



**GARCIA & BODAN**

Attorneys & Counselors at Law

# **DOING BUSINESS** El Salvador







# El Salvador

**E**l Salvador is located in Central America, bordering Guatemala to the north, Honduras to the east, The Pacific Ocean to the west and Nicaragua to the south, by the Gulf of Fonseca. It has a population of 6,518 million and a total area of 21,040 km<sup>2</sup>, making it the smallest country in the region. El Salvador's labor force is composed of 2.8 million people, 60% of whom is 39 years or younger.

## Legal Framework and Incentives

- The investment law seeks to encourage private and foreign direct investment enouncing the next benefits:
  - ✓ Procedure streamlining.
  - ✓ Equal rights to all investors. This implies equal opportunities and obligations regardless of whether they are local or foreign investors; as well as the non-application of discriminatory measures that hinder the establishment, administration, use, extension, sale and liquidation of the investment.
  - ✓ Freedom to invest.
  - ✓ Transfer of funds abroad (foreign investors are guaranteed of being able to transfer funds abroad, without delay and with the freedom to convert currency through the banking system).
- Protection of property and security (in accordance with the Constitution, foreign and national investors are guaranteed protection of their property).

# Business overlook

- El Salvador has evolved over the last two decades. Today it offers to its business partners:
- ✓ An economy among the freest in Latin America.
- ✓ Proven macroeconomic stability, with the U.S. dollar as legal tender.
- ✓ Openness to global trade and investment.
- ✓ Democracy and political stability.
- One of the most important policies implemented to open country's economy to world trade and investment is the adoption of the U.S. dollar as legal tender in 2001. As a result, El Salvador has achieved a single-digit inflation rates for over a decade, remaining below the average of the rest of Latin American countries.

## Law on Industrial and Commercial Free Zones

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- El Salvador offers generous tax incentives to export-oriented manufacturing companies located in Free Zones or warehouses for inward processing. Free Zones are industrial parks considered outside the national territory for fiscal purposes, and thus raw material or merchandise required by companies are imported free of taxes and tariffs. If a company, due to technical reasons, is unable to operate inside a free zone, it can be authorized to operate outside as a warehouse for inward processing and enjoying the following benefits:
- ✓ Full exemption from customs duties and other taxes on the import of machinery and equipment used for production.
- ✓ Full exemption from customs duties and other taxes on the import of raw materials and other goods used for production.
- ✓ Full exemption from taxes on the transfer of real estate property, for the acquisition of real estate that will be used in the incentivized activity.
- Companies may be established and operate inside a Free Zone, if their owners are natural or legal persons that engage in:
- ✓ The production, assembling or maquila, manufacturing, processing, transformation or commercialization of industrial goods, with exception of those that are mentioned in article 6 of this Law.
- ✓ Fishing of maritime species to be subject to industrial transformation.
- ✓ Cultivation, processing and commercialization of flora species produced under protective structures in greenhouses and laboratories.
- ✓ Breeding and commercialization of amphibious species and reptiles in captivity.
- ✓ Ethyl alcohol dehydration.
- Natural and legal persons may obtain benefits from this law, when they own any of the following type of companies:
- ✓ Developers of Free Trade Zones.
- ✓ Administrators of Free Trade Zones.
- ✓ That are established in Free Zones as users.
- ✓ Those that their facilities are declared as warehouses for inward processing.

## International Service Law

- An individual or legal entity, national or foreign, that meets the requirements of this Law, will enjoy the benefits set herein, when engaged in the provision of international services, specifically the following: international distribution, international logistics operations, international call center (known internationally as “call center” or “contact center”), information technology, research and development, repair and maintenance of marine vessels, repair and maintenance of aircrafts, business processes, physician-hospital services, international financial services, repair and maintenance of containers, repair of technological equipment, elderly and nursing care, telemedicine, filming.
  - Notwithstanding the foregoing, an individual or legal entity, national or foreign, may settle in a services park to engage in the provision of the services listed below, without enjoying benefits and tax incentives granted under this Law; and thus, being obliged to comply with existing national tax regulations:
- ✓ Hotels.
  - ✓ Airlines.
  - ✓ Supply, generation and distribution of electricity.
  - ✓ Communications and telecommunications services except information services provided by international call centers, known in the trade as call centers and telephone companies that do not have their own fixed networks and that exclusively engage in international brokerage services of termination and incoming traffic; however, these latter ones will not enjoy the benefits conferred under Articles 21 and 25 of this Law.
  - ✓ Banking, financing and insurance services.
  - ✓ Air, land and sea transportation.
  - ✓ Tourism, travel agencies, expresses mail or couriers.
  - ✓ Technical and professional such as: juridical, taxation, construction, real estate, publicity, consulting services.
  - ✓ Food provision whether prepared or not, destined to employees or companies beneficiaries of this Law and by any other liberating regime.
  - ✓ Any type or private security mechanism.
  - ✓ Leasing of any kind, except those provided by administrators to direct users of the services park.





## Law of Fiscal Incentives to promote Renewable Energies in Electricity Generation

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- This law aims to promote investment in renewable energy sources (hydraulic, geothermal, wind, solar and biomass) to generate electricity; fostering research, exploration and project development activities, offering the next benefits:
- ✓ Full exemption (during the first 10 years) from customs duties on imports of machinery, equipment, materials and supplies intended exclusively for pre-investment and investment activities in the construction of the electrical power generation centrals.
- ✓ Full exemption from income tax for a period of five years, for projects between 10 and 20 megawatts (MW), and for ten years, for projects under 10 megawatts (MW).
- ✓ Total exemption from taxes on revenues originated from the sale of Certified Emissions Reductions (CER) in the framework of the Clean Development Mechanism (CDM) or similar carbon markets.
- ✓ In addition, projects over of 20 megawatts (MW) of capacity may deduct from income tax (for a maximum period of 10 years), all expenses or costs on research, exploration and preparation of projects to generate electricity based on renewable energy sources, as well as geothermal reinjection projects.

## Tourism Law

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- Tourism projects with a minimum investment of USD 25,000.00 are eligible to be declared of “national touristic interest” and enjoy the following benefits:
- ✓ Full exemption from taxes on the acquisition of real estate property, intended for the project.
- ✓ Full exemption from customs duties and other taxes on the import of goods, equipment and accessories, machinery, vehicles, aircrafts or maritime vessels and construction materials used for buildings until the completion of the project.
- ✓ Full exemption from income tax for 10 years period.
- ✓ Partial exemption from municipal taxes (up to 50%) for a period of 5 years, beginning in the fiscal year in which the business initiate operations.



## Special Law of Streamlining Procedure for the Promotion of Construction Projects

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- This law aims to speed up the approval of permits and authorizations for construction and land fragmentation projects throughout the national territory, regardless of its nature. This law describes the next benefits:
- ✓ Creation of a One-Stop-Office for the reception and processing of construction and land fragmentation project applications.
- ✓ Development of a centralized information technology system to track applications.
- ✓ Publication of updated information about requirements, administrative procedures, criteria and environmental and cultural zoning.
- ✓ Procedure streamlining (if a public authority doesn't take decision within the established deadlines, it shall be understood that the resolution has been issued in favor of the applicant, enabling him to continue with the process).

## Special Law of Public & Private Partnerships

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- This law establishes a legal framework for the development of Public and Private Partnership (PPP) projects regarding public infrastructure, public services or national interest activities:
- ✓ The PPP Law is applicable to projects in which a private sector investor is entrusted by a public entity to design and build an infrastructure project and its related services, or to build, rehabilitate, upgrade or equip, as well as the responsibility to operate and maintain such infrastructure. It will also be applicable to infrastructure projects for the provision of public services or the exploitation or the execution of a national interest activity.
- ✓ The minimum investment to qualify for a PPP project is 45 thousand times the trade and services minimum wage (approximately USD 11.3 million).
- ✓ 40 years-is the maximum period for a PPP contract.
- ✓ Private initiative regime: Private investors may propose new projects to be publicly tendered if such are declared of national interest by a government institution. This provides attractive advantages for those who submit project proposals.
- ✓ PROESA is the advisory and governing authority of Public and Private Partnerships (all PPP projects are approved by its Board of Directors).





## Law of Legal Stability for Investments

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- This law guarantees legal certainty to investors on taxes, customs and immigration issues through Legal Stability Contracts.
- Individuals and legal entities, national or foreign, with new investment projects or the expansion of existing investments within the following eligible activities, may benefit from this law:
  - ✓ Aeronautics
  - ✓ Agroindustry
  - ✓ Aquaculture
  - ✓ Electronics
  - ✓ Energy
  - ✓ Health Services
  - ✓ Light Manufacturing
  - ✓ Logistics
  - ✓ Offshore Business Services
  - ✓ Science and Technology
  - ✓ Strategic Infrastructure
  - ✓ Telecommunications
  - ✓ Tourism
- Once a Legal Stability Contract is signed, private investors shall benefit with the following guarantees:
  - ✓ Tax stability at national level.
  - ✓ Tax stability at the municipal level.
  - ✓ Stability in tax exemptions provided by special legislation for the period of time in which these were granted by the relevant institution.
  - ✓ Stability on customs procedures.
  - ✓ Stability on the right to transfer funds abroad as stated in the Investment Law.
  - ✓ Stability on the immigration regime, concerning the investor's residence status.
- To be eligible for these benefits, investor's shall comply requirements stated in this law. Among which is the commitment to invest an amount on fixed assets, greater than or equal to four thousand two hundred and twenty times the industry minimum wage (USD 246.60); this is equal to USD 1,040,652.00 in new investment projects or the expansion of existing investments.
- Benefits are granted for a period of up to 20 years, depending on the amount of the investment.



# Taxes

## Income Tax

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- A 30% tax rate is applied over taxable income. For legal entities with a taxable income less than or equal to USD 150,000.00, a reduced tax rate of 25% is applied. Income tax exemptions are described as it follows:
- ✓ 100% of exemption for 15 years to entities in a Free Trade Zone operating in San Salvador Metropolitan Area. If it is a warehouse for inward processing, the exemption term would be for 10 years. If the Free Zone operates outside San Salvador Metropolitan Area, the exemption is 100% for 20 years. In case of a Warehouse, the exemption will be of 15 years.
- ✓ 60% of exemption for the following 10 years to entities in a Free Trade Zone operating in San Salvador Metropolitan Area. For a warehouse for inward processing, the exemption will be 60% for the following 5 years. If the Free Trade Zone operates outside San Salvador Metropolitan Area, the exemption is 60% for the following 15 years. If it is a warehouse, the exemption will be 60% for the following 5 years.
- ✓ 40% of exemption for the following 10 years to entities in a Free Trade Zone operating in San Salvador Metropolitan Area. If it is a warehouse for inward processing, the exemption will be 40% for the following 10 years. The same exemption applies both if they are located outside San Salvador Metropolitan Area.

## Branch Profits Tax

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- Branches of foreign companies are subject to the same tax rates as Salvadoran companies.

## Dividend Tax

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- Dividends paid or credited to shareholders (individuals or legal entities) are subject to a 5% income tax rate.

## Tax on Transfers of Real Estate Property

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- The transfer of real estate is subject to a tax rate of 3% applicable on amounts over USD 28,571.43.

## Value Added Tax

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- Transfer of services and goods are subject to a 13% of tax (IVA). The following items are exempt from IVA: public health, home rentals, education, state titles, public water, public transportation, pension funds and public lottery.

## Company and Establishment License

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- All industrial and commercial businesses are required to have an annual license to operate. This tax is paid based on the company's total assets according to the following rates:
- ✓ From USD 2,000.00 to USD 57,150.00 the entity pays USD 91.43.
- ✓ From USD 57,151.00 to USD 114,286.00 the entity pays USD 137.14.
- ✓ From USD 114,287.00 to USD 228,572.00 the entity pays USD 228.57.
- If assets exceed USD 228,572.00, USD 11.43 will be paid for every USD 100,000.00, up to a limit of USD 11,428.57.

## Municipal Taxes

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- Taxes are paid according to a table established by each municipality based on the company's total assets. For example, in San Salvador rates are determined by the company's activity (industrial, commercial or other).





# Investment Opportunities in El Salvador

## Aeronautics

- El Salvador has more than 30 years of successful experience operating an aircraft maintenance, repair and overhaul (MRO) industry, placing the country on the global aeronautics map.

### Advantages of investing in Aeronautics

- ✓ Aeronautics Clusters with renowned companies such as Aeroman, Avianca and Volaris.
- ✓ Labor costs up to 40% more competitive than United States/Mexico border operations.
- ✓ Geostrategic Positioning, proximity to the world's largest aviation market.
- ✓ High productivity.
- ✓ Low employee turnover with less than 2% per year, key factor for training and performance.
- ✓ Engineering and technical degrees in Aeronautics.
- ✓ Availability for Industrial Land.
- ✓ Attractive Fiscal Incentives.

## Energy

- The government of El Salvador has an energy policy for the 2010-2024 period. Among its strategic lines we can find:

- ✓ Diversification of the energy matrix.
- ✓ The promotion of renewable energy sources.
- ✓ Innovation and technological development.
- ✓ Regional energy integration

### Advantages of investing in Energy

- ✓ Processes of international bidding and long term contracts of up to 20 years based on implemented market costs.
- ✓ Diversification of the energy matrix: wind, geothermal, hydroelectric, biomass, biogas, solar, coal and natural gas.
- ✓ Distributed generation projects at industrial level.
- ✓ Large hydraulic, geothermal and solar projects in national public generation.
- ✓ Categorization of activities or projects for the better use of renewable energy sources in conjunction with the Ministry of Environment and Natural Resources.
- ✓ SIEPCA interconnection line.



## Tourism

- In recent years, the tourism sector in El Salvador has undergone a significant expansion, creating lots of investment opportunities. The natural wealth of the country, attractive fiscal incentives provided by the Tourism Law as well as the strategic support from the government, has made tourism one of the most booming sectors of the country.

### Advantages of investing in Tourism

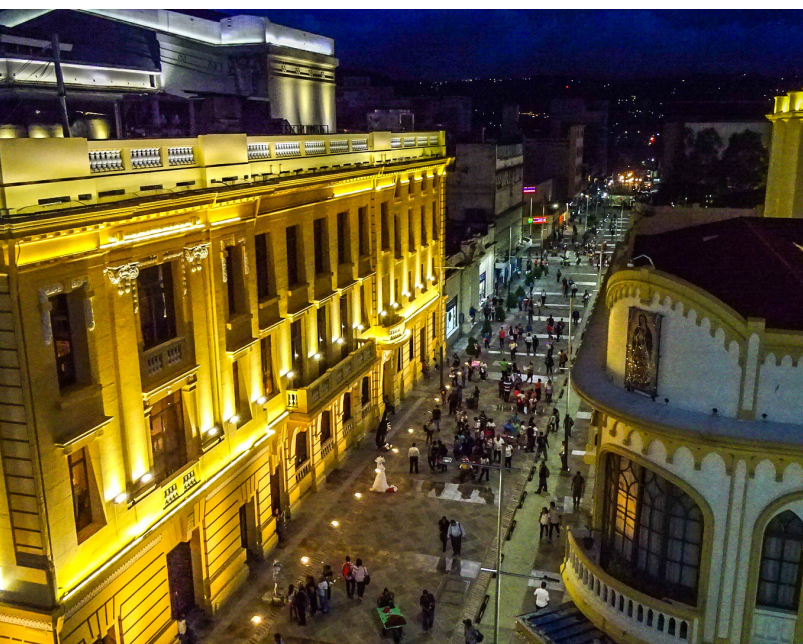
- ✓ Solid and growing tourism demand.
- ✓ Political stability.
- ✓ Healthy and completely dollarized economy.
- ✓ Air traffic hub with over 470 weekly arrivals and departures.
- ✓ Hard-working and service-oriented work force.
- ✓ Pleasant climate throughout the year.
- ✓ Attractive fiscal incentives provided by the Tourism and International Services Laws.
- ✓ Availability of human resources.
- ✓ Health services provided at costs significantly lower than the United States and Canada.

## Agroindustry

- El Salvador offers an ideal location for the production and processing of foods, as well as to address specific market niches that goes beyond the tradition agricultural industries.

### Advantages of investing in Agroindustry

- ✓ Suitable climatic (temperature and altitude) and soil conditions to grow ornamental plants and fruits.
- ✓ Excellent road and port infrastructure.
- ✓ Free trade agreements that provide favorable market conditions to access major markets in America and Europe.
- ✓ Availability of water resources for sustainable aquaculture development.





# Labor Law

- El Salvador's Labor Code regulates employer-worker relations. Salvadoran legislation states that wages are determined freely, but cannot be lower than the minimum salary established by the National Wage Council, revised every three years.

## Working shifts

- ✓ Day Shift between 6:00 am and 7:00 pm.
- ✓ Night Shift between 7:00 pm and 6:00 am.

## Fringe benefits

- ✓ Annual paid vacations.
- ✓ Social Security (ISSS).
- ✓ Training fund.
- ✓ Christmas bonus.
- ✓ Retirement fund.
- ✓ Compensation for voluntary resignation.
- ✓ Compensation for unjustified dismissal.

- Besides all the benefits previously describe, El Salvador integrates a new modern legislation to attract investment such as the Electronic Signature Law, E-commerce Law and the Special Law against Informatic Crimes and other Related Offences.

# Electronic Signature Law

- With the main purpose of equate the simple and certified electronic signature with the handwritten signature, this new regulation comes to: Consider documents on electronic support using electronic signature, will have the same effects that those consigned on a traditional way. This new law will allow:

- ✓ Save costs: It would not be necessary to mail documents for the clients of various services affixed their signature.
- ✓ Save time: It would allow distributing, organizing, visualizing and signing any document completely online. With the new law, a signing process that could last for days, now can be solved in minutes.
- ✓ More security: Technology allows easily implementing a handwritten signature. In this way, electronic signature has more secure systems to avoid falsification.



# Special Law against Informatic Crimes and other Related Offences

- In order to protect fundamental rights such as honor, privacy, image, property and computer security, the Computer Crimes Law was introduced in our legal system. This legislation seeks the prevention and punishment of crimes committed through the use of Information and Communication Technologies (ICT), which attempt against natural and legal persons.
- This regulation is aimed at combating criminal activities committed through ICTs, by establishing mechanisms to facilitate their detection, investigation and punishment, under new criminal offenses created in such standard.
- The law shall apply even if the execution of the action or execution of the act begins in foreign territory and is consummated in El Salvador, or if it has been carried out using the ICT installed in the national territory, when the responsible party has not been tried for the same act by foreign courts or has evaded trial or conviction.





We, at García & Bodán, are ready to support you in all legal matters of interest to your company or business, we have highly qualified lawyers on investment issues.

For further information related to investment matters or any of the topics included on this document, please contact:



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