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Global Tax Alert

News from EY Americas Tax

Ecuador issues regulations implementing 2019 tax reform

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Ecuador has issued regulations implementing the tax reform enacted on 30 December 2019. Specifically, the regulations implement: (1) corporate income tax rules; (2) income tax rules for the banana, agricultural and farming industries; (3) dividend withholding rules; and (4) value-added tax (VAT) rules for digital services.

Income tax

The regulations establish that the capitalization of profits (i.e., when a company increases its capital by using profits) will not be considered a distribution of dividends, even if the capitalization results from the reinvestment of profits. The increase in the share value generated will not be subject to income tax.

Profits, income or benefits (i.e., income that does not enter a company as cash, such as assets) of companies or trusts in Ecuador whose only economic activity is investing in real estate assets will not be subject to income tax. Companies that make new productive investments in sectors considered as basic industries may obtain an income tax exemption for the income derived from those investments for 10 years. The exemption will apply in proportion to the value of the new productive investments. The exemption amount could be more than 10% of the income.

Companies may voluntarily make advance payments of the income tax. Those payments will be considered a tax credit. The payments may be equal to 50% of the income tax incurred in the prior tax year, minus the withholdings from that same tax year.

Income tax for the banana industry

The regulations require the income tax on bananas to be reported and paid with the regular income tax. The tax rate is based on the number of banana boxes produced weekly.

Companies with a certificate of good agricultural practices issued by an Ecuadorian control authority called *AGROCALIDAD* may be eligible for a 1% tax rate.

The regulations also require banana exporters to perform a monthly settlement and report the income obtained from the exports.

Income tax for the agricultural and farming industries

The regulations require taxpayers that qualify for the income tax regime for the agricultural and farming industries to remain under the regime for at least three years. The regime applies to all of the taxpayer's activities.

The regulations treat fruits, legumes and vegetables, grains, rice, corn, coffee, cocoa, potato, soy, sugar cane, and flowers, among other products, as goods of agricultural origin. Milk, meat, skin, eggs, wool, fibers and honey, among other products, are treated as goods of farming origin.

The income tax under this regime is based on the gross sales value, which is the market price or the amount set by the control authority, whichever is higher.

Dividend withholding

Under the tax reform, dividend distributions are taxable. The regulations require tax to be withheld on dividend distributed by Ecuadorian companies and permanent residents.

The tax is levied in the tax year in which the dividends are distributed, regardless of the period in which the profits that give rise to the dividends are generated. The tax must be withheld at the time of the distribution and applies to 40% of the distributed dividend.

VAT

The tax reform enacted a VAT on digital services, which will be effective 16 September 2020.

Digital services are defined as those provided or contracted through the internet or any adaptation or application of protocols, platforms or technology used by the internet or other network, through which similar services are provided. By their nature, these services are automated and require minimal human intervention. This definition applies regardless of the device used for downloading, viewing or use.

Special consumption tax

The regulations exempt certain alcohol or alcohol imported through an annual quota provided by the Internal Revenue Service from the special consumption tax. For Ecuadorian alcohol, the exemption only applies if the alcohol is made up of at least 70% Ecuadorian ingredients.

Alcoholic beverages, including beer, that are produced in Ecuador are exempt from the special consumption tax.

Alcoholic beverages, including beer, may be eligible for a tax rate reduction of 50% when they are made in Ecuador with Ecuadorian alcohol, sugar cane or other products.

The special consumption tax also applies to plastic bags. Biodegradable and compostable plastic bags, however, may be eligible for a tax rate reduction of 50% if the conditions established by the control entity (i.e., government agency) are satisfied. Plastic bags made with at least 50% of recycled material are exempt from this tax.

Remittance outflow tax

The remittance outflow tax will apply to exports of goods in which the payment for those goods does not return to Ecuador, and it is impossible to determine the delivery date of the goods. The tax will be imposed six months after the shipping date recorded on the customs declaration.

An exemption from the remittance outflow tax will apply to loan payments made abroad, provided the company receiving the financing abroad registers it with the Central Bank of Ecuador. The exemption, however, will not apply if the loan financed foreign trade operations of goods and services between unrelated parties. The exemption also will not apply when the loan term equals or exceeds 180 days and the beneficiary of the loan makes one or more extraordinary loan payments within the first 180 days that equal or exceed 50% of the loan balance at the time of the payment.

This tax does not apply to the anticipated payment of dividends abroad (i.e., when the company pays dividends before the end of the tax year). The exemption will not apply when the beneficiary of the dividends is an Ecuadorian resident.

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