



TAX TREATMENT OF LOSSES OR DECREASES IN PRODUCTION STAGES UNDER THE INCOME TAX LAW.



RECENT AUTHENTIC INTERPRETATION ISSUED BY THE LEGISLATURE.

One of the situations inherent in the productive activities that most occupies the efforts of the companies is the reduction of losses or decreases resulting from their own production or marketing activities.

Decreases in production is understood as the loss in the volume, weight or unit of measurement used on the goods due to different factors that may include the nature of the product itself, its storage, conservation, transport and handling for sale. On the other hand, a loss in the sense that it is incumbent on the fiscal regulation is understood as the effective absence of the goods without these have been commercialized and have been able to produce income to the Company.

Salvadoran income tax legislation, in defining the deductible cost of goods, establishes in Article 28 the general rules of deductibility, which provides that net income shall be determined by deducting from the income obtained the costs and expenses necessary for the production of the income and for the conservation of its source that such law determines, as well as the deductions established by it, which must comply with all the deductibility requirements prescribed in the Law, not being deductible costs and expenses that are linked to activities that

generate non-taxed income or that do not constitute income.

Article 29 numeral 11 of the Income Tax Law provides that the cost of products sold shall be deductible from the income obtained. The interpretations that the Tax Authorities in such sense, excluded from the possibility of deduction those products or goods that for any reason did not conclude with an effective sale, among them for reasons of losses on such products or losses of the same, since the same article in mention establishes that is deductible from the income obtained only the cost of production corresponding to the goods that have been sold in the respective fiscal year or period of taxation.

Thus, the differences between the products produced and those sold were to be considered as non-deductible expenses, with the consequent economic injury to the companies, which in addition to receiving the impact of the loss itself are affected by the fact that they are unable to take advantage, for tax purposes, of the amounts incurred for the production of such goods.

However, through Legislative Decree No. 345, dated May 30, 2019, an Authentic Interpretation was made to article 28 of the Income Tax Law in the

sense that according to such Decree should be understood as cost and expense necessary for the production of income and for the conservation of its source, purchase costs and all those that are necessary and proper to the business, destined exclusively for the purposes of the same and as a deductible consequence of the income obtained, such as all those losses, decreases, or expenses necessarily incurred for the production of income and to maintain the source generating income, regardless of the item in question, in the sectors of industry, commerce or services that involves a measurable, recognizable, inherent to the activity and with a real cost, in the activity developed, such as for example the trade of perishable goods, the trade of consumer goods, textiles, the electrical industry in all its stages, the hydrocarbons sector in all its stages, among others. However, the same Decree establishes as a requirement to be deductible that the decrease, loss, expense or cost be duly documented and recognized or accredited by the corresponding current bodies or regulatory entities.

Consequently, it will be necessary, in order to consider a loss as a deductible, for there to be recognition by a regulatory body of the economic sector to which the Taxpayer corresponds. In this sense, in principle it would seem that the deductibility of losses or losses could be exploited by companies that are in regulated markets. In any case, it is advisable to analyze the particular situation of each company before making a decision on whether or not to deduct the production losses or decreases for tax purposes.

Written by:



Emilio Rivera
Associate
emilio.rivera@ariaslaw.com
(503) 2257-0900

