Peru

Peruvian Tax Court Issues Decision on Treaty Shopping Case

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The Peruvian Tax Court has ruled on the migration of a Panamanian entity – owning the shares of a Peruvian company – to Canada, and whether such action is considered "treaty shopping" under the Double Tax Convention (DTC) between Canada and Peru.

Background

A parent entity of a Peruvian entity migrated from Panama to Canada to facilitate the management of the entity, since the majority shareholders are residents of Canada.

After the migration, the parent entity (now based in Canada) transferred the Peruvian shares to another company; a transaction which is subject to 30% withholding tax in Peru. The DTC between Peru and Canada had not been requested, given that at the time of the transaction the company had not obtained a certificate of residence in Canada (*see* Note).

However, once they obtained the certificate, the parent entity applied the Peru-Canada DTC and filed a refund request for the 30% withholding tax. It was specified in its request that the parent entity complied with declaring to the Canada Revenue Agency (CRA) the income tax applicable on the transfer of shares and paid it by offsetting tax credits that the entity had in its favor in Canada.

The Peruvian Tax Authority denied the refund of the 30% withholding tax based on the following arguments:

- there is no double taxation, since there was no effective payment of the tax, and it does not recognize the offsetting of tax credits as a form of payment;
- the migration of the parent entity is an artificial structure, since it does not have an economic connection in Canada, nor bank accounts in Canada, and the control over the economic funds of the company are performed by individuals located in the Cayman Islands; and
- the migration of the transferor entity from Panama to Canada was made for the purpose of applying the Peru-Canada DTC and obtaining the tax benefits granted under the treaty (i.e. Treaty Shopping).

Tax court conclusion

The Tribunal reversed the judgment of the Peruvian Tax Administration and concluded that the transaction carried out by the non-resident entity does not qualify as treaty shopping, based on the following reasoning:

- according to the exchange of information between the Peruvian Tax Authority and the CRA, the parent entity is registered in Canada and the authenticity of the certificate of residence was confirmed;
- in accordance with jurisprudence principles, the true place of business is where the central management and control is executed. However, in this case it has not been proved that the control and management is carried out in Panama (instead of in Canada), as claimed by the Peruvian Tax Authority; and
- the fact that the parent entity does not have any fixed assets in Canada or that the declared domicile corresponds to a law firm are not enough to determine that there is no economic connection with Canada or that a treaty shopping scenario has taken place.

It should be noted that Ruling No. 08835-12-2022 does not establish a binding precedent and it is only applicable to the specific case at hand.

The Ruling No. 08835-12-2022 can be accessed here (as a PDF and in Spanish only).

Note: Paragraph 6 of article 13 of the Peru-Canada DTC establishes that capital gains from the transfer of Peruvian shares can only be taxed in Canada (and not in Peru), provided the principal value of the Peruvian entity does not come from real estate located in Peru.
