

THE 2022 TAX REFORM (LAW 2277 OF 2022)

The latest tax reform was enacted on December 13th. Below, we present our general comments on some highlights of the reform. This document does not contain a summary or analysis of all the measures approved.

A. Modifications for individuals and families

1. Income Tax

- For Colombian tax residents, dividends will be taxed at the existing marginal rates of the income tax ranging from 0% to 39%, depending on the total amount of their net income. Additionally, a tax discount of 19% on the net income obtained from dividends is granted, so the effective rate applicable to dividends will be up to 20%. This measure eliminates the special rate for dividends that was 10%.
- The dividend decree will be withheld by the company at a rate of 15% (currently 10%) for resident individuals and 20% for non-residents. For resident individuals, this withholding will not be the final tax and can be credited in their income tax return.
- In addition, the distribution of dividends that were not taxed in the name of the company in favor of Colombian residents will be subject to a tax with an effective rate ranging between 35% and 48%.
- For non-resident individuals, the income tax rate will remain at 35%, the rate for capital gains will increase from 10% to 15%, and the rate for dividends will increase from 10% to 20%.
- The reform includes an express prohibition on deducting from the corporate income tax, certain payments associated with personal expenses of the partners that are not related to the company's income-producing activity. In addition, for the first time, it provides that these personal expenses made by companies, in addition to not being deductible, will be considered income for their shareholder beneficiaries, and therefore will be taxed at rates from 0% to 39% for those beneficiaries. This is an issue that deserves special attention as we believe it will have a great impact in the coming years.

- The exemption on income from labor payments for individuals will continue to be 25% of its total amount, with a limit that will decrease from approximately COP 10,000,000 per month to approximately COP 34,000,000 per year.

2. Wealth Tax

- The reform introduces a permanent wealth tax on (i) resident individuals with respect to their worldwide assets, (ii) non-resident individuals with respect to their assets held in Colombia, and (iii) certain foreign companies that have assets in Colombia other than certain types of investments with respect to their assets held in Colombia.
- The tax is generated on net assets equal to or greater than approximately COP 3,000,000,000. A marginal rate will be applied which will be calculated by imposing a rate of 0.5% for the part of the assets between approximately COP 3,000,000,000 and COP 5,000,000,000 and a rate of 1% on the amount exceeding COP 5,000,000,000. During the years 2023 to 2026, there will be an additional marginal rate of 1.5% for those assets exceeding approximately COP \$10,000,000,000. The tax will be generated annually, so the subjection to the tax and the applicable rate will be determined year by year.
- The value for purposes of this tax of shares in national companies that are not listed on the Stock Exchange must be calculated according to their updated fiscal cost from the year of acquisition with a limit of January 1, 2006. Only if the adjusted fiscal cost value is higher than the intrinsic value, the intrinsic value of the shares will be taken as the taxable base. This provision will not apply to shares in start-ups that meet requirements including their incorporation time, their vocation for innovation, and the amount of investments received.
- Assets held through trusts, private interest foundations, insurance with a material saving component, investment funds, or other fiduciary businesses in Colombia or abroad must be declared by the founder, constituent, or originator; or by the beneficiary, depending on the specific features of each vehicle.
- We draw attention to the fact that, under certain double taxation treaties "DTTs" signed by Colombia, assets held by tax residents in certain jurisdictions with DTT's with Colombia will have limitations on being taxed by this proposed tax. This should be reviewed for each specific case.

3. SIMPLE Regime

- Some of the rates of the SIMPLE Regime will decrease from 2023, except for those applicable to professional, consulting, and scientific services (including liberal professions).

- Although it is still necessary to obtain annual gross income of less than 100,000 UVT (approximately COP 4,000,000,000) to be part of the SIMPLE Regime, the reform introduced a lower threshold of 12,000 UVT (approximately COP 509,000,000) for professional, consulting, and scientific services (including liberal professions).
- The first approximately COP 43,000,000 that a taxpayer receives monthly for retirement pensions obtained both in Colombia and abroad will also be exempt from Income Tax.

4. Stamp Tax

- The Stamp Tax on documents raised to public deed through which real estate or ships are sold whose value is equal to or greater than 42,000 UVT (approximately COP 850,000,000) is reintroduced. The tax will also be applied to the mortgage of these assets. The rate will be up to 3%, depending on the value of the document.

5. Modifications to the sanctions regime and tax crimes

- The crime of omitting assets or including nonexistent liabilities is modified to extend it to other declarations in addition to the income tax return and to decrease from 5,000 Minimum Monthly Wage "MMW" to 1,000 MMW the value of the assets or liabilities from which the crime is configured.
- The amount from which the crime of fraud or tax evasion is configured, applicable to the omission of income, or inclusion of nonexistent costs or expenses, or claim of improper tax credits, withholdings, or advance payments, is decreased from 250 MMW to 100 MMW.
- For these two crimes, it is established that the taxpayer can only extinguish the criminal action with the correction of the corresponding declaration and payment up to two times.

B. Modifications for business taxation

1. Income Tax

- The reform does not modify the general rate of corporate income tax (35%), but does increase the rate of capital gains for national and foreign entities from 10% to 15%.
- Between 2023 and 2027, some financial entities will be subject to a surcharge on the income tax of 5%. Entities subject to this surcharge include financial institutions, insurance and reinsurance entities, stockbrokerage firms, agricultural brokerage firms, agricultural and agroindustrial commodity exchanges, and providers of stock market infrastructure that have a taxable income greater than approximately COP 5,000,000,000.

- A permanent surcharge on the income tax will be applicable to entities that carry out extractive activities such as (i) coal extraction; (ii) lignite coal extraction; and (iii) crude oil extraction. The surcharge could be up to 15% depending on the specific activity and the average price of the extracted resource.
- Between 2023 and 2026, taxpayers whose main activity is the generation of electricity through water resources will be subject to a surcharge on the income tax of 3%.
- A minimum effective tax rate of 15% applicable to income tax taxpayers, except for foreign legal entities without residence in Colombia, is established, and will be the result of dividing the Total Net Tax by Total Net Profit. We would like to draw attention to the fact that this measure does not apply, among others, to companies exclusively dedicated to book publishing, companies providing hotel services, or ecotourism theme parks. To the extent that dividends, among others, are excluded from the equation, this does not affect holding companies in principle either.
- The reform increases the tax rate on dividends paid by Colombian companies to foreign entities from 10% to 20%. This tax rate may be reduced if the effective beneficiary of the dividends is an entity located in a jurisdiction with which Colombia has a Double Taxation Treaty in force. For more information on the network of DTTs signed by Colombia, we recommend consulting our Tax Overview 2022 ([click](#)).
- The withholding tax rate applicable to dividends distributed among national companies will increase from 7.5% to 10%.

2. Modifications to tax benefits

- The reform also eliminates some tax benefits for investments in hydrocarbons and mining, such as the ability to amortize investments in the exploration, development, and construction of mines and oil and gas deposits over 5 years, and the incentive for investments in hydrocarbons and mining (CERT reimbursement certificate).
- Other benefits that are eliminated include (i) the deduction of contributions to mutual investment funds; (ii) the deduction for donations and investments in research, development, and innovation; (iii) some incentives for the orange economy; and (vi) the mega investments regime, among others.
- The 50% discount on the Industry and Commerce Tax is also eliminated, which will become deductible. The deduction of royalties paid for the exploitation of non-renewable resources is prohibited.

- Some specific tax incentives are limited to 3% of the taxpayer's annual net income. Among the limited benefits, we highlight: (i) the discount for investments in environmental projects; (ii) the exemption of profits distributed to workers through shares; (iii) the deductions provided for employee education; (iv) the deduction for investments in infrastructure for public performances; and (v) the discount for donations to non-profit entities.
- The reform also contains a clause on acquired rights that seeks to guarantee to taxpayers who have met the conditions to access the tax benefits repealed or limited by the entry into force of the tax reform, the possibility of maintaining them during the term for which they were initially provided under the legislation that created them. The scope of this provision must be analyzed with respect to each specific case in order to determine whether the benefits enjoyed by a taxpayer are consolidated in their favor.

3. Modification to the Free Trade Zone regime

- From 2024, in order to maintain the preferential rate of 20%, industrial users of Free Trade Zones will have to obtain approval for a "Plan for Internationalization and Annual Sales." In any case, net income from income other than the export of goods and services will be taxed at the general rate of 35%.

4. Significant Economic Presence (SEP)

- In order to be able to tax the profits of foreign companies that, despite not having a physical presence in the country, do have a connection to the country through their digital presence or by taking advantage of the Colombian market, the reform introduced the concept of Significant Economic Presence (SEP).
- According to this new concept, from January 1, 2024, foreign companies that maintain a deliberate and systematic interaction with users or customers in Colombia will be taxed on the income received from the sale of goods or the provision of services to customers or users located in national territory.
- In the case of the sale of goods, a SEP is deemed to exist when the following conditions are met: (i) the acquisition of gross annual income equal to or greater than approximately COP 1,300,000,000, derived from transactions with people located in Colombia; and (ii) interaction with more than 300,000 Colombian users during the taxable year, or the display or payment of the previous ones in Colombian pesos is allowed.
- In the case of the provision of services, those who provide, among others, the following services will be subject to tax without the need to meet additional requirements to those indicated in the previous point: (i) mobile applications; (ii) e-books; (iii) online intermediation platform services; and (iv) digital subscriptions to audiovisual media.

- Foreign companies with SEP in Colombia may choose to pay income tax at a rate of 3% on the total gross income derived from the sale of goods and/or digital services from abroad, sold or provided to users in Colombia. When this mechanism is chosen, it will be possible to request the non-application of the applicable withholding tax. Otherwise, a withholding tax of 10% must be applied and the withholding agents will be, among others, credit card issuers.
- It is advisable to evaluate, in specific cases, the interaction between this rule and the provisions of the DTTs subscribed by Colombia.

5. Definition of Place of Effective Management

- Foreign companies with its Place of Effective Management ("PoEM") in Colombia are considered Colombian companies for income tax purposes.
- The reform modifies the definition of PoEM by eliminating the reference to the place where the "senior management" carries out its activities and emphasizes the place where the entity's daily activities are carried out.
- We recommend that foreign entities whose management may be understood to be carried out in Colombia verify their corporate governance regime in order to analyze their exposure to configuring a PoEM in Colombia. It is worth highlighting that the tax effects of the eventual double residence of a foreign entity for having its PoEM in Colombia can be mitigated if this entity is constituted or resident in one of the countries with which Colombia has signed DTTs, a situation that must be analyzed for each specific case.

6. Other measures

- The reform also includes new taxes that aim to discourage the consumption of sugary drinks and ultra-processed foods, as well as a new tax on the consumption of single-use plastics. In this regards, it modifies the existing carbon tax provisions in different aspects including the non-causation of this tax on the exports of fuels only when the producer exports it directly.
- A provision is added that provides that payments from customers to payment platforms and from these to businesses constitute a single operation that must be taxed only once with VAT.
- Payments made to individuals who are not VAT responsible through transfers or wires through payment service providers may no longer be subject to income tax withholding.
- A 50% reduction in the rate of default interest is established for tax and customs obligations that are fully paid until June 30, 2023 and for payment facilities that are signed before that date.

- The reform includes a temporary 60% reduction in the sanction and interest rate for those who have not filed tax returns and are required to do so before December 31, 2022. This benefit will apply to taxpayers who file the corresponding returns before May 31, 2023.
- A maximum cap is set for penalties related to the failure to send information of up to approximately COP 318,000,000.
- A temporary 60% reduction in the sanctions and interests applicable to omissive taxpayers who have not filed their tax returns by December 31, 2022 is established.

C.

Aspects not included

- Unlike the last 4 tax reforms, this one did not include a new Normalization Tax.
- In contrast to the last tax reform bills, this one does not provide for terminations by mutual agreement of tax processes, nor does it provide for audit benefits.
- This reform does not include the determination of taxable net income through the presumptive income system.

If you have questions about these topics, you can contact: Federico Lewin flewin@lewinywills.com; Juan Andrés Palacios jpalacios@lewinywills.com.