

Guide to Doing Business
in
Nicaragua
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SELECTED LEGAL ASPECTS OF DOING BUSINESS IN NICARAGUA

This memorandum provides basic guidance to persons or companies that are willing to establish business operations, investment, or exporting to Nicaragua. It covers briefly the most important legal aspects of doing business in Nicaragua, whether the operations will (i) serve the national market, (ii) serve the region from Nicaragua as a strategic base or (iii) use Nicaragua as a manufacturing base.

I. FOREIGN INVESTMENT AND EXCHANGE CONTROLS

Nicaragua's foreign investment promotion law (2000) establishes rights for foreign investors, regarding tax incentives and other benefits. In order to obtain these benefits Investor must register with the Ministry of Industry and Commerce (*Ministerio de Fomento, Industria y Comercio*, or *MIFIC*). Exchange controls were lifted in the early 90s. Nicaraguan law permits national and foreign companies to operate bank accounts in córdobas or in dollars, both in Nicaraguan banks and abroad. There are no technology transfer requirements. Foreign remittances are taxed (see section on taxes) and some tax incentives include export performance requirements (see sections on free trade zones and *maquiladoras*). In general, there are no limitations on foreign investment, although some industries such as mass media have percentage limitations on foreign investment. Nicaragua has opened previously state-owned industries (e.g., telecoms, electricity generation and distribution, Gas, among others) to private investment regardless of nationality.

There are other laws that may promote investment development; La Ley de Incentivos Turísticos (Tourism Incentives law) for instance establishes many incentives for local or foreigners investors. Nicaragua is recently opening to Tourism as a tool for economic growth therefore is implementing many incentives to reach all the investment possible. There is a law initiative, Bonos de inversión Turística, (Tourism Investment Bonds) which will create a wonderful platform for tourism investors. The law regards on tax exemption for more than 10 years convertible to bonds that may be offered or placed in a stock market. Nicaragua is also searching for new energy sources, therefore is providing concessions to Hydro, wind, solar or gas distributors.

II. REAL PROPERTY: OWNERSHIP AND LEASING

The general rule in Nicaragua is that foreigners have the same property rights as local investors. Thus, there are no legal restrictions that would specifically affect a foreign entity or a Nicaraguan entity owned by foreign capital that desires to lease

or purchase real estate. Nicaragua's Civil Code generally regulates all types of leases in the national territory. In addition to the basic provisions of the Civil Code, urban leases are also subject to a separate Law for Urban Leases.

There are no seize or confiscations actions over private property by the government. The State protects investment and Property rights are a priority.

Real State is a very interesting investment opportunity since land in Nicaragua has not yet reached global market value; this is the opportunity to obtain large coastline properties at cadastral value. Many investors are buying coastline properties aiming to housing development or tourism, such as Hotels and Marinas.

Nicaragua is surrounded by the Pacific and Caribbean Ocean, moreover has one of the largest navigable lakes around the world with a habitable island in it. This benevolent land is propitious for the development of an Inter oceanic canal, not yet built or projected.

III. IMMIGRATION LAW

Although thirty- or ninety-day tourist visas are readily available for most nationalities, work permits are more time-consuming to obtain and must be secured from the Nicaraguan consulate in the place of residence of the individual who is applying for the visa. There is no change- in-immigration-status procedure as there is in other jurisdictions, such as Mexico. Administrative proceedings to obtain the work permit take three to six months on average. Some investors prefer to obtain a resident visa status.

The National Congress had recently approved a law that motivates Nicaraguans to return to their country from abroad. This law states tax exemption to those Nicaraguans that had lived abroad for more than five years. The beneficiaries of this law may return bringing, besides their belongings, operational machinery or equipment tax free.

IV. CORPORATIVE LAW

Nicaraguan law recognizes a wide variety of organizations, including corporations (*sociedad anónima*, or SA), general or limited liability partnerships (*sociedad colectiva* or LLP) and limited partnerships (*sociedad en comandita simple*), foundations, civil associations and cooperatives. Although Nicaraguan law does not include any entity similar to the LLC, its limited liability partnerships provide for limited liability for all partners. Foreign companies may operate legally in Nicaragua through local branches, joint-ventures, wholly-owned subsidiaries and other variations of the standard organizations.

Regardless of the method of operation, an enterprise doing business requiring a legal representative domiciled in Nicaragua must register with the Commercial Section of the area (*department*) Public Registry (*Registro Público*), along with tax

and relevant municipal authorities, thus becoming a national enterprise and taxpayer for Nicaraguan purposes, regardless of the nationality of its owners or officers. Foreigners may (i) act as officers, directors, partners or trustees in local companies, (ii) make use of negotiable commercial documents and (iii) execute any kind of legal contract.

The corporation is by far the most common form of business entity in Nicaragua. In recent years, however, US and European tax advantages have made the limited liability partnership more desirable for some businesses. Corporations and LLP's are relatively easy to manage, especially with respect to powers of representation, decision making issues and other day-to-day business administration activities. They both limit the financial exposure and liabilities of shareholders vis-à-vis third parties.

For Nicaraguan companies, a single document (the "deed of incorporation") contains the provisions generally contained in both the articles of incorporation and bylaws of a U.S. company.

Foreign companies may register branch offices in country, which are only liable for income tax on Nicaraguan source income (see section on Taxes below). Although branch offices are not separate legal entities and therefore do not limit the potential liabilities of the foreign company in Nicaragua, foreign companies may in effect achieve limitation of liability by forming a special purpose subsidiary in their own or a third jurisdiction and registering a branch office of the special purpose company in Nicaragua, thus limiting liability in Nicaragua to the capital of the special purpose company.

A. Corporations

1. Formation

A Nicaraguan corporation may be established either by private capital (closely held) or by public subscription. The members must execute a deed of incorporation or constitution before a Nicaraguan notary public and register the deed of incorporation at the Commercial Section of the Registry Office. The corporation must establish a street address domiciled in Nicaragua. Then it is required to register as a commercial entity at the Tax Authorities, in order to obtain a RUC (Unique Tax Number).

2. Shareholders and Shares

The corporation must be formed by a minimum of two members, with no nationality requirements, and may receive contributions from any number of additional shareholders. Corporations have no minimum capital requirements, and no minimum paid-in requirements. The organizers must state a number of authorized shares of stock in the deed of incorporation and establish a par value 3 in Nicaraguan *córdobas*. Each year, 5% of the net profits of the company must be

deposited in a reserve account, until the account reaches 10% of the company's stated capital. Common shares have equal rights and one vote each. However, the deed of incorporation may provide for the issuance of different classes of shares with different voting rights, denominations, preferences, privileges, restrictions and limitations, as well as the establishment of other terms and conditions regarding profits and assets. The corporate secretary maintains a private stock registry book not open to the public, to record share ownership and transfers. Shares are freely transferable unless the deed of incorporation provides otherwise. Bearer shares are permitted by law, although some attorneys avoid them due to the lack of transparency in ownership. Dividends may only be paid from profits (see section on Taxes below regarding withholding taxes).

3. Shareholder Meetings

The shareholder meeting is the ultimate authority in the corporation and it retains all the powers not vested in any other corporate body by the deed of incorporation. The deed of incorporation can establish supermajorities for voting on selected issues. Unless otherwise specified in the deed of incorporation, shareholder voting on the election of directors is non-cumulative. Meetings may be held by proxy or outside Nicaragua when so provided by the deed of incorporation, but may not be held by circular resolution or by telephone. Ordinary meetings must be held at least once a year for (i) approval or rejection of the financial statements pursuant to the auditor's report; (ii) distribution of profits; (iii) appointment or dismissal of members of the board of directors and auditors when necessary; and (iv) any other matters proposed in the agenda and not reserved for special meetings. Special meetings must be convened for: (i) amendment of the bylaws; (ii) issuance of classes of shares not provided for in the bylaws; and (iii) other purposes when so required by law or the bylaws. Unless the percentage is lowered in the bylaws, shareholders representing at least 5% of the capital of the corporation may request that a special meeting be called.

4. Management

A Nicaraguan corporation is managed by a board of no less than three directors (*directores*), who must be individuals and must be either shareholders themselves or representatives of shareholding entities, but need not meet any nationality requirements.

The directors may be named in the deed of incorporation or appointed later by a shareholders meeting, which may also remove them at any time. If specifically contemplated in the deed of incorporation, board of directors meetings may be held outside Nicaragua but may not be held by circular resolution or by telephone. The corporation must name at least one local representative agent (who must be a Nicaraguan national or permanent resident and may be but need not be a director) to be vested with management powers and legally authorized to represent the corporation (*agente residente*). In practice, the chairman (*presidente*) of the board is usually the managing director and the other two directors act as treasurer and

secretary. Thus, directors, officers and managers are often the same people. The deed of incorporation may designate other legal representatives and may permit them to delegate some or all of their powers to other persons. The board of directors may also appoint one or more corporate managers (*gerentes*) with powers and authorities of the board's choosing.

5. Supervision and Auditors

One or more statutory controllers (*vigilante*), who may be or need not be shareholders, report to the shareholders on the performance of management. The controller is appointed by the shareholders, and cannot be a member of the board, hold any other office or be related to any other officer. In most privately held companies, the controller may be a figurehead employee of the company. The controller's legal duties include requesting monthly balance sheets, reporting on yearly balance sheets, calling shareholders meetings, being present at board of directors and shareholders meetings, receiving complaints from shareholders and reporting on such complaints to the board of directors.

6. Formation and Registration expenses and duration.

Formation and registration procedures typically take six weeks from the time of the filing date. Government filing fees and legal fees for establishing a simple wholly-owned corporation average less than US\$4,000.

B. Limited Liability Partnerships

1. Formation

A Nicaraguan limited liability partnership (*sociedad colectiva*) can possess many of the same attributes as the corporation, such as having independent legal existence and providing liability limited to capital contributions of its owners. The organizers must execute the deed of organization before a Nicaraguan notary public, register it with the Commercial Registry and publish notice of the organization in the Official Gazette.

2. Partners and Partnership Interests

The SC (LLP) must be formed by a minimum of two partners, whether individuals or companies, with no nationality requirements, and may receive contributions from any number of additional partners. LLPs have no minimum capital requirements, and no minimum paid-in requirements. Subscription of partnership interests cannot be offered to the public. The number of partnership interests and the value of each in Nicaraguan cordobas must be stated in the deed of organization. The name of the LLP must include either the names of all partners or the name of at least one partner along with the words "*y compañía*" ("and Company"). To limit the liability of the partners, the LLP's name must end with the word "*limitada*." Partnership interests have equal rights and one vote each, and for this reason the

LLP may be less suitable for special or complex control or equity structures than the corporation. Partnership interests may only be transferred with the prior approval of all of the other partners.

3. Partners Meetings

Partners meetings may be held as, when and where desired by the partners, outside of Nicaragua when so provided by the deed of organization. When so provided by the deed of organization, meetings may be attended by proxy, by telephone or circular resolution.

4. Management

Management may be structured in any way desired by the partners and expressed in the deed of organization or partners resolutions.

5. Time and Expenses of Formation and Registration

Formation and registration procedures are similar to those applicable to corporations.

C. Branches

Foreign companies may establish branch offices in Nicaragua by appointing a local legal representative with a general power of attorney for all of the branch's business, and filing the following documentation with the Public Registry:

- i) A shareholders or board of directors resolution of the foreign company on the establishment of a Nicaraguan branch, describing the business purpose, operational name and local address of the branch and the capital "assigned" to it, and appointing a local attorney for registration purposes and a local legal representative;
- ii) Power of attorney formally registering the local legal representative and assigning broad powers of attorney ("*poder generalísimo*"), which by law cannot be limited except with respect to real estate or amount. This document is prepared locally based on the resolution described in i) above;
- iii) Certified copy of certificate or articles of incorporation of foreign company, translated to Spanish by official Nicaraguan translator; The foreign investor establishes the branch by presenting the foregoing documents to the Commercial Registry, legalized by the appropriate Nicaraguan consulate abroad. The branch office must then register with tax and municipal authorities. Apart from any translation costs, branches cost approximately the same amount to establish, and usually require approximately the same amount of time to register as subsidiaries (six weeks).

V. TAXES

A. INTRODUCTION

In May of 2003 the Nicaraguan legislature overhauled the national tax system, replacing among other laws the old income tax law (1974) and the old value added tax law (1984) with a comprehensive Tax Equity Law, and added Regulations in June 2003. Currently a new Tax Code has been approved by the Nicaraguan Congress (2005) and a reform has been recently approved. The creation of this new Tax Code has been due to the signing of the Central American Free Trade Agreement (CAFTA), in order to improve the dispositions provided.

B. INCOME TAX

1. General Principles

Tax Equity Law and its regulations, taxes income that is originated by commercial activity in National Territory (domestic source or “source income”); regardless of its nature; it includes profits, employment income, and remittances to foreign persons. It does not tax based on residency or citizenship. Unless exempt under one or more provisions (such as Free Trade Zone status), all entities with a “permanent establishment”⁵ in Nicaragua are subject to the income tax. Individuals are taxed at 30% for income over C\$ 500,000 (approx. US\$ 30,000 at C\$17/US\$).

Corporations and SRLs are currently taxed at 30% on all net income, with 1% of gross receipts due on a monthly basis as a proxy until final year-end calculations. A net assets tax of 1% functions as an alternate minimum tax. A Nicaraguan subsidiary of a foreign company may deduct as expenses certain documented payments to its foreign parent company. Specifically, the subsidiary may deduct from gross income payments to its foreign parent for technical, financial (up to national market interest rate) or other assistance, or for patents, formulae, trademarks and similar items. The deduction is available only if the Nicaraguan company has duly withheld any corresponding withholding tax due.

Nicaragua has not adopted the standard OECD test for “permanent establishment.” In practice, any activity carried out in Nicaraguan territory is taxable: there is no safe harbor provision.

Dividends and other profit distributions received by the owners of taxpaying Nicaraguan companies are excluded from gross income, regardless of the nationality of the owners. In general, other capital gains are taxed as ordinary income. Dividends and other distributions received by owners of tax exempt entities (such as those operating in Free Trade Zones) are considered gross income for the owners and may therefore be subject to a withholding tax (see subsection on Withholding Tax in this section).

By law, the fiscal year of Nicaraguan taxpayers ends on June 30. However, companies, individuals and other taxable entities may request a special fiscal year if they reasonably justify their need for it. Nicaraguan tax law does not allow for consolidation of tax reporting. Nicaraguan corporate taxpaying entities may carry forward up to three years operating losses for most activities. Carrybacks are not allowed. Although Nicaraguan legislation generally requires accrual method accounting, companies may use cash-flow accounting upon prior approval of the tax authorities. Nicaragua does not currently have any asset or equity tax, apart from the alternate minimum tax (see above) and local real property taxes (see section on real property tax). Nicaragua does not have any tax treaties currently in effect, except for a tax information exchange agreement with the United States.

2. Reorganizations

Nicaraguan tax law and regulations do not include any specific provisions governing corporate reorganizations, including mergers and spin-offs. However, Nicaraguan tax authorities have taken the position that transfers of real estate that are related to mergers are exempt from real estate transfer taxes, unless the real property is depreciable. All fiscal attributes of the merged company are transferred to the surviving company.

3. Withholding Tax on Remittances to Foreign Countries

The income tax includes a withholding tax on income sourced in Nicaragua that will be remitted to a person or company in a foreign country. The types of income to which the tax applies include: dividends, salaries, rents, royalties, and interest. The withholding tax rate for non-exempt profit distributions and payments for services is 10.5%, for royalties 21%, for interest 22.5%, and for salaries the full amount of the applicable tax (maximum rate 30%). Interest payments by Nicaraguan residents to foreign financial entities or banks are exempt from this tax. There are no provisions for exempting remittances in the event they are not offset by foreign tax credits abroad.

C. VALUE ADDED TAX

The Nicaraguan Value Added Tax (*Impuesto al Valor Agregado*) of 15% applies to all imports and sales of goods and rendering of services, with significant exceptions, mostly for basic goods and services. Like standard VATs, each entity involved in the chain of supply from raw material to finished product or service nets its tax collected (from the next purchaser) against its tax paid (to its supplier) to determine the amount it must pay to the tax authority. The tax falls completely on the end-user but is remitted to the government by merchants and businesses along the value chain. By the fifteenth day of each month, the Nicaraguan VAT taxpayer must remit to the tax authority the difference between VATS collected and the VAT paid for the previous month. In addition to the sales tax, some goods, including alcoholic beverages, tobacco, petroleum and automobiles, are subject to a consumption tax (*Impuesto Selectivo al Consumo*) of up to 30%.

C. REAL PROPERTY TAX

A yearly national property tax of 0.8% of appraised value is collected and managed each municipal government locally. Sales of real property are taxed at 4% of the property's registered value (see Reorganizations above for exemption).

D. REGISTRATION TAX AND MUNICIPAL INCOME TAX

Each municipality collects a yearly registration tax of 2% of gross receipts during the final quarter of the foregoing year and an additional monthly tax of 1% of gross receipts, with some exceptions related primarily to food and financial services. Local governments have the constitutional right to levy additional taxes and fees, which vary by location.

VI. IMPORTS AND EXPORTS

A. INTRODUCTION

The backbone of Nicaragua's current Customs Regime was established in 1958 when Guatemala, El Salvador, Honduras and Nicaragua signed the Central American Economic Integration General Treaty (*Tratado General de Integración Económica Centroamericana*) and formed the Central American Common Market. Nicaragua signed on to the treaty in 1960. Other related treaties and regulations affecting customs in Nicaragua have subsequently been approved, including a common Tariff Schedule for the countries. Since 1993, the Central American countries have adopted a Central American Tariff Schedule (*Sistema Arancelario Centroamericano*) (the "SAC"), which is based on the Harmonized Commodity Description and Coding System ("HTS"). Nicaragua formally adopted the SAC in 1993.

Nicaragua also became a Contracting Party to the General Agreement on Tariffs and Trade ("GATT") in 1950. Nicaragua is now a member of the World Trade Organization ("WTO") established in 1995 as part of the Uruguay Round of Multilateral Trade Agreements.

In Nicaragua, imported goods are subject to import duties in accordance with the SAC classification. Central American integration rules require that all member countries apply the same import duties. However, there have been exceptions for many years, and one of the integration treaties, the Agreement on the Central American Tariff and Customs Regime (*Convenio sobre el Régimen Arancelario y Aduanero Centroamericano*), ratified in 1985 allows countries to modify import duties unilaterally in certain cases. That provision has been broadly interpreted and used by the Central American governments. Specifically, Nicaragua has used this unilateral modification authority in relation to the computation of import charges on various types of goods.

Nicaragua has bilateral trade agreements with the Dominican Republic, Mexico and Chile. In addition, Nicaragua has concluded in January 2004 region-wide negotiations with the United States for a free trade agreement (Central American Free Trade Agreement – CAFTA), which is now approved by the relevant legislatures in 2005. Each treaty imposes various reduced import duties on originating goods. This treaty has great expectation for investors in the Region, since all Central American countries had signed with the exemption of Costa Rica. Investors now see the region as a whole for good investment.

B. CUSTOMS LAW

The Import Tariff Act of 1986 (*El Derecho Arancelario a la Importación (DAI)*) implements Nicaragua's commitments under the Central American Agreement on Tariff and Customs Regime, and governs imports to and exports from Nicaragua. Upon import, goods are subject to import tariffs and duties, which range between 0% and 15%. The SAC classification, along with any applicable trade agreements, determines the applicable ad valorem tariff rate in accordance with the type of goods. The value added tax, specific consumption tax, and other applicable taxes are regulated by their respective legislations and are collected upon importation. Nicaragua has enacted several temporary importation regimes to encourage value-added manufacturing activities that use foreign sourced inputs.

C. FREE TRADE ZONES

Nicaragua created its Free Trade Zone program in 1991, and currently has over 80 active companies operating under its provisions located either in 17 government Free Trade Zone Parks or in over 30 in stand-alone facilities. Although current WTO Subsidies and Countervailing Measures Agreement provisions provide that most countries in the world must eliminate or modify this type of program, Nicaragua has at least until 2012, and possibly longer if its per capita GDP does not rise above US\$1,000. The principal requirement for establishing a FTZ company is to be engaged in the exportation of goods or services.

The advantages of operating in Free Trade Zones are:

- (a) A temporary exemption from the Income Tax, including withholding tax for remittances on interest and fees for certain services paid to foreign providers. The full exemption is for ten years, and a 60% exemption applies to all subsequent years;
- (b) A permanent exemption from all import duties and taxes imposed on raw materials and other of materials required in the production process, machinery and equipment, spare parts and supplies;
- (c) A permanent exemption from all export and re-export duties on goods produced in the FTZs;

- (d) A permanent exemption from all property transfer taxes in the event of shut-down;
- (e) A permanent exemption from value added and consumption taxes;
- (f) A permanent exemption from all municipal taxes;
- (g) A permanent exemption from all transportation taxes; and
- (h) A permanent exemption from all formation, merger, and transformation taxes, and the Stamp Tax.

FTZ parks are restricted non-residential areas with infrastructure designed to meet industrial needs. With the exception of the exemptions listed above, all FTZ companies must comply with the laws of Nicaragua, including environmental and employment laws. They must maintain a “reasonable” number of employees at substantially the salaries offered to the government authorities in negotiations for the initial approval.

The Free Trade Zone Commission receives and issues recommendations on all applications for FTZ status. If the FTZ Commission recommends the application, the Executive branch decides whether or not to approve the application. This entire review process normally takes between four and six weeks.

D. TEMPORARY IMPORTATION STATUS (*REGIMEN DE ADMISION TEMPORAL PARA PERFECCIONAMIENTO ACTIVO*)

For companies that will process goods in Nicaragua for export, the Temporary Importation regime (2001), sometimes referred to as the *maquiladora* regime, offers a mutually exclusive alternative to the FTZ regime. To qualify, the *maquiladora* company must directly or indirectly export at least 25% of its production (by sales price) and sell at least US\$50,000 to foreign buyers. Although the *maquiladora* company does not qualify for exemption from taxes based on net income, it does benefit from customs tax and VAT relief and it is free to establish its operations anywhere a comparable national company would be permitted to do so. If the *maquiladora* company will sell less than 100% of its production abroad, the tax benefits will apply pro rata based on the percentage of export sales.

Once it has paid the customs bond if required by law, a *maquiladora* company may import raw materials, intermediate goods and capital goods directly related to its operations, free of customs tariff or VAT and other customs-related taxes, or with later duty drawback. The *maquiladora* company must engage in transformation, repair, remanufacture, assembly, or other similar processes with the imported goods and then re export them within the required time-period (6 months, with extensions of up to six months). Capital goods may remain in the country for up to 5 years.

The National Commission for Export Promotion receives and issues recommendations on all applications for *maquiladora* status. If the Export Commission recommends the application, the tax authority (*Ministerio de Hacienda y Crédito Público*) decides whether or not to approve the application. This entire review process normally takes between four and six weeks.

VII. INTELLECTUAL PROPERTY AND TECHNOLOGY TRANSFER

Trademarks, trade secrets, and copyrights generally receive adequate protection under the relevant Nicaraguan legal regimes, which comply with international standards. Nicaragua does not restrict or require prior authorization for licensing agreements. Nicaraguan laws do not set any absolute limits on fee royalties.

VIII. CONSUMER PROTECTION AND ANTITRUST

Although it has not been widely used so far by consumers, the Consumer Protection Law (1994) in general terms gives consumers the right to quality goods and services. Although the Trademark Act prohibits some forms of unfair competition, Nicaragua has not enacted an antitrust or competition law. Nevertheless, the Nicaraguan Congress has already a draft for Competition Law. That shall be review this year.

IX. LABOR AND EMPLOYMENT

Employment and labor laws are an important part of Nicaragua's legal structure. Basic labor rights have enjoyed constitutional status since 1987, and include minimum conditions of liberty and dignity for all workers, equal pay for equal work, an 8-hour workday and 48-hour workweek as a maximum, a minimum wage, double pay for overtime, a Christmas Bonus given on 12 continuing working months (consisting on a full month salary, and severance payment and the right to reinstatement for "unjust" dismissal. The Labor Code (1996) follows the principle of minimum standards that can only be negotiated in the direction of improvements for the employee. The Labor Code also addresses collective bargaining rights, including the right to unionize and the right to strike pursuant to a mandatory conciliation process.

The Labor Code defines an employment relationship as one in which the employee receives money in exchange for services and is subject to direction and control by the employer. Employment agreements need not be in writing, but oral agreements are typically interpreted in favor of the employee. Even in the case of written agreements, the minimum standards of employment in the Labor Code cannot be reduced.

No specific legislation regarding trade secrets, but private agreements covering these issues is generally enforceable.

Nicaraguan legislation provides a (non-mandatory) Internal Work Regulation system that employers may choose to establish to avoid disputes with employees. Employers must submit the Internal Work Regulation (if any) to the Ministry of Labor and Social Security for approval. Nicaraguan employees are generally accustomed to working under an Internal Work Regulation, and expect it to cover the following areas, which are provided by law, but may be improved upon by the employer:

Work Schedule. Standard daytime (6AM to 8PM) working hours: 8 or 9 hours per day, 48 hours per week; night shift (7 hrs/day, 42 hrs/wk). These provisions do not apply to employees who set their own work-schedule, such as salespersons and upper-level management. At least a 30- minute lunch break is part of the paid day's work and at least one day of rest per week.

Overtime. Payable as double-time on daily basis, with the workday not to exceed 12 hours and workweek not to exceed 57 hours.

Holidays. Eight mandatory paid holidays: January 1, Thursday and Friday of Holy Week, May 1st, July 19, (August 1 and 10 – Managua only), September 14 and 15 and December 8 and 25. Work on these holidays is voluntary and must be paid at double time rates. Holidays that fall on a Sunday are taken on the Monday following the date.

Wages/Payment. The minimum wage in Nicaragua depends on the region and industry, and is reviewed every six months by the legislature. The current minimum rate for a line worker in a typical manufacturing operation in Managua is C\$3.00 cordobas per hour and C\$3.95 per hour in free trade zones and maquiladoras (approximately US\$0.18 and US\$0.23, respectively at C\$18/US\$). Payment is by time period or unit/piece of work. The company is free to determine method and timing of payment, which may be weekly, biweekly or monthly or at its convenience.

Paid Vacations . Employees have a right to fifteen days of uninterrupted paid vacation for each six months worked. The Employer may determine when vacations are taken. Only half of the vacation time earned each year may be compensated with money, except in the event of termination. Employees may not allow vacations to accumulate for use in subsequent years.

Training period. The law permits a one- month trial period. If the employee is dismissed without cause during this time, no benefits accrue.

Social Security and employee income tax retention. Nicaragua has a mandatory social security system that provides all citizens with medical care, disability payments, and retirement benefits. The employer acts as a collector of percentage deductions made to the employee's salary (6.25%). In addition, the employer contributes 15% of payroll for 14 Social Security and 2% for the National Institute for Technology (a government training program). The employer is also

responsible for retaining the employee's estimated income tax (an employee at minimum wage up to approximately US\$2950 per year would have a 0% tax rate).

Health Leave. Unless otherwise agreed, the Social Security system pays all health leave. Social Security pays 60% of salary from the fourth day of hospitalized or no hospitalized sick leave (unless it's an on-the-job injury, in which case payment begins on the day after the injury). Maternity leave is paid by Social Security at 60% of salary for three months (one month before birth and two months after).

Thirteenth Month Bonus. The law requires payment of a Thirteenth Month Bonus (*decimotercer mes*) equal to the most recent monthly salary received, payable no later than December 10th. In the event of termination before the Thirteenth Month Bonus is paid, the employer must pay within 10 days the amount accrued at the time of dismissal.

Reserve Provisions. The Law does not establish any mandatory reserves for labor contingencies.

Termination of employment Nicaraguan employment law does not recognize the concept of at-will employment common in the United States. To avoid severance payments, an employer must only dismiss an employee if the employer has "just cause" as defined by the Labor Code. Employees terminated for "just cause" are due only accrued vacation time and Thirteenth Month Bonus, and any current wages. The following constitute "just cause" for termination:

- i) Physical or moral acts or libel committed against the employer or against a fellow worker at any time;
- ii) Criminal acts or property damage related to the workplace;
- iv) Acts that endanger security and working conditions in the workplace;
- v) Release of the employer's confidential information;
- v) Unjustified absence for 2 consecutive days or 3 or more days during any month; or
- vi) Disobeying rightful instructions or orders from the employer.

To terminate for any of these causes, the employer must request authorization from the Labor Ministry within thirty days from the employee behavior. Failure to obtain authorization will forfeit the "just cause" for termination and render any termination unjustified. The employee may also terminate employment at any time and with or without cause, with the employer being liable for severance payment in the event of just cause. In the event of dismissal without "just cause" or employee resignation, the employer must give severance payment proportional to the total

time worked by the employee. Only in the event of termination without just cause is the employer obligated to give a 15-day notice.

Severance Pay (*Cesantía*). If the employer dismisses an employee without “just cause” or if the employee quits for a “just cause” attributable to the employer, the employee will be entitled to severance pay of one month’s salary for each of the first three years worked and 20 days’ salary for each year worked over three, calculated based on average salary over the last 6 months. Severance pay may be no less than one month’s salary and no more than five months’ salary.

Accumulated Vacation Pay and Bonus. Independent of cause, the employee is entitled to payment for unused vacation time and pro rata Thirteenth Month Bonus upon termination.

Workers compensation insurance. There is no workers compensation system separate from the Social Security System. Unless otherwise agreed between the parties.

Foreign employees. Headcount for all companies operating in Nicaragua must be at least 90% Nicaraguan. No percentage of payroll requirements apply. The Ministry of Labor may allow variations based on technical requirements. Foreign employees must obtain work visas from the immigration service (*Dirección General de Migración y Extranjería*).

Workplace Discrimination. The Nicaraguan constitution guarantees employees the right to work in an environment free from discrimination based on ethnicity, sex or religious beliefs. The legislature has not yet attempted to implement these right in more specific legislation, however, and this area is not a source of significant litigation at this time.

XI. PROTECTION FOR DISTRIBUTORS AND SALES REPRESENTATIVES OF FOREIGN COMPANIES

In 1998, Nicaragua abolished its law protecting dealers (both buy-sell distributors and commission sales representatives) of foreign companies, entitling them to damages similar to wrongful employment termination damages. Agreements entered into before that time may be governed by the provisions of the old law.

XII. PLEDGES AND MORTGAGES

Nicaraguan law generally allows pledges over property that remains in the pledgor’s possession. However, it does not have a centralized national pledge registry, so pledge searches must be made by state Public Registry of Commerce, according to the location of the goods at the time the pledge was created. The subject-matter of the pledge can include any movable property, and may cover a collection of items that need not be individually listed as well as after-acquired property, such as new items coming into inventory. Mortgages over real estate are

also available, and registered at the Public Real Estate Registry (by state where the real estate is located).

XIII. THE ENVIRONMENT

Despite recent efforts to protect the environment of Nicaragua, most Nicaraguan attorneys agree that Nicaragua continues to struggle in the enforcement of its pollution and environmental norms. Nicaragua's environmental legislation is scattered among various laws, decrees and internal regulations, which range from the Health Law to mining, forestry and wildlife laws to ministerial circulars. The Nicaraguan legislature passed a comprehensive General Law on the Environment and Natural Resources in 1996. Among other goals, the law attempts to organize companies' and individuals' obligations to mitigate pollution and conserve wilderness areas, but the obligations are drafted in very general language. The law places broad responsibility on polluters for the damage they cause, establishes governmental agencies for approving required environmental impact studies, and creates an Environmental Tribunal to hear environment-related complaints. Foreign investors should keep in mind that, as in all nations of the world, foreigners who degrade the environment may be resented and even singled out for prosecution because of political pressures. This is especially the case when the legislation in the foreign investor's country of origin would have prohibited the offending behavior.

XIV. REGISTRATION REQUIREMENTS AND PERMITS

Company registration. Every company that desires to do business in Nicaragua must register either as a Nicaraguan company or a branch of a foreign company with the local state Commercial Public Registry.

Taxpayer registration. Before beginning operations, the corporate vehicle must register as a taxpayer (for income and other taxes) with the Ministry of Treasury's General Tax Administration (*Tributación Directa*). The filing includes a description of activities, as well as a designation of legal representatives and domicile.

Construction and land use permits. Construction and land use permits must be obtained from local governments prior to groundbreaking.

Health operations permit. All operations that will include employees must obtain a health permit from the Ministry of Health (*Ministerio de Salud*), which includes a ministry inspection of the premises.

Municipal tax registration. It Must be obtained right after the opening of operations (see taxes section of this memorandum).

Environmental impact assessment. All new physical projects must file a preliminary environmental assessment application with the Ministry of Environment and Natural Resources to determine whether a partial or full environmental impact

assessment will be required, or whether a more moderate plan for environmental management will suffice.

Free trade zone status grants and permits. Companies desiring to operate under FTZ provisions must file with the Free Trade Zone Commission (*Corporación de Zonas Francas*) as discussed in the section of this memorandum dealing with free trade zone status.

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Respectfully submitted,
September 2006

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