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Summary of Law N° 125/91 **Paraguayan Tax Reforms**

I. TAXES ON REVENUE

A. INCOME TAX

The tax applied to income from Paraguayan sources derived from commercial, manufacturing, service and farming activities as defined below.

1) Taxable Incomes

Income from commercial, manufacturing or service activities other than from personal services:

1. Income derived from the sale-purchase of immovable property when the activity is carried out as a permanent business;
2. Income generated by assets, and other income shown on commercial balance sheets, excluding income from farming which shall be governed by specific rules applicable for the sector, analyzed in subsequent chapters;
3. Income earned by commercial partnerships, as well as corporations established overseas, or branches, agencies, or business establishments in this country. Income derived from farming activities is excluded;
4. Income earned by the following activities: extractive industries such as mining and forestry, as well as activities in the farming sector to which the law gives special treatment such as flower farming, forestry, bee keeping, poultry farming and others;
5. Income earned by consignees of merchandise;
6. Income derived from providing certain services listed in the law but omitted at this time for the sake of brevity. The list is subject to amendment and should have been left to regulations.

2) Taxpayers

Taxpayers subject to income tax

1. Individual businesses, partnerships, associations, corporations and other private businesses.
2. Government-owned enterprises, self-governing government businesses, decentralized government corporations, and mixed capital corporations.
3. Branches, agencies or businesses operating in this country owned by corporations constituted overseas.
4. Corporations constituted overseas shall pay tax on income paid or accredited to them.
5. Individuals applying capital resources and personal labor jointly for the purpose of obtaining economic gain, except those involving strictly personal services or those engaged in farming.

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3) Paraguayan Sources

The following incomes shall be deemed to proceed from Paraguayan sources:

1. Income derived from businesses carried out, from goods situated in or from entitlements used for gainful purposes in this country;
2. Interest on securities and movable properties;
3. Technical assistance provided within the national territory when utilized or applied in this country;
4. Assignment of the use of goods and entitlements when used even partially during an agreed period, such as the use of a trademark or patent;
5. International freight on goods carried to bordering countries or Uruguay shall be deemed as 50 percent from Paraguayan sources.
6. All other freights shall be deemed 30 percent from Paraguayan sources.

4) Tax Obligation

At the close of a fiscal period all income accrued (billed) during the period shall be taxable. The fiscal period shall coincide with the calendar year but the Tax Administration may, in the case of businesses keeping their books according to generally accepted principles, allow the fiscal year to coincide with the economic season.

INCOME

Gross income is the difference between total billings and the cost thereof.

Net income is the difference resulting from deducting from gross sales any returned goods, gratuities and price discounts as applied in local business custom. When the business consists in the sale of goods, gross income shall be computed as total sales, less the cost of acquisition or production thereof.

Also considered as taxable income are:

1. Proceeds from the sale of fixed assets which shall represent the difference between the sale price and the cost or the revalued cost of the assets, minus amortization or depreciation allowed by law.
2. Proceeds from the sale of movable or immovable properties received in payment.
3. Any exchange rate differences resulting from transactions in foreign currencies.
4. Net benefits resulting from the collection of insurance or indemnities.
5. Proceeds from any transfer of enterprises or business firms.
6. Interest on loans or investments. (The law provides that such interest shall not be lower than the average rate applicable to fixed term bank deposits which rate shall be published monthly by the Tax Administration)
7. Deposits placed in entities governed by Law N° 861/96 (General Law on Banks and other Financial Institutions), a principle which should be extended by regulations to deposits in the Savings and Loan System.

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8. Any increase in net worth occurring during the fiscal year other than that arising from a revaluation of fixed assets or capital contributions or from exempt or non taxable businesses.

NET INCOME

Net income is calculated by deducting from gross income all expenses incurred to obtain the income and to maintain the source of income, provided they are real expenditures, duly documented.

The following expenses shall also be deductible:

1. Any taxes and social benefits applicable to the business assets and entitlements involved in the generation of income, except Income Tax;
2. Operating expenses of the business;
3. Personnel compensation provided contributions are made thereon to Instituto de Prevision Social (Social Welfare Institute) or retirement and pension funds established or admitted by law. Also deductible shall be any compensation paid to owners, partners or directors and to relatives and spouses, as limited by regulatory decree.
4. Organization or incorporation expenses;
5. Expenditures on interest and rentals or sums paid for the assignment of goods or entitlements;
6. Losses suffered through casualties not covered by insurance;
7. Reserves or write-offs for bad debts;
8. Losses incurred through crimes committed by third parties against property not covered by indemnities or insurance;
9. Depreciation;
10. The amortization of incorporeal entitlements such as trademarks and patents;
11. Expenses and payments made overseas whenever necessary to produce taxable income from export and import operations.
12. Travel expenses, per diem, and other similar payments in cash or kind.
13. Gifts to the State, Municipalities and religious entities or to entities dedicated to social welfare or education, recognized by the Tax Administration.
14. Professional fees and other compensation for personal services not subject to taxation;
15. Expenses and contributions paid to staff for health care, education, cultural development, or training;
16. Losses incurred in any fiscal year may be set off against earnings generated in the three following fiscal years. Regulations shall determined the method of application of set-off, whether they can be set off entirely in one fiscal year or whether they are to be deferred.

NON DEDUCTIBLE EXPENSES

Non deductible expenses include:

1. Interest on loans or advances from the owner of the business, partners or shareholders;

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2. Penalties for tax offenses;
3. Earnings in any fiscal period retained in the business as capital increases or reserve accounts.
4. Amortization of payments for good will.
5. Personal expenses of the owner, partners or shareholders, and advances drawn on account of future earnings.
6. Direct expenses involved in earning non taxable income.
7. Value Added Tax (VAT).

INCOME FROM PARAGUAYAN SOURCES EARNED BY BENEFICIARIES NOT DOMICILED IN THIS COUNTRY

When a beneficiary of Paraguayan income is not domiciled in this country, shall be taxable separately from taxes applicable to a branch or agency according to the following rules:

Income shall be deemed to be net income from Paraguayan sources according to the following percentages:

10% Rate

1. Insurance or reinsurance premiums;
2. Sales of travel tickets, radio message services, telephone calls and other similar services sent overseas from Paraguay;
3. Freight on international shipments.

15% Rate

1. Gross income earned by international news agencies;
2. Gross income earned by leasing of shipping containers;

40% Rate

Rentals on motion picture films or television programs or those of any other projection medium.

50% Rate

Income earned from sources other than branches, agencies or businesses situated in Paraguay.

100% Rate

Income earned by any other business arising from branches, agencies, or businesses situated in this country. Taxpayers may in such cases choose to pay taxes according to general tax rules by keeping adequate books of account for the verification of expenses and income.

PRESUMPTIVE INCOME

Taxpayers who do not keep regular books of account run the risk that the Tax Administration may establish a presumptive income on which to apply net income which in turn shall be subject to the tax rate established by law.

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Taxpayers engaged in businesses the character of which places difficulties to the application of generally accepted accounting principles may request the Tax Administration to apply a tax regimen based on presumptive income.

REVALUATION OF FIXED ASSETS

The law defines as fixed assets any goods owned or leased from third parties except those held for sale. Annual revaluation shall be mandatory and the updated value shall result from applying to the book value shown in the previous fiscal year the percentage variation based on the consumer price index as determined by the competent government body.

Revaluation shall be subject to a special tax equal to 1.5 percent and depreciation shall proceed on the basis of the upgraded value.

VALUE OF INVENTORIES

Merchandise in stock shall be carried on the books either at cost of production, cost of acquisition, or at market cost at the close of the fiscal year, at the taxpayer's option. The Tax Administration may accept other systems of inventory valuation.

Negotiable securities and valuables shall be computed at their market value at the close of the fiscal year. If they are not quoted on the market the purchase price shall be used.

Fixed assets and intangible assets shall be carried at their purchase cost without prejudice to their revaluation on an annual basis.

EXEMPTIONS

I. EXEMPT INCOME

1. *Dividends and earnings, except those paid to beneficiaries not domiciled in this country, which shall be taxed at a rate of 5 percent;*
2. *Interest on securities representing government or municipal debt;*
3. *Income declared to be exempted under Law N° 60/90 "Establishing a System of Fiscal Incentives for Investment of Domestic and Foreign Capital";*
4. *Interest on deposits in authorized banking institutions;*
5. *Interest on loans to authorized financial institutions;*
6. *Income from the professions and from labor under employment;*

II. EXEMPTED TAXATION ORGANIZATIONS

1. Recognized religious entities;
2. Charities, social welfare organizations, and similar entities, including legally recognized political parties, provided they are non-profit organizations and do not distribute surpluses to their membership;
3. Taxpayers subject to Sole Tax.

III. TEMPORARY EXEMPTION COOPERATIVES

The New Law N° 438/98 ruling Cooperatives grants exemptions to same.

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REINVESTMENTS

Exemption benefits manufacturers and reforestation projects. In the first case the investment must be applied to the installation, expansion or renewal of fixed assets devoted directly to the production of manufactured goods; or to reforestation projects in rural areas.

Investments shall involve new productive goods, except in the case of imported goods in which case they shall be in good usable condition and well maintained, suitable for the proposed manufacturing process.

Reinvestments must be effected in the same fiscal period, extendable to the following fiscal year, in which case they may not be distributed as dividends but shall be kept in a reserve account for the purpose of capitalization. The value of reinvestments in excess of net income for the fiscal period may be employed in future years.

Companies reinvesting as indicated above shall pay income tax at the rate of 10 percent and shall be exempt from the tax on remittances or accreditations of earnings or dividends to beneficiaries not domiciled in the country.

Branches or agencies of companies constituted overseas shall keep separate accounts from those of their head office. Payments of interest, royalties and for technical assistance made by branches or agencies to their head office shall be deductible items for the tax payers but taxable for the payees.

RATES

1. The general tax rate is 30 percent.
2. Sums paid or credited to head offices by branches, agencies, or businesses situated in this country shall be subject to an additional tax of 5 percent.
3. Income of individuals not domiciled in the country, earned independently from that paid or credited on activities conducted by branches, agencies or businesses shall be subject to the taxes listed above, limited to 5 percent in the case of earnings or dividends.

The Tax Administration is hereby empowered to require quarterly advances on annual income taxes, which shall not exceed the amount of taxes paid in the previous fiscal year.

INCOME FROM FARMING

Farming is the business conducted for the purpose of obtaining primary products, either vegetable or animal, by the utilization of land, excluding the business of handling, processing or treating farm products unless carried out by the same producer.

TAXPAYERS

1. Individuals.
2. Partnerships, whether incorporated or otherwise.
3. Associations, corporations and other private entities.
4. Government enterprises, self governing agencies, decentralized entities.

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5. Individuals or corporations engaged in taxable businesses, including foreign corporations and their branches and agencies.

GROSS INCOME FROM FARMING

Income is determined on the basis of the presumptive income which is estimated at 12 percent of the fiscal valuation of all lands held by the taxpayer under any title. Gross income shall be determined independently of whether or not exploitation actually takes place.

The National Catastral Service shall determine annually the fiscal value of land, excluding improvements and buildings, on the basis of average prices prevailing on the internal market during the twelve months prior to every November first.

DETERMINATION OF NET INCOME

The following shall be deducted from gross income:

1. Expenses necessary to produce and maintain income: up to 40% of gross income;
2. The value of any areas occupied by natural or planted forests and by permanent ponds;
3. The value of 20 hectares in the case of properties with less than 100 hectares.

TAX RATE

1. Tax rate is 25% on net income as determined.
2. The fiscal year shall coincide with the calendar year.
3. The Tax Administration may require advance payments on account of taxes.
4. This tax shall be applied once the Catastro Nacional directorate sets the value of rural lands in this country.
5. Once this tax becomes applicable the Tax on Marketing of Bovine Cattle shall be repealed.

SOLE TAX

Sole tax shall apply to commercial, manufacturing and service businesses other than personal services, conducted by individuals using their personal labor and capital to pursue economic gain, provided their total income in the previous year did not exceed an amount which is determined by the Government from time to time.

The tax base shall be determined on the basis of presumptions based on economic indicators according to taxpayer categories, allowing for factors such as salaries and wages paid, payments of utilities, rents, merchandise, raw materials and inputs purchased. Once the tax base is determined, a presumptive rate of return shall be established for each business or trade. The tax rate shall vary between 1 and 4 percent according to the category of each taxpayer.

In the determination of the tax payable deduction shall be allowed for 50% of all value added taxes actually paid by the taxpayer as evidenced by vouchers in his possession. Taxpayers in this category paying Sole Tax shall be exempted from payment of income tax. Once the tax base is determined, a presumptive rate of return shall be established for each business or trade. Current rate is 4%.

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TAXES ON CAPITAL

LAND TAX

Land tax applies to immovable properties situated in the national territory, and taxpayers shall be the owners or usufructuaries thereof. When the ownership is shared the tax shall be paid by any one of the owners.

TAX EXEMPTIONS

The following are exempted from land tax:

1. Immovable properties owned by the State and Municipalities.
2. Those owned by religious entities recognized by the competent authorities devoted on a permanent basis to the public service.
3. Lands declared to be historic national monuments, lands owned by recognized public welfare associations and in general any establishment devoted to hospitals or public welfare services.
4. Real estate owned by foreign governments.
5. Immovable properties used as permanent premises by political parties and educational, cultural, social, sports entities or labor unions whether owned or held in usufruct.
6. Properties of Chaco War veterans provided they or their surviving spouse live thereon.
7. Properties owned by the Rural Welfare Institute and lands set aside for settlement by the IBR.
8. National parks and ecological nature reserves.

In the event of natural disasters such as floods, land owners may request and the government may reduce land tax by as much as 50%.

TAX BASE

The base shall be the fiscal valuation of properties as set by the National Cadastral Service. Property values shall be increased until they match prices set by the market following the consumer price index, but increases shall not exceed 15% per annum. In the case of rural properties any improvements or buildings shall not be computed in the tax base.

TAX RATE

The tax rate shall be 1% of the fiscal value per year, reduced by 50% in the case of rural properties under five hectares in areas utilized for small scale farming.

No real rights shall be constituted on real estate nor may such rights be recorded by the General Directorate of Public Registries unless a certificate is exhibited evidencing payment of land tax.

Notaries Public involved shall be joint and severally liable for the land tax should they fail to comply with this rule.

Additional assessment on waste land

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Waste land is any property devoid of buildings or improvements or where the value of such represents. Municipalities shall be entitled to 50% of the revenue produced by the land tax in their districts and the entire revenue from duties on waste land.

TAXES ON CONSUMPTION

A. VALUE ADDED TAX (VAT)

Value added tax shall apply to any assignment of chattels, to services rendered and to the importation of goods. Excluded are personal services performed under employment.

The law defines "assignment" as any transaction for consideration or otherwise intended to transfer ownership of goods or granting to the assignee power to dispose of the goods as the owner thereof.

"Services" means any transfer, for consideration or otherwise which, while not being an assignment shall procure for the other party an advantage or profit.

Excluded are personal services rendered under employment, "employment" meaning any situation where the person employed contributes to a pension scheme or to the social security system allowed by law. "Importation" means the introduction on a definitive basis of goods into the national territory.

TAXPAYERS

1. Individuals engaged in individual or commercial activities when their gross income in the previous year exceeded approximately US\$ 5.000.
2. Partnerships and private entities in general engaged in the activities listed in paragraph a) including, specifically, those engaged in imports and exports.
3. Independent government entities, government enterprises and decentralized agencies engaged in any of the businesses listed above.
4. Importers of goods into this country not defined in the previous paragraphs.

The amounts provided in the law shall be adjusted in accordance with the consumer price index.

ORIGIN OF THE TAX LIABILITY

The tax obligation arises upon delivery of the goods sold, the issue of an invoice, or whichever happens first.

In the case of public services, such as energy, telephone water and sewage, on the due date of the invoice.

In the case of services, upon the issue of an invoice or payment, upon expiration of the payment term or upon termination of the service. In the case of imports the tax becomes payable at the time of entry of the goods into Customs.

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TERRITORIALITY

Sale of goods and provision of services in the national territory are subject to tax. In the case of technical assistance when it is used in the country; in the case of assignment of entitlements or the use of goods when such goods or rights are used even partially within the national territory.

In the case of insurance and reinsurance when they cover risks within the Republic or when the goods or persons covered are situated in or are residents of Paraguay.

TAX BASE

In transactions for a consideration the tax base is the accrued (billed) net price for the goods or services. To establish net price and in determining the price of goods used or consumed privately the same rules apply as in the case of income tax, in addition to any special provisions. When the price is not determined the price shall result from adding a 30% markup to the cost of goods. In the case of services subject to fixed price scales such prices shall be deemed to be minimum prices. The tax base shall in all cases include the value of other taxes applicable to the transaction but excluding value added tax.

In the case of imports the taxable base shall be the Customs value plus Customs duties in addition to other taxes applicable to the delivery of goods (Customs and dock fees) and internal revenue taxes, but excluding value added tax.

Imports by persons not listed in paragraphs a) through d) of Article 79 of this law (occasional importers) shall be subject to an additional 30% surcharge on the tax base.

EXEMPTIONS

I. SALE OF GOODS

1. Farm products in their natural state;
2. Foreign currencies, government or private bonds, securities including shares of stock;
3. Immovable properties;
4. Lottery tickets, betting slips;
5. Petroleum based fuels including alcohol fuel;
6. Goods received through inheritance;
7. The assignment of credits.

II. SERVICES

1. Interest on government or private bonds;
2. Leases of real estate;
3. Financial intermediation businesses as governed by the Law on Banks and Other Financial Institutions, including loans granted by overseas banks, with the following exceptions:
4. Commissions earned by brokering the purchase and sale of securities and as agents serving as payers of dividends, amortizations and interest;
5. Commissions earned on the issue and renewal of credit cards.
6. Sums earned by carrying out mandates and commissions unrelated with financial businesses.

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7. Management of securities portfolios, debt collections, technical and administrative assistance, leasing of movable goods.
8. Loans to and deposits in financial institutions authorized by the Central Bank of Paraguay, and in cooperatives, Credito Agrícola de Habilitación (Supervised Credit Farm Loans), the Home Savings and Loan system, National Development Bank, and Fondo Ganadero (Cattlemen's bank).

III. IMPORTS

1. Crude petroleum;
2. Travelers baggage;
3. Diplomatic service imports;
4. Goods to be applied directly to the productive cycle in manufacturing or farming in projects benefited by the incentives offered under Law 60/90, except when such goods can be produced locally.

IV. EXEMPTED ENTITIES

Non profit incorporated entities whose surpluses are not subject to distribution to their membership and whose sole aims are those for which they were created, and recognized religious entities, on acts related exclusively to worship and religious services. Importation of goods by them is subject to VAT.

V. EXPORTS

Exports and freight thereon for transportation of goods is exempted. Regulations shall list the requirements to be met by vouchers evidencing exports to qualify.

VI. BILLING-VOUCHERS

Every sale or service rendered shall be invoiced and the tax shown separately unless regulations authorize including the tax in the price.

VII. LIQUIDATION OF THE TAX-DEFINITIONS

Fiscal Debit is the sum of taxes accrued (invoiced as opposed to collected) by the taxable transactions in each month.

Fiscal Credit is the sum of taxes included in purchases of goods and services on the local market during the month or on imports. The tax shall be liquidated on the sum representing the difference between fiscal debits and fiscal credits.

Deduction of any fiscal credit is conditional on such credit arising from goods or services devoted directly or indirectly to the transactions subject to taxation.

Taxpayers rendering personal services may not deduct any fiscal credits arising from the purchase of motor vehicles.

When the fiscal credit exceeds fiscal debits the surplus may be carried over to future liquidations.

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LIMITS TO FISCAL CREDIT IN GOVERNMENT AGENCIES

Government agencies applying a tax rate lower than that in general use shall limit application of fiscal credit to the amount of their fiscal debit. Surpluses, if any, shall be a cost item for the taxpayer.

EXPORTERS FISCAL CREDIT

Exporters are entitled to a fiscal credit on their purchases of goods and services for export. The fiscal credit shall be set off against fiscal credits and any surplus may be applied to the payment of other taxes or returned by the tax authorities within 60 days of filing of the application for such return, supported by the necessary documents under applicable regulations.

Farm producers shall be entitled to similar treatment but fiscal credits shall be limited to 50% of the tax on goods and services acquired on the local market. Goods introduced into this country under the rules of temporary admission shall be entitled to the same tax treatment applicable to exports.

IMPORTS

VAT shall be paid at Customs before imported goods are released into this country. VAT paid by occasional importers shall be final. VAT paid by other taxpayers shall be booked as a fiscal credit.

The law provides for special treatment in the case of purchases and sales of used goods, for taxpayers that do not meet the prescribed minimum or when practical reasons recommended facilitating tax collection.

TAX RATE

Current tax rate is 10%.

CARRIAGE OF GOODS

Any goods transported within the national territory shall be accompanied by an invoice or equivalent voucher. Goods in violation of the law may be retained by the authorities together with the vehicle on which they are carried. The carrier shall be joint and severally liable for taxes due on the carried goods.

B. SELECTIVE TAX ON CONSUMPTION

This tax applies to imports of goods and to their initial sale in the case of domestic products. They are divided in four sections listed as follows:

Section I

All kinds of cigarettes, with a tax rate of 7 to 8%

Section II

Mineral water, juice, beer with a tax rate of 8 to 10%

Section III

Alcohol with a rate of 5 to 10%

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Section IV

Oil byproducts with a tax rate of 50%

Importers and manufacturers of the taxable domestic products shall be liable for this tax, excluding any exported goods. In the case of imports the taxable base shall be the value for Customs plus Customs duties and fees for services. In the case of domestically manufactured goods the taxable base shall be the ex-factory price excluding VAT and this tax. In the case of petroleum - based fuels the taxable base shall be the sales price to the public established by the Executive Power, except on items not subject to price controls, which shall be subject to the rules governing imports.

LIQUIDATION AND PAYMENT

The tax shall be liquidated on a monthly basis except in the case of fuels which shall be liquidated weekly, from Sundays through Saturdays.

C. TAX ON ACTS AND DOCUMENTS

This tax replaces the Stamped Paper and Stamp Tax. It applies to obligations, acts and contracts evidenced in writing by documents. Acts involving financial intermediation shall be taxed.

EXEMPTED ENTITIES

1. The government and its agencies, municipalities and universities;
2. Religious entities endowed with legal existence.
3. Independent government enterprises and decentralized entities with respect to their establishment, recognition and internal operations.
4. Political parties and social, educational, and charitable organizations with legal existence.
5. Farm production cooperatives with respect to certain taxable transactions;
6. Transactions with the government land office (IBR) and supervised farm credit agency (CAH).
7. Farming and manufacturing development loans up to the amount of Gs.50 million, which amount shall be upgraded annually by the Administration.

In the case of contracts between an exempted party and one which is not, the latter shall pay 50% of the tax.

As a general rule the amount mentioned in the document is the tax base. Fixed amounts are established for certain transactions. When goods are transferred to a corporation as paid in capital the tax is doubled, being taxable as subscribed capital and as a conveyance of property.

Capital assignment to branches shall constitute a tax base independently of the capital of the home office.

The tax rates are provided on the list below. It is worth noting that the percentage tax rate on bills of exchange and promissory notes on financial intermediation is 1.74% per annum payable pro rata of the time set forth in the relevant instrument.

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Banks and financial institutions and notaries public shall act as withholding agents for taxes on acts and contracts in which they take part.

Any person granting, endorsing, authenticating, acknowledging, presenting, processing or authorizing acts, deeds, or documents in violation of this law shall be joint and severally liable for payment of the tax.