of the principal purposes of any arrangement or transaction, or of any person concerned with an arrangement or transaction, was to obtain those benefits. Pursuant to Article 7(15)(c), reserves the right for the provisions contained in Article 7(8) through (13) not to apply to its Covered Tax Agreements that already contain the provisions described in Article 7(14).
- **Art. 8 Dividends** — Pursuant to Article 8(3)(a) of the Convention, reserves the right for the entirety of Article 8 not to apply to its Covered Tax Agreements.
- **Art. 9 Capital Gains** — Pursuant to Article 9(6)(d), reserves the right for Article 9(1)(a) not to apply to its Covered Tax Agreements that already contain a provision of the type described in Article 9(1) that includes a period for determining whether the relevant value threshold was met.

Chile reservations (continued)



Multilateral Instrument



- **Art. 10 PE in 3rd** — Pursuant to Article 10(5)(b), reserves the right for the entirety of Article 10 not to apply to its Covered Tax Agreements that already contain the provisions described in Article 10(4).
- **Art. 11 Saving Clause** — Pursuant to Article 11(3)(b), reserves the right for the entirety of Article 11 not to apply to its Covered Tax Agreements that already contain the provisions described in Article 11(2).
- **Art. 14 PE** — Pursuant to Article 14(3)(a), reserves the right for the entirety of Article 14 not to apply to its Covered Tax Agreements.
- **Art. 16 MAP** — Pursuant to Article 16(5)(a), reserves the right for the first sentence of Article 16(1) not to apply to its Covered Tax Agreements on the basis that it intends to meet the minimum standard for improving dispute resolution under the OECD/G20 BEPS Package.
- **Art. 17 Corresponding Adjustments** — Pursuant to Article 17(3)(a), reserves the right for the entirety of Article 17 not to apply to its Covered Tax Agreements that already contain a provision described in Article 17(2).
- Chile has decided not to apply arbitration rules.

Colombia reservations



Multilateral Instrument



- **Art. 3 Transparent Entities** — Pursuant to Article 3(5)(a), reserves the right for the entirety of Article 3 not to apply to its Covered Tax Agreements.
- **Art. 6 Preamble** — Pursuant to Article 6(4), reserves the right for Article 6(1) not to apply to its Covered Tax Agreements that already contain preamble language.
- **Art. 10 PE in 3rd** — Pursuant to Article 10(5)(a), reserves the right for the entirety of Article 10 not to apply to its Covered Tax Agreements.
- Colombia did not support the arbitration mechanism in the MLI, by exception it is included in CDI with France.

Costa Rica reservations

Multilateral Instrument



- **Art. 3 Transparent Entities** — Pursuant to Article 3(5)(a), reserves the right for the entirety of Article 3 not to apply to its Covered Tax Agreements.
- **Art. 4 Dual Resident Entities** — Pursuant to Article 4(3)(e), reserves the right to replace the last sentence of Article 4(1) with the following text for the purposes of its Covered Tax Agreements: “In the absence of such agreement, such person shall not be entitled to any relief or exemption from tax provided by the Covered Tax Agreement.”
- **Art. 5 Elim. DT** — Pursuant to Article 5(8), reserves the right for the entirety of Article 5 not to apply with respect to all of its Covered Tax Agreements.
- **Art. 9 Capital Gains** — Pursuant to Article 9(6)(a), reserves the right for Article 9(1) not to apply to its Covered Tax Agreements.
- **Art. 10 PE in 3rd** — Pursuant to this Article 10(5)(a), reserves the right for the entirety of Article 10 not to apply to its Covered Tax Agreements.
- **Art. 11 Saving Clause** — Pursuant to Article 11(3)(a), reserves the right for the entirety of Article 11 not to apply to its Covered Tax Agreements.
- **Art. 14 PE** — Pursuant to Article 14(3)(a), reserves the right for the entirety of Article 14 not to apply to its Covered Tax Agreements.
- **Art. 17 Corresponding Adjustments** — Pursuant to Article 17(3)(a), reserves the right for the entirety of Article 17 not to apply to its Covered Tax Agreements that already contain a provision described in Article 17(2).

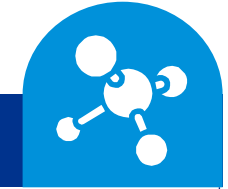
Mexico reservations

Multilateral Instrument



- **Art. 4 Dual Resident Entities** — Pursuant to Article 4(3)(c), reserves the right for the entirety of Article 4 not to apply to its Covered Tax Agreements that already address cases where a person other than an individual is a resident of more than one Contracting Jurisdiction by denying treaty benefits without requiring the competent authorities of the Contracting Jurisdictions to endeavor to reach mutual agreement on a single Contracting Jurisdiction of residence. Pursuant to Article 4(3)(d), reserves the right for the entirety of Article 4 not to apply to its Covered Tax Agreements that already address cases where a person other than an individual is a resident of more than one Contracting Jurisdiction by requiring the competent authorities of the Contracting Jurisdictions to endeavor to reach mutual agreement on a single Contracting Jurisdiction of residence, and that set out the treatment of that person under the Covered Tax Agreement where such an agreement cannot be reached.
- **Art. 6 Preamble** — Pursuant to Article 6(4), reserves the right for Article 6(1) not to apply to its Covered Tax Agreements that already contain preamble language.
- **Art. 7 PPT/S-LOB** — Pursuant to Article 7(15)(b), reserves the right for Article 7(1) not to apply to its Covered Tax Agreements that already contain provisions that deny all of the benefits that would otherwise be provided under the Covered Tax Agreement where the principal purpose or one of the principal purposes of any arrangement or transaction, or of any person concerned with an arrangement or transaction, was to obtain those benefits. Pursuant to Article 7(15)(c), reserves the right for the provisions contained in Article 7(8) through (13) not to apply to its Covered Tax Agreements that already contain the provisions described in Article 7(14).

Mexico reservations (continued)



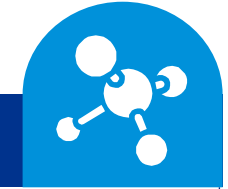
Multilateral Instrument



- **Art. 11 Saving Clause** — Pursuant to Article 11(3)(b), reserves the right for the entirety of Article 11 not to apply to its Covered Tax Agreements that already contain the provisions described in Article 11(2).
- **Art. 14 PE** — Pursuant to Article 14(3)(a), reserves the right for the entirety of Article 14 not to apply to its Covered Tax Agreements.
- **Art. 17 Corresponding Adjustments** — Pursuant to Article 17(3)(a), reserves the right for the entirety of Article 17 not to apply to its Covered Tax Agreements that already contain a provision described in Article 17(2).
- Mexico denied the arbitration rules.

Peru reservations

Multilateral Instrument



- **Art. 3 Transparent Entities** — Pursuant to Article 3(5)(a), reserves the right for the entirety of Article 3 not to apply to its Covered Tax Agreements.
- **Art. 4 Dual Resident Entities** — Pursuant to Article 4(3)(d), reserves the right for the entirety of Article 4 not to apply to its Covered Tax Agreements that already address cases where a person other than an individual is a resident of more than one Contracting Jurisdiction by requiring the competent authorities of the Contracting Jurisdictions to endeavour to reach mutual agreement on a single Contracting Jurisdiction of residence, and that set out the treatment of that person under the Covered Tax Agreement where such an agreement cannot be reached. Pursuant to Article 4(3)(e), reserves the right to replace the last sentence of Article 4(1) with the following text for the purposes of its Covered Tax Agreements: “In the absence of such agreement, such person shall not be entitled to any relief or exemption from tax provided by the Covered Tax Agreement.”
- **Art. 11 Saving Clause** — Pursuant to Article 11(3)(a), reserves the right for the entirety of Article 11 not to apply to its Covered Tax Agreements.
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- **Art. 16 MAP** — Pursuant to Article 16(5)(a), reserves the right for the first sentence of Article 16(1) not to apply to its Covered Tax Agreements on the basis that it intends to meet the minimum standard for improving dispute resolution under the OECD/G20 BEPS Package.

Reservations summary



Multilateral Instrument

	Transparent entities	Dual resident entities	Elim. DT	Preamble	PPT/S-LOB	Dividends	Capital gains	PE in 3 rd	Saving clause	PE			MAP	Corresponding adjustments	Arbitration	
	Art. 3	Art. 4	Art. 5	Art. 6	Art. 7	Art. 8	Art. 9	Art. 10	Art. 11	Art. 12	Art. 13	Art. 14	Art. 15	Art. 16	Art. 17	Art. 18
				X	X			X*			X					
	X	X*		X	X	X*	X	X*	X*			X*		X	X*	
	X*			X				X*								
	X*	X	X*				X	X*	X*			X*			X*	
	X	X*		X	X				X*			X*			X*	
	X*	X*							X*			X*		X		

* The Country reserves the right for the entirety of the article.



Interest deductions



Juan Martín Jovanovich
Partner
KPMG in Argentina



BEPS Action 4 report

**Limiting base erosion involving interest deductions and
other financial payments**

Quote slide



BEPS Action 4 calls for the development of recommendations regarding best practices in the design of rules to prevent base erosion through the use of interest expense to achieve excessive interest deductions or to finance the production of exempt or deferred income...”



BEPS Action 4 issues tackled in different ways

▶ Arm's length tests

▶ Withholding taxes

▶ Disallowance of specific % of interest expense

▶ Debt/equity or interest/earnings limitations

▶ Limitations with reference to Group's overall debt position

BEPS Action 4 – Best Practice Approach



***De minimis* monetary threshold to remove low risk entities**

Optional



Based on net interest expense of local group



Fixed ratio rule



Allows an entity to deduct net interest expense up to a benchmark net interest/EBITDA ratio. Relevant factors help a country set its benchmark ratio within a corridor of 10%–30%



Group ratio rule



Allows an entity to deduct net interest expense up to its group's net interest/EBITDA ratio, where this is higher than the benchmark fixed ratio. Option for a country to apply an uplift to a group's net third party interest expense up to 10%



Carry interest/unused interest capacity and/or carry forward of disallowed back of disallowed interest



Optional



Targeted rules to support general interest limitation rules and address specific risks



Specific rules to address issues raised by the banking and insurance sectors

LATAM Pre-BEPS interest limitation rules



Rules before BEPS

- Most countries had thin-cap rules based on debt/equity ratios
 - Argentina, Colombia, México, Perú and Chile
- Thin-cap rules disallowed the deduction of interest expense
- Except Chile: 35% tax on interest



LATAM new interest limitation rules



Rules after BEPS

- Some countries completely replaced the old rules (Argentina, Perú)
- Some countries kept the old rules combined with new BEPS compliant rules (México)
- Colombia and Chile modified old rules without adopting BEPS best practices
- Costa Rica adopted BEPS based rules



LATAM new interest limitation rules



Ratios

- Interest/EBITDA ratio
 - Argentina and Perú: 30%
 - Costa Rica: 20%
- Debt/equity ratio
 - Colombia: 2:1
 - Chile 3:1
- Combination of debt/equity and interest/EBITDA ratios
 - Mexico: 3:1 debt/equity (thin cap) + 30% “Net Interest”/EBITDA



LATAM new interest limitation rules

Related-party interest vs. related and unrelated-party interest

- Argentina and Colombia
 - Only related-party interest
- Costa Rica and Perú
 - Related and unrelated-party interest
- Chile
 - 35% tax only on related-party interest
 - 3:1 ratio calculated on both related and unrelated-party debt
- México
 - Thin cap limit: only related-party interest
 - Interest/EBIDTA limitation: both related and unrelated-party interest



LATAM new interest limitation rules

Group ratio rule

- Argentina
 - Limitation not applicable if entity's interest/EBIDTA ratio is equal or less than Group's ratio with unrelated creditors

Passive vs. active interest

- Argentina
 - Limitation not applicable to the passive interest not exceeding the active interest earned by the entity
- México
 - Limitation applicable to "Net Interest": passive interest — active interest



LATAM new interest limitation rules

▶ Carry-forward rules (excess interest)

- Argentina, Costa Rica and Perú: 5 years
- México:
 - 10 years on Net Interest/EBIDTA limit
 - No carry-forward on thin-cap
 - Colombia: No carry-forward
 - Chile: Tax (then no carry-forward)

▶ Carry-forward rules (excess EBIDTA)

- Argentina:
 - Excess EBIDTA in 3 prior years may be carried forward



LATAM new interest limitation rules

Economic substance — Back-to-Back — GAAR

- Chile and Colombia have specific rules against back-to-back arrangements
- Chile has rules regarding arrangements involving performance guarantees
- México has specific economic substance rules
- Argentina has general anti-avoidance rules (GAAR)

Sectors excluded from limitations

- Financial sector: Argentina, Colombia, Costa Rica, México, Perú and Chile
- Infrastructure: Colombia, Chile, México, Perú and Chile (if arm's length)



LATAM new interest limitation rules



Specific country considerations

- Argentina
 - Only financial debt (commercial debt excluded)
 - Interest subject to WHT excluded
 - FX losses included (except where inflationary adjustment is applicable)
- Chile
 - WHT creditable against 35% tax





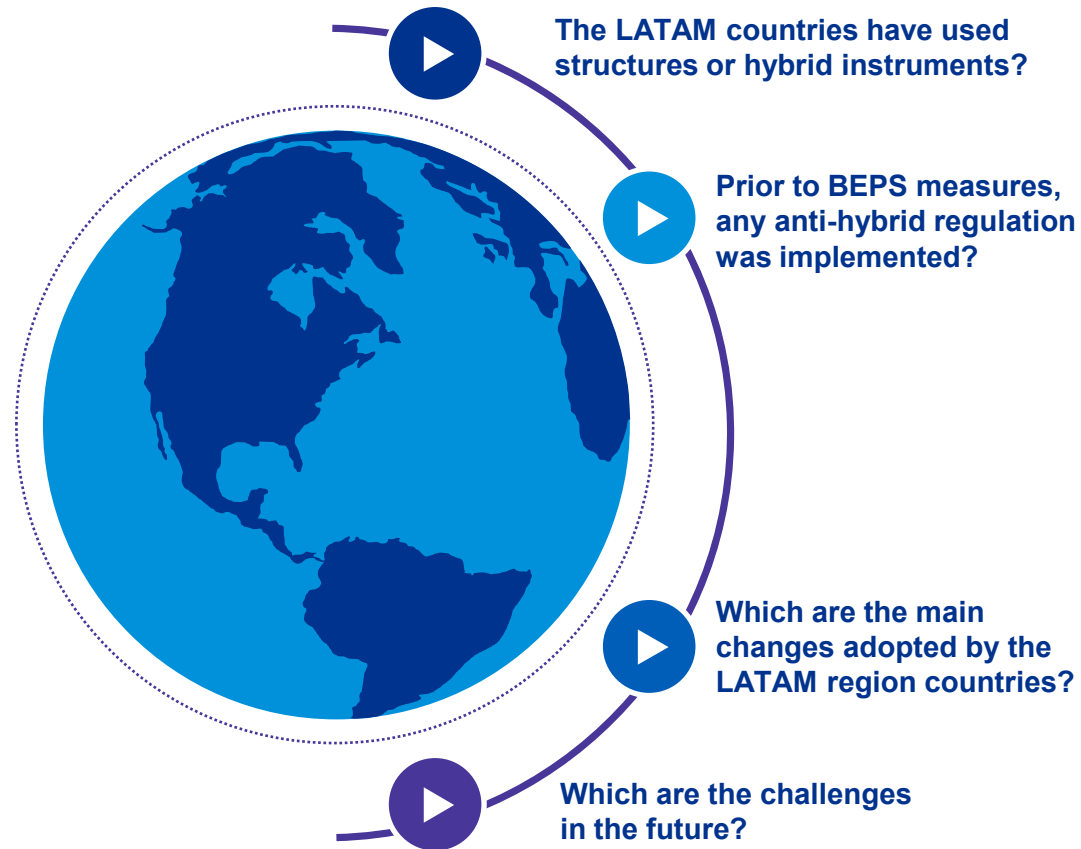
BEPS Action 2 Report

Hybrid mechanisms

— Neutralizing the effects of hybrid mismatch arrangements

Discussion

Hybrid mechanisms



- **Costa Rica, Mexico and Peru** have used hybrid mechanisms in some structures; i.e., Hybrid or transparent entities and financial instruments.
- Only **Mexico** implemented certain measures before BEPS, which consisted on the non-deductibility of payments made for interest, royalties or technical assistance when they were not taxable or considered as non-existent for the party receiving the payment; and the party was controlling or controlled by the Mexican taxpayer.
- **Costa Rica**, as of 2019, is considering as non deductible the payments made through an hybrid entity or instrument, if it is not a taxable income in the other jurisdiction.
- **Mexico** will consider as taxable entities for Corporate Income Tax purposes, the transparent entities and figures, as of 2021 and; payments made directly or indirectly to related parties subject to “Low taxation”, through a structured agreement or hybrid mechanisms are not deductible, as of 2020.
- **Peru** does not have specific anti-hybrid rules; however, specific regulations are applied to derivative financial instruments.



Low tax jurisdiction

Pre-BEPS and Post-BEPS highlights

Discussion

Low tax jurisdictions highlights (MEX/ARG/COL/CL/PE/CR)



Counter-Measures pre-BEPS: All (except CR)



Changes post-BEPS: All (except CL)



Except ARG all apply a mix of local and international standards. ARG, MEX, CR and CL use a percentage threshold to trigger the categorization



All apply some measures within a mix of deduction restrictions, special withholding tax rates or transfer pricing regulations



Preferential Regime target: All (except CR)



Official list of targeted jurisdictions: All (except MEX, ARG) CL *also issued a list of preferential regimes*



Q&A

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