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## **OUTCOME OF PROCEEDINGS**

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From: General Secretariat of the Council  
To: Code of Conduct Group (Business Taxation)  
Subject: Cabo Verde's International Financial Institution regime (CV002)  
– Final description and assessment

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### **ROLLBACK REVIEW PROCESS (JANUARY 2019)**

The Budget Law 2019 has equalised the CIT rate applicable to International Financial Institutions to the baseline CIT in force in Cabo Verde in a two step approach. For companies that already benefitted from the regime, starting from the fiscal year 2019, the CIT is increased from 0 to 10% until 31 December 2021. After that date, the level of taxation will be equal to the baseline CIT rate applied in Cabo Verde, which is currently 25%. Newly licenced entities are subject to the baseline CIT rate as per 1 January 2019.

Although Cabo Verde is not addressing the issues identified during the 2017 screening process, the amendment to the regime removes the preferential tax features of the regimes. In fact, the partial increased rate for companies already benefitting from the regime could be considered as a grandfathering clause, as accepted under the current Code rules, and the level of taxation applicable to new applicants would not be preferential. For this reason, the Code of Conduct gateway criterion is not met as the regime does not provide for a significantly lower level of taxation. Therefore, the reformed regime falls outside the Code of Conduct's scope.

The Code of Conduct Group meeting of 30 January 2019 approved the rollback of the old CV002 regime. This conclusion was endorsed by the ECOFIN Council on 12 March 2019.

*Annex 1: Assessment of the old CV002 regime in 2017 (standstill review)*

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**Assessment of the old CV002 regime in 2017 (standstill)**

Categories:

Financial services, group financing and royalty payments

**a. Description**

International financial institutions within the scope of Law 43/III/88 of 27 December 1988 benefit from various tax benefits:

customs duties exemption on the importation of materials and equipment that are exclusively destined to the establishment of the financial institution;

exemption from single tax on income until 31 December 2017, and a single rate of 2.5% from 1 January 2018 onwards;

stamp duty exemption on transactions with non-residents;

According to paragraph 2 of Article 28 of the Tax Benefit Code, “the non-resident individuals and companies who are clients of the eligible institutions, (...) as well as the resident entities who have funds placed abroad and that hire financial services to the eligible institutions benefit from (i) an income tax exemption, regardless of the type of income, and (ii) a stamp duty exemption...”. Furthermore, according to paragraph 3 of the same Article, the income tax exemption applicable to the eligible financial institutions until 31 December 2017, followed by a 2,5%-flat-rate onwards, “does not apply to income deriving from operations carried on with residents; therefore, the accounting registers should separate the revenues and costs so as to enable the calculation of the different taxable results”.

*Source: IBFD, Cape Verde - Corporate Taxation - Country Surveys – Section 1.7.4 (Last Reviewed: 20 September 2015)*

**b. Preferential (lower taxation than normal):**

Individuals and companies considered clients of such international financial institutions benefit from:

- an exemption from the single tax on income, regardless of the type of income;
- stamp duty exemption.

Exemption from single tax on income until 31 December 2017, and a single rate of 2.5% from 1 January 2018 onwards.

**c. Possible concern (ring fenced / transparency / no substance):**

Our concern is that the International Financial Institutions regime might be targeted to foreign enterprises and/ or for activities with foreign entities/markets.

**d. Assessment:**

Criterion	1a	1b	2a	2b	3	4	5	OA
Cape Verde - IFI	V	V	V	V	V	X	X	HARMFUL

V = harmful

X = not harmful

Explanation

**Significantly lower level of taxation:**

“Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code”

The standard corporate income tax rate is 25 %. A company operating within the ambit of the International Financial Institutions regime benefits from an exemption on corporate income tax, applicable until 31 December 2017, and a 2.5% flat rate onwards (among other tax benefits: exemption on importation and Stamp Duty). The measure therefore provides for a significantly lower level of taxation and is potentially harmful under the Code.

**Criterion 1**

“whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents”

Criterion 1 contains two elements. The first element, concerns *de jure* element, aims at measuring whether the regime is exclusively available to non-residents or transactions with non-residents (criterion 1a). The second element, *de facto* element, measures whether the regime is only or mainly used by non-residents or for transactions with non-residents (criterion 1b).

The International Financial Institutions regime is *de lege* available to “international financial institutions”, whose by legal imposition are licensed to carry on operations with entities not resident in Cape Verde, in foreign currency. Domestic operations are available but under very restrictive circumstances. Moreover, paragraph 3 of Article 28 expressly foresees that the corporate income tax benefits do not apply to operations with residents in Cape Verde.

### **Criterion 2:**

“whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base”

As regards criterion 2 the division between criteria 2a and 2b is done in the same way as in the case of criterion 1 (i.e. *de jure* interpretation and *de facto* analysis). In general, a measure is caught by criterion 2 if the advantages are ring-fenced from the domestic market so that they do not affect the national tax base. In most cases, the evaluation against criterion 2 follows closely that of criterion 1.

As referred previously, the International Financial Institutions regime is targeted at activities with non-residents in Cape Verde. Thus, the tax advantages are ring-fenced from the domestic market and, consequently, do not, affect the national tax base.

### **Criterion 3:**

“whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages”

According to the standard practice for the evaluation of a measure against criterion 3, a measure is found harmful under this criterion if there are no specific requirements with regard to real economic activities and notably any requirement with respect to employment obligations.

The measure covers banking activity and do not require for real economic activity or substantial economic presence.

### **Criterion 4:**

“whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD”

The Tax Authorities of Cape Verde inform that the transfer pricing regime is applicable to entities benefitting from the regime in question.

### **Criterion 5:**

“whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way”

All preconditions necessary for the granting of a tax benefit should be clearly laid down in publicly available laws, decrees, regulations etc. before a measure can be considered transparent.

The measure is fully set out and published in the relevant legislation and the practice should not involve any administrative discretion.

**Overall assessment:**

In light of the assessment made against the Code of Conduct criteria, the regime qualifies as harmful under criteria 1, 2 and 3 of the Code of Conduct.

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