International Tax
Ecuador Highlights 2019

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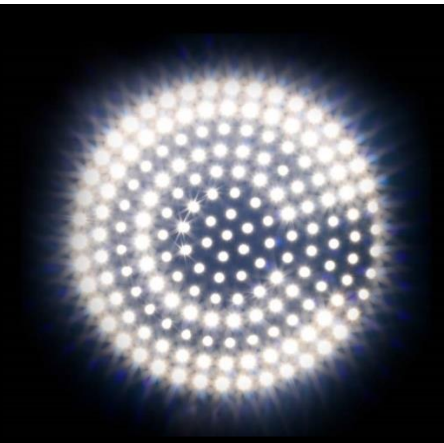

Recent developments:

For the latest tax developments relating to Ecuador, see Deloitte tax@hand.

Investment basics:

Currency – US Dollar (USD)

Foreign exchange control – No

Accounting principles/financial statements – Companies must follow International Financial Reporting Standards. Financial statements must be filed annually.

Principal business entities – These are the corporation (SA), limited liability company (*Cía. Ltda.*) and branch of a foreign company.

Corporate taxation

Residence – A company is resident in Ecuador if it is incorporated there.

Basis – Resident entities are taxed on worldwide income. Nonresidents are subject to tax only on Ecuadorian-source income.

Taxable income – Taxable income comprises gross income derived from business activities. Expenses incurred in deriving taxable income may be deducted, provided they are supported by documentation.

Foreign income taxed in another jurisdiction is not taxed in Ecuador (unless the income is derived from a tax haven or low-tax jurisdiction, in which case the taxes paid abroad may be taken as a tax credit for Ecuadorian tax purposes).

Taxation of dividends – Dividends paid by a resident corporation to a resident or nonresident corporation out of profits that previously have been subject to corporate income tax are exempt from income tax (even if the recipient is located in a tax haven or low-tax jurisdiction) if the beneficial owner of the recipient corporation is not an Ecuadorian resident individual and the complete chain of the payer corporation’s shareholders up to the ultimate beneficial owner has been duly disclosed to the tax authorities.

Capital gains – Capital gains are treated as ordinary income and generally are taxed at the applicable corporate income tax rate. However, as from 21 August 2018, capital gains from the direct or indirect transfer of shares, titles or other rights with respect to an interest in an Ecuadorian entity are taxed based on an “income tax bracket table” (with progressive rates ranging from 0% to 10%). Where the seller is a nonresident, the Ecuadorian target entity must act as a “substitute agent” responsible for collecting and paying the tax.

Losses – Losses may be carried forward for five years, but may be offset only against 25% of the profits earned in each tax year. The carryback of losses is not permitted.

Rate – The standard corporate tax rate is 25%, and a 22% rate applies to micro and small enterprises. An increased rate of 28% applies where: (a) companies have at least one direct or indirect shareholder resident in a tax haven or low-tax jurisdiction and the company has a beneficial owner that is an Ecuadorian resident individual; or (b) companies have not duly disclosed the complete chain of their shareholders up to the ultimate beneficial owner to the tax authorities. The higher rate of 28% applies proportionally where the “participation level” (i.e. the participation percentage of direct or indirect shareholders resident in a tax haven or low-tax jurisdiction and Ecuadorian resident individual beneficial owners, or of shareholders not disclosed in the chain of ownership) is less than 50% and in full where the participation level is 50% or more.

The corporate tax rate is reduced to 15% or 18% for inbound tourism companies, certain exporters (i.e. "habitual exporters," as defined) and companies engaged in the production of goods with a 50%-or-more "national component" that reinvest their profits in Ecuador.

Surtax – No

Alternative minimum tax – The advance income tax (see "Filing requirements" under "Compliance for corporations") previously operated as a minimum tax, but as from the 2019 fiscal year (the year ending 31 December 2019) this is no longer the case because the tax is refundable where the amount paid (plus the tax withheld for the year) exceeds the actual annual income tax liability.

Foreign tax credit – If income is subject to tax abroad, it generally is considered exempt in Ecuador. If income is derived from a tax haven or low-tax jurisdiction, the income is taxable and the tax paid abroad may be taken as a tax credit.

Participation exemption – See under "Taxation of dividends."

Holding company regime – No

Incentives – Under the standard incentive rules, new productive investments are entitled to a five-year corporate income tax exemption (as well as an exemption from payment of advance tax), subject to compliance with requirements related to the sector in which the investment is undertaken and provided the investment is not undertaken in the cantons of Quito or Guayaquil. However, new productive investments made from 1 September 2018 to 31 August 2020 outside of the cantons of Quito or Guayaquil are entitled to a 12-year corporate income tax exemption (as well as an exemption from payment of advance tax), subject to compliance with requirements related to the sector in which the investment is undertaken. An eight-year corporate income tax exemption (as well as an exemption from payment of advance tax) is available if a productive investment is made from 1 September 2018 to 31 August 2020 in the cantons of Quito or Guayaquil, and a 15-year exemption if investment is located in certain border areas.

New investments in six "basic industries" generally are tax-exempt for 10 years. However, new productive investments made in basic industries from 1 September 2018 to 31 August 2020 are tax-exempt for 15 years (regardless of whether they are made within or outside the cantons of Quito or Guayaquil), and a 20-year exemption applies if investment is located in certain border areas.

Enterprises set up in special development zones (ZEDES) are granted a 10% reduction in the corporate income tax rate. ZEDES incorporated during or after the 2019 fiscal year are tax-exempt for 10 years (effective from the first year in which they derive operating income), and then are granted the 10% corporate income tax rate reduction. ZEDES incorporated prior to the 2019 fiscal year may be eligible for a tax exemption for any portion of the 10-year period (effective from the first year in which they derived operating income) that still is remaining as of the 2019 fiscal year, and then are granted the 10% corporate income tax rate reduction.

Entities set up to develop projects under public-private partnerships are entitled to a 10-year income tax exemption as from the first year in which operating income is generated. Dividends or earnings generated by such entities also are exempt from income tax. An exemption from the special tax on remittances abroad is available, provided certain requirements are met (see below under "Withholding tax," "Other").

Withholding tax:

Dividends – Dividends paid to a nonresident out of profits that were subject to corporate income tax generally are not subject to withholding tax, but dividends paid to a recipient that is a nonresident corporation with a beneficial owner that is an Ecuadorian resident individual are subject to a 7% or 10% withholding tax, as are dividends paid in cases where the payer corporation has not duly disclosed the complete chain of its shareholders up to the ultimate beneficial owner to the tax authorities, unless the rate is reduced under a tax treaty. The 7% rate applies where the payer company's income was taxed at the 28% corporate income tax rate, and the 10% rate where the payer company's income was taxed at a rate of 25% or lower.

Dividends paid to a resident corporation are not subject to withholding tax.

Dividends paid to a resident individual are subject to withholding tax at a rate equal to the difference between the maximum progressive personal income tax rate and the applicable corporate income tax rate for the year to which the dividends relate, which could be 22%, 25% or 28%, depending on the year. The withholding tax rate will be 7% if the applicable corporate tax rate was 28%, 10% if the corporate tax rate was 25% or 13% if the corporate tax rate was 22% (which was the standard corporate tax rate for the 2017 fiscal year and certain other prior years).

Interest – Interest paid on loans obtained from nonresident financial institutions, specialized non-financial entities qualified by the Ecuadorian control authorities and multilateral organizations is not subject to withholding tax, unless the interest rate exceeds the maximum rate set by the central bank. Any excess interest must be subject to withholding tax at a 25% rate (unless the rate is reduced under a tax treaty), or it will not be deductible for the Ecuadorian company.

All interest payments made abroad, other than those mentioned above, are subject to withholding tax at the 25% rate (unless the rate is reduced under a tax treaty), and any excess interest exceeding the maximum rate set by the central bank will be considered nondeductible by the Ecuadorian payer company.

Royalties – Royalties paid to a nonresident are subject to a 25% withholding tax, unless the rate is reduced under a tax treaty. The rate increases to 35% when royalties are paid to a recipient in a tax haven or low-tax jurisdiction.

Technical service fees – Technical service fees paid to a nonresident are subject to a 25% withholding tax, unless the rate is reduced under a tax treaty. The rate increases to 35% where fees are paid to a recipient in a tax haven or low-tax jurisdiction.

Branch remittance tax – No

Other taxes on corporations:

Capital duty – No

Payroll tax – The employer is required to pay 0.5% of payroll to a national training fund, and 0.5% to an education credit program.

Real property tax – Urban property tax is levied annually by the municipalities on the owner of property, at progressive rates ranging from 0.025% to 1%.

Social security – Employers pay social security tax at a rate of 11.15% on an employee's total salary.

Stamp duty – No

Transfer tax – Transfer tax is levied by the municipal governments on the transfer of immovable property, the creation of trusts and certain gifts.

Other – Credit transactions are subject to a 0.5% tax, calculated on the loan principal. The tax is withheld by the financial institution.

All remittances abroad are subject to a 5% special tax (ISD), charged by the bank transferring the funds, which is then declared to the tax authorities. The tax is deductible for the company transferring the funds abroad. Payments made from overseas, whether for goods or services, also are subject to the ISD.

Tax paid on the import of raw materials, capital assets and supplies for production may be used as a tax credit to offset income tax payments in the current financial year, provided certain requirements are met.

Anti-avoidance rules:

Transfer pricing – The transfer pricing regime is based on the OECD guidelines. Transactions between related parties must carried out in accordance with the arm's length principle. Documentation rules apply. Taxpayers are required to file a schedule of transactions with related parties where the amount of the transaction exceeds USD 3 million in the fiscal year. If related party transactions exceed USD 15 million in a fiscal year, the taxpayer also must also file a transfer pricing report with the tax authorities.

Thin capitalization – Interest payments on foreign loans granted by a related party are deductible only if the foreign debt does not exceed 300% of the entity's equity. Any excess must be considered a nondeductible expense.

Controlled foreign companies – No

Disclosure requirements – No

Other – Ecuador has a general anti-avoidance rule.

Compliance for corporations:

Tax year – Calendar year

Consolidated returns – Consolidated returns are not permitted; each company must file a separate return.

Filing requirements – Companies are required to make two advance payments of corporate income tax (July and September). The amount is calculated using a formula based on specified factors. The final return must be filed between 10-28 April of the year following the tax year. If the total amount of advance income tax paid plus the tax withheld for the year is higher than the actual annual income tax liability, the difference may be requested as a refund, as from the 2019 fiscal year.

Penalties – Interest and penalties apply for late filing, failure to file or filing an incorrect return.

Rulings – The tax authorities may respond to taxpayers' questions, but the response is binding only on the taxpayer.

Personal taxation:

Basis – Resident individuals are taxed on their worldwide income; nonresidents are taxed only on Ecuador-source income.

Residence – An individual is deemed to be a resident if he/she is present in Ecuador for more than six months in a year or other 12-month period, if his/her principal activities or economic interests are in Ecuador or if his/her close relatives are in Ecuador. A change in tax residence will not become effective for five years if the individual moves from Ecuador to a tax haven or low-tax jurisdiction, unless the individual can demonstrate that he/she was physically present in the new jurisdiction for at least 183 days during the tax year.

Filing status – Married couples or common law spouses living in a common law union must file separate income tax returns. Any "joint basis" income must be divided equally between the spouses.

Taxable income – Taxable income includes income from employment, income from a profession or business, capital gains and investment income, such as dividends. Expenses related to the income can be deducted.

Foreign income that has been subject to tax in another jurisdiction is not taxed in Ecuador. For resident individuals, dividends (see under "Withholding tax," above) are deemed to form part of worldwide income (the income tax paid by the distributing company may be credited against the individual's income tax liability).

Capital gains – Capital gains are treated as ordinary income and generally are taxed at the progressive personal income tax rates. Capital gains from the direct or indirect transfer of shares, titles or other rights with respect to an interest in an Ecuadorian entity are taxed based on an income tax bracket table (with progressive rates ranging from 0% to 10%).

Deductions and allowances – Special deductions are permitted up to a maximum amount equivalent to 1.3 times the basic tax-free allowance for individuals (USD 14,703 for 2019) for personal expenses (housing, education, food, health, clothing, art and culture.).

Rates – Rates are progressive from 0% to 35%.

Other taxes on individuals:

Capital duty – No

Stamp duty – No

Capital acquisitions tax – No

Real property tax – Urban property tax is levied annually by municipalities on the owner of property, at progressive rates ranging from 0.025% to 1%.

Inheritance/estate tax – Inheritance tax is levied at progressive rates up to 35% on donations, inheritances and legacies. A tax-free allowance (USD 72,060 for 2019) is granted.

Net wealth/net worth tax – No

Social security – Resident employees are required to make monthly social security contributions of 9.45% of their monthly salary.

Compliance for individuals:

Tax year – Calendar year

Filing and payment – Tax returns must be filed between 1 February and 10-28 March of the year following the tax year.

Individuals whose sole source of income is derived from employment are not required to file a return. Self-employed individuals who fulfill the conditions to be required to maintain accounting records are subject to the same rules as companies.

Individuals, as well as professionals, commission agents, craft workers, agents, representatives and other self-employed workers, are required to maintain accounting records when the gross income of the immediately preceding fiscal year (i.e. 2018) exceeds USD 300,000.

Penalties – Interest and penalties apply for late filing, failure to file or filing an incorrect return.

Other – Individuals whose total assets exceed 20 times the basic income tax-free allowance (USD 226,200 for 2019) must file information on their net worth in May of each year, stating the beginning balances at 1 January of the relevant year. Married couples or common law spouses living in a common law union generally must file a combined net worth return if their joint assets exceed 40 times the basic income tax-free allowance (USD 452,400 for 2019). However, if either of the spouses/partners holds assets outside of the conjugal community, returns must be filed separately and must include the individual assets and liabilities, as well as the assets and liabilities that form part of the conjugal community or common law union.

Value added tax:

Taxable transactions – VAT is levied on the supply of goods and the provision of services and services received from overseas, such as rights and royalties.

Rates – The VAT rate is 12%. Certain transactions are exempt or zero rated.

Registration – No

Filing and payment – VAT returns must be filed on a monthly basis.

Source of tax law: Tax Code, Tax Law, Production Code, Productive Investment Law, regulations, resolutions

Tax treaties: Ecuador has 20 tax treaties. For further information on Ecuador's tax treaty network, visit Deloitte International Tax Source.

Tax authorities: Internal Revenue Service (IRS)

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