COLOMBIAN TAX FLASH®

13 Years

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2016 TAX REFORM ACT

In this issue, Colombian_Tax_Flash® provides a summary of the main (not all) changes introduced to the Colombian tax system by the 2016 Tax Reform Act in connection to:

(1) CORPORATE INCOME TAX: (1.1) Rates; (1.2) Dividend Taxation; (1.3) Withholding Tax on Cross-Border Payments; (1.4) New Items of Foreign Source Income; (1.5) Taxable Base; (1.6) Income Tax Deductions; (1.7) Depreciation and Amortization; (1.8) Exempt (non-taxable) Items of Income Repealed; (1.9) Tax Loss Carry-Forward; (1.10) Adjustment Due to the Fluctuation of the Exchange Rate of Foreign Currencies. **(2)** ANTI-ABUSE PROVISIONS: (2.1) Tax Evasion as Criminal Offence; (2.2) Controlled Foreign Entities Regime; (2.3) General Anti-Avoidance Rule; (2.4) Tax Havens (Non Cooperative Jurisdictions); (2.6) Disclosure of Beneficial Ownership. **(3)** TRANSFER PRICING: (3.1) Country-by-Country Report; (3.2) Transactions with Foreign Related Parties; (3.3) Domestic Transactions. **(4)** SPECIAL TAX FRAMEWORKS: (4.1) Public Private Partnerships and Concession Agreements; (4.2) Regulated Fiduciary Arrangements; (4.3) Carbon Dioxide Tax; (4.4) Joint Ventures; (4.5) Leasing; (4.6) Stock Options. **(5)** VAT AND CONSUMPTION TAXES: (5.1) VAT Rate; (5.2) Broadened Scope of Transactions Taxable with VAT; (5.3) Broadened Scope of Transactions Taxable with Consumption Taxes; (5.4) Income Tax Deduction of VAT paid in the Acquisition or Import of Capital Assets; (5.5) Payment and Filing. **(6)** TAXES ON CAPITAL: (6.1) Wealth Tax Unchanged; (6.2) Alternate Minimum Taxable Income; (6.3) Normalization Tax. **(7)** BANK DEBITS TAX. **(8)** NEW STATUTE OF LIMITATIONS.

HIGHLIGHTS

	Previous	New	More info
Corporate Income Tax – Colombian entities and PEs of foreign entities	25%	34% (2017) 33% (As of 2018)	§1.1.
Corporate Income Tax - Foreign Entities	42% (2017) 43% (2018) 33% (As of 2019)	34% (2017) 33% (As of 2018)	§1.1.
Corporate Income Tax Surcharge (for tax bases equal or higher than COP 800.000.000)	N/A	6% (2017) 4% (2018)	§1.1.
CREE (Equity tax)	9%	Repealed	§1.1.
CREE Surcharge (for income equal or higher than COP 800.000.000)	8% (2017) 9% (2018)	Repealed	§1.1.
Free Trade Zones Reduced Corporate Income Tax Rate	15%	20%	§1.1.2.1

Regular Withholding Taxes on Cross-border Payments:				
-Dividends already taxed at the corporate level (including branch profits), paid to:	Resident individuals	0%	0%, 5% or 10%	§1.2.2.
	Colombian companies	0%	0%	
	Non-resident individuals	0%	5%	
	Foreign entities	0%	5%	
	PEs of foreign entities	0%	5%	
-Dividends untaxed at the corporate level (including branch profits), paid to:	Resident individuals	33%	35%, 38,25% or 41,5%	§1.2.2.
	Colombian companies	33%	34% (2017) 33% (as of 2018)	
	Non-resident individuals	33%	38,25%	
	Foreign entities	33%	38,25%	
	PEs of foreign entities	33%	38,25%	
-Interest on credit facilities for a term exceeding 1 year.		14%	15%	§1.3.
-Royalties (on software)		33% (26.4%)	15% (26.4%)	§1.3.
-Technical Assistance, Technical Services and Consultancies		10%	15%	§1.3.
-Tax Havens		33%	34% (2017) 33% (as of 2018)	§1.3.
Tax Loss Carry-forward Term		Unlimited	12 years	§1.9.
General VAT Rate on Sales, Services and Imports		16%	19%	§5.1.
Consumption tax on franchised restaurant sales.		N/A	8%	§5.3.
VAT on (i) the sale of intangibles (at the general rate), (ii) the first sale of residential estate (at a 5% rate), and (iii) the services rendered from abroad (at the general rate).				§5.2.
First-time adoption of a CFC-type regime applicable not only to companies, but also to other entities.				§2.2.
Failure to report assets and reporting non-existent liabilities to be regarded as a criminal offence for the first time				§2.1.
Alternate Minimum Taxable Income		3%	3,5%	§6.2.
General Statute of Limitations		2 yrs.	3 yrs.	§8

1. Corporate Income Tax

1.1. Corporate Income Tax Rates

The Tax Reform Act modifies the Corporate Income Tax ("CIT") rate, as explained herein below.

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Under previous regulations the CIT rate for Colombian entities and Colombian permanent establishments of foreign entities was 25%, plus the 9% income-based Equity Tax "CREE" and the 8%[1] CREE surcharge.

The Tax Reform Act repeals both CREE and CREE Surcharge and:

(a) increases the CIT rate to 34% (for FY 2017), 33% (as of FY 2018); and

(b) introduces a new CIT surcharge for taxpayers with a CIT taxable base equal or higher than COP 800.000.000 (approx. USD 266.845) at a rate of 6% (for FY 2017) and 4% (for FY 2018).

Hence, while under the previous law, in FY 2017 the applicable CIT rate would have been 25% (income tax) + 9% (CREE) + 8% (CREE Surcharge) = **42%**, the applicable CIT rate under the Tax Reform Act for FY 2017 will be 34% + 6%= **40%**. This implies a reduction of 2 percentual points for 2017.

In FY 2018 the CIT rate will be 33% + 4% = **37%** and as of FY 2019 it will be **33%**.

For foreign entities that have to file a CIT return in Colombia, the CIT rate was set at **34%** for FY 2017 and **33%** as of FY 2018. It is worth highlighting that the change to this rate does not override currently applicable reduced withholding tax rates for certain cross-border payments.

1.1.2. Special Rates

1.1.2.1. Free Trade Zones ("FTZ")

Under the previous regulations FTZ users were subject to CIT, CREE and CREE surcharge as shown in the table below. The Tax Reform Act unifies the reduced CIT rate for FTZ at **20%**. The CIT Surcharge should not apply to FTZ users.

Type of FTZ	Previously			Now
	CIT	CREE	CREE Surcharge	CIT
Continental FTZ incorporated before 31/12/12	15%	N/A	N/A	20%
Continental FTZ incorporated after 31/12/12	15%	9%	8% (2017) 9% (2018)	
Offshore FTZ	15%	9%	N/A	

[1] Rate applicable for FY 2017. The CREE surcharge was introduced by the 2014 Tax Reform and was meant to operate through FY 2015 (at a 5% rate), FY 2016 (at a 6% rate) and FY 2017 (at an 8% rate)

1.1.2.2. 9% Rate Applicable to Certain Activities

The 2016 Tax Reform Act establishes that, as of fiscal year 2017, a special 9% CIT rate should apply to:

(a) income from hotel services rendered in newly built or refurbished facilities, which according to the previous regulation should have benefited from a 30-year exemption, will now be subject to the reduced 9% CIT rate as of 2017, and throughout the 10 years following the entry into force of the Tax Reform Act;

(b) income received by certain companies owned or partially owned by the State; and

(c) income from certain leasing facilities for the acquisition of dwelling, which under the previous regulation should have benefited from a CIT exemption.

1.1.2.4. Progressive CIT Rate for small companies benefiting from Law 1429/2010

Under previous regulations, small companies (i.e. companies with less than 50 employees and assets worth less than approximately USD 1 million) were subject to CREE at a 9% rate, but were eligible for a progressive CIT rate as shown in the table below. The Tax Reform Act changes the CIT regime applicable to these companies, establishing a new progressive CIT rate, as follows:

	Previous Regime	Current Regime
First two years	0% of the general CIT rate	9% + (general CIT rate - 9%)*0
Third year	25% of the general CIT rate	9% + (general CIT rate - 9%)*0,25
Fourth year	50% of the general CIT rate	9% + (general CIT rate - 9%)*0,5
Fifth year	75% of the general CIT rate	9% + (general CIT rate - 9%)*0,75
As of the sixth year	100% of the general CIT rate	100% of the general CIT rate

1.2. Dividend Taxation

For three decades Colombia did not tax dividend distributions, provided that the distributed profits had previously been taxed at the level of the distributing entity. However, the Tax Reform Act modifies this system by taxing both the distributing company and the shareholder receiving the distributed dividends, as explained herein below.

1.2.1. Definition of Dividend

The Tax Reform Act modified the definition of dividends as follows:

(a) It was broadened, establishing that dividend distributions comprise any distribution of benefits, in cash or in kind, out of equity (and not only out of profits);

(b) The new definition explicitly clarifies that distributions corresponding to paid-in capital or share premiums paid-in by the beneficiary of the distribution are not deemed dividends and are, therefore, not taxable; and

(c) The transfer of profits from permanent establishments in favour of their home office should continue to be a deemed dividend distribution.

1.2.2. Rates

The following chart summarizes the applicable rates:

Beneficiary	Profits taxed at the corporate level	Profits untaxed at the corporate level
Colombian companies	0%	34% (2017) 33% (As of 2018)
Resident individuals	0%, 5% or 10%	35%, 38,25% or 41,5%
Foreign companies	5%	38,25%
Non-resident individuals	5%	38,25%
Permanent Establishments (including branches)	5%	38,25%

It is worth highlighting that

(a) except in the case of Colombian companies, the new provision establishes that dividends paid out of profits that were not taxed at the corporate level, are subject to an additional withholding, after applying the "general" 35% withholding. This provision should be carefully reviewed under the treaties to avoid double taxation that have been executed by Colombia, particularly considering that in many of them a 0% withholding on dividends has been agreed upon.

(b) dividends received by a Colombian Company would be untaxed while dividends received by a Colombian branch of a foreign company would be taxed at a 5% withholding tax rate.

(c) the fact that non-resident individuals are always subject to a 5% rate, while resident individuals can be subject to either a 0%, 5% or 10% rate could be considered discriminatory. A lawsuit in connection to the constitutionality of this provision was already filed before the Constitutional Court.

The new regime is applicable to distributions of profits generated as of 2017, i.e. distributions of profits generated on of before December 31st 2016 would be subject to the previous regime, even if distributed in 2017 or thereafter.

1.3. Withholding Tax on Cross-Border Payments

The 2016 Tax Act modifies the withholding tax rates applicable to cross-border payments. The principal changes are the following:

Payment	Previous withholding rate	New withholding rate
Interest, Commissions, fees, royalties (except for royalties on software), leases, as well as any other payment made in consideration for personal services	33%	15%
Royalties on software.	26,4%	26,4%*
Consultancy services, technical services and technical assistance	10%	15%
Interest from loans with a term equal or higher than 1 year	14%	15%
Reinsurance premium	Untaxed	15%
Any payments performed in favour of a person or entity resident, domiciled or functioning in a non-cooperative jurisdiction (i.e. tax haven) or subject to a preferential tax regime.	33%	34% (2017) 33% (as of 2018)
In consideration for services provided by international transport companies, either by air or sea	3%	5%
General withholding tax rate	14%	15%**
Capital Gains	Not specified	10%***

*The Tax Reform Act unified the withholding tax rate applicable on most cross-border payments at 15%. However, royalties on software will continue to be subject to a 26,4% withholding tax.

**This tax rate is not applicable to investors subject to the tax regime provided in section 18-1 of the CTC (portfolio investors).

***The withholding rate for capital gains was set at 10% (i.e. the same rate as that of the final tax); taking into account that the withholding is performed on the gross payment, while the tax is assessed on a net basis, the taxpayer will always have a balance, which can only be recovered by claiming it back from the Tax Authorities.

1.4. New Items of Foreign Source Income

The Tax Reform Act established that income from international transport (aerial or maritime) received by an enterprise resident in Colombia is now considered foreign source income.

Although the wording of this provision could be misleading, as it refers to enterprises (i.e. business activities) and not to companies or individuals, in our view it implies that Colombian tax residents carrying out such activities should have the right to a statutory foreign tax credit with regards to any taxes paid abroad in connection thereto.

1.5. Taxable Base

Due to a recent change in the accounting regulatory framework, currently Colombian companies must keep their accounting records in accordance with International Financial Reporting Standards ("IFRS").

The 2016 Tax Act introduced changes that imply that, as of FY 2017, the taxable base of the CIT will be calculated using the financial information deriving from the accounting records kept in accordance with IFRS. Nonetheless, according with the 2016 Tax Act, various adjustments should be made, in order to avoid that the taxpayer is obliged to pay tax on theoretical income or allowed to deduct theoretical expenses.

Hence, despite the tax assessment process continues unchanged, there are various changes as to align, for accounting and tax purposes, among others, (i) the moment of accrual of income and costs, (ii) the deductible expenses, (iii) the calculation of the useful life of the assets, and (iv) the applicable methods of depreciation.

It is important to note that, a large amount of adjustments for tax purposes are comprised in the 2016 Tax Act, which will most likely imply that, notwithstanding IFRS will be the basis both for accounting and tax purposes, (i) the taxpayers will still need to keep, besides the regular accounting records, special accounting records for tax purposes, and (ii) there might arise important differences between accounting and tax records, which will most likely generate untaxed profits at the level of the company, taxable therefore at a higher rate at the level of the shareholder.

On a separate matter and as further explained in §6.2 below, the 2016 Tax Act increased the percentage used to calculate the alternate minimum taxable income to 3,5%.

1.6. Income Tax Deductions

The 2016 Tax Act introduces various changes in connection to income tax deductions. The main ones are:

(a) the impossibility to deduct payments consisting in (i) penalties or sanctions, and (ii) taxes that should have been paid by a third party. The latter could affect the deductibility of payments made further to certain gross-up clauses.

(b) complimentary gifts and parties for clients, suppliers and employees are recognized as deductible, but limited to 1% of the net taxable income.

(c) royalties paid to foreign related parties or to related parties operating in a FTZ, with regards to intangible goods formed in Colombia, are not deductible.

(d) royalties paid in consideration for the acquisition of finished products are not deductible.

(e) as further explained in §5.4 below, taxpayers would be allowed to deduct 100% of the VAT paid in the acquisition/import of capital assets during the first year; previously VAT was deductible via depreciation during the lifespan of the assets.

(f) the 15% deductibility limit in connection to costs and expenses incurred abroad was broadened as a consequence of the elimination of part of the exceptions to its applicability.

(g) a 6-month term is set for the registration of contracts regarding the import of technology, as a requirement for the corresponding payments to be deductible.

(h) cross-border payments to the home office of Colombian branches and subsidiaries in consideration for management are subjected to withholding tax, regardless of whether they are deemed to generate Colombian source income or not.

1.7. Depreciation and Amortization

1.7.1. Depreciation

According to the 2016 Tax Reform Act assets' depreciation remains deductible. Nevertheless, the following substantial changes should be taken into account:

(a) the applicable depreciation term that was previously set by the tax regulations, now depends on the lifespan of the asset. IFRS regulations should be regarded, however, the lifespan of an asset determined for tax purposes may differ from the lifespan determined for accounting purposes;

(b) a maximum depreciation rate that varies between 2,22% and 33% is set. Depreciation rates for specific assets are set in the Tax Reform Act. Nonetheless, the Government will be able to establish other depreciation rates, within the aforementioned range;

(c) if the machinery and equipment are daily used at least for 16-hour shifts, depreciation can be accelerated, increasing the depreciation rate in 25%.

Considering that the Tax Reform Act substantially modifies the previous regime, transitional rules are established and should be considered by taxpayers on a case-by-case basis.

1.7.2. Amortization

Subject to meeting the eligibility requirements, certain investments –such as expenses paid in advance, establishment investments and research expenses- listed and defined by particular articles of the 2016 Tax Reform Act will be treated as a deduction. Intangible assets deemed as necessary investments for the taxpayer's business activities that must be capitalized can be amortized (certain limitations may apply).

It is worth highlighting that, although under IFRS preoperative expenses are deductible when completed, for tax purposes it would be necessary to register an asset and deduct its value via amortization.

A special treatment concerning the exploitation of oil, gas and mines is included in the 2016 Tax Reform. Some of the main points to highlight are the following:

(a) investments that could be amortized are specifically defined in an article of the Tax Reform – the previous regimen did not provide such definitions-;

(b) in order to establish the amortizable amount, the 5-year period criterion that used to apply was replaced by a new criterion that combines the *productive units and proven reserve* items; and

(c) costs incurred improving the exploitation of non-renewable natural resources can be capitalized and subsequently amortized.

Considering that the Tax Reform Act substantially modifies the previous regime, it comprises a transitional rule that should be considered by the taxpayers on a case-by-case basis.

1.8. Exempt (non-taxable) Items of Income Repealed

According to the 2016 Tax Reform Act, as of fiscal year 2018, some items of income that were exempt are repealed, including the following:

(a) income from hotel services rendered in newly built or refurbished facilities, which will now be subject to a reduced 9% CIT rate;

(b) income from the provision of seismic services to the hydrocarbons industry;

(c) income from eco-tourism activities, which will now be subject to a reduced 9% CIT rate;

(d) income from new medical products and software;

(e) the profit on the sale of properties intended for public utility, contributed to a regulated fiduciary arrangement "*patrimonio autonomo*".

Likewise, under the previous regulation, certain retained earnings, even if untaxed at the corporate level, could be capitalised and the shares received by the shareholders as a consequence of such capitalisation were a deemed non-taxable income. This special treatment applied to a reserve (the "Reserve") that had to be created whenever the taxpayer had taken higher depreciation rates for tax purposes than for accounting purposes.

The 2016 Tax Act repealed the abovementioned tax treatment. However, according to the transitory regime, any Reserve created before December 31st, 2016 can be distributed to the shareholders, or capitalised after January 1st, 2017 as non-taxable income, as of the moment in which the depreciation rates for tax purposes become lower than those for accounting purposes.

1.9. Tax Loss Carry-Forward

According to the previous regulation, taxpayers had a right to an evergreen carry-forward of their tax losses. The 2016 Tax Act limited this carry-forward to the 12 fiscal years following the year in which the tax loss accrued.

A transitory regime was introduced, according to which tax losses generated before January 1st, 2017 will continue to be subject to the previous regime.

1.10. Adjustment due to the Fluctuation of the Exchange Rate of Foreign Currencies

The 2016 Tax Reform modifies the previous regime as follows

(a) Income, expenses, costs, assets and liabilities in foreign currency should be accounted for at the exchange rate of the day of its initial recognition.

(b) For tax purposes exchange differences shall be recognized as income or expense for the fiscal year in which (i) the asset is sold or exchanged; or (ii) the liabilities are liquidated or paid.

(c) the taxable income or the deductible costs or expenses correspond to the difference between the exchange rate at the initial recognition and the exchange rate at the day of the payment or accrual of the payment.

Considering that the Tax Reform Act substantially modified the previous regime (formerly the relevant regulation stated that the adjustment to be made due to the fluctuations in the exchange rate of assets in a foreign currency owned by a taxpayer on the last day of the fiscal year or taxable period constituted income in such fiscal year), the 2016 Tax Reform Act provides a transitional rule that should be reviewed on a case-by-case basis.

2. Anti-Abuse Provisions

2.1. Tax Evasion as Criminal Offence

The 2016 Tax Reform Act introduces two new criminal offences, one in connection to income tax and one in connection to VAT.

2.1.1 Income Tax: Criminal Offence for Omitting Assets or Reporting Non-Existent Liabilities

The corresponding provision establishes a Criminal Penalty for taxpayers that intentionally affect their income tax due or their reported income tax balance by (i) omitting assets or filing inaccurate information regarding their assets; or (ii) reporting non-existent liabilities, or filing inaccurate information regarding their liabilities. The omitted assets or non-existent liabilities should be equal to or higher than 7.250 minimum wages (approx. COP 5.000.000.000 or USD 1.667.779).

The penalty comprises (i) imprisonment from 48 to 108 months and (ii) 20% of the amount of the omitted asset or the non-existent liabilities. The criminal liability would extinguish when the taxpayer presents or corrects the tax return and performs the corresponding payments.

2.1.2 VAT and Consumption Tax: Criminal Offence for not Collecting VAT or Consumption Tax

Formerly there was a criminal offence referring only to taxpayers that, having collected taxes, did not pay them to the Tax Service. This provision continues to apply but was broadened to comprise taxpayers that having the obligation to collect and pay to the Tax Service VAT or Consumption Tax fail to do so.

The penalty comprises (i) imprisonment from 48 to 108 months and (ii) double of the amount of the unpaid VAT/Consumption Tax. The criminal liability would extinguish when the taxpayer presents or corrects the tax return and performs the corresponding payments.

It is important to highlight that the corresponding provision explicitly states that if the criminal offence is committed by an entity, the natural persons in charge of fulfilling the tax obligations of the entity would be held liable.

2.2. Controlled Foreign Entities Regime

The 2016 Tax Reform Act introduces Controlled Foreign Entities rules (CFE rules). Therefore, individuals and national companies subject to income tax in Colombia that directly or indirectly control a foreign entity and hold participation equal or higher than 10% in it are subject to this regime.

The Tax Reform Act defines CFE as investment vehicles such as corporations, regulated fiduciary arrangements, trusts, mutual funds, other trust, and business and private foundations, that are incorporated or domiciled abroad, regardless of whether they have legal personality, and/or whether they are transparent for tax purposes.

A CFE is deemed to be controlled by one or more Colombian residents when one of the following criteria is met:

(a) the CFE is subordinated of a Colombian resident according to §260-1 of the CTC;

(b) the CFE is a related party of one or various Colombian residents according to §260-1 of the CTC; or

(c) the CFE is domiciled in a non-cooperative jurisdiction (tax haven).

The CFE should not be a tax resident in Colombia. Income, costs and deductions relating to passive income obtained by the CFE are deemed to have accrued at the level of the Colombian residents that directly or indirectly control the CFE, in the same taxable year in which such income, costs and deductions accrued in the CFE. The tax recognition of these assets, costs and deductions should be made in

proportion to the participation held by each Colombian resident in the CFE. However, it is important to highlight that the applicable provisions explicitly forbid the use by the controlling Colombian tax resident of any tax losses accrued at the level of the CFE.

Passive income comprises:

(a) Dividends or any other form of distribution, except for profits that have their origin in real economic activities carried out by the CFE or its subsidiaries. This rule shall be carefully considered in a case-by-case basis;

(b) Proceeds except those obtained by either a CFE controlled by a company that is subject to "surveillance" from the Colombian Superintendence of Finance, or a foreign financial institution, not domiciled in a non-cooperative jurisdiction;

(c) Royalties;

(d) Income from the alienation of the CFE's participation in a passive-income-producing entity;

(e) Income derived from alienation or rental of immovable property;

(f) Income from the trade of goods that (i) are acquired from, on behalf or for a related party; (ii) are produced, manufactured, built, farmed, or extracted in a jurisdiction different from that of residence of the CFE; and (iii) are consumed, used or disposed of in a jurisdiction different from that of residence of the CFE;

(g) Income from intercompany services (technical assistance, and technical, management, engineering, architectonic, scientific, qualified, industrial or commercial services) rendered for or on behalf of a related company in a jurisdiction different from that of the CFE.

This regime is not applicable to profits from active income. However, all revenues, costs and deductions of the CFE are presumed to give rise to passive income, when passive income represents 80% or more of the total revenues of the CFE.

The fact that (i) the income from trading and from the provision of services is deemed passive income, and (ii) entities controlled by Colombian tax residents are deemed CFEs, regardless of whether they are subject to a low or high level of taxation in their tax residence, is rare and implies the need to review the impact of this new regime on a case-by-case basis for taxpayers with operations abroad.

2.3. General Anti-Avoidance Rule

In 2012, for the first time in Colombia a General Anti-Avoidance Rule (GAAR) was introduced. The Tax Reform Act modifies the GAAR, to facilitate its applicability for the Tax Service.

The GAAR broadens the definition of tax abuse to comprise the use or implementation of one or more contrived acts or legal transactions, without an apparent economic or commercial purpose, in order to obtain a tax benefit, which is defined as the alteration, disfigurement or modification of the tax effects, for instance, the elimination, reduction, or deferral of a tax due, or increasing the balances or tax losses, or the extension of tax benefits and/or exemptions. In our view, this definition does not imply a material change.

This GAAR introduces the following non-exhaustive list of cases in which a business is deemed to lack commercial or economic purpose:

(a) The legal act or transaction is executed in a way that, in economic and/or commercial terms, is unreasonable;

(b) The legal act or transaction results in a higher tax benefit that is not proportional to the economic or business risks borne by the taxpayer; or

(c) An act or business apparently correct hides the true and real intention of the parties.

The previous regulation set quantitative thresholds and the need to meet 3 out of 5 criteria to shift the burden of proof from the Tax Service to the taxpayer. These requirements are eliminated through the Tax Reform Act; under the new regulation the Tax Service should always bear the burden of proof. Additionally, the Tax Reform Act establishes a new administrative procedure for these cases and an inaccuracy penalty of 160%.

The new rule maintains the provisions according to which the Tax Service could (i) re-characterize or reconfigure every transaction or series of transactions that are deemed abusive for tax purposes, as well as disregard their effects in order to prove the reality of the transaction; and (ii) pierce the corporate veil from the companies or entities that were part of the transaction(s) considered abusive. The new rule introduces a new definition of re-characterization that in our view does not represent a material modification.

2.4. Tax Havens (Non-Cooperative Jurisdictions)

The concept of tax havens' is replaced by and broaden by the concept of "non-cooperative jurisdictions, with no or low imposition and preferential tax regimes".

On the one hand, the Government will define which jurisdictions are non-cooperative, according to the following criteria: (i) absence of imposition or low

imposition regarding tax regime parallel to Colombian standards; (ii) lack of effective information exchange; (iii) absence of transparency at a legal or regulatory level; (iv) the absence of a requirement of either a substantive presence, or the exercise of a real activity which has economic substance; and (v) other criteria internationally accepted for the identification of non-cooperative jurisdictions. Not all of the criteria need to be met; meeting only one criterion could be enough for a jurisdiction to be classified as non-cooperative.

On the other hand, the taxpayer will have to identify the preferential regimes. For that purpose, the relevant provision of the Tax Reform Act states that preferential regimes are those that meet at least 2 out of the following 5 criteria: (i) absence of imposition or low imposition regarding tax regime parallel to Colombian standards; (ii) lack of effective information exchange; (iii) absence of transparency at a legal or regulatory level; (iv) the absence of a requirement of either a substantive presence, or the exercise of a real activity which has economic substance; and (v) the fact that the regime is available only for non-residents (ring fencing).

Notwithstanding the above, the Government could issue a list of preferential regimes, based on the aforementioned criteria and on any other internationally accepted criteria.

Without prejudice of other effects, the relevant provision explicitly refers to the following:

(a) non-deductibility of payments made to individuals or entities resident, domiciled or located in non-cooperative jurisdictions or subject to preferential tax regimes if either (i) the relevant withholding tax is not performed, except for payments in connection to financial transactions dully registered before the Central Bank, or (ii) the taxpayer fails to document and prove the functions performed, the assets used and the risks borne, as well as the costs incurred by the individual or entity resident, domiciled or located in a non-cooperative jurisdiction or subject to a preferential tax regime; and

(b) application of the Colombian Transfer Pricing Regime, including the obligation to prepare and file a transfer pricing study and return, regardless of whether the regular thresholds established in the relevant regulations for this requirement to apply are met or not.

In the previous regime, as in most cases dividends were untaxed and when taxed were subject to a 33% withholding, the applicable withholding tax rate applicable to tax havens did not have a major relevance. However, under the new regulation it will have a big impact, as the Tax Reform Act introduced a tax on dividends distributed out of profits already taxed at the corporate level. This means that, when paid to a company or individual that is domiciled, resident or functioning in a non-cooperative jurisdiction/preferential tax regime, such payment will be subject to a 34% rate, instead of the 5% rate generally applicable to dividends.

2.5. Disclosure of Beneficial Ownership

A new rule, according to which the Colombian companies owned Colombian or foreign companies, as well as the Colombian permanent establishments (including branches) of foreign companies, regulated fiduciary arrangements and mutual funds owned by foreign companies, shall report to the Tax Service information in connection to their Beneficial Owners. For instance, they shall report the following information: name, date of birth, identification number, and participation in the capital of the company, among others.

The concept of Beneficial Owner comprises individuals that meet any of the following conditions:

(a) Have effective direct or indirect control of a Colombian company, an agent, a regulated fiduciary arrangement, an investment fund or a permanent establishment of the foreign company; or

(b) Be a direct or indirect beneficiary of the operations and activities carried out by the Colombian company, agent, regulated fiduciary arrangement, investment fund or permanent establishment of the foreign Company; or

Certain entities, to be defined by the Government, will collect and disclose information in connection to the beneficial owners of financial accounts.

3. Transfer Pricing

3.1. Country-by-Country Report

As of FY 2016, a country-by-country report will have to be filed in Colombia by:

(a) Colombian taxpayers that are controlling entities of multinational groups of companies; or

(b) Entities (resident or non-resident) that have been designated by the controlling entity as responsible for the filing of the country-by-country report; or

(c) One or more entities and/or permanent establishments pertaining to the same multinational group and having a foreign home office, provided that (i) the income generated by these entities and/or permanent establishments corresponds to at least 20% of the total income of the multinational group; (ii) the home office did not file a country-by-country report in its country of residence; and (iii) the total income of the multinational group in the previous year was equal or higher than USD 800.000.000 (approx.).

The country-by-country report should contain all information relating to the allocation of income and the taxes paid by the multinational group globally. Certain indexes in connection to the economic activity carried out by the multinational group should also be included.

3.2. Transactions with Foreign Related Parties

The Colombian transfer pricing regime is based on the OECD Guidelines on Transfer Pricing.

The 2016 Tax Act sets the comparable uncontrolled price method (the "CUP Method") as the preferred method for operations involving commodities. The relevant provision of the Tax Reform Act clarifies that, when applying this method for commodities, index prices can be used as relevant comparables.

The CUP Method can only exceptionally be discarded if the taxpayer finds a method that is more appropriate for the specific case. The taxpayer should be able to prove the grounds for choosing a different method if audited by the Tax Service.

3.3. Domestic Transactions

For domestic transactions, §90 of the CTC establishes that, for tax purposes, the price of alienated assets cannot vary in more than 25% from their market value.

Although it was not regulated, traditionally had been interpreted that for the sale of stock that is not listed, the market value of shares should be their intrinsic value (i.e. the market value of each share should be calculated dividing the equity of the company by the number of issued shares). The 2016 Tax Reform Act sets forth that, unless the taxpayer can prove otherwise, the market value of unlisted shares should be their intrinsic value plus a 15% increase. This rule should also apply to alienations of participations in regulated fiduciary arrangements and similar investment vehicles holding shares in Colombian unlisted companies.

4. SPECIAL TAX FRAMEWORKS:

4.1. Public Private Partnerships and Concession Agreements

A new special tax framework for Public Private Partnerships and Concession Agreements is introduced by the 2016 Tax Act. This new framework aims to arrange an existing mismatch between the moment of accrual of the income with the moment in which the amortization and depreciation expenses could be deducted by the taxpayer. This new tax framework applies whenever the concession agreement comprises both the construction and the operation and administration stages.

Whenever a concession agreement is granted only with regards to one of the stages the new rules are not applicable and the general rules for the accrual of income, depreciation and amortization deductions should be applied.

4.2. Regulated Fiduciary Arrangements

The 2016 Tax Act is enhancing the transparency of the Fiduciary Arrangements to a full transparency tax regime, by stating that the beneficiary should report in its income tax return the income, costs and expenses accrued at the level of the fiduciary arrangement. Under the former tax framework (partial transparency) the beneficiary only had to report in its income tax return the profit or loss accrued at the level of the fiduciary arrangement.

New rules on income accrual have been enacted and should be carefully reviewed on a case-by-case basis, as they could have important tax implications for beneficiaries and settlors of the fiduciary arrangements.

4.3. Carbon Dioxide Tax

The 2016 Tax Reform Act creates a "Carbon Dioxide Tax" which intends to be triggered by the first sale or import of fossil fuels, including oil-derived products and all types of gas that may be used as energy sources. This tax is triggered only once, either on the import or on the first sale made by the local producer. Neither exports, nor subsequent sales or operations are taxed.

The rate is COP15.000 (Approximately USD5) per ton of CO2 that a determined fossil fuel is estimated to generate. This rate will be annually readjusted. In order to ease the taxable base of this Tax, the government included the following table, which contains an already calculated estimate of the tons of CO2 produced by each of these common fuels, and therefore, already has a fix rate per unity.

Fossil Fuel	Unit of Measure	Rate/unity
Natural gas	Cubic meter	$29
Oil liquified gas	Galon	$95
Gasoline	Galon	$135
Kerosene and Jet Fuel	Galon	$148
Diesel	Galon	$152
Fuel Oil	Galon	$177

4.4. Joint Ventures

The 2016 Tax Reform Act states a common fiscal treatment for joint venture agreements, applicable to consortium agreements, associations (temporary company union), other joint ventures and joint accounts agreements, among others. Joint venture agreements, under this Tax Reform, continue to be regarded as non-taxpayers for CIT purposes and, therefore, as fully transparent from the tax perspective; however, additional formal obligations are established. It is important

to highlight that under the Tax Reform Act the parties of the joint venture agreements maintain the obligation to report the assets, liabilities, income, costs and deductions of the joint venture in their CIT returns, according to their participation in the agreement. The 2016 Tax Reform Act allows the parties of the joint venture to decide that the agreement should keep accounting records.

According to the new framework commercial relationships between the joint venture and its parties that imply a fixed remuneration for one of the parties should not be considered as contributions to the joint venture. The implications of this provision should be carefully reviewed on a case-by-case basis.

4.5. Leasing

The 2016 Tax Reform Act introduces (a) a definition of *financial leasing agreements*, including the features of this type of agreements, and its particular tax treatment and (b) a definition of *operative leasing agreements*, with its own tax rules. It is worth highlighting that the features listed by the provision as requirements for a leasing to be classified as a financial leasing for tax purposes does not necessarily match the definition of leasing agreements provided by the Colombian financial rules and the commercial regulation.

Concerning the proposed tax treatment, the 2016 Tax Reform Act introduces special accounting recognition rules based on the new accounting frameworks and other particular considerations.

The new framework is intended to apply to all leasing agreements executed as of January 2017.

4.6. Stock Options

The 2016 Tax Reform Act introduces a new chapter dedicated to the tax treatment of stock options.

The relevant provision of the 2016 Tax Reform Act establishes the tax regime applicable to (a) stock options, i.e. when shares of a company are offered to employees and the employee has the right to decide wether to accept the offer or not; and (b) when shares are transferred to an employee as part of his labor remuneration.

The applicable provision establishes rules for accrual of taxable income and the method to calculate the taxable base both for the company offering the stock option or transferring the shares and for the employee receiving either the stock option or the shares.

5. VAT and Consumption Taxes:

The 2016 Tax Reform Act has included major modifications to the current Colombian VAT regime. Among others, the Tax Act introduces the following changes:

5.1 VAT Rate

Under the previous regulation the general VAT rate was 16%. The 2016 Tax Reform Act modified the general VAT rate from 16% to **19%**. Certain goods and services will still keep the reduced 5% VAT rate. Also, certain goods and services will continue to be excluded or exempted (taxed at a rate of 0% with refund of paid VAT available).

5.2. Broadened Scope of Transactions Taxable with VAT

5.2.1. Sale of Goods

Under the previous VAT regime, Colombian VAT was triggered by the sale of tangible movable property whenever the goods sold were not fixed assets for the seller. The 2016 Tax Reform Act introduced the following relevant modifications regarding VAT over the sale of assets:

(a) A reduced 5% VAT for the first sale of residential real estate with a value greater than COP 800 millions approximately[2] (approximately USD 270.000).

(b) A modification of the types of goods that trigger VAT when sold in Colombia. As a consequence of such change, sales of intangible property related with intellectual property now also trigger VAT at the general rate. It is also important to note that any sale of intangible property or any licensing of intangible property made from outside Colombia, but with a buyer/beneficiary located in, and resident of Colombia is deemed as an operation that occurred inbound, and therefore triggers the corresponding Colombian VAT (this includes Colombian Permanent Establishments as buyers/beneficiaries of intangible property).

(c) Under the previous regulation, only certain services (e.g. technical services and consultancies) were taxed with VAT when rendered from abroad. The new regulation establishes that all services rendered from abroad levy VAT.

[2] The values are calculated for 2016. The proposed values are not fixed and will be readjusted on a yearly basis. Also, the approximate value in US dollars is calculated using a COP 3.000 per dollar rate, which is close to the real exchange value as of November 1st, 2016

It is worth highlighting that under the 2016 Tax Reform Act the sale of any type of good considered as a fixed asset does not trigger VAT.

5.2.2. Digital Services

The 2016 Tax Reform Act establishes a presumption under which any service rendered from abroad but with a beneficiary located and resident in Colombia is deemed as a service rendered inbound, and therefore, subject to VAT unless otherwise provided. This presumption especially has an impact over electronic services rendered to Colombian beneficiaries through software, mobile applications, and satellite broadcasting, among others.

In order to enforce the VAT triggered by the above-mentioned services, the 2016 Tax Reform Act states that the Colombian entities that issue credit cards or debit cards, as well as the sellers of gift cards or prepaid cards in Colombia for such services, and any other Colombian entity or person who receives payments on behalf of foreign renderers of the following services should withhold the VAT triggered as a consequence of the provision of such services at the general rate of 19%:

(a) Streaming services (including movies, TV shows, music, sports and any other kind of streaming).

(b) Digital platform for the digital distribution of mobile applications.

(c) Supply of online marketing/advertisement services.

(d) Educational or instructional electronic supply.

It is worth highlighting that the VAT withholding referred to above will be applicable only after 18 months as of the entry into force of the Tax Reform Act.

5.3. Broadened Scope of Transactions Taxable with Consumption Taxes

In addition to the goods and services that are currently taxed with the general consumption tax (restaurant services, bar, grills, pubs), the 2016 Tax Reform Act taxes with consumption tax (not creditable): (i) franchised restaurant sales, at the general 8% rate; and (ii) mobile internet services provided by the carriers at a reduced 4% rate. This is on top of the already existing 4% for the telephone service component of the mobile plans.

5.4. Income Tax Deduction of VAT paid in the Acquisition or Import of Capital Assets

The 2016 Tax Reform Act states that as of fiscal year 2017 taxpayers can deduct 100% of the VAT paid in the acquisition/import of capital assets. This implies the possibility to deduct in the first year the VAT paid, instead of recovering it via

depreciation throughout the lifespan of the asset. However, this change in the regulation does not imply a full credit; it is worth highlighting that in accordance with the Andean Pact Directives Colombia should be offering taxpayers a full credit, however, under the current regulation this commitment is not being fulfilled.

The deduction of the paid VAT will only be allowed on the CIT return of the year in which the capital asset is imported or acquired, and cannot be concurrently applied in the import of heavy machinery for basic industries since an independent, yet similar treatment is available.

5.5. Payment and Filing

Under the previous regulation, Colombian VAT is paid bimonthly, every four months or annually depending on the taxpayer's gross income from the previous year. The 2016 Tax Reform Act eliminates the annual filing and payment, leaving only two groups of taxpayers: those who should file and pay bimonthly and those who should file and pay every four months.

6. Taxes on Capital:

6.1. Wealth Tax Unchanged

On December 2014 a Wealth Tax assessed on net-worth and applicable on companies from 2015 through 2017, and on individuals from 2015 through 2018 was approved.

The 2016 Tax Act does not create a new Wealth Tax, however it does not repeal the Wealth Tax introduced by the 2014 Tax Reform either and, therefore: (i) taxpayers still have to pay the corresponding tax for the pending years in which the Wealth Tax will be in force; and (ii) there is no certainty that the government will not propose a new Wealth Tax for companies in 2018 and/or for individuals in 2019.

Under previous regulation, there was no way of assessing a filling penalty applicable for foreign companies required to file a wealth tax return for fiscal years 2016, 2017 and 2018, because, in most cases, they had not filed a CIT return in the previous year (the penalty for not filing the wealth tax return was estimated over this basis). A new penalty for not filing the wealth return for foreign companies was introduced. The penalty is 160% of the tax due, determined by the Tax Service according to the net equity reported in the last CIT return or determined by the Tax Service for such period by other means.

Nevertheless, there are important inquires in connection to (i) if this new penalty could be imposed for fiscal years 2016 and 2017 or if the previous regime shall apply to these years, and (ii) if according to this provision when the tax due is $0, then the minimum penalty should apply.

6.2. Alternate Minimum Taxable Income

As part of the corporate income tax assessment process taxpayers have to calculate their taxable income using two different methods. The regular method is based on income and the alternate method is based on capital. If the result of applying the alternate method is greater than the result of applying the regular method the taxpayer should continue the assessment process using the alternate minimum taxable income.

Under previous regulation the alternate minimum taxable income was equal to the taxpayer's net-worth as of December 31st of the year immediately preceding the taxable year multiplied by 3%. The 2016 Tax Reform Act increased this percentage to 3,5%.

6.3. Normalization Tax

The 2016 Tax Reform Act did not extend the temporary normalization tax created by the 2014 Tax Reform Act for the years 2015 to 2017.

Therefore, the last opportunity for taxpayers to report non-reported assets is filing and paying the normalization tax with their 2017 wealth tax return (in May).

7. Bank Debits Tax

Currently Colombia has in place a bank debits tax. This tax is withheld by the financial authorities and has a taxable base of 4 per thousand applicable on any withdraw or transfer made from savings and/or checking accounts. Very few exceptions regarding this tax exist.

According to the 2014 Tax Reform Act, a sunset on the Bank Debits Tax was supposed to happen, decreasing gradually the rates as of 2019 and this tax was supposed to totally disappear as of 2022. However, the 2016 Tax Reform Act repeals the sunset of the tax, making it permanent, with a fix rate of 4 per thousand.

8. New Statute of Limitations

Through the 2016 Tax Reform Act, the statute of limitations that the Tax Service has to audit taxpayer's returns was modified. Prior to the 2016 Tax Reform Act, with only few exceptions, the Colombian Tax Service had a 2-year term to audit tax returns. The general statute of limitations was extended to a 3-year term. A special 6-year term statute of limitations for income tax returns of taxpayers obliged to comply with the transfer pricing regime was created.

The statute of limitations of tax returns that report tax losses or carry them forward was also extended. Formerly, the statute of limitations to audit these tax returns was 5 years and such term was extended to 6 years. Please bear in mind that the 6-year statute of limitations for tax returns reporting losses would be

extended for 3 additional years if the taxpayer offsets the tax losses during the last two years of the initial 6-year term.

It is important to highlight that under an alternative interpretation, which might be defended by the Tax Authorities, the statute of limitations for returns in which tax losses are reported could be of 12 years. This new rule lacks clarity and is extremely complex and could, therefore, be construed in different ways.

Please bear in mind that this is a selective summary, for informational purposes only, that focuses on certain topics of interest. Therefore, it is not intended to be a detailed and comprehensive dissertation of the topics discussed. It is advisable that our readers do not exclusively rely on this document and thoroughly review their queries, seeking qualified advice from professional tax attorneys duly admitted to the practice of law in Colombia.

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