

Legal 500

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Ecuador

Tax

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This country-specific Q&A provides an overview of tax laws and regulations applicable in Ecuador.

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Ecuador: Tax

1. How often is tax law amended and what is the process?

In the last 10 years many reforms have been generated, even temporary taxes and contributions have been created in other Laws that, without being tributary, contain one or two chapters that reform taxes, all to attend to socio-economic needs and the country's development.

In this context, the approval of new national taxes, rates, and contributions corresponds to the Legislative power, and the local governments, in their jurisdictions.

The creation, modification, or abolition of taxes is executed through a legislative project proposed by the Executive, which has the power to approve or veto the reform.

2. What are the principal administrative obligations of a taxpayer, i.e. regarding the filing of tax returns and the maintenance of records?

There are formal obligations that taxpayers must comply with, including the following:

Register in the official records (Single Taxpayers Registry, Exporters Registry, etc.);

Keep the information updated for a limit of not less than six years.

Keep the Accounting Books and Records and keep them for six years.

Submit tax returns, the frequency of which depends on the type of tax, and the regime that applies to it, the most usual being:

- Submit the annual or semi-annual income tax return.
- VAT monthly or semi-annually depending on the taxpayer's category.
- Transactional report with the monthly purchase and sales report.
- Declaration of Withholdings at the Source of Income Tax, monthly.
- Declaration of Tax on currency outflow.
- Dividend distribution report, once a year.

- Income Tax Report of the company's employees.

3. Who are the key tax authorities? How do they engage with taxpayers and how are tax issues resolved?

There are three types of Tax Administration: Central, Sectional, and Exception.

The Central Tax Administrations are the Internal Revenue Service (SRI), and the National Customs Service (SENAE). The SRI administers these national taxes, while SENAE's institutional function is to control the entry and exit of merchandise, people, and transport, as well as the management and administration of taxes on foreign trade.

The sectional tax administration corresponds to the Provincial Prefect or the Mayor.

The Exceptional Tax Administration is the one that is exercised in cases in which the law expressly grants tax management to the tax creditor public entity itself.

The relationship with the tax authorities is regulated in the special regulations to which they must submit their actions, so there should be no cases of abuse of authority.

For administrative matters, the authorities have a maximum period of 120 business days to attend to requests and resolve claims.

4. Are tax disputes heard by a court, tribunal or body independent of the tax authority? How long do such proceedings generally take?

Administrative acts may be challenged before the District Court of Tax Litigation, an independent body that corresponds to the judicial function.

These judicial processes are resolved, in a single instance, in an approximate time of one year. Based on this ruling, the party that considers itself affected may file an Extraordinary Cassation Appeal before the Specialised Chamber of the National Court of Justice; The resolution of said appeal may take between one and three years.

5. What are the typical deadlines for the payment of taxes? Do special rules apply to disputed amounts of tax?

The filing of the tax return has a deadline set, by the ninth digit of the RUC.

Regarding VAT, Special Consumption Tax, and Withholdings at the Source, depending on the applicable regime, they must be declared on a monthly or semi-annual basis.

Income tax is declared in April of the following year.

Filing the declarations outside the term established by law carries a fine and interest.

If an administrative claim is filed, all collection action is suspended. In case of presenting the judicial demand, the suspension of the challenged act can be requested, paying a deposit of 10% of the amount in favour of the creditor authority of the tribute.

6. Are tax authorities subject to a duty of confidentiality in respect of taxpayer data?

The Law establishes that the administrative procedures are reserved and confidential and that the information provided to the Administration may only be used for tax purposes. However, there is cross-checking of information between government entities.

Ecuador is currently subscribed to the Global Forum on transparency and exchange of information for tax purposes of the OECD.

One last reform, introduced in 2023, strengthened the tax information reserve.

7. Is this jurisdiction a signatory (or does it propose to become a signatory) to the Common Reporting Standard? Does it maintain (or intend to maintain) a public register of beneficial ownership?

In 2019, Ecuador adhered to the Multilateral Convention on Mutual Administrative Assistance in Fiscal Matters (CAAM), which established a common reporting standard.

Regarding beneficial ownership information, Ecuador has two regimes, one tax-related and another corporate, which requires legal entities to declare the ultimate beneficial owner (natural person) of corporate structures.

In the event of non-compliance with the tax obligation, legal entities will be required to pay an increased rate of 3% on the income tax, currently set at 25%.

8. What are the tests for determining residence of business entities (including transparent entities)?

In Ecuador, the main commercial structures (businesses) are considered to have a fiscal residence in the country, when they have been incorporated in Ecuadorian territory; and, in the case of foreign companies, they will also be considered tax residents in the country if they adopt any of the corporate forms indicated in the Companies Law.

There are no transparent entities.

9. Do tax authorities in this jurisdiction target cross border transactions within an international group? If so, how?

Yes, our legislation states that related parties are persons or companies, whether or not domiciled in Ecuador, in which one of them participates directly or indirectly in the direction, administration, control, or have part of its capital in the other (if you have minus 25%); or in which a third party participates directly or indirectly, in the direction, administration, control or capital of these.

Related parties will also be considered taxpayers who carry out transactions with companies domiciled, incorporated, or located in a tax jurisdiction with lower taxation, or Tax Havens. Related parties may be established by presumption when the transactions carried out do not comply with the arm's length principle.

In this order, the law establishes limitations to the deduction of expenses for payments abroad with related parties, as well as regulations on indirect expenses assigned from abroad by related parties. Payments for reimbursements, interest on external credits, and commercial leases are some of the figures that the Tax Administration is most responsible for verifying.

10. Is there a controlled foreign corporation (CFC) regime or equivalent?

Ecuadorian legislation does not contain specific provisions regarding controlled foreign corporation (CFC) rules.

11. Is there a transfer pricing regime? Is there a "thin capitalization" regime? Is there a "safe harbour" or is it possible to obtain an advance pricing agreement?

There is a Thin Cap regimen to deduct the interest paid on external credits. The external credit and its payments must be registered in the Central Bank of Ecuador.

Additionally, there are several limitations: 1) Only interest paid up to the rate authorized by the Monetary and Financial Policy and Regulation Board will be deductible; 2) The relationship between the total external indebtedness and its equity may not exceed 300%; 3) The total amount of net interest in operations carried out with related parties must not exceed 20% of EBITDA (not applicable for Financial Institutions).

In Ecuador, there is a transfer pricing regime, aimed at regulating for tax purposes the transactions carried out between related parties. The considerations between them are similar to those carried out between independent parties. The arm's length principle allows the Tax Administration to analyze this type of operation, to determine the profits that would have been obtained by one of the parties if the operations had been carried out at market prices and conditions.

It is important to consider that taxpayers who carry out operations with related parties and are not exempt from the transfer pricing regime are required to submit an annual Transfer Pricing Report.

Advance price agreement is not possible; however, the regulations allow raising a query regarding the methodology that should be used to determine transfer prices and request that the Tax Administration determine the valuation of the operations carried out between related parties before carrying them out. For this, you must present all the necessary information, data, and documentation and you can obtain a binding acquittal for the current fiscal year, the previous one, and the following three.

12. Is there a general anti-avoidance rule (GAAR) and, if so, how is it enforced by tax authorities (e.g. in negotiations, litigation)?

Yes, the general anti-avoidance rule is established in article 17 of the Tax Code. This rule recognizes the principle of the legal and economic reality of the form and allows the Tax Administration to disregard the legal form of the operations that had been adopted by the parties if

it considers that it differs from the true legal or economic essence of the transaction.

This rule is quite ambiguous, which has allowed the Tax Administration to use it repeatedly as an argument in determination processes, in a discretionary manner. This led to the filing of action of unconstitutionality; before The Constitutional Court with ruling No. 47-15-IN/21, which determined the conditional constitutionality of this anti-circumvention rule, and established that to be applied, reasoned reasoning must be carried out, with sufficient premises, reasons and evidence, thus limiting, for the first time, its use since 2021.

The same year, and as a result of the last tax reform, criteria were established for the qualification of legal and economic substance (Art. 30.3); thus, the legal form adopted by the parties will have to be accepted, and article 17 cannot be applied in the following cases:

- a) If the legal or economic form chosen is part of the modalities applicable to the type of economic activity or sector.
- b) When the result is neutral in revenue terms: Savings vs. increase in income, provided they are fiscal residents in Ecuador.
- c) When there is jurisprudential precedent.

13. Is there a digital services tax? If so, is there an intention to withdraw or amend it once a multilateral solution is in place?

There is no single tax on digital services.

However, with the tax reform of 2019, and as of 2020, it was established that digital services would also be subject to VAT. The generating event is verified at the time of payment by the resident or a permanent establishment of a non-resident in Ecuador, in favor of the non-resident provider of the digital services.

Digital services are understood to be those provided and/or contracted through the internet, or any adaptation or application of the protocols, platforms, or technology used by the internet, or another network through which similar services are provided that, by their nature. They are automated and require minimal human intervention, regardless of the device used for downloading, viewing, or use, among others.

There is, however, no direct tax on the income of digital service providers.

14. Have any of the OECD BEPS recommendations, including the OECD's recent two-pillar solution to address the tax challenges arising from digitalisation of the economy, been implemented or are any planned to be implemented?

Ecuador is not part of the OECD; however, although a formal BEPS implementation process has not been implemented in the country, legislative reforms have been carried out that show a tendency to follow the recommendations of said plan.

Although Ecuador did not sign the tax agreement of the OECD, on the Inclusive Framework, regarding the erosion of the bases and the transfer of benefits, the highest authority of the Tax Administration affirmed that thanks to the implementation of internal public policies, added to the country's adherence to the Multilateral Convention on Mutual Administrative Assistance in Fiscal Matters (CAAM), suggested actions will be implemented in the future in the plan, including the possibility of creating a tax that implies the establishment of a minimum and effective tax base for large multinationals, to tax their income.

15. How has the OECD BEPS program impacted tax policies?

As previously mentioned, although Ecuador is not part of the OECD, the Beps Plan has had an impact on the legislative reforms carried out in recent years, this influence is verified in the establishment of a transfer pricing regime, limitations on deductions of certain expenses between related parties, the taxation of digital services, the limitation of the application of the benefits of the Agreements to Avoid Double Taxation, etc.

16. Does the tax system broadly follow the OECD Model i.e. does it have taxation of: a) business profits, b) employment income and pensions, c) VAT (or other indirect tax), d) savings income and royalties, e) income from land, f) capital gains, g) stamp and/or capital duties? If so, what are the current rates and how are they applied?

The Ecuadorian tax system follows the OECD model.

a) Business benefits are subject to a flat rate of 25%, there are certain reasons why the rate can be increased to 28% or reduced to 22% or 20%.

b) Income from work by natural persons is taxed at a gradual rate from 0% to 37%.

c) About VAT in Ecuador, this tax is made up of two flat rates, one of 12%, which is the general rate; and a 0% rate mainly for goods and services classified as essential.

d) Savings income is subject to general income tax, however, income from fixed-term deposits in national financial institutions, as well as from investments in fixed-income securities that are traded through stock markets of the country with a term of 180 days or more, is exempt.

e) Regarding the tax on land income, it is necessary to classify between:

- Income from the use of the asset – in this case, the income must be taxed according to the regime to which the person who obtains the income is subject.

- Profit from the sale of land – has recently undergone a modification and is currently subject to income tax, however, there are 2 exceptions:

or the occasional sale of real estate, which is used for housing, by natural persons; or the first occasional sale until November 29, 2026.

f) Regarding capital gains, Ecuador has a single tax on profits generated by the alienation of rights representing capital, at a flat rate of 10%. There is an exemption in case of sales that:

1. Generate income of less than \$565,500 (this amount changes every year);

2. The sale is made through the Ecuadorian stock exchange.

3. The representative rights of capital are listed on the stock exchange.

4. Amount transferred is less than 25% of the subscribed capital of the company.

g) Finally, regarding dividends, these are taxed at 40% of the total amount of the distributed dividend. If the dividend is paid to non-residents, the rate is 25% and if it is paid to residents, the rate is progressive from 0% to 25%.

17. Is business tax levied on, broadly, the revenue profits of a business computed in

accordance with accounting principles?

Since 2012 in Ecuador, the International Financial Reporting Standards (IFRS) have been mandatory for all companies; however, the accounting result can be modified with the rules established by the Internal Tax Regime Law and its Regulations to establish the tax base of the Income Tax.

18. Are common business vehicles such as companies, partnerships and trusts recognised as taxable entities or are they tax transparent?

Ecuador recognises as vehicles to carry out economic activities the following:

- Companies.
- Associations with or without legal personality.
- Trusts.
- Consortia.
- Investment Funds.

The peculiarity is that, regardless of the selected vehicle, Ecuadorian legislation grants it the same treatment in the tax field, in short, they must pay similarly.

In Ecuador, there are no transparent entities for tax purposes.

19. Is liability to business taxation based on tax residence or registration? If so, what are the tests?

The taxation of economic activities is linked to a concept of residence that in the case of companies refers to a registry, the legislation establishes that a company has a fiscal residence in Ecuador when it has been incorporated or created in Ecuadorian territory, in accordance with the legislation national.

In the case of natural persons, there are four criteria:

1. Stay more than 183 days within a calendar year in Ecuadorian territory
2. When their permanence in the country is one hundred and eighty-three (183) days in twelve months within two continuous fiscal periods.
3. The main nucleus of their economic activities or interests resides in Ecuador
4. That they have not stayed more than 183 days in any territory.

The main nucleus will be understood when the person is the owner of assets located in Ecuador for a value greater than 1 million dollars, provided that:

- Has been a tax resident in Ecuador.
- Has had Ecuadorian nationality.
- Has been a representative of a company resident in Ecuador.

Additionally, any person who wishes to carry out an economic activity legally in Ecuador has the obligation to register in the Single Taxpayer Registry (RUC).

20. Are there any favourable taxation regimes for particular areas (e.g. enterprise zones) or sectors (e.g. financial services)?

Yes, regarding the special income tax regimes we have:

a) Banana sector – those who carry out activities of production, sale, and export of bananas are taxed according to the income generated, applying a rate of 1% to 3%.

b) Agricultural sector – those who carry out activities of production, sale, and export of products of agricultural, poultry, livestock, beekeeping, rabbit, and meat origin, which remain in their natural state, will be taxed on the total amount of their income applying a rate of 0 % to 2%.

c) Simplified Regime for Entrepreneurs and Popular Businesses (RIMPE) – companies that generate income of less than \$300,000 and that are not included in the excluded activities will pay income tax taking the total amount of their income as the taxable base and applying a rate of 0% to 2%.

The last reform of 2021 annulled the special regimes for the Special Zones of Economic Development in Income Tax.

About VAT, there are the following special regimes:

- RIMPE;
- Usual exporters.

21. Are there any special tax regimes for intellectual property, such as patent box?

No, in Ecuador there are no tax regimes for intellectual property, such as the patent box.

22. Is fiscal consolidation permitted? Are groups of companies recognised for tax purposes and, if so, are there any jurisdictional limitations on what can constitute a tax group? Is there a group contribution system or can losses otherwise be relieved across group companies?

In the tax field, it is not possible to apply a consolidation regime by companies belonging to a corporate group.

23. Are there any withholding taxes?

Yes. In income tax, with few exceptions, taxable income is subject to withholding at source, in percentages that vary from 1% to 10% of the amount paid or credited.

Regarding VAT, the retention varies between 30%, 70% and 100% of the Tax caused, determining on the invoice.

In reference to the Foreign Currency Outflow Tax, financial institutions and natural persons who hire, promote, or manage a public show with respect to the payments they make due to contracts for public shows with the participation of non-residents are obliged to withhold 100 % of the tribute.

24. Are there any environmental taxes payable by businesses?

If there is the "Redeemable Tax on Non-Returnable Plastic Bottles", used to contain alcoholic, non-alcoholic, carbonated, non-carbonated beverages and water. The fee is up to 0.02 USD, which can be returned.

There is within the Tax on Special Consumption the plastic covers that the consumer requires the business establishment to carry or load the products sold by it. Plastic sleeves used as primary packaging are exempt.

25. Is dividend income received from resident and/or non-resident companies taxable?

Dividends distributed by resident companies or

permanent establishments in Ecuador or to a permanent establishment in the country of a non-resident company, do not constitute taxable income for those who receive them.

If the distribution is made to natural persons tax residents in Ecuador, the taxed income will form part of their global income. The companies that distribute these dividends will be withholding agents applying a rate of up to 25% on said taxed record. The taxable income will be 40% of the dividend effectively distributed.

It should be emphasised that if a company grants its beneficiaries of respective capital rights loans in money, this will be considered as payment of anticipated dividends, and the company must make the withholding corresponding to the rate established for companies.

26. What are the advantages and disadvantages offered by your jurisdiction to an international group seeking to relocate activities?

Ecuador offers great advantages among which we highlight:

- Reduction of 3 percentage points of the income tax rate for new investments made after January 1, 2022.
- Reduction of 5 percentage points in the income tax rate for taxpayers who sign investment contracts in new investments made after January 1, 2022.
- Exemption from the payment of Taxes on Foreign Trade and Foreign Currency Outflow Tax (ISD) on the import of capital goods and raw materials made by taxpayers who sign investment contracts.
- Additional 100% deduction for depreciation and amortization of machinery, equipment and sustainable construction technologies.
- Additional deductions for the determination of the tax base of the Income Tax for sponsorship of athletes, contributions to promote art and culture.

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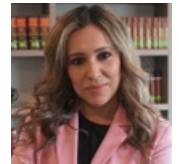
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