Group of Companies – Taxation in Argentina

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1. CONCEPT OF "GROUP OF COMPANIES"

The concept of "group of companies" has been thoroughly and widely studied since the 19th century from a commercial law perspective, and groups of companies have received a specific tax treatment in Argentina as well as in other countries. From a commercial law viewpoint, some of the main concerns include the liability aspect, the characterization of groups, and the studies focusing first on groups of businesses and then on groups of companies. These studies concentrate mainly on the presence of a group of businesses or companies and the conditions under which several companies may be considered as being grouped around a common will and a common interest, thus resulting in a legal person or a de facto economic person having a diversity of legal structures and organized to accomplish a common purpose, which ultimately is a single one.

Just as there are legal entities that are not business enterprises, there are business enterprises that are not legal entities. Associated businesses, their legal and/or economic independence, and their many manifestations in reality make it difficult to characterize groups of companies as a single economic unit. Consequently, there are usually serious characterization difficulties in the area of antitrust law.[1]

In tax law, commercial law perspectives are useful to characterize groups of companies which constitute a unit. Groups of companies forming a single business are tools helpful to determine the relationships among the members of a group, whether they are companies or businesses of the same economic group, and thus whether it is necessary to give the group a specific treatment suiting its reality, so as to adjust the tax results of its operations to that reality. Each group of companies is considered to form one economic unit and is therefore treated as a single company.

More specifically, one of the main areas under discussion is whether companies in the same group can offset their profits and losses to arrive at a result that consolidates their various partial positive and negative results, as would occur with different divisions of the same company. Another area under discussion regarding the various laws on groups of companies is the tax impact of intra-group transfers of assets. Under many laws, intra-group transfers of assets imply a deferral of the tax on the gains until the assets are alienated or simply leave the group as a result of a transfer to a third party.

We can say that, from the perspective of Argentine law, the economic reality of groups of businesses or companies and the legislative acceptance of such groups are key underlying factors. Indeed, accepting that the losses of a group's business unit can be offset against the profits of another business unit in the same group implies that the group's taxable capacity is determined as if it were a single taxable person. Of course, for this to happen, the conditions normally set by law for such a consolidation must be met.

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1. In view of these phenomena, an Argentine author has studied this subject exhaustively and has made some reflections that are worth citing (author's translation):
"(i) After reviewing the opinions of legal scholars on the subject, we have in our hands a notion of economic science and reality that is almost impossible to grasp, although anyone, whether a legal expert or layman, believes that he or she knows what the concept of 'business' means.
(ii) None of the countless authors who have written on this subject ... has been able to provide specific guidelines for qualifying as a business a productive unit based on a specific level of complexity or a certain size.
(iii) It has been impossible to reach agreement on a precise and universally valid definition of the concept of business.
(iv) ... from the now classic proposal of considering the group as a single business with a plurality of subjects – which does not grant legal personality to the group itself – to the notion of not considering that there are agreements between companies that could violate antitrust laws when the parties to the agreements are companies forming part of a single group since those companies would not meet the requirement of being autonomous from an economic, financial and/or decision-making viewpoint."

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This is also true of deferring the tax on the gains from the transfer of intra-group assets until they are transferred to third parties. While the assets circulate within a group of companies, there is no actual circulation of the gains, and therefore it does not seem timely to tax them.

When, as in Argentina, there are no specific rules authorizing the offset of profits and losses and if, instead of two separate companies in a group, there are two divisions in the same company, tax costs could result from adhering to the formal aspects of the group's legal structure, e.g. the independence of companies as legal entities.

The tax costs mentioned above also result when intra-group transfers of assets are considered to be taxable transactions because it is not taken into account that the transferor does not generally realize actual gains since the gains are offset against the deductible disbursement of the other company forming part of the same group of companies. To avoid such tax costs, tax planning decisions are implemented that are not always the best option for the companies from an economic perspective.

Any obstacle to intra-group transactions within a country, justified or motivated by the aim to prevent evasion tactics, results in higher business organization costs and in less flexibility, which are keys to optimizing profits and eventually improving tax collections. But the fact that Argentina has no specific rules recognizing these effects on groups of companies, a topic discussed at the 2004 IFA Congress in Vienna,[2] should not lead to the conclusion that Argentina's legislation has ignored this phenomenon. Quite the contrary, there are countless provisions on matters stemming from relationships among companies in the same economic group. This has given rise to a rich set of rules and legal institutions, as well as many court decisions and works of legal scholars, to which this article refers briefly.

2. MAIN TAX-RELATED TOPICS UNDER ARGENTINE LAW

2.1. Tax treatment of losses

This section considers the tax treatment of a company's losses and the legal possibilities of offsetting the losses against the profits of another company in the same economic group.

The tax losses of a company in a given year may be accumulated and carried over and offset against the same company's gains in a later year. If after the end of the fifth year from the year in which the losses were incurred, they have not been offset against gains, the right to offset is lost.[3]

Therefore, it is not possible to transfer losses to another business or company in the group and offset them against the gains derived in the same year; thus, the parent company may not report income on a consolidated basis with its subsidiaries and affiliates. Only as a result of a company's restructuring can accumulated losses be transferred to other companies; the losses can then be treated as an income deduction for the remaining portion of the five-year period following the year in which the losses were incurred.

The options available under the Income Tax Law (ITL) of Argentina are discussed below.

2.2. Merger of companies

Mergers are regulated by Sec. 77 ITL and Sec. 105 of the ITL Regulatory Executive Order (REO). A merger is defined as (i) an amalgamation of two or more corporations where both are dissolved (without liquidating) to form a new corporation or (ii) the absorption of one company by another. Both the ITL and REO establish a number of requirements designed to prevent tax-free restructurings from being used for the exclusive purpose of obtaining tax benefits. Originally, some of these requirements were included only in the REO, resulting in regulatory excesses that made the rules unconstitutional. These regulations, however, were later added to the amended text of the ITL, including them as valid provisions in a sort of ex post facto delegation of rights to the administering authority.

The ITL and REO requirements applicable to mergers are:

(a) The business of the restructured companies or of a supplementary company must be continued by the surviving companies for at least two years after the restructuring date.

2. See García, Fernando Daniel, Branch Reporter for Argentina on Subject II: Group taxation, in *Cahiers de droit fiscal international*, Vol. 89b (2004), at 99 (58th Congress of the International Fiscal Association, Vienna, 2004).

3. Sec. 19 (Offset of losses against gains) of the Income Tax Law provides as follows (author's translation): "To establish the total net profits, the net results obtained in the year shall be offset within each and between each category.

When in a given year a loss is recognized, such loss may be deducted from the taxable profits obtained in the immediately following years. After five years from the one in which the loss was recognized, no deduction can be made of any remaining portion of that loss in subsequent years.

For purposes of this section, the amounts authorized by law to be deducted under the concepts indicated in Section 23 are not considered to be losses.

Losses shall be updated by applying the variation of the wholesale price index, general level, as published by the National Institute of Statistics and Censuses, taking place between the closing month of the year when losses were incurred to the closing month of the year when they are settled.

Notwithstanding the provisions of the above paragraphs, losses resulting from the disposal of shares, quotas or ownership interests in companies, including ownership shares in mutual funds, of the individuals and companies referred to in Sections 49(a), (b), (c) and last paragraph, can only be offset against the net gains resulting from the disposal thereof. The same limitation applies to individuals and estates with respect to losses stemming from the disposal of shares. Losses from activities not to be considered of an Argentine source can only be offset against profits of that same nature.

If the offset described in the above paragraphs cannot be made in the year the loss was incurred, whether in full or in part, the amount that remains to be offset, updated in the manner prescribed herein, can be deducted from the net gains generated from the same type of transactions and activities obtained in the immediately following five years. Also, losses arising from the rights and obligations resulting from derivative instruments and/or contracts, except for hedging transactions, can only be offset against net profits from that type of rights within the year the losses were incurred or in the immediately following five years.

For purposes of the provisions set forth in the above paragraph, a transaction or contract involving derivative products shall be considered as a 'hedging transaction' if it seeks to reduce the impact of future prices or market rate fluctuations on the results of the main economic activity or activities."

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(b) The shareholders of the merging companies must keep, for a period of at least two years from the restructuring date, an ownership interest not less than the interest they held on that date in the equity of the surviving company or companies. This requirement does not apply if the surviving company's or companies' shares are listed on self-regulated stock markets, which listing must be maintained for a period of at least two years from the restructuring date.

(c) The REO requires, among other things, that, for the merger to be effective in the event of a consolidation (i.e. when two or more companies are dissolved to set up a new company), at least 80% of the new entity's equity at the time of the merger must be held by the shareholders of the preceding companies; in the case of incorporation or absorption, the value of the ownership interest to be held by the shareholders of the incorporated company or companies in the equity of the incorporating company must represent at least 80% of the incorporated company's or companies' equity.

(d) On the restructuring date, the companies being restructured must be a going concern. This requirement is satisfied (i) if the companies are engaged in the business identified as their corporate purpose or (ii) if the companies are no longer in business, they stopped doing business within 18 months before the restructuring date.

(e) For a period of at least two years from the restructuring date, some of the businesses of the restructured company or companies or other companies related to them must continue to be developed (continuity of the company's operation in the same industry) so that the goods or services manufactured, marketed or provided by the surviving companies have essentially the same characteristics as those manufactured, marketed or provided by the merging company or companies.

(f) The companies must have developed identical or related businesses during the 12 months immediately preceding the restructuring date or the cessation of business if the cessation occurred within the period established in 1., or, in both cases, during the period of their existence, if shorter. A related business is defined as any business supporting or adding to an industrial, commercial or administrative process or having a purpose or end relating to the other business (horizontal and/or vertical integration).

(g) The restructuring must be reported to the Federal Administration of Public Revenue, *Administración Federal de Ingresos Públicos* (AFIP), and the applicable requirements must be satisfied within the time frame determined by the AFIP.

(h) For the restructuring to have the anticipated tax consequences, the publication and registration requirements in the Business Companies Act No. 19,550, as amended, must be met.

(i) In the case of a partial transfer of assets, authorization must be obtained from the tax administration.[4]

Going back to transfers of accumulated losses, the ITL was amended in 1999 to add a specific requirement applicable to such transfers. The purpose of the amendment is to prevent restructurings whose sole purpose is the transfer of losses. This requirement is discussed below (see 2.5.).

2.3. Break-up of companies

Transactions involving the break-up of companies can also result in the possibility of transferring a loss to one of the new companies. Commercial law experts have coined specific terms for the various cases of company break-ups. According to the REO, company break-ups are classified as follows:
- spin-off and merger: when some the assets of a corporation are transferred to an existing corporation;
- partial merger: when a corporation, together with another corporation, sets up and funds a new corporation;
- split-off: when some of the assets of a corporation are transferred to create a new corporation; or
- split-up: when a corporation is divided into new corporations which are legally and economically independent.

Although the REO has taken the terminology from the Business Companies Act, these rules also apply to businesses and business associations, not just to companies.

The ITL establishes the same tax requirements for company break-ups as for mergers.

2.4. Sales and transfers within the same economic group

2.4.1. Sale and transfer as a restructuring

The type of restructuring involving sales and transfers within the same economic group was added to the ITL by Act No. 18,527. Although some writers do not regard this as a form of restructuring, in this author's opinion, it is indeed a restructuring since the transfer of assets and liabilities from one company to another belonging to the same economic group implies precisely the restructuring of a business or company without an actual transfer of equity or wealth.

These sales and transfers have been considered as the transfer of a legal universality in some cases and a divestiture of a factual universality in others. According to Asorey,[5] the transfer of assets could be considered as partial, not necessarily as the transfer of a universality. The legislation recognizes these transactions as a restructuring because they are carried out by an economic group. Asorey's interpretation[6] was later confirmed by Act No. 21,604, which abolished the expression "going concern".

4. It must be noted that, except for the requirements relating to going concern and identical or related business, which for now do not apply to transfers within the same economic group (although certain opinions of the AFIP seem to indicate otherwise), the other requirements are applicable to the three restructuring arrangements dealt with in the ITL.
5. Asorey, Rubén O., *Business Restructurings* (La Ley, 1999), at 94 et seq.
6. Id.

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This author shares this interpretation, although recent opinions of the AFIP have not upheld this view.[7]

The General Tax Bureau, predecessor of the AFIP, had accepted the transfer of particular assets between entities within the same economic group. This has been accepted by legal scholars as well.[8]

Even if the most restrictive opinions are disregarded, not all transfers of assets between companies can be qualified as a business restructuring. It is therefore reasonable that, in those cases, authorization should be obtained from the AFIP. The reason is that, in certain cases, the assets, including a partial transfer thereof, could be so significant for business continuity that, if the assets are transferred to another company or business, the transfer could amount to a restructuring of the transferor.

The mere transfer of a single asset, such as an industrial plant or commercial warehouse, no matter how significant the asset, does not, however, necessarily amount to the restructuring of a company. This is precisely what, in this author's opinion, the AFIP should assess when deciding whether or not to authorize a partial assignment of assets.

2.4.2. Tax requirements applicable to sales and transfers

In reorganizations involving sales and transfers within the same economic group, the requirements mentioned above regarding mergers must be satisfied. For example, the business of the preceding company must be maintained, and the shareholders or members of the preceding company must hold at least 80% of the equity held therein for two years following the transfer.

This requirement makes sense as the entity at issue is an economic group. The regulation provides a definition of economic group for sales and transfers and specifies that "eighty per cent (80%) or more of the surviving entity's equity must be held by the owner, members or shareholders of the company being restructured. Further, at the time of the transfer, they should maintain individually in the new company at least eighty per cent (80%) of the equity they held on that date in the preceding entity".

As is appreciated, the requirement in this case is twofold: (a) 80% of the surviving entity's equity must be held by the owners, members or shareholders of the preceding entity, and (b) they must individually hold at least 80% of the equity they held in the preceding company.

The publication and registration requirements set forth in the Business Companies Act apply to mergers and break-ups, but they do not apply to transfers within the same economic group. The publications required by Act No. 11,867 for the transfer of going concerns seek to protect the creditors of the selling entity and, if the publications are not made, the buyer is jointly and severally liable for the debts of the going concern before the transfer. In this case, as the transfer is a transaction within the same economic group, the liability for the debts of the preceding company is obviously maintained within the group. The AFIP, however, has declared certain restructuring processes ineffective if the taxpayer failed to publish the required legal notices because they were considered unnecessary.

The requirement the AFIP seeks to enforce is not based on reasonable grounds; the AFIP's sole purpose is to tax a transaction that was previously considered to be tax free. Regarding transfers of assets and liabilities within the same economic group, no interest is left unprotected if the legal notices are not published. Neither the creditors nor the tax authorities, which in any event must be informed as required by Resolution 2,245, are adversely affected, and both entities are liable as they belong to the same economic group.[9]

Some requirements do not apply to sales and transfers. In accordance with Sec. 105 REO, it is not required that the companies be going concerns at the time of the restructuring or that they be engaged in identical or related businesses. In any case, the new opinions issued by the AFIP on these issues should be closely monitored as there was recently an increase in the requirements supposedly resulting from anti-evasion efforts, which (requirement) had not been imposed for decades (AFIP Ruling DAL 62/2002).

2.5. Transfer of tax rights and obligations

The transfer of tax rights and obligations is one of the most significant effects of a restructuring. The transfer of losses is perhaps the most important effect for companies and obviously for the tax authorities. In the case *Papelera Pedotti S.A.*,[10] the Supreme Court upheld the transfer, and the minority held that, even before Act No. 18,527, the transfer should have been authorized because it shared the same legal status as a merger. Giuliani Fonrouge and Navarrine arrived at the correct conclusion when stating that such a transfer is inherent in the conveyance of a legal universality.[11]

In the case of a merger, it may not be necessary to enact a special rule, given the nature of mergers and the effects of mergers recognized in the Business Companies Act. The generic transmission is expressly mentioned in the regulations. Some of the rights are listed in Sec. 78 ITL. They are transferred in proportion to the equity transferred and, in company break-ups, they are based on the value of the assets transferred.

According to Sec. 78 ITL, the rights and obligations transferred include:

(a) *Accumulated unbarred tax losses*. This applies only to corporations as they are taxable persons. This is not the

7. See AFIP Ruling DAL (Legal Advisory Direction) Opinion 31/2003, which clearly states that a transfer within the same economic group must be that of a going concern in order to be treated as a tax-free business restructuring.

8. See Raimondi, C.A. and A. Atchabahian; see also Krause Murguiondo, G.; and "General Tax Bureau Opinion *Sofitur S.A.*", D.A.T. (Technical Advisory Direction), August 1978.

9. AFIP Ruling DAL 62/2002 states that the publication requirement must be met.

10. *Papelera Pedotti S.A. v. Fisco Nacional* (Supreme Court), 143 *Rev. La Ley* 145, at 143-145.

11. Giuliani Fonrouge, C.M. and S.C. Navarrine, *Tax Procedure* (Desalma, 6th ed.). On this subject, see General Report, in *Cahiers de droit fiscal international*, Vol. 24 (1953) (Congress of the International Fiscal Association, Paris, 1953). The system's neutrality was recommended at the IFA Congresses held in Paris in 1953 and in Brussels in 1952.

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case with partnerships, where the individual members are the taxpayers.

Asorey[12] holds that, if the fiscal year is irregular in length, the deduction for the loss existing at year-end is not subject to a proportional calculation based on time. According to Argentine law, if all of the fiscal requirements are met, losses are transferred without prejudice as to whether the new entity or the old entity incurred them.

After the enactment of Act No. 25,063 in 1999, the transfer of losses and unused tax incentives must satisfy a new requirement. The last paragraph of Sec. 77 ITL provides (author's translation):

> ... accumulated unbarred tax losses and unused tax incentives resulting from the special promotional systems referred to in Section 78(1) and (5) can only be transferred to the new company or companies if the shareholders of the preceding company or companies show that they have maintained, for a period of at least two (2) years before the restructuring date, or if applicable, from its incorporation if such circumstance covers a shorter period, at least eighty per cent (80%) of their ownership interest in those companies, unless they list their shares on self-regulated stock markets.

This rule was enacted in an effort to prevent restructurings whose sole purpose is to transfer losses from troubled companies to profitable ones so that the losses can be charged against the taxable income of the healthy company. The requirement of maintaining a certain shareholding or equity interest for two years before the restructuring date poses a very serious obstacle to many restructurings with genuine business purposes. The two-year period, if required as a test or evidence that the restructuring is not geared only to obtain a tax benefit, should be much shorter, as nowadays businesses or companies have much greater mobility. A two-year period is too long in this new scenario, and it has an unjustified adverse impact on the intended effect of restructurings.

(b) *Balances of tax incentives or unused special deductions due to limits on the amount deductible each year, which may be carried over to the following year.* The idea is that the benefits outstanding (if any) should not be adversely affected because of the restructuring. This author agrees with Asorey that the rule is comprehensive enough to allow the enjoyment of any tax benefit even if it does not result from the ITL.

(c) *Undeducted deferred charges.* After the restructuring, the estimated expenses for future years may continue to be deducted. These charges could actually be transferred simply because they are part of the continuing company.

(d) *Outstanding tax incentives to which the preceding company or companies was/were entitled as a result of special promotional programmes, provided the basic conditions taken into account when the incentives were granted continue to exist.* The agency reviewing the application should decide this specific item. The provincial authorities have already approved mergers of companies included in promotional programmes. In some cases, prior approval should not be required, and a mere notice should suffice.

(e) *Tax valuation of fixed assets, inventory and intangible assets, notwithstanding the value assigned to them for purposes of the transfer.* It is a right and duty to take the tax valuation of the assets transferred in a restructuring even if the market value considered for purposes of the restructuring is different. In these cases, no tax is levied on the differences in value.

Depreciation of the surviving entity's assets depends on their tax value; therefore, those values cannot be altered by the mere fact of the restructuring.

(f) *Returns to the tax balance from the sale of assets or an inventory reduction when tax incentives were used or the tax value of assets was reassessed by the preceding entity to the extent possible under the applicable laws.*

(g) *Depreciation schedule for fixed and intangible assets.*

(h) *Computation of the periods referred to in Sec. 67 ITL when the tax treatment depends on them.* This is the option of recording the profits from the sale of an asset at its replacement cost.

(i) *Recording of legally deductible provisions.*

In the author's opinion, transfers of tax rights and obligations are clearly to be included in the overall concept of business continuity. To the extent that recording or depreciation systems differ from those applied by the preceding companies, a particular system should be chosen in the first year after the restructuring.

The discussion so far has described in detail the rules governing the restructuring of companies in Argentina, but without considering the various conflicting aspects arising from the opinions issued by the AFIP (because they are outside the scope of this article). It is clear that, through these business restructurings, losses can be carried over and set off against future taxable income, provided each and every requirement of form and substance is met – requirements designed to prevent restructurings whose sole purpose is to take advantage of the "benefit" of setting off the losses of one company against the profits of a related company.

3. INTRA-GROUP TRANSFERS OF ASSETS

Another main topic in the "group of companies" concept from a tax law perspective is the treatment of intra-group transfers of assets. Many countries consider that, as long as the assets in question are not transferred outside the group of companies, no tax should be levied because the transfer is between related companies. Only when assets are transferred to third parties are the profits from the transfer (i.e. the difference between the sales price and the acquisition price) taxed, charging the first transaction (the purchase) against the last one (the sale).

Under Argentine law, pursuant to Sec. 77(c) ITL, "the sales and transfers between two entities which, although legally independent, constitute a single economic group"

12. See Asorey, supra note 5.

are comprised in the concept of business restructuring (tax-free transaction). That is, in principle, to the extent the restructuring is effected, assets can be transferred within the group without any tax impact.

It should be taken into account, however, that pursuant to Sec. 77(5) ITL, "when due to the type of restructuring no total transfer of the restructured company or companies takes place, except in the case of a company break-up, the transfer of tax rights and obligations shall be subject to the prior approval of the General Tax Bureau". This rule seems to indicate that the full effects of a tax-free restructuring apply only to total company transfers, i.e. all assets and liabilities are transferred, and do not apply to partial transfers.

In any event, it is important that what is subject to the approval of the tax administration is the transfer of the disposing company's rights and obligations to the acquiring company, but nothing seems to contradict the exemption resulting from Sec. 77(1) ITL. Of course, it should always be a business restructuring; therefore, in the author's view, the exemption will be applicable based on the nature of the assets being transferred. That is, if only one or some assets are transferred (instead of the whole business), whether or not the results of the transfer will be subject to tax depends on the extent to which it is a true restructuring and on whether the legal and regulatory requirements are met. If only isolated assets are assigned or transferred and the assignment or transfer does not indicate a business structuring, the results of the transfer will undoubtedly be subject to tax, even if the transfer is an intra-group transaction.

If it is considered that a restructuring, although partial, has indeed taken place, the transfer of rights and obligations resulting therefrom must be approved by the AFIP. If approval is obtained, the results of the transfer are exempt from tax.

In the past, the commercial courts have repeatedly decided whether a transfer of a going concern had taken place, even if only some assets had been transferred. In cases where the assets transferred represented an activity or business, i.e. if, without the assets, the activity or business could not be pursued by the same legal entity, the transfer was considered to be of a going concern. This same criterion can be applied to partial transfers of assets, and possibly of liabilities, to determine whether or not a business restructuring has occurred.

4. OTHER TAX ASPECTS OF GROUPS OF COMPANIES UNDER ARGENTINE LAW

4.1. Transfer pricing and thin capitalization

Exchanges of goods and services between the various business units of a company, if done internationally, are treated under Argentina's transfer pricing system, in force since early 1999, pursuant to Act No. 25,063. Before this Act, the economic relations between related companies whose transactions extended beyond Argentina's national borders were governed by Secs. 8 and 14 ITL. Sec. 8 established how to determine the Argentine source in cross-border export and import transactions between independent parties; the price was adjusted, if applicable, if a relationship was assumed to exist between the parties.

Sec. 14 regulated the benefits enjoyed by local companies with foreign capital in their economic relations with their parent or holding companies. In general terms, the local companies were considered to be separate entities as long as the transactions were at arm's length and, when technology transfers or loan agreements were involved, special rules applied within the broad concept of financing (former Sec. 14 ITL). In these cases, companies resorted to the National Institute of Industrial Technology for technology transfers, technical assistance and brand licences and to the Central Bank of Argentina for financial services.

These issues are today regulated by the ITL through the rules applicable to transfer pricing (Secs. 14, 15 and 15.1 ITL) when goods and services are exchanged and through the rules applicable to financing between related companies which together fall within the thin capitalization concept (Sec. 81(a) ITL). For transfer pricing, see the article by Cecilia Goldemberg, in this issue of the *Bulletin*.

4.2. "Substance over form" and concept of "economic group"

In the local context, other concepts prevail, such as "substance over form" as a method of legal construction and the "economic group" concept as a derivative thereof.

Many years ago, the Supreme Court of Justice of Argentina rendered an interesting decision in which it adopted an unusual solution in a tax matter. It is difficult to know whether, if faced with the same controversy today, the Supreme Court would apply the same criterion. At that time, the Supreme Court accepted that the economic group concept with tax effects could be alleged by Kellogg Co. Argentina, a local company with foreign capital, in its dealings with a related branch through which the company distributed its products in Argentina. The local company calculated its profits using the economic group theory and consolidated the profits and losses of both related companies. The tax authorities rejected this approach even though it was precisely the same criterion the tax authorities applied to object to the deductions for payments made for various reasons by the local company to its parent company abroad. Thus, the criterion established for the relationship between the local company and its parent company abroad was not applied with respect to the related branch in Argentina.

Using the "substance over form" method of construction, i.e. the economic substance prevails over the legal form of two distinct legal entities, the Supreme Court sustained the position of the local company. To deny the deductions, the tax authorities claimed that the economic group concept should be used for payments to a foreign company, but should not be used in a similar relationship with a local related company.

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The Supreme Court ruled that, for tax purposes, Kellogg Co. Argentina could consider itself included in an economic group at a domestic and international level. In connection with this and regarding the subject being discussed, some of the Supreme Court's grounds are worth noting (author's translation):

> ... renewed prevalence is given to the assertion that, also within our territory, only the transactions carried out between a group and third parties involving the actual movement of goods increasing or decreasing the group's assets have relevance and tax effects. And for that purpose, the company that entered the transaction from a legal and accounting perspective is not what interests us the most; rather, the form adopted to fulfil the transaction does. (*Supreme Court Decisions*, Vol. 287 at 79)

If the criterion used in this decision still applied today, the conclusion to be drawn would be that companies based in Argentina, in their relations with their parent or holding companies, affiliates and subsidiaries abroad, must comply with the transfer pricing and thin capitalization rules. Conversely, in their domestic relations, the tax authorities should not raise any objections if companies based in Argentina behave as members of an economic group and if the economic reality of their transactions indicates that, regardless of the legal independence of two distinct legal entities, their results belong to a single company, a single interest and a single economic group.

In this author's opinion, despite the full effect as a precedent of the *Kellogg* decision, which so far has not been modified by another ruling, the Argentine tax authorities will find various ways to raise objections to the results of companies belonging to a single economic group but operating under separate legal forms. This has in fact occurred, and it has brought about interesting and somehow novel case law by the Federal Tax Court; see the *Fiat Concord* and other cases discussed below.

The ITL has a rule, Sec. 73,[13] according to which the transfer of funds or goods in favour of third parties which is not made in the interest of the company making the transfer will be considered as generating taxable income equivalent to an interest rate not lower than the rate applied by the Central Bank of Argentina for discount operations. The key concepts for applying this rule are: (a) transfer of funds or goods by companies or businesses, (b) in favour of third parties, and (c) not made in the interest of the company. These features create a presumed interest rate.

This premise shows a rule that relates, not to transactions between related companies, but to transactions with third parties. In the case discussed below, the tax administration denied the relationship between companies in the same group to which funds were transferred or which obtained financing even when evidence of the relationship was given. The tax administration thus maintained the concept of separate companies within a group, forgetting the lesson of the well-remembered *Kellogg* case.

Regarding the Federal Tax Court's position in the *Fiat Concord* case,[14] it should be explained that the Court held that Sec. 73 ITL did not apply. In the situations covered by Sec. 73, it is presumed, without allowing proof to the contrary, that there is taxable income consisting of the presumed interest. In *Fiat Concord*, the financing provided by a company to another company within the same group was held not to be taxable because the judge was not faced with a transaction involving a third party, which undoubtedly must exist for Sec. 73 to apply. This means that, in this case, the Federal Tax Court, just as the Supreme Court had done over 15 years earlier, made economic substance prevail over form, recognizing the existence of the group rather than the legal form it adopted, which consisted of separate legal entities.

The same criterion was applied by Division D of the Federal Tax Court in *Lavadero Virasoro*[15] and followed by Division C of the same Court in *Agropecuaria KKHA TU S.A.* (ruling dated 29 June 2004, in *Lexco Fiscal*). There was, however, a decision in the opposite direction, with a 7% interest rate agreed in favour of the creditor, in *Supercanal Internacional S.A.*, heard by Division C (ruling dated 20 September 2004, in *Lexco Fiscal*). It is still not known what criterion will be adopted by the appellate court, that is, the Federal Court of Appeals for Administrative Litigation Matters and, if the occasion requires, the Supreme Court.

4.3. Presumptive alternative minimum tax – double taxation of intra-group financing

The presumptive alternative minimum tax is levied on the assets of any type of business organizations (e.g. companies, associations and sole proprietorships) and is estimated at year-end in the manner prescribed by law. The liabilities of a business organization are disregarded, and the taxable base therefore consists of the organization's gross assets, not its net assets or net worth. This constitutes a tax penalty on the transactions between companies of the same economic group if they are resident in Argentina. Indeed, a financial loan or a loan for the sale of goods between two related companies implies some sort of double taxation for the consolidated group because the seller considers the loan an asset and the buyer considers ownership of the goods an asset, while the liability arising from the amount owed, which is the buyer's liability, cannot be charged against the value of the goods.

This effect, resulting from the method of computing the taxable base of this rudimentary tax which is levied on assets even when no profits are obtained, also penalizes the transactions between members of a group of companies if they are resident in Argentina.

13. Sec. 73 provides (author's translation): "Any disposal of funds or assets in favour of third parties by the subjects comprised in Section 49(a), which does not correspond to transactions carried out in the company's interest, shall raise the presumption, without allowing proof to the contrary, of taxable income equal to an interest rate with annual capitalization that shall not be less than the one established by the Central Bank of Argentina for discount operations or an update equal to the variation of the wholesale price index, general level, plus an interest rate of eight per cent (8%) per annum, whichever is the highest.

The preceding provisions do not apply to the deliveries made to their shareholders by the companies listed in Section 69(a)(2). Neither shall they apply when Section 14, paragraphs (3) and (4) are applicable."

14. *Fiat Concord S.A.*, Federal Tax Court, Division D, 16 October 2002, *Revista Impuestos 2003-A*, Issue No. 1 at 39.

15. *Lavadero Virasoro S.A.*, Federal Tax Court, Division D, 10 July 2003, *Lexco Fiscal*.

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4.4. Group of companies – VAT and excise taxes

Secs. 43(1) and (3) of the Value Added Tax Act[16] establish that exporters may charge any tax to them invoiced on assets, services and leases actually used for export purposes or used in any of the stages of the export process against the tax owed on their taxable transactions as long as the tax is connected to export operations and has not been used before by the taxpayer. In addition, when the "substance over form" concept indicates that the exporter enjoying the VAT exemptions in the domestic market is the beneficiary of the treatment, the estimate, return or transfer should not exceed the amount to which the latter would have been entitled, no matter who the exporter was.

On the other hand, Sec. 76 of the VAT Regulatory Decree establishes (author's translation):

> For the purpose of Section 43(3) of the Act, it will be presumed, without allowing proof to the contrary, that the situation described in the Act arises when the beneficial owner of the tax exemption system in the domestic market is exporting through individuals or companies that may from an economic perspective be considered related to the beneficial owner. Such relation may arise from capital origin, actual management of the business, profit distribution or any other circumstance constituting evidence of an economic group. Moreover, it will be assumed that there is such a relationship – unless proof to the contrary is provided – when all or certain categories of the operations of the beneficial owner are absorbed by said exporter or when nearly all or certain categories of the purchases of the exporter are made to the beneficial owner.

Thus, the VAT exemption does not apply in cases where a related intermediary is involved in export operations. This situation has created a new body of rules on transfer pricing in the VAT Act (which is beyond the scope of this article).

As to excise taxes and their relation with groups of companies, Secs. 77(2) and (3) of Act No. 3,764, as amended, should be mentioned. The wording of the rule is (author's translation):

> ... When the taxpayer effects its sales through individuals or companies that may from an economic perspective be considered related to the taxpayer by virtue of the capital origin, the actual management of the business, the profit distribution, or of any other circumstance, the tax to be paid shall be assessed based on the highest sales price obtained. The tax authority may also demand payment from those other individuals or companies as well as fulfilment of all provisions of this Act.
>
> The economic relation will be assumed, unless proof to the contrary is provided, when all or certain categories of the operations of the taxpayer are absorbed by the other companies or when nearly all or certain categories of the purchases of the latter are made to the same taxpayer.

This is one of the oldest rules embracing the economic group concept. It was later followed by the Sales Tax Act, predecessor of the VAT Act, which also levied the tax on the first sale of goods, that is, when goods came out of the manufacturing plant. Therefore, the law had to prevent the typical manoeuvre of keeping the taxable price low in the first sale and applying the market price later when the goods left the group to be sold to third parties.

4.5. Group of companies – gross income tax

The gross income tax is a local tax, not a federal tax, levied by the provinces and the City of Buenos Aires. The tax is levied on the gross income (taxable base) derived from commerce, industry, services and any other regular activity carried out for valuable consideration (taxable event) and also provides rules relating to groups of companies. In fact, the law applicable in the City of Buenos Aires expressly denies recognition of the concept of "groups of companies" with respect to transactions between related companies. Sec. 131 of the law states: "Any transactions between entities that are separate from a legal standpoint shall be subject to the tax even if they belong to the same economic group."

This means that the fact that there is a group of companies or an economic group cannot be alleged to avoid the tax on sales or transactions between the group members. The cascading effect of the tax results in double taxation for the group. This is why a vertical scheme or organization of companies in the same group is usually avoided. The tax cost resulting from the mechanics of the gross income tax is so high that any restructuring along those lines is unacceptable.

As a final statement, under Argentine tax law, the group of companies concept is a long-standing one, but it has always been recognized or denied depending on what position led to higher taxation. In other words, there has been no stimulus in Argentine legislation for groups of companies or businesses as such, and they have been treated mistrustfully having, in general, been penalized from a tax viewpoint.

16. Art. 43 provides (author's translation): "Exporters may charge any tax to them invoiced on assets, services and leases actually used for export purposes or used in any of the stages of the export process against the taxes owed for their taxable transactions as long as the tax is connected to export operations and has not been used before by the taxpayer, as well as any corresponding update thereof, calculated by applying the wholesale price index, general level, of the month of the invoice, according to the table prepared by the Federal Administration of Public Revenue, which is an autonomous entity within the scope of the Ministry of Economy, for the month when the export is made. ...

When the 'substance over form' concept indicates that the exporter that is enjoying VAT exemptions in the domestic market is the beneficiary of said treatment, the estimate, return or transfer should not exceed the amount to which the latter would have been entitled, no matter who the exporter was."

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