

TAX REGIME

Overview, types of national, departmental and municipal taxes, tax incentives and BEPS.

For taxable year 2017, the new Tax Reform enters into force. The amendments that you need to know are as follows:

- Unification of income tax. For 2017, the rate is 34% and, for the following years, 33%.
- Creation of an income tax surcharge of 6% for 2017 and 4% for 2016, and its elimination for 2019 and subsequent years.
- Unification of income tax rate for free trade zones at 20%.
- Creation of a new dividend tax.
- Reorganization of cross-sectional and sectoral incentives.
- Increase in the general VAT rate to 19%⁵.

Overview

The Colombian tax regime has mainly three (3) types of taxes: national, departmental, and municipal.

National taxes

The main national taxes applicable to companies and individuals in Colombia are presented below in general terms.

1. Income tax

a. Concept of income tax and capital gains tax

The income tax is levied on profits obtained by taxpayers that increase their equity and come from their ordinary transactions. Furthermore, the capital gains tax is levied on other income that are not regarded as revenue for taxpayers.

b. Taxpayers

Income tax payers may be individuals or legal entities. National companies and individuals residing in Colombia are taxed on their revenue (income and capital gains) of global source (domestic and foreign sources).

Moreover, non-resident foreign companies and individuals are only taxed on their income and capital gains of national source, regardless of whether they receive such income and capital gains directly or through their branches or permanent establishments located in the country.

c. Income of domestic source

Revenue that gives rise to income of domestic source includes:

- Revenue derived from exploitation of tangible and intangible assets within the country.
- Provision of services within the Colombian territory. In addition, and applying the principle of objective territoriality, technical, technical assistance, consultancy and other services provided to individuals related by administration and management are considered to be rendered in the country, even if they are physically rendered from abroad.
- Revenue derived from disposal of tangible and intangible assets that are in the country at the time of disposal.



Types of taxes in Colombia

National taxes	<ul style="list-style-type: none"> Income tax Value added tax (VAT) National excise tax Debit tax (GMF as per its acronym in Spanish) National gasoline and diesel tax Carbon tax Stamp tax
Departmental taxes	<ul style="list-style-type: none"> Registration tax Cigarettes, beer and alcoholic beverage excise tax Vehicle tax (district tax in the case of Bogotá)
Municipal taxes	<ul style="list-style-type: none"> Industry and commerce, signs and boards tax (ICA) Unified property tax Urban works tax Surplus tax

d. Income that is not considered to be of domestic source

Some types of income that are not considered to be of Colombian national source, in spite of falling into the general definitions to be of such source, include:

- Interest derived from certain types of credits such as (i) short term credits arising from the import of goods and bank overdrafts; (ii) credits intended for financing or pre-financing exports; and (iii) credits for foreign trade transactions made by means of financial corporations, financial cooperatives, financing companies, Bancoldex and banks incorporated under the current Colombian laws.
- Revenue derived from technical services provided abroad for the repair and maintenance of equipment.
- Revenue obtained from disposal of foreign goods owned by foreign companies or individuals not residing in the country that have been introduced from abroad into International Logistic Distribution Centers, located in sea ports authorized by the Internal Revenue and Customs Service and certain river ports.

e. Frequency and rate of income tax

Frequency of the income tax and capital gains tax is annual.

The income tax rate for companies is 34% for 2017 and 33% for 2018 and subsequent years.

In addition, net income exceeding COP 800 million (about USD 263,000) is subject to an income tax surcharge of 6% for 2017 and 4% for 2018. Therefore, the combined income tax rates are approximately 40% for 2017, 37% for

2018 and 33% from 2019.

Some activities that generated exempted income in the past are now subject to a 9% rate (instead of 34% for 2017 and 33% from 2018), plus the income tax surcharge, if applicable.

In the case of free trade zones, the income tax rate is generally 20% and they are not subject to income tax surcharge.

For individuals, the income tax rate varies depending on the type of income. Generally, for earned income, rates range between 19% and 33% and, for non-earned income, between 10% and 35%. For non-resident individuals, the rate is 35%.

The capital gains tax rate, for both individuals and legal entities, is 10%.

Income tax rate in the case of dividends

Dividend distribution of national companies to non-resident foreign shareholders (legal entities or individuals) is subject to an income tax on dividends at a 5% rate. This tax only applies to the extent that the profits based on which dividend distribution is made have been generated from January 1, 2017.

In the event that dividends are distributed to another Colombian company, income tax on dividends does not apply. If they are received by an individual residing in Colombia, the dividend tax rate ranges between 0% and 10%.

In case that dividend distribution abroad is based on profits that did not pay income tax at the level of the Colombian company (for instance, due to the application of a tax benefit), a 35% tax shall apply at the time of distribution

abroad (except for certain benefits that can be transferred to shareholders).

In case that dividend distribution abroad is also subject to the 5% dividend tax, this tax shall be applied on the amount of dividend distribution, once it has been reduced by the 35% income tax.

If dividend distribution based on profits that did not pay taxed at the level of the Colombian company is made to another Colombian company, the company receiving the dividends shall be applied the income tax rates for companies discussed above (as mentioned, the additional dividend tax does not apply in this case). Finally, if this type of dividend distribution is made to an individual residing in Colombia, a 35% rate shall apply, and the amount of dividend distribution, once reduced by the 35% income tax, shall be applied a rate between 0% and 10%, in accordance with the amount of dividends.

f. Tax basis of the income tax

Generally, the tax basis of income tax is determined by the greater of: (i) the regular system or (ii) the presumptive income system..

i. Regular system

In the regular system, the tax basis is the taxable net income, which is determined as follows: from the sum of all revenue and extraordinary income realized in the taxable year or period, which are likely to produce an increase in net worth at the time of receipt and which have not been expressly exempted, all refunds, discounts and deductions are subtracted to obtain the net revenue.

In turn, from the net revenue, realized costs attributable to such income are subtracted, as the case may be, to obtain the gross income. From the gross income, the relevant deductions are subtracted to obtain the net income. Thus, the net income is calculated and the rates laid down in the law are applied thereto.

ii. Presumptive income system

For income tax purposes, presumptive income applies given that tax regulations assume that the equity of taxpayers has had minimum profitability.

In Colombia, the presumptive income applicable from the second year of existence of a company in Colombia

will be 3.5% of the taxpayer's net worth, counting from the last day of the immediately preceding taxable year.

g. Non-income or non-capital gain revenue

Some revenue that, by legal provision, does not constitute income or capital gains, including profits from the disposal of publicly traded shares (under certain requirements), certain non-taxed capitalizations for partners or shareholders, compensations for damage insurance, among others.

Some comments on special deductions, exemptions and discounts of income tax are below, in the tax incentives section.

h. Agreements to avoid double taxation

Colombia has been negotiating international agreements to avoid double taxation and prevent tax evasion by taxpayers in terms of income tax and, in some cases, equity tax, particularly in cross-border transactions.

Currently, there are double taxation agreements of general application in force between Colombia and Spain, Canada, Mexico, Chile, Switzerland, India, Portugal, Czech Republic and South Korea. Similarly, for certain activities related to air and marine transport, there are agreements in force with Argentina, Germany, Brazil, Venezuela, Italy, the United States, Panama, Turkey and France. In addition, under Decision 578 of 2004 by the Andean Community, a system was implemented to avoid double taxation and prevent tax evasion among member countries (Bolivia, Ecuador, and Peru).

Furthermore, the agreements with France and the United Kingdom have been signed and are pending the process of internal approval. Some of the countries with which Colombia is also negotiating double taxation agreements of general application are Japan, the Netherlands, Belgium and the United States.

2. Value Added Tax (VAT)

a. Concept

VAT is levied on the following transactions or taxable events:

- Sale of corporal personal or real property.
- Sale or assignment of rights on intangible assets associated with industrial property.
- Provision of services in the national territory or from abroad.
- Import of corporal goods.
- Circulation, sale, or operation of games of change or gambling.

b. Rate

The general rate is 19%; however, there are some differential rates between 5% and 10% for certain products or services. There are also goods and services that are VAT excluded.

c. Responsible parties

The person responsible to the tax authority in Colombia for collecting and paying the tax is any person involved in taxable events, even when the economic burden levies on the end consumer. In that vein, the persons responsible for this tax are merchants, non-excluded service providers and some importers.

Corporal personal property that is exported, export services (meeting the parameters set forth in the regulation), and the sale and import of certain machinery and equipment, among others, are exempted from the sales tax, according to current regulations.

d. Discountable taxes

Discountable taxes are an integral part of VAT because, in each process of production or marketing of goods or services subject to VAT, the tax already paid in the stage prior to such process may be discounted.

3. National Excise Tax

a. Concept

It was created in January 1, 2013 and its taxable event is the provision or sale to end consumers, or import by end consumers, of the following services and goods:

- Provision of mobile phone services, including data services.
- Sale of some corporal personal property, domestically produced or imported.
- Sale of food and beverages prepared in restaurants, cafes, buffet restaurants, ice cream shops, fruit shops, pastry shops, and bakeries.
- Sale of food and alcoholic beverages for consumption inside of bars, pubs and discos.

This tax will be levied at the time of customs clearance of the good imported by the end consumer, material delivery of the asset, provision of service, or issuance of bill, sales ticket, invoice, or equivalent document by the responsible party to the end consumer.

Goods and services levied with the excise tax are not generally levied with the sales tax (VAT).

b. Responsible parties

The parties responsible for the excise tax are providers of mobile phone services, sellers of food and beverages, importers as end users, sellers of goods subject to the excise tax, and professional intermediaries in the sale of used vehicles.

c. Discountable taxes

The national excise tax is not a discountable tax and, for the buyer, is a deductible cost of the income tax as greater book value of the purchased goods or services.

d. Rate

- The mobile phone service is taxed at a rate of 4% on total service amount.
- Goods such as automobiles, pick-up trucks, certain motorcycles, yachts, and other boats are taxed at a rate between 8% and 16%.
- Restaurants, bars, pubs, discos, and establishments providing restaurant and bar services are taxed at a rate of 8% on total consumption.

4. Debit Tax (GMF)

a. Concept

The GMF is a tax levied on financial transactions under which one makes use of funds deposited in current or savings accounts in any financial entity established in Colombia, as well as in any deposit account of the Central Bank and cashier's checks.

Transfers among current accounts of a single holder in the same credit establishment, as well as some other financial transactions and certain stock market transactions, are exempted from this tax.

b. Frequency and rate

This tax rate is 0.4%. This tax is collected by the Central Bank and other entities surveilled by the Financial Superintendence or the Superintendence of Solidarity Economy, in which the respective current account, savings account, deposit account, or collective portfolio is held or where accounting activity involving the transfer or use of funds is carried out.

5. National gasoline and diesel tax

a. Concept

The national gasoline and diesel tax is levied on the sale, withdrawal, import for own consumption, or import for sale.

The tax is levied on sales made by producers, on the issue date of invoice; on withdrawals for consumption of producers, on the date of withdrawal; and on imports, on the date

gasoline or diesel is cleared by customs.

b. Responsible parties

The taxpayer of this tax is the person who purchases gasoline or diesel from the producer or importer; the producer when he makes withdrawals for own consumption; and the importer when, after customs clearance, he makes withdrawals for own consumption.

The persons responsible for the tax are the producer or importer of goods subject to the tax, regardless of their capacity as taxpayer, when the taxable event occurs.

c. Rate

The rates for calculating the national gasoline and diesel tax are as follows:

- Regular gasoline: \$490 per gallon.
- Premium gasoline: \$930 per gallon.
- Diesel: \$469 per gallon.

The tax amount will be adjusted every February 1 based on inflation for the previous year by Resolution issued by the DIAN.

6. Carbon Tax

a. Concept

The carbon tax is a single-phase tax that falls on the carbon content of all fossil fuels, including all petroleum products and any type of fossil gas used for energy purposes, provided they are used for combustion.

b. Taxable event

The taxable event is the sale within the national territory, withdrawal, import for own consumption or import for sale of fossil fuels.

c. Responsible parties

The persons responsible for the tax are producers and importers, regardless of their capacity as taxpayer, when the taxable event occurs (as in the case of withdrawal for own consumption).

d. Rate

The rate shall be fifteen thousand Colombian pesos (\$15,000) per ton of CO₂ and the rate amount per unit of fuel shall be as follows:

- Natural gas: \$29 per cubic meter.
- Petroleum liquid gas: \$95 per gallon.
- Gasoline: \$135 per gallon.
- Kerosene and jet fuel: \$148 per gallon.
- Diesel: \$152 per gallon.
- Fuel oil: \$177 per gallon.

The following are not subject to the carbon tax:

- Petroleum liquid gas, except for the sale to industrial users.
- Natural gas, except for the sale to the oil & gas refining and petrochemistry industries.
- Alcohol fuel intended for the mixture with

gasoline for automobiles and biofuel of plant or animal origin or produced from urban solid waste nationally produced for the mixture with diesel for use in diesel engines.

- Products exported.

Carbon tax may be taken as a deductible expense in determining net income for income tax purposes.

8. Stamp Tax

Article 73 of Law 1111 of 2016 provided that, from 2010, the general stamp tax rate is 0%.

However, reduction did not consider all the taxable events. Currently, the stamp tax applies to very limited situations (checks that need to be paid in Colombia, issue of passports, etc.) and its rates are nominal.

Departmental Taxes

Below is a general description of the main departmental taxes applicable in Colombia.

1. Registration tax

a. Concept

The registration tax is levied on registration of documents containing acts, rulings, contracts, or legal business to which individuals are parties or beneficiaries and, by law, must be registered with the chambers of commerce or registries of public records.

b. Rates

- For acts, contracts, or legal business with amounts subject to registration with registries of public records, the rate ranges between 0.5% and 1% of the act amount. If registration is with chambers of commerce, the rate ranges between 0.3% and 0.7%.
- Contributions to companies under the heading of capital are subject to a 0.7% rate; contributions under the heading of share placement premium have a 0.3% rate.
- For acts, contracts, or legal business without amounts subject to registration with registries of public records or chambers of commerce, the rate ranges between 0.5% and 1% of the act amount between two (2) and four (4) current legal daily minimum wages.

2. Cigarette, beer and alcoholic beverage excise tax

The taxable event of this tax is the consumption of cigarettes, beers and liquors (including wines, aperitifs and the like) in the jurisdiction of departments.

The cigarette excise tax is composed of: i)

an ad valorem component on the retail price (certified by the DANE) of 10%, and ii) a specific component, which is a fixed amount per pack of 20 (or proportionally) that varies in accordance with type of product.

The beer excise tax is 48% (20% applies to beer-based drinks and mixes). The tax basis of the beer excise tax is the retail price. In case of foreign products, the retail price is determined as the amount of goods at customs, including customs duties plus a marketing margin of 30%.

The liquor excise tax is composed of: i) an ad valorem component on the retail price (before taxes and share certified by the DANE) at a 25% rate for liquors and 20% for wines, and ii) a specific component that varies according to the alcohol content of each liquor or wine.

3. Vehicle tax

a. Concept

The vehicle tax is levied on the ownership or possession of vehicles. It is a departmental tax, but in the case of Bogotá, the tax collector is the Capital District of Bogotá.

b. Tax basis, frequency and rate

The base for calculating the tax is the amount of commercial appraisal that is annually fixed by resolution of the Ministry of Transport. In Bogotá, the applicable rates vary between 1.5% and 3.5% of the market value of the vehicle.

The tax is incurred annually on January 1 of each year. In the case of new vehicles, the tax is generated on the date of application for registration in the vehicle registry, which shall be the same date as that on the bill of sale or application for admission.

c. Responsible parties

The owner or possessor of vehicles, including public transport vehicles.

Municipal Taxes

Below is a general description of the main municipal or district taxes applicable to companies and individuals in Bogotá.

1. Industry and commerce, signs and boards tax (ICA)

a. Concept

The ICA is a municipal tax that is levied on every (i) industrial, (ii) commercial, or (iii) service activity undertaken in the jurisdiction of a municipality or district. These activities may be carried out, directly or indirectly, by individuals, legal entities, or de facto companies, whether

permanently or occasionally, in a given property, with or without business establishments.

b. Tax basis, rate and frequency

The industry and commerce tax is calculated based on the taxpayer's net revenue obtained in a municipal or district jurisdiction. In Bogotá, the tax is generally paid semiannually.

In Bogotá, rates vary between 4.14 per thousand and 13.8 per thousand, depending on the activity. In other jurisdictions, rates are between 2 per thousand and 10 per thousand.

100% of the amount paid of this tax is deductible from the company's income tax return, as long as it is related to the company's economic activity.

2. Unified property tax

a. Concept

The unified property tax is levied on real property.

b. Tax basis and responsible parties

The tax basis of this tax consists of the current property valuation at the time of taxation, adjusted by the consumer price index (CPI), of land or real estate located in urban, suburban or rural areas, with or without buildings.

Owners, possessors or beneficial owners of property are responsible for the tax. Therefore, unlike other countries, the property tax is not transferred to the tenant of the property.

c. Rate and frequency

The property tax rate in Bogotá is between 2 per thousand and 33 per thousand and is incurred annually. The rates applicable to non-urbanized developable plots and unbuilt urbanized plots may not exceed 33 per thousand.

100% of the amount paid for this tax is deductible from the company's income tax return, as long as it is related to the company's economic activity.

3. Urban works tax

a. Concept

The taxable event of the urban works tax is the performance of works or constructions that have been granted and notified of a building permit in any of the following forms: new works, expansion, adaptation, modification, restoration, structural reinforcement, demolition, and enclosing of new buildings.

b. Frequency and rate

The tax basis for calculating the urban works tax in the Capital District is the total amount of the works or construction budget.

For the urban works tax return, two forms must be submitted. The first one (initial return) is submitted before the beginning of works, and the applicable rate is 2.6% of the works or construction budget amount. The second one (final return) is submitted at the end of the works, and the rate is 3% of the works or construction budget executed. The amount paid in the initial return is regarded as an advance of the tax and applied to the amount payable in the final return.

4. Surplus tax

a. Concept

Surplus is the tax obligation of owners or possessors of property regarding which there has been an increase in land price as the result of urban planning actions that modify its use or increase its exploitation (property appreciation).

The taxable events of surplus derived from urban planning action in Bogotá, Capital District, include specific authorizations to either allocate a property for a more profitable use or increase land exploitation, allowing a greater built-up area, as formally set forth in the Land Use Plan (POT as per its acronym in Spanish) or instruments that develop it, in the following cases:

- Incorporation of rural land into urban expansion land.
- Establishment or modification of the land use system or zoning.
- Authorization for greater use of land in construction, increasing either the occupancy rate or the construction rate, or both at the same time.
- When performing public works considered part of “infrastructure macro projects” provided for in the Land Use Plan and/or instruments that develop it, and the appreciation contribution has not been used for their financing.

b. Frequency and rate

The surplus tax rate varies between 30% and 50% of the greater book value per square meter of the plot or property subject to the benefit.

References

- Internal Revenue and Customs Service (DIAN): www.dian.gov.co
- Governorate of Cundinamarca: www.cundinamarca.gov.co
- Bogotá City Hall: www.Bogotá.gov.co
- Bogotá Finance Secretary's Office: www.shd.gov.co

Tax incentives of the income tax

Some of the existing tax incentives in Colombian regulations to attract investment include the following:

a. Special deductions of the income tax

- Investments in research, development, technology or innovation may be 100% deducted in the taxable period in which they are made. In addition, a tax discount for these investments may apply as explained below.
- Additional deduction equivalent to 50% of investment in production and use of non-conventional renewable energy sources, which shall be requested within five years of the period in which investment is made.
- Possibility of using accelerated depreciation (up to an annual rate of 20%) in machinery, equipment and civil works necessary for pre-investment, investment and operation of generation based on non-conventional renewable energy sources.
- 100% of the industry and commerce, signs and boards tax and the property tax that have actually been paid during the taxable year or period is deductible, as long as they have a causal relationship with the taxpayer's economic activity.
- Fifty percent (50%) of the debit tax actually paid by taxpayers during the respective taxable year will be deductible, even if there is no causal relationship with the taxpayer's economic activity.
- From taxable year 2017, taxpayers will be entitled to deduct, for the calculation of their income tax basis, the amount paid under the heading of Sales Tax for the purchase or import of capital goods taxed at the general rate.

b. Exempt income

In the following events, among others, income will be deemed exempt for income tax purposes.

- Exempt income established in Decision 578 by the CAN (in this case, income is only taxed in the country of origin and exempted in the country of residence).
- Payment of principal, interest, commissions, and other items related to foreign public credit transactions, provided they are paid to persons without residence or domicile in the country.
- Sale of electrical energy generated by wind resources, biomass, agricultural waste, solar energy, geothermal energy or sea energy, made only by the generating

companies, for a period of fifteen (15) years from 2017, provided the established requirements are met.

- Provision of river transport services with vessels and shallow draft barges, for a period of fifteen (15) years from the entry into force of Law 1819 of 2016.
- Exploitation of new forestry plantations.
- Income associated with public housing.
- Compensations for life insurance.

c. *Discounts from the income tax*

The following items have been established by Colombian regulations as discounts from the income tax, i.e., they can be directly subtracted from such tax. For each item, scope of the discount must be reviewed. In addition, total discount cannot be greater than 75% of the tax determined by the taxpayer's presumptive income system.

- Income taxes paid abroad for income of foreign source may be taken as a credit / tax discount against income tax generated by such income in Colombia.
- 25% of investments in environment control and improvement and investments in research, development, technology and innovation made in the year.
- 25% of donations made to non-profit organizations listed in Article 22 and 23 of the Tax Code.
- Discount from the income tax of parafiscal and other payroll contributions for taxpayers hiring displaced people, individuals in the process of reintegration, or disabled people.
- Discount from the income tax of parafiscal and other payroll contributions for taxpayers hiring women who, at the beginning of the employment contract, are over forty (40) years old and have not had an employment contract in the last twelve (12) months.
- Discount from the income tax of parafiscal and other payroll contributions for taxpayers hiring employees who, at the beginning of the employment contract, are under twenty-eight (28) years old.

Base Erosion and Profit Shifting (BEPS)

BEPS is an ambitious project led by the Organization for Economic Cooperation and Development (OECD) to prevent elusion and fiscal abuse worldwide by updating tax regulations around the world.

Colombia is currently seeking to become a member of the OECD and has been part of the countries that have actively participated in the BEPS initiative.

On October 5, 2015, the OECD issued final reports on the 15 actions that make up the BEPS action plan. In November 2015, the reports were backed by the countries that make part of the G-20, which comprises the biggest 20 economies in the world (the G-20 includes countries that are not OECD members such as China, Russia, Brazil, Argentina, India and Indonesia, and South Africa).

The reports contain recommendations that fall within the categories mentioned in the chart below.

In BEPS, there are also analytical reports on: (i) tax challenges of digital economy (action 1), (ii) methodologies for data collection and analysis on BEPS (action 11), (iii) and multilateral instruments for implementing BEPS initiatives (Article 15).

The last tax reform (Law 1819 of 2016) introduced several regulations that are inspired by BEPS recommendations such as regulations on controlled foreign companies (CFC) (action 3), establishment of a master file and country-by-country report for transfer pricing purposes (action 13), the methodology applicable to transfer pricing for commodities (actions 8 to 10), among others. However, certain BEPS type proposals in the bill, which became Law 1819 of 2016, such as that related to the disclosing of aggressive tax planning, were not adopted in the bill passed.

Finally, on June 7, 2017, about 70 jurisdictions signed the multilateral instrument that was prepared pursuant to action 15 and that seek to implement several BEPS measures in existing double taxation agreements. Colombia was one of the signors and it is expected that, in the short term, the process of approval of this instrument (approval by the Congress and review by the Constitutional Court) be conducted so that such multinational regulation starts to apply to the agreements signed by Colombia, and countries ratify it and adopt it under their internal legal procedures.

BEPS reports contain recommendations that fall into the following categories:

Agreements on minimum standards	Reinforced international standards	Common approaches and best practices in local regulations
<ul style="list-style-type: none">• Recommendations to fight against harmful tax practices (action 5)• Abuse of treaties (action 6)• Country-by-country reporting (action 13)• Mechanisms for dispute resolution (action 14)	<ul style="list-style-type: none">• Revision of transfer price guides (actions 8, 9 and 10)• Revision of the OECD model convention to avoid double taxation (including action 7 on permanent establishment)	<ul style="list-style-type: none">• Neutralization of the effects of hybrid instruments and mechanisms (action 2)• Rules for controlled foreign companies (CFC) (action 3)• Limitation in the payment of interest (action 4)• Disclosure of aggressive tax planning (action 12)

