



PrimeGlobal

*An Association of
Independent Accounting Firms*

DOING BUSINESS IN ECUADOR





COMPANY FORMATION IN ECUADOR

MAIN FORMS OF COMPANY/BUSINESS IN ECUADOR

Ecuador produces land and sea products throughout all seasons of the year to meet domestic and global demands, which has made it the world's leading banana, cocoa, and passion fruit pulp exporter, and has placed it among the top three shrimp and flower exporters, to mention a few.

- Gross Domestic Product (GDP) Main productive sectors in thousands USD, 2014
- Manufacturing (excluding oil refining) \$ 13,503,773
- Oil and mines \$11,312,447
- Construction \$22,229,192
- Trade \$10,300,512
- Education, social services, health \$8,035,608
- Agriculture, hunting, forestry \$7,391,854

Exports

The Guayas province generates 56% of the total revenues for private exports and owns 33% of export companies. While on the other hand the Pichincha province has 39% of export companies. According to the Federation of Ecuadorian Exporters- FEDEXPOR, most of the products that yield higher revenues to the country are grown in Guayas; i.e., shrimp and banana.

Due to Ecuador's dependence on oil for the trade balance, the importance of promoting traditional private sectors becomes evident, and at the same time it is required to find other value-added products that incorporate other provinces into the exports map, generating socioeconomic movement in the country. For this reason, the government is promoting public-private partnerships.

SPECIFIC TAX CONCERNS RELATED TO ESTABLISHING A COMPANY

From the first moment the company is established, it is committed to tax payments, fees and contributions to state bodies. The obligations are explained below.

Fees and sectional contributions

- Contributions to the Company's Superintendence
- Fees and patents payment to the Municipality where the company is located
- Payments to the Fire Department
- Others

Taxes

Taxes are subjected to the type of economic activity performed by the company. Designated by the taxation law, the following taxes are among the most popular.

- Value added-tax (IVA) (14%)
- Tax for currency outflows (5%)
- Transport taxes
- Income tax for natural person (related to an annual table)
- Income tax for a legal entity (22%)



LEGAL ISSUES RELATED TO ESTABLISHING A COMPANY

See Form 2: Permanent Establishment in Ecuador: Branch or Subsidiary?

CULTURAL CONCERNS RELATED TO ESTABLISHING A COMPANY

Ecuador has four regions: The Pacific Coast, The Andes The Amazon and The Galapagos Islands.

The Ecuadorian consumer differs in their tastes and preferences depending on the region where they live. However, their consumption patterns are based on global trends, prioritizing the purchase of tech products, appliances, clothing and personal care items, especially in December for Christmas holidays.

Regarding strategies to enter the Ecuadorian market, a businessmen should perform market intelligence processes, partner search, and prospectives visits will allow interested businessmen to find the most suitable Ecuadorian counterparts to do business. In addition, it is a characteristic of the Ecuadorian market to have contact people in each productive sector. It is necessary to learn about the associated networking to maximize market entry, as keeping constant control of the country situation in order to take advantage of market conditions.

In terms of business etiquette in Ecuador, meetings are formal but at the same time personal. Ecuadorian businessmen are not entirely familiar with punctuality at meetings. Also, it is customary that in a formal business meeting, Ecuadorians start with casual conversation such as health, sports, among others.

Businessmen from the coast are faster decision-makers than Andean businessmen due to their traditions and corporate culture.

OTHER COUNTRY-SPECIFIC ISSUES RELATED TO ESTABLISHING A COMPANY

Investment incentives

- Income tax: 22% for productive investments that do not come from tax havens.
- Exemption of the prepaid income tax for 5 years, applied only to new companies, from the beginning of their productive period and to companies whose shares (at least 5%) are transferred to their employees.
- Additional 100% reduction of depreciation expenses for new eco efficient machinery.
- Exemption of the currency outflow tax for dividends paid abroad by companies in favor of foreign companies or persons, except fiscal havens.
- Additional 10% reduction on income tax, on the amount reinvested in productive assets.

Labor information

- Working hours: 40 hours per week
- Standard work day: 8 hours daily
- Vacations: 15 days per year

Schools with higher percentage of students enrolled in universities

- Business administration and law 34.59%
- Education 12.89%
- Health and Welfare 12.76%
- Industrial Engineering and construction 12.21%

An important consideration for potential investors is Ecuador's geolocation. From the middle of the world Ecuador is equidistant from the main markets and destinations in the two hemispheres, north and south. This results in competitive advantages like shorter transport time and lower transport costs. In addition, the country's infrastructure makes production, shipping and trade easier.



PERMANENT ESTABLISHMENT IN ECUADOR: BRANCH OR SUBSIDIARY?

DEFINITION OF A PERMANENT ESTABLISHMENT

Article 9. Permanent establishment of foreign companies

- 1) For taxation purposes, permanent establishment is the fixed place where an organization performs all or part of its activities. Under such circumstances, it is considered that a foreign company has a permanent establishment in Ecuador if:
 - a) The company maintains fixed-locations of economic activity such as
 - I) Any branch, agency or office that performs on behalf a foreign company name
 - II) Manufactures, workshops, real properties or other type of instalments.
 - II) warehouses
 - b) The company maintains an office for
 - I) Technical consulting, finance or any other type of consulting for the development of projects related to contracts done inside or outside the country.
 - II) Service provision by people that perform in public shows, such as: theater actors, movie actors, tv, radio, bullfighters, athletes etc.
- 2) However, besides the data exposed on 1), a foreign company is also considered as a permanent establishment in Ecuador if it posses a person or entity that acts on behalf of that company; and performs any economic activity different from the activities established in item #3 of this article. In any of the following ways:
 - a) If the society has power that allows it to conclude contracts in the name of the company or legally bind the people or companies who they work for.
 - b) If it is linked through a contract in order to develop economic activities on behalf of the people or companies they work for;
 - c) If it provides with the storage of products that belong to a foreign company, intended for sale in Ecuador and;
 - d) If it pays in the name of a foreign company for the rent of commercial locations, for services or expenses involved on the development of an economic activity.
- 3) The definition of a permanent establishment does not include:
 - a) The use of facilities with the only purpose of exposing goods or products
 - b) Having a location with the only purpose of collecting data for the company
 - c) Develop activities through and intermediary, agent, distributor, or any other that posses and independent statute. Only if this intermediaries act under the legal frame of its economic activity.

DEFINITION AND MAIN DIFFERENCES BETWEEN A BRANCH AND A SUBSIDIARY

Branch: Is a new selling point established for the company growth and with the purpose of capturing more clients or cover a larger target market in a city or in a country. The branch will only sell the same products that the main office does.

Subsidiary: Is a society with an independent value, and it does not have any type of corporate link with the



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society that has control over this subsidiary. One main office can have dozen of subsidiaries, or just one. In any case, the main office is able to exert control when it has more than half of the voting rights. Wich provides the main office with authority over finance and functional decisions.

TAX AND ACCOUNTING OBLIGATIONS

Tax Obligations

- 1) Obtain RUC: Unique registration of taxpayers, known as RUC, corresponds to the identification of taxpayers performing an economic activity in a legal way. This is why, every society, national or international, that start any economic activity or own properties that need to be taxed are obliged to stop by inmediately to the SRI offices to obtain a RUC number. Likewise, if the society ends its activities, it should inform the SRI with 30 days in advance.
- 2) Present tax returns and statements: Societies are required to present the following tax statements online to the Statements System or at the Finance System window office. These statements should be consolidated balance sheets independently from the number of branches, agencies or stablishments that the company holds.

* Value added-tax (IVA) statement: Should be done monthly, in the Form 104.

* Income tax Statement: Should be done every year, inside the Form 101, indicating the corresponding values in the blanks related to the statement of financial position and income statement.

* Income tax withholdings at source statement: Should be done monthly, in the form 103.

* Excise taxes statement: This applies specifically to the societies that provide services agravated with this tax, these companies are required to present this statement in the Form 105.

REGISTRATION FORMALITIES

Steps to set up a business

Starting in 2014 , the new online system of the Superintendence of Companies to set up a business is simpler and faster, since it can be done via internet. Setting up a new company within only 6 steps in 2 days, is the shortest time for the procedure in Latin America.

- 1) Go to the website www.supercias.gob.ec and select the option "Portal de constitución electrónica de compañías". The system takes you to the main menu where a user name must be registered.
- 2) In the "Reserva de denominacion" link, register the name of the company. Enter data of partners/ shareholders, address, activities; also, enter the completion of capital in shares and then legal representatives' data. Also attach the documents required from shareholders.
- 3) Select the public notary according to the new company's location and address. The notary is responsible for entering the system, validating the information and assigning the date and time for appointments to sign the deed and appointment of the legal representatives.
- 4) The Commercial Registry will validate the information and facilitate the registration of the deed and by-laws.
- 5) The system will forward the information to the Internal Revenue System (SRI) and issue the Registro Unico de Contribuyentes (RUC) of the company.
- 6) The system will also issue the registration number and will notify the legal existence of the company.





HOW TO HIRE MY FIRST EMPLOYEE IN ECUADOR

MAIN LEGAL STEPS TO FOLLOW TO HIRE A FIRST EMPLOYEE

- 1) Sign the contract (between employer and employee)
- 2) Develop the employee entry notification to the IEES (INSTITUTO ECUATORIANO DE SEGURIDAD SOCIAL)

DESIGN AND CONTENTS OF AN EMPLOYMENT CONTRACT

Contents of an employee contract

- Contracting parties
- Subject of contract
- Salary and form of payment
- Term of the contract
- Place of work
- Working time
- Assignability of wage increases
- Sanctions or penalties
- Inventions
- Mobility
- Confidentiality
- Acceptance
- Subscription or enrollment

CAN SOMEBODY DO BUSINESS FOR ME AND NOT BE AN EMPLOYEE?

Every natural person and legal person can do business between each other, without being employees. This is possible due to the existence of invoices issued for services provided.



HOW TO READ FINANCIAL STATEMENTS IN ECUADOR

CIA XYZ

STATEMENT OF FINANCIAL POSITION COMBINED

CIA X; CIA Y.; CIA Z. (AUDITED REPORTS)

AT DECEMBER 31, 2015 - 2014 AND 2013
(Express in american dollars currency)

ASSETS		DECEMBER, 31	
CURRENT ASSETS	NOTES	2015	2014
Cash and cash equivalents			
Financial assets held to maturity			
Trade accounts receivables			
Other accounts receivables			
Account receivables to related companies			
Inventories			
Taxes receivables			
Prepaid expenses			
Other assets			
Total Current Assets			
 NON CURRENT ASSETS			
Properties, plant and equipment, net			
Investment property			
Other assets			
Other accounts receivables			0
Total Non Current Assets		-	-
TOTAL		-	-



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CIA XYZ STATEMENT OF COMPREHENSIVE INCOME COMBINED

CIA X; CIA Y.; CIA Z. (AUDITED REPORTS)

AT DECEMBER 31, 2015 - 2014 AND 2013
(Express in american dollars)

	NOTES	December 31,	
		2015	2014
NET SALES			
COST OF SALES			
Gross Income			
OPERATING COSTS:			
Administration Expenses			
Expenses for sells			
Total of operation Costs:		-	-
Profit before interes and taxes		-	-
Other Expenses (Incomes):			
Other Incomes			
Financing Expenses			
Profit before employee profit - sharing		-	-
EMPLOYEE PROFIT - SHARING			
Profit before income tax		-	-
INCOME TAX	23 c		
Current			
Defered			-
Net Benefits		-	-
Losses Absortions with shareholders contributions for future capital increase			-
Net Benefits		-	-