



IS YOUR INACTIVE ENTITY PREPARED TO REPORT TO THE TAX AUTHORITIES?

MONTHLY NEWSLETTER THE LAW FIRM OF CENTRAL AMERICA

Since the Law for the Strengthening of Public Finances entered into force in July 2019, a new condition was created for all those legal entities incorporated in the country that do not carry out an economic activity (“inactive entities”) since they were given the characteristic of taxpayer. Although, in essence, these entities do not seek profit.

This new requirement created associated duties, mainly the need to file an income tax return. The tax return was recently modified to become an informative statement of assets, liabilities, and equity. Although this obligation will not generate a tax determination, it would provide relevant information for related tax purposes.

The inactive asset-holding entities became an easy way to protect the assets of individuals but also allowed many people to acquire assets with resources not necessarily reported to be taxed in the country.

The Tax Administration seeks to have the possibility of executing controls for the acquired goods and have a basis for possible future transactions that must pay taxes through this information along with other data sources that it has access.

If the entity has done things right, should the owner worry? The obvious answer would be no. However, although the entity made the acquisitions in order, these must be properly documented. In an audit process, the first thing that would be required are documents (accounting and legal), which, if they do not reflect the reality of the entity, can lead to headaches and long administrative and even judicial processes.

The owners of inactive entities must consider the importance of meeting the obligations and requirements to comply with them. One of the central axes of this new requirement is the preparation of accounting records under the "IFRS" standard (International Financial Reporting Standards). Several sectors have argued against using this standard for an entity that does not carry out an economic activity. However, it must be applied as a special tax requirement and not as the standard for financial purposes.

Another important axis is the legal documentation that should reflect the entity's properties and how it came to own them without carrying out an economic activity generating value. Thus, there must be integrity between the entity's assets, its economic value, and its documentary and legal support.

Many people might think that there are no consequences derived from this obligation since it does not result in tax payment. However, failure to file the return can become a wake-up call for the Tax Administration. Additionally, with the recent changes in the informative tax declaration, the failure to comply with the obligation could be subject to a fine of 3 basic salaries (approximately ₡1,400,000).

If you do not have the information of your inactive entity prepared, we recommend using the additional time given by the Tax Administration to prepare the data. November 15, 2022 is the due date to file the information for periods 2020 and 2021.

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