

BERETTA GODOY

BEATING THE SYSTEM - HOW TO MANUFACTURE EFFICIENTLY IN LATIN AMERICA'S SOUTHERN CONE

Tierra del Fuero is the closest Argentine province to Antarctica. It is an island located approximately 3,000 km away from Buenos Aires, our nation's capital. It has a population of 130,000 people, a large number of which play a key role in the Province's major business activities, hydrocarbons production, fishing, industrial production and tourism. Tierra del Fuego infrastructure provides access to large ports as well as airports and road connections with the continental territory of Argentina. Tierra del Fuego has enjoyed the benefits of a Tax and Customs Promotional Regime created in 1972, that grants significant tax incentives (exemption of import and export duties, income and asset taxes, and significant federal subsidies) and have turned Tierra del Fuego into a key location for the incorporation of high-end technology industries to supply the Argentine, Mercosur and Latin American markets. This document comments on the main aspects related to the organization of manufacturing business under the Promotional Regime and provides practical insights based on our experience assisting foreign companies in arranging tax efficient manufacturing projects in Argentina's southernmost province.

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BEATING THE SYSTEM: HOW TO LOWER YOUR MANUFACTURING AND DISTRIBUTION COSTS IN ARGENTINA'S SOUTHERNMOST PROVINCE

The purpose of this document is to summarize the most relevant aspects relating to the Promotional Regime currently in force in the Province of Tierra del Fuego, Republic of Argentina.

Tierra del Fuego is the southernmost Argentine province. It is an island located approx. 3,000 km away from Buenos Aires, our nation's capital, and it has a population of 130,000 people, approximately. The average temperature in Ushuaia, Tierra del Fuego's capital city, is 6°C. The Province's GDP is approximately 1% of our nations' GDP.

The main economic activities in the Province are hydrocarbons production, fishing, industrial production and tourism. It is connected by ports and airports located in Ushuaia and Rio Grande. There is also a road that connects the island with the rest of the Argentine continental territory (through the Chilean part of the island and a ferryboat).

The Promotional Regime was created in 1972 with the purpose of promoting economic activities in Tierra del Fuego, since the economy of such territory was not developed due to its geographical and climate situation.

I. TIERRA DEL FUEGO'S SPECIAL REGIME

The Special Regime sets forth the following tax and customs benefits:

1. Income Tax

Activities carried out in the Province of Tierra del Fuego under the Special Regime are totally exempted from income tax.

If the beneficiary sells its products to end customers situated in the rest of Argentina through unrelated companies, the income tax exemption is not limited. If the sale is made in a direct manner by the beneficiary, the income tax exemption is limited to 70% of the products' sales price. If the products are sold to such end customers by means of related companies¹, the income tax exemption is limited to 85% of the products' sales price.

2. Value Added Tax ("VAT")

Activities and transactions performed within Tierra del Fuego are exempt from VAT².

On the other hand, sales performed between a company located in Tierra del Fuego and a company situated the continental territory of Argentina are levied by VAT. According to the Special Regime regulations, the VAT debits arising from such transactions (which should normally be paid to the Federal Tax Administration) can be retained by the seller, thus, the VAT debits represent a gain for the seller located in Tierra del Fuego.

In case of sales to end consumers located in the rest of Argentina, the seller can only retain 70% of the VAT debits.

3. Other Tax benefits

Other tax benefits are granted in relation with the Promotional Benefit, including:

¹ Applicable regulations presume that there is a relationship between companies if the company located in Tierra del Fuego performs more than 60% of its sales transactions with any client or group of related clients located in the Argentine continental territory, even if there is no economical or corporate relationship between them. This presumption does not apply if the price of each product line of the sales transactions is arm's length.

² VAT is a federal tax that is levied on all different stages of the domestic trade, production and import of movable goods, as well as a wide range of services.

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- Excise tax exemption on imports into Tierra del Fuego and transactions within the Province,
- Excise tax reduction on sales of certain electronic and electric products to the rest of Argentina and reduction of the tax payment at the moment of the import into the rest of Argentina,
- Tax on debits and credits on bank accounts reduced rate, and
- Minimum presumed income tax exemption on assets located in Tierra del Fuego.

4. Customs aspects

From a customs standpoint, the Special Regime grants the following benefits:

- Sales of goods from Tierra del Fuego to the rest of Argentina and *vice versa* are treated as exports and imports, respectively,
- Imports into Tierra del Fuego and exports from Tierra del Fuego are exempted from import and export duties, respectively,
- Imports into the rest of Argentina of Tierra del Fuego's products are exempt from import duties, and
- Exports from Tierra del Fuego are exempt from export duties.

II. PROJECTS BENEFITED BY THE SPECIAL REGIME

In the case of industrial projects, it is required to obtain the corresponding authorization by federal and provincial authorities.

The companies that had their projects authorized on or before September 18, 2007 can use the benefits of the Special Regime until December 31, 2023. Otherwise, *i.e.* in the case of any projects authorized after September 18, 2007, the benefits will be in force until December 31, 2013. However, the approval of new industrial projects is suspended.

In order to apply the Special Regime benefits, the goods must have origin in the Province of Tierra del Fuego, which occurs if they are entirely produced in such Province or if they are subject to a process therein that implies a substantial transformation. Operations such as mere packing in the Province of Tierra del Fuego are not enough to confer Tierra del Fuego origin to the products.

Tierra del Fuego's origin of the products is evidenced if they are manufactured according to any of the production processes authorized by the federal authorities.

Last, the Special Regime foresees the possibility for its beneficiaries to substitute the products of their projects, provided that certain requirements are met in order to evidence that the substitution does not imply a distortion of the project and that it does not affect the companies that produce such products in the rest of Argentina. Any substitutions of products must be approved by the Federal Industry Office.

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If you have any question or comment regarding the foregoing, do not hesitate to contact us by calling at (54-11) 4326-7386, via fax to (54-11) 4326-7396 or via e-mail addressed to godoy@berettagodoy.com.

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