Transparency Regime

The Fundamentals

Aruba exempt companies (AVV), corporations (NV), and the limited liability company (VBA), can opt to become transparent, i.e. for corporate income tax, individual income tax and dividend withholding tax purposes the AVV, NV, or VBA is treated as a partnership. In case the AVV, NV, and VBA has foreign shareholders, the shareholders will only be subject to Aruba taxes if the shareholders have a taxable presence on Aruba via either a permanent establishment or a permanent representative, or perform one or more relevant activities.

Summary of the changes per 2019

The most important changes per January 1, 2019 are the following:

I. A permanent establishment is deemed present for corporate income tax purposes when one or more of the relevant activities are performed as mentioned in the State Decree.
II. If one or more of the relevant activities are performed, the substance requirements apply. We note that the substance requirements have been very broadly defined and may result in discussions with the tax authorities.
III. If the transparent entity does not meet its obligations, the fiscal transparency will be revoked per the beginning of the financial year in which the obligations are no longer met. However, the former sanction of the transparent entity becoming subject to 150% times the normal corporate income tax rate has been abolished.

Permanent establishment or permanent representative

A permanent establishment is deemed present for corporate income tax purposes when one or more of the relevant activities are performed as mentioned in the State Decree

A permanent establishment is otherwise deemed present in case of (i) a permanent representative or (ii) a foreign enterprise which builds, installs, maintains, cleans or repairs capital assets (whether movable or immovable) on Aruba for more than 30 days. Included in these 30 days are e.g. the technical preparation and cleaning up of the site. If the fiction does not apply, the commentary to article 5, paragraph 3, OECD model convention will be used to determine if a permanent establishment is present.

If a permanent establishment or permanent representative is (deemed) present, the corporate income tax rate on the profits is 25%.

Relevant activities

The State Decree appoints the following relevant activities that will need to meet the substance requirements:

a. Head Office, i.e.:
   1. Taking relevant management decisions;
   2. Making costs on behalf of related entities;
   3. Coordinating activities of related entities.
b. Distribution and other services, i.e.:
   1. Transport and storage of goods;
   2. Managing stocks;
   3. Taking orders;

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    4. Advisory and other administrative services.

c. Financing and lease, i.e.:
    1. Agreeing to financing terms;
    2. Identifying or acquiring of assets intended for leasing out;
    3. Determining conditions of lease and lease terms;
    4. Monitoring and revision of lease agreements;
    5. Controlling and managing risks.

d. Wealth management, i.e.:
    1. Taking decisions relating to movements in investment portfolio’s;
    2. Calculating risks and reserves;
    3. Taking decisions relating to currencies, interest fluctuations or hedging positions;
    4. Preparing regulatory and other reports on behalf of governmental institutions or investors.

e. Banking, i.e.:
    1. Acquiring monies, managing risks, including credit risks, currency risks and interest risks;
    2. Taking hedging positions;
    3. Providing loans, credit facilities or other financial services to clients;
    4. Meeting regulatory capital requirements as well as regulatory reporting and returns.

f. Insurance, i.e.:
    1. Determining and calculating of risks;
    2. Insurance or reinsurance of risks and providing insurance services to customers.

g. Shipping, i.e.:
    1. Organizing crews, including hiring, payment and supervision thereof;
    2. Maintenance of ships and vessels;
    3. Supervision and tracking of supplies;
    4. Ordering goods and how these will be delivered, as well as organizing and supervision on travels.

h. Holding of participations, i.e. solely holding of shares with sole revenue sources the dividends and capital gains.

i. Intellectual property, i.e.:
    1. Patents and relating R&D, which includes:
        - Taking of strategic decisions, managing en carrying the main risks relating to the development and following exploitation of these intellectual property rights;
        - Taking of strategic decisions, managing en carrying the main risks relating to the purchase of intellectual property rights from third parties and following exploitation of these intellectual property rights;
        - Trade activities in which the intellectual property rights are used, which activities result in income received from third parties;
    2. Brands, client information, marketing, branding and distribution.
    3. High risk intellectual property, i.e.:
        - Intellectual property acquired from related entities;
        - Intellectual property which was financed via a cost sharing agreement with a related foreign entity;
        - Intellectual property rights put at the disposal of a foreign related party.

    It should be noted that unless the transparent entity can make credible that the revenues directly relate to such activities performed in or from Aruba, the activities performed do not qualify.

Substance requirements for relevant activities

The above-mentioned relevant activities need to meet the following substance requirements:

- Adequate material fixed assets are at the disposal of the transparent entity.
- Adequate number of FTE’s works directly or indirectly for the transparent entity, whereby adequate relates to the nature and size of the activities of the transparent entity.
- Adequate minimum, annually recurring, operational expenses are made, which fit the nature and size of the activities of the transparent entities.

It is allowed if the above-mentioned requirements are met by other entities situated in Aruba that are actively managed and monitored by the transparent entity.

Formalities

The AVV/NV/VBA must opt for the transparent status within one month after its incorporation. It is not possible for an existing AVV, NV or VBA to opt for the transparent status. Furthermore, within six months after the end of the financial year, the shareholders of the AVV, NV, or VBA must be disclosed to the tax authorities. Special forms exist for the notification, which notification should be accompanied by a balance sheet and profit & loss account.

Transparency and turnover tax

Transactions between the transparent entity and its shareholders are in principle subject to turnover taxes (refer to Fundamentals “turnover taxes”), unless the shareholder is established in Aruba and holds 100% of the shares in the transparent entity.

Transparency and dividend withholding tax

Due to the transparency, dividend distributions by the transparent entity are not subject to Aruba dividend withholding tax, since the profits are already (by fiction) allocated to the shareholder.

Transitional regulation

For transparent entities that have already opted for fiscal transparency, the substance requirements will only enter into effect as per January 1, 2022.

Cancellation of transparency regime

The fiscal transparency will be cancelled per the beginning of the financial year in which the transparent entity:

- No longer has solely registered shares;
- Does not meet the substance requirements as per the State Decree; or
- Does not comply with the filing requirements at the tax authorities, i.e. within six months after the end of the financial year the following information should be provided:
  - Overview of the shareholders;
  - Balance sheet and P&L of the last financial year.

However, contrary to the past, the sanction of non-compliance is no longer an increased corporate income tax rate as of the moment the transparent entity loses is fiscal transparent status (150% x applicable rate).

Country of residence shareholder

For the transparent regime to be fully effective, it is essential that the country of residence of the shareholder does not tax profits until realized. This because in the absence of a taxable presence on Aruba, Aruba does not levy taxes, while the shareholder does not pay taxes either because no income (in the form of a dividend or capital gain) has been realized yet. The definition of the relevant activities creates a broader scope however than under the prior legislation.

Disadvantages transparency

If the shares in a transparent entity are sold, for corporate income tax, individual income tax, and dividend withholding tax purposes, the share transaction is disregarded and instead the assets of the transparent entity are deemed to have been sold. Any selling gain (including “goodwill”) will be subject to corporate income tax or individual income tax against the normal rates applicable.

The above is not intended to constitute, nor should it be relied upon, to replace any professional advice. No action should be taken without first consulting your tax advisor. The above reflects the law effective January 1, 2019.