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## Tax return filings now in question!

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Special to A.M. Costa Rica

"Round and round it goes, where it stops, nobody knows."

Does that quote refer to a roulette table or to Costa Rica's tax Law 9635? Apparently, to the latter. The country's decision-makers cannot make up their minds whether or not companies that are not active will have to file income tax returns on the due date Dec. 16.

The law passed the legislature Dec. 3 and was valid Dec. 4. However, it had no bylaws, the nitty-gritty regulations and rules that make a law work in practice.

Article 2 of Law 9635 is very clear and defines tax contributors as, ". . . todas las personas jurídicas legalmente constituidas, con independencia de si realizan o no una actividad lucrativa, las sociedades de hecho, las sociedades de actividades profesionales, las empresas del Estado, los entes colectivos sin personalidad jurídica y las cuentas en participación que haya en el país."

Notary and professional translator Ulises Obregón put the Spanish text into English for this article as ". . . all legally formed entities in regard to whether or not they conduct commercial activity and profit from it, de facto partnerships, professional business, state-run organizations, unregistered collectives without legal and participation standings in the country."



Almost all tax experts interpret this text in the law to mean all those entities listed need to file an income tax return. Hacienda, the tax department, agreed and published the rule in its first version of the bylaws April 12.

The tax department is still working on those bylaws, and now in the second version of them published May 16, it appears officials are vacillating on their original decision. Now they propose to make a distinction between active and non-active companies and suggest that entities not doing business or otherwise not generating revenue will not have to file income tax returns because they have no, well, income.

Could it be they have figured out that receiving six times the number of returns they receive now might overload their system? Based on estimates, there are around 310,000 companies registered with the national registry according to Hacienda on April 12, but only an estimated 50,000 or so are doing business and filing income tax returns.

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They also have several significant problems. Here are two of the most important.

1. Many of the owners of the non-active companies that only hold assets cannot file timely because they are not in the country. This fact alone would create a real mess trying to track down all the non-filers and penalize them.

2. Most of the companies created by notaries over the years have very low capital values. This practice creates a nightmare for tax practitioners and auditors because tax cheaters play with capital to hide income. If companies that only hold assets with low capital values filed, the tax department's computers would spit them all out with to-be audited flags.

For example, John and Jane Doe bought a house to retire in Costa Rica valued at \$100,000. When they went to a notary, he suggested a company to hold the asset and protect it from personal liability. He created the entity with a capital value of ₡10,000 colons or about \$20. This practice is still prevalent today.

From a property registration point-of-view, this is just fine, but on a tax return, it looks like there is \$99,980 in unreported and untaxed income. So what is the tax department to do with that error when Law 9635 incorporates severe penalties for that type of discrepancy?

The bottom-line: The verdict is still out, but the good news is that it is possible companies registered as non-active with the Registro Nacional (Costa Rica's national registry) may not have to file a tax return Dec. 16 or March 16, 2020.

Now for the bad news. Costa Rica wants to know what non-active companies hold in assets. So if, in fact, no tax return is required, some other requirement not yet known may be necessary.

What is essential for all expats who hold companies to do is check the information at the Registro Nacional and correct it if necessary to ready themselves for whatever happens. The instructions to do so are in the article: How expats can prepare to file tax returns published May 6.

Here is a summary of the events and information concerning whether expats need to file income tax returns.

Law 9635, call "Fortalecimiento de las Finanzas Públicas" or just the "plan fiscal," fiscal plan in English, became law Dec. 4. The legislation did not have corresponding bylaws.

The first version of those missing bylaws published on April 12 included a mandate requiring all companies, whether active or non-active, to file tax returns.

Version two, published May 16, states non-active companies do not have to file income tax returns as reported on April 12 but may have to present something else yet undetermined.

Is Costa Rica playing games with its taxpayers in general and expats individually?

Probably not. The country is notorious for making short-sighted decisions without concern for logistics. That is pretty obvious considering officials planned to process six times the number of tax returns they do now loaded with blatant errors guaranteed to screw up the system.

The deadline or all revisions to the bylaws is July 1. Check back here for an update.

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