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**CAPE VERDE: A NEW (AFRICAN)
HOLDING JURISDICTION**

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Cape Verde: a New (African) Holding Jurisdiction

1. Getting acquainted with Cape Verde

The Republic of Cape Verde is located on an archipelago in the Macaronesia eco-region of the North Atlantic Ocean, off the western coast of Africa. Cape Verde is named after *Cap-Vert* (meaning Green Cape), now in Senegal, the westernmost point of continental Africa.

The archipelago is formed by 10 main islands and about 8 islets. The main islands are Santo Antão, São Vicente, Santa Luzia, São Nicolau, Sal, Boa Vista (in the northern island group, called *Barlavento*) and Maio, Santiago, Fogo and Brava (in the southern island group, called *Sotavento*). Of these, only Santa Luzia (presently a natural reserve) and the islets are uninhabited.

All islands are volcanic, but the only active volcano that subsists is on the island of Fogo. It has a temperate climate, with warm winters and dry summers.

With a total area of 4,033 square kilometres (approximately 1,557 square miles), Cape Verde has a population of approximately 420,000. The country's largest city is Praia, its political capital and one of Santiago's counties (or municipalities).

Cape Verde was uninhabited when the Portuguese arrived in 1456, and the islands were thus made part of the Portuguese empire. Due to its location off the coast of Africa, Cape Verde became an important water-

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ing station, then sugar cane plantation site, and later a major centre of the slave trade. In 1975, the islands achieved independence, partially due to the efforts of the African Party for the Independence of Guinea-Bissau and Cape Verde (*Partido Africano Para a Independência da Guiné-Bissau e de Cabo Verde* – PAIGC).

Portuguese is Cape Verde's official language, and the language of instruction in official schools. There is also a widely spoken range of Portuguese-based Creole languages, which vary considerably from island to island.

Its political system is that of a parliamentary representative democratic republic, whereby the Prime Minister of Cape Verde is the head of government, with a multi-party system. Executive power is exercised by the government. Legislative power is vested in both the government and the national parliament. The judiciary is independent of the executive and the legislature.

Its economy suffers from a poor natural resource base, including serious water shortages exacerbated by cycles of long-term drought. The economy is service-oriented, with commerce, transport, tourism, and public services accounting for 66% of GDP.

Although nearly 70% of the population lives in rural areas, the share of the primary sector in the GDP in 2004 amounted to only 12%, of which fishing accounted for 1.5%. About 82% of food is currently imported. The fishing potential, mostly lobster and tuna, is not fully exploited. Cape Verde runs a high trade deficit, financed by foreign aid and remittances from emigrants, the latter accounting for more than 20% of the GDP.

Economic reforms have been aimed at developing the private sector and attracting foreign investment to diversify the economy. Future prospects depend heavily on the maintenance of aid flows, the encouragement of tourism, remittances, and the momentum of the government's development program. Although Cape Verde is ranked in the 106 position out of 177 countries in the 2006 Human Development Report of the United Nations Development Programme, it is one of most developed countries in Africa. For purposes of comparison, it is worth noting that South Africa is listed in 121.

Cape Verde's official currency is the Capeverdean Escudo, which is pegged to the Euro (1 Euro = 110.265 Escudos), and with a current exchange rate per US dollar of 85.36 (January 2007).

Cape Verde is a member of most principal international and regional organizations, including the United Nations (UN), the International Monetary Fund (IMF), the International Bank for Reconstruction and Development (IBRD), the Multilateral Investment Guarantee Agency (MIGA), the Economic Community of West African States (ECOWAS), and is an observer to the World Trade Organisation (WTO). Along with Portugal, Angola, Brazil, Guinea-Bissau, Mozambique, São Tomé e Príncipe and East Timor, Cape Verde is one of the members of the Community of Portuguese Language Countries (*Comunidade dos Países de Língua Portuguesa*, hereafter “CPLP”), founded in 1996.

Cape Verde enjoys special ties with the European Union (EU) which may be further enhanced. Indeed, former Portuguese Prime Minister José Manuel Durão Barroso, now president of the European Commission, has promised to help integrate Cape Verde within the EU’s sphere of influence via greater cooperation with Portugal, and in March 2005 former Portuguese president Mário Soares launched a petition urging the EU to start membership talks with Cape Verde.

Cape Verde’s economy is currently booming with the construction of international airports in the islands of Santiago, Boa Vista and São Vicente, and with the many new tourist and residential projects surging therein. The World Bank expects Cape Verde to grow 6% in 2007, and the International Monetary Fund is even more optimistic, setting the estimate on 6.5%. The Bank of Cape Verde envisages an inflation rate below 1,5% in 2007, but this is probably not too realistic, as prices have increased 5.4% in 2006.

2. Company Law and Investment Statutes

Two main types of companies exist in Cape Verde: the *Sociedade Anónima* and the *Sociedade por Quotas*.

The first is a public limited liability company, whose shares must be held by a minimum of two shareholders and whose minimum capital is of approximately 22.700 Euro, 10% of which must be deposited in a local bank, and the second is private limited liability company, whose minimum capital is of approximately 1.800 Euro and is divided into quotas.

A Foreign Investor Statute (incentives and guarantees for inbound

investment) and a Free Company Statute (incentives and guarantees for off-shore investment by Capeverdean resident companies carrying out activities exclusively aimed at exportation or at other Free Companies) may be granted through an application to the Ministry of Finance and Planning.

3. Tax Law incentives

Basis of tax residence

Individuals staying for more than 183 days in Capeverdean territory or having a habitual abode therein and companies with their head office or place of effective management in Cape Verde are treated as residents for tax purposes, being subject to a single tax on income¹ according to a much mitigated world-wide-income principle or quasi-territorial principle.

Indeed, income obtained by foreign branches or subsidiaries of Capeverdean resident companies is excluded from the territorial scope of the IUR. Additionally, Cape Verde applies the exemption method for the elimination of international double taxation in a very generous way. In fact, the requirement for exemption of foreign source income in Cape Verde is that such income is “liable to tax, even if exempt” in the state of source.

Recent changes

Law 59/VI/2005, of April 18, has introduced relevant changes in four main areas to Cape Verde’s IUR and IUP, leading to:

- a) a shift from the credit method to an exclusion method for the elimination of double taxation of profits;
- b) the creation of a participation exemption for dividends of non-resident companies and for capital gains deriving from the sale of shares in resident and non-resident companies;

¹ Cape Verde has this single tax on income (“*Imposto Único sobre o Rendimento*”, hereafter “IUR”), comprising both individuals’ and corporations’ income taxation, created by Law 127/IV/95, of June 26 (hereafter “IUR Law”) and regulated by Decree Law 1/96, of January 15 (hereafter “IUR Regulation”). Cape Verde also levies a single tax on property ownership, property transfer and some real estate capital gains, the “*Imposto Único sobre o Património*” (hereafter “IUP”), created by Law 79/V/98, of December 7 and regulated by Decree Law 18/99, of April 26 (hereafter “IUP Regulation”).

- c) the introduction of tax benefits for investment funds, including the extension of the said participation exemption to income distributed by them and to capital gains deriving from the sale of participation units, in order to encourage the growth of the securities market;
- d) the IUP exemption on the acquisition and sale of real estate by collective investment undertakings.

More specifically, this Law has displaced capital income deriving from the distribution of profits, including those deriving from the liquidation of companies and collective investment undertakings, from the objective scope of the IUR. Income obtained by foreign branches or subsidiaries of Capeverdean resident companies is excluded from the territorial scope of the IUR. Finally, dividends and other forms of remuneration of capital invested by Capeverdean residents in shares, quotas, bonds and other debt instruments issued outside the Capeverdean territory by non-resident companies are also excluded from the territorial scope of the IUR.

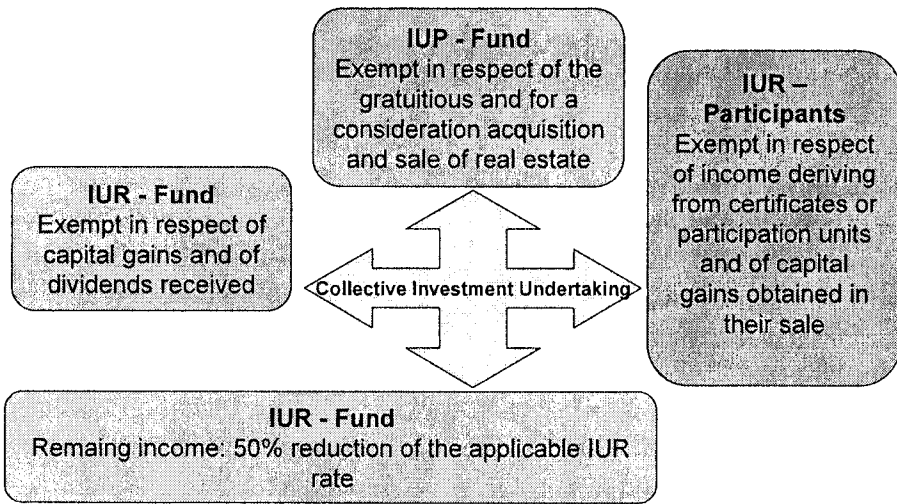
Capital gains derived by Capeverdean residents from the sale of shares or of any other securities issued by non-resident companies are also not liable to IUR. Additionally, the new wording of the IUR Regulation only includes in the objective and territorial scopes of this tax capital gains deriving from the sale of shares issued by Cape Verde resident companies held for less than one year, therefore exempting capital gains deriving from the sale of shares of Capeverdean companies held for a longer period.

Capital gains deriving from the sale of participation units in collective investment undertakings are also not liable to IUR and the tax rate applicable to these entities has been lowered to 50% of the standard company IUR applicable rate². Additionally, exemptions from IUP have also been granted to property acquired or sold by pension and real estate investment funds and to capital gains derived by real estate inventory companies from the sale of property, although the latter are liable to IUR.

The tax liability of collective investment undertakings and of their participants can be summarised in the following diagram:

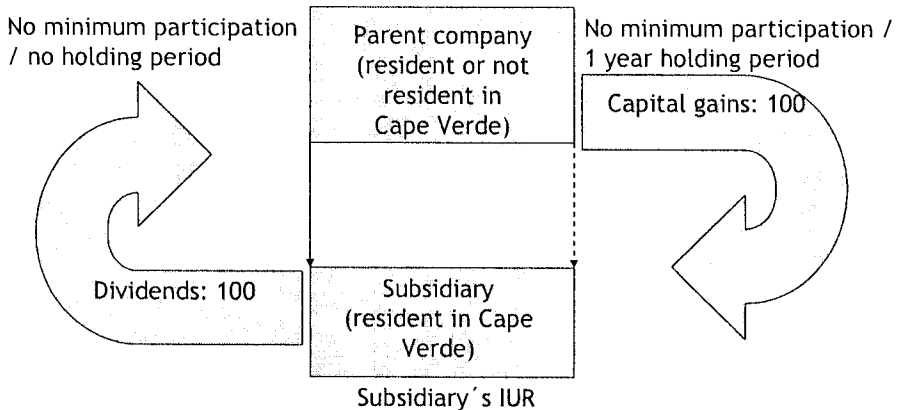
²Which is of 30% for taxpayers under the "verification method" – based on the book profits – and of 20% for taxpayers under the "estimative method" – a presumptive taxation regime.

IUR liability of collective investment undertakings and of their participants



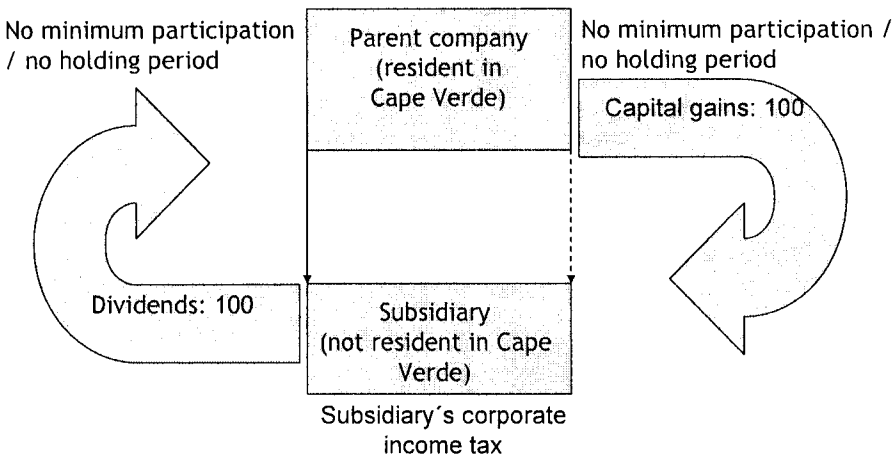
The favourable participation regime for inbound investment can be summarised in the following diagram:

Participation exclusion for capital gains and dividends in domestic investments



The favourable participation regime for inbound investment can be summarised in the following diagram:

Participation exclusion for capital gains and dividends in foreign investments



Free Company Statute

The above changes strongly reinforce a unique background for investment, further helped by the existence of a Free Company Statute³, which grants a 10-year IUR exemption on profits earned and dividends distributed, a limitation of the IUR payable in the following years to 15% of the profits obtained or dividends distributed in each financial year, and an exemption of all indirect taxes and customs duties to Cape Verde resident companies whose activity is solely aimed at exportation or at other Free Companies. Additionally, a limitation of the registration fees due on the incorporation of such companies is also granted by the Statute.

³ Created by Law 99/IV/93, of December 13.

International Financial Institutions

Simultaneously, the already well established International Financial Institutions (IFI) regime has also been amended⁴. This regime, created in 1988, establishes IUR⁵ and indirect and property tax exemptions to the institutions, their partners and their clients. The institutions may be branches or subsidiary companies of foreign financial entities⁶ operating in the banking, insurance, financial services and collective investment undertakings sector, and have to conduct operations exclusively with non-resident entities and in foreign currency.

As such, these branches or subsidiaries remain under the supervision of the competent authorities of their State of origin (although the Bank of Cape Verde is also entitled to exercise certain supervisory powers over them) and have to comply with reduced minimum share capital requirements.

They are, nevertheless, compelled to pay an annual operating license, to annually acquire a minimum amount of Cape Verde government bonds, to keep formal accounting records and to appoint an accountant and a legal representative resident in Capeverdean territory. IFIs have to comply with standards of know-your-customer rules in the course of their activity, thus providing for a sound reputation of this regime before the international financial community.

Foreign Investor Statute

Finally, IUR exemptions are also available to companies operating in Cape Verde under the Foreign Investor Statute. These exemptions are granted by a period of 5 years, notwithstanding the exemption granted to profits reinvested in Cape Verde, after which a reduced 10% IUR rate is applicable. More favourable conditions may be negotiated with the Capeverdean government on a case-by-case basis.

⁴ Created by Law 43/III/88, of December 27, and previously revised by Law 32/N/97, of June 30. Law 60/VI/2005, of April 18, has detailed in clearer way the operations institutions under this regime can carry out and the scope of the IUR exemptions granted to them, namely regarding operations with Capeverdean residents. Additionally, Decree-Law 12/2005, of February 7, has also introduced changes to the IFI Regulation, concerning the rules of establishment, operation and supervision of these institutions.

⁵ This exemption will remain in force until December 31, 2017.

⁶ In the case of subsidiary companies, the controlling entities must reside in member States of the Organisation for Economic Co-operation and Development (OECD). An IFI may exceptionally be incorporated by local partners, but in this case it will have to comply with additional share capital requirements.

Finally, there is an advance written tax ruling system⁷, not subject to any formalities, save that the ruling must be addressed to the Director-General of Taxes. Only rulings issued by the central services of the Tax Administration are binding⁸.

4. Cape Verde and International Taxation

Cape Verde-Portugal Double Taxation Treaty

One of the proclaimed goals of the described 2005 tax amendments was to attract foreign investment to Cape Verde, through the creation of an advantageous tax regime.

As the Capeverdean legislator also refers in the preamble of Law 59/VI/2005, one of the key aspects of a foreign capital attraction policy is the establishment of a wide network of Double Taxation Treaties (hereafter "DTTs"). Notwithstanding this, Cape Verde has so far negotiated a single DTT, that with Portugal, which has entered into force in December 15, 2000.

This DTT binds Portugal to grant its resident taxpayers a tax sparing credit for taxes that should have been paid in Cape Verde in light of its own tax legislation, but have been eliminated or reduced by exemptions or rate reductions granted by incentives aiming at the economical development of Cape Verde, such as the Free Company and Foreign Investor statutes.

This provision will only remain in force until December 31, 2007, consultations between the two contracting States having to occur in order for it to be kept in force after this date.

Portugal new dividend participation exemption for CPLP African dividends

Notwithstanding the above, the Portuguese State Budget Law for 2007⁹ contains a change to the Tax Incentives Statute ("*Estatuto dos Benefícios Fiscais*") whereby the economic double taxation of dividends

⁷ See article 57 of the General Tax Code.

⁸ See article 20(1)(c) of the General Tax Code.

⁹ Law 53-A/2006, of December 29.

elimination mechanism currently established in the Portuguese Corporate Income Tax (CIT – “*Imposto sobre o Rendimento das Pessoas Colectivas*”) Code is to be widened to profits distributed by subsidiaries of Portuguese companies resident in one of the African member States of the CPLP, provided that the following conditions are met:

- i) the Portuguese company is not exempt from CIT in Portugal and its subsidiary is not exempt from an identical or substantially similar income tax in their State of residence;
- ii) the Portuguese company must hold a direct participation of, at least, 25% of the subsidiary for a minimum period of 2 years;
- iii) the dividends must arise from profits that have been subject to a minimum rate of tax of 10% and must not derive from passive income generating activities, such as royalties, capital gains and other securities related income, income from real estate located outside the subsidiary’s State of residence, income from the insurance activity arising from the insurance of assets located outside the subsidiary’s State of residence or insurance of persons not resident therein and income from banking activities not mainly directed at the subsidiary’s State of residence market.

The China connection

There is a well-known trend of Chinese investment developing in Africa. Chinese investors may view Portugal as their gateway to Cape Verde, taking advantage from the mentioned Portugal-Cape Verde DTT, but also from the new Portuguese dividend participation exemption regime and the Portuguese Madeira Free Zone¹⁰. Conversely, Cape Verde investors may find in Portugal a stepping stone into China through the use of the Portugal-Macau and the Portugal-China DTTs.

These flows may be further enhanced by the fact that the Portuguese Madeira Free Zone (in both the Portugal-Macau and the Portugal-China DTTs) and the recently remodelled Macau Offshore regime¹¹ (in the Portugal-Macau DTT) are not excluded from the scope of the treaties.

¹⁰Which grants tax benefits to foreign-source income arising from the industrial, shipping and commercial and services activities, including holding functions.

¹¹Which grants tax benefits to management and administration of ships and aircraft, hardware consultancy, software consultancy, data processing, database related activities, research and development activities, tests and technical analysis activities, packaging and back office activities.

Unlike most DTTs, the Portugal-Macau one allows Portuguese resident companies to deduct from their taxable base 95% of the dividends distributed by Macau resident subsidiaries, if these develop an air transportation activity, or if they develop a manufacturing, electricity, gas and water or tourism activity mainly located in Macau, as long as a participation of at least 25% is held in the capital of the dividend distributing company for a period of two years, thus significantly eliminating the economic double taxation of dividends.

Finally, the Portugal-China DTT also binds both States to grant a bilateral tax sparing credit for business profits, dividends, interest and royalties until December 31, 2010, consultations between the two contracting States also having to occur in order for it to be kept in force after this date.

5. Conclusion

Cape Verde now positions itself as a highly competitive holding jurisdiction, as it has both the exemption method for the elimination of double taxation and a mostly theoretical world-wide-income taxation rule for its residents, while simultaneously granting full participation exclusion regimes for capital gains deriving from the sale of shares held for longer than one year and of participation units in collective investment undertakings, and for dividends distributed by resident companies.

The singularity of being an African country with a holding regime, together with the fact that it not generally considered to be a blacklisted tax haven by most countries, now render Cape Verde a interesting country for investors and tax planners alike.