



JUNE
2013

Newsflash

Introduction of the Beneficial Tax Policy II

Introduction

On January 13, 2013 we sent you a newsflash informing you about a series of measures introduced under the beneficial policy (begunstigend beleid). Those measures were the result of the Social Dialogue about tax reforms and the water and energy policy, and have yet to be formalized in legislation.

Earlier today, in anticipation of further legislative amendments, the Minister of Finance, Communication, Utilities and Energy announced the introduction of a further series of attractive tax measures. The main points of those measures, essentially constituting a tax reform, are explained below.

Extension of temporary investment deduction facility

A temporary investment deduction facility was introduced on January 1, 2011 under which, if certain conditions are met, a deduction may be claimed for income tax and profit tax purposes of up to 6% of amounts invested in operating assets. Originally this temporary investment deduction facility was to be offered for the years 2011 and 2012 only. However, based on the beneficial tax policy that has now been published the temporary investment deduction facility will remain in place for investments made during the years 2013 and 2014.

Deductibility of interest relating to participations

Dividends originating from ownership of shares are exempt from profit tax if certain conditions are met. The same is true of profits realized from sales of those shares. These facilities constitute what is commonly known as the “participation exemption”. The flipside of this exemption was that interest paid to finance the acquisition of such participations was non-deductible.

The situation is now set to change for interest relating to ownership of shares in Aruban companies. The interest paid during the first and second years after the shares were acquired is initially not deductible; however, over the three following years it may as yet be deducted in equal portions from the profit. Interest paid during the third year and beyond is immediately and wholly deductible.

The facility for deducting participation interest will come into effect from the beginning of this year. However, no information

has been provided about how interest on domestic participations acquired in the past should be declared.

Changes to the IPC regime

The “IPC regime”, as it is commonly known, was introduced in 2003. It provided for imputation payments by the Constituent Country of Aruba to shareholders. Essentially, it offered a partial rebate on the profit tax paid by the company, bringing the effective tax rate to no more than 2%. The IPC regime applied to a small number of activity types, including commercial operation of luxury hotels. To qualify, the average consideration per hotel room (“RevPAR”, or revenue per available room) had to be AWG 354.

In practice, few taxpayers made use of the IPC regime. Reasons included the numerous formalities involved and the fact that only a small number of hotels in Aruba have a RevPAR of AWG 354. As such, the authorities have decided to modify the IPC regime: the imputation payments will cease, but the profit tax rate will be lowered and taxpayers will be granted an exemption from dividend withholding tax.

Hotels are divided into four categories for purposes of the modified IPC regime, each with a separate rate for profit tax:

Category	Status	Rate
I	RevPar USD 185	10%
II	RevPar USD 175	12%
III	RevPar USD 160	15%
IV	4 diamond status	12%

These lower RevPAR requirements mean that many more hotels will qualify than was previously the case. However, to qualify they must satisfy two additional requirements also: Firstly, the hotel must be certified by Earth Check or possess a similar certificate, or else the certification process must have commenced. In the latter situation, certification must as yet be awarded no later than January 1, 2015. Secondly, investments must be made annually in “sustainability”. The amount that must be invested is linked to the category in which the hotel falls and depends in part on whether the hotel has more or fewer than 100 rooms:

Category	More than 100 rooms	Fewer than 100 rooms
I	AWG 250.000	AWG 120.000
II	AWG 165.000	AWG 75.000
III	AWG 90.000	AWG 45.000
IV	AWG 165.000	AWG 75.000

For these purposes, 1/3 of the amount invested must go toward “green” projects aimed at reducing energy consumption. A further 1/3 of the investment must be spent on improving the training and education of employees and on providing internship positions. The remainder of the investment must be used for purchasing products manufactured locally in Aruba.

Other types of activities besides hotel operation qualify for the modified IPC regime also. The first group consists of the activities that, if certain conditions were met, similarly qualified for the former IPC regime, such as holding company and financing activities, for example. Four further qualifying types of activities have been added;

- ▶ activities relating to green energy;
- ▶ activities aimed at sustainable development;
- ▶ activities whose purpose is to stimulate the knowledge economy;
- ▶ scientific activities.

These activities are subject to profit tax at a rate of 10% and are exempt from dividend withholding tax.

It appears that the changes to the IPC regime will not have retroactive effect from the beginning of this year, but instead will enter into force today. If so, this means that taxpayers will need to split their profit: Their profit to date will be taxed at 28%, and only the profit that they record during the remainder of the year can benefit from the reduced rate and the exemption from dividend withholding tax when it is distributed. Conversely, the question arises of whether companies that already qualified for the IPC regime no longer qualify. The effective profit tax rate under the previous version of the IPC regime was lower than under the modified IPC regime. In our view, until the law is amended imputation payments may as yet be claimed in such situations.

Free Zone

Changes have been rung for the Free Zone also. Firstly, the scope of the tax facilities has been expanded, with the introduction of an exemption from dividend withholding tax for businesses in the Free Zone. Secondly, the FreeZone Facility Charge (“FFC”) has been set at 0.75%, effective the beginning of this year. However, it has been announced also that different rates for the charge will be introduced later in the year: The higher the revenue, the lower the FFC will be (only 0.01% if revenue is more than AWG 200 million).

At the same time, three additional possibilities for utilizing the Free Zone have been introduced.

Firstly, the services that may be supplied from the Free Zone are now given a broad interpretation. For example, activities in the fields of consultancy, training courses, and certification will qualify. However, financial services are still excluded.

Secondly, a new method will be used for designating specific locations as Free Zones. Simple rules will apply under which more locations can be designated as Free Zones. This will chiefly apply in respect of the activities of service providers, which need not be supervised by the Customs authorities. In anticipation of the legislative amendments that will enable this, it will be possible for service providers to set up their offices at an address outside designated Free Zones, which address will then be designated as such. This is subject to the approval of Free Zone Aruba NV, however.

Lastly, additional possibilities will be introduced for businesses in the Free Zone to supply to recipients in Aruba. In principle, a non-variable maximum of 25% of revenue will apply. Previously, this percentage was gradually reduced to 5% over a seven-year period. Income generated by local sales will be subject to the normal tax rate of 28%, while income from export will continue to qualify for the reduced rate of 2%. However, for some types of activities relating to sustainable development or aimed at promoting Aruba as a “gateway”, businesses will be permitted to generate up to half of their revenue from domestic sales (e.g., medical tourism and sustainable transportation). Finally, special cases may be designated where an even higher percentage of revenue may be generated locally. Such cases must involve operating activities that contribute to achieving lower utilities rates, better medical facilities, waste management, or lower food prices. In those situations, the taxpayer’s entire income will be taxed at a rate of 2% – regardless of whether it comes from local sales or export – while an exemption from import duties will also apply.

Special Zone in San Nicolas

Part of the beneficial tax policy involves the introduction, for a minimum duration of 10 years, of a Special Zone in San Nicolas. Companies that meet certain conditions and that conduct their activities in the San Nicolas district may be awarded “Special Zone Company” status. To this end, they must submit an application to the Aruba Financial Center (“AFC”), which will award the status after it has consulted the San Nicolas Business Association (“SNBA”). This status is subject to requirements in terms of:

- ▶ Investments: In principle a minimum investment of AWG 150,000 is required, though additional requirements apply in respect of hotels;
- ▶ Employment: The business must have at least 3 employees (FTEs) if its revenue is less than AWG 1 million, and must have three more employees for every additional AWG 1 million;

- ▶ Maintenance work on the business premises: A minimum of AWG 30,000 must be spent on maintenance over a period of 5 years

Businesses already based on the San Nicolas district may also apply for Special Zone Company status. Businesses that already existed on January 1, 2013 are deemed to satisfy the investment requirement. However, they must still meet the employment and maintenance requirements.

Special Zone Company status offers an extensive parcel of far-reaching tax advantages:

- ▶ A reduced rate for profit tax: The rate is 15% for activities aimed primarily at the local market, 10% for activities of which more than 75% is aimed at export and for hotels, and 2% for reinsurance companies, green energy, and agriculture. However, the reduced rate can only be claimed for green energy and agriculture if at least 75% of the taxpayer's revenue is generated locally;
- ▶ An exemption from dividend withholding tax;
- ▶ An exemption from BBO (sales tax) insofar as the operating revenue is realized from supplies of goods to other countries or from supplies of services to foreign businesses;
- ▶ A 50% discount on the land tax charge for a period of 5 years;
- ▶ The possibility that the Minister of Infrastructure will establish lower land value;
- ▶ The possibility that, if certain conditions are met, the Central Bank of Aruba will grant requests for exemption from foreign exchange commission for payments concerning other activities besides supplies of goods or services to domestic recipients;
- ▶ An additional investment deduction facility of 10%: This additional deduction is offered on top of the temporary investment deduction facility discussed above. Unlike that temporary facility, the additional investment facility is not contingent upon the operating asset being purchased from a local business. Businesses already based in San Nicolas that do not need to meet the investment requirement discussed above may only claim the additional investment deduction on investments in excess of AWG 50,000.

Expatriate facility

In connection with the desire to improve the climate for establishing businesses, a special facility will be introduced, effective January 1, 2013, under which highly-qualified expatriates are offered tax advantages. Expatriates who satisfy certain conditions are eligible for:

- ▶ tax-free remuneration of AWG 15,000 per calendar year;
- ▶ a tax-free allowance for school costs of AWG 25,000 per child per calendar year;
- ▶ a tax-free allowance for renting a home up to a maximum of AWG 2,500;

- ▶ a net wages arrangement, under which it is possible for the employer to pay the wage tax and income tax charge and the wages need only be grossed up once, unlike under the standard system.

Expatriates may opt for the expatriate facility if:

- ▶ they lived outside Aruba for a consecutive period of at least 5 years immediately before starting their work in Aruba;
- ▶ their gross annual wages are AWG 150,000 or more; they possess an expertise that is scarce or unavailable on the local labor market;
- ▶ they train a local employee during the period that they work in Aruba.

The last of these requirements does not apply in respect of expatriates who are directors/major shareholders.

On request, the expatriate facility may be applied for a maximum of four years. That period may be extended once by a further two years if reasonable proof can be offered that lack of the specific expertise on the labor market renders it necessary for the employment to continue. Requests for application of the expatriate facility must meet a number of requirements in terms of form.

The expatriate facility is also available to expatriates who are hired by companies that qualify for the modified IPC regime, the Free Zone, or the San Nicolas Special Zone.

Lower import duties on furniture and fittings

Hotels as defined in the Licensing Regulation (Vergunningsverordening) are offered incentives to furnish and refurbish their rooms. To this end, the import duties on furniture and fittings will be reduced from 22% to 12%. For purposes of the beneficial tax policy, furniture and fittings are understood to mean furniture, appliances, bathroom furnishings and fittings, and mattresses. It is unclear whether this is an exclusive list or meant simply as a series of examples. The lower rate for import duties is linked to a minimum expenditure of USD 10,000 per room on furnishings and refurbishments.

In principle, the lower rate for import duties should become effective on July 1, 2013. However, its introduction has been made contingent upon the introduction of an environmental tax on hotels, timeshares, and car rental on the same date. If that environmental tax is introduced on a later date, the lower rate for import duties will become effective on that later date also. As matters currently stand, the latter situation appears more probable.

Reinvestment reserve facility for timeshare resorts

Timeshare resorts are generally operated on a non-profit basis: their only object is to generate sufficient revenue to cover the costs in the longer term. As a consequence, in many cases no profits are recorded on which profit tax can be levied.

The beneficial tax policy provides for the possibility to add a surplus from a particular year to a “reinvestment reserve”. The amounts reserved must then be used within 10 years for maintenance work on the timeshare resort. Any reserved amounts that are not used for that purpose will be released and added to the resort’s income.

In principle this aspect of the beneficial policy will become effective on July 1, 2013 also, depending on the introduction of an environmental tax for hotels, timeshares, and car rental.

Reinvestment reserves formed in the past will similarly qualify for this facility.

Improved attachment-free base

The Tax Collector has the authority to levy attachment on the salaries of taxpayers who fail to pay their tax debts on time. As a consequence, employers in these situations must pay up to 1/3 of the employee’s salary to the Tax Collector, which sum is then deducted from the outstanding tax debts.

Effective July 1, 2013, that maximum will be lowered to 25% for incomes up to AWG 50,000 per year, and any income up to 90% of the net minimum wage must at all times remain free of attachment. The possibilities for levying attachment on alimony, child support, and pensions remain unchanged, however.

Further information about previously announced beneficial tax policy

Lastly, further information has been provided about the beneficial tax policy that was published at the beginning of this year and about which we sent you a newsflash on January 13, 2013.

The beneficial tax policy announced at the time provided for an increase in the reparation allowance from AWG 50 to AWG 100 per month for individuals receiving old age pension. This increase was made subject to the condition that the pensioner did not receive any other benefits or income. However, this condition has now been relaxed: the increased reparation allowance will be awarded also if the pensioner receives other forms of income, provided that that income is less than the old age pension.

In addition, further information has been published clarifying the conditions for commuting pensions at a reduced rate of 15%, as introduced on January 1, 2012. Additional details have been released also about the reduced rate of 2%, effective January 1, 2012, for import duties on specific energy-efficient appliances. However, a discussion of those conditions goes beyond the scope of this newsflash.

The information presented in this newsflash is of a general nature. For expert advice about the beneficial tax policy and how it will affect your specific situation, please feel free to contact one of the ATLAS tax lawyers.

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