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Corporate Tax 2023

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Colombia: Law & Practice

Federico Lewin and Juan Andrés Palacios
Lewin & Wills

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COLOMBIA

Law and Practice

Contributed by:
Federico Lewin and Juan Andrés Palacios
Lewin & Wills **see p.17**

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1. Types of Business Entities, Their Residence and Basic Tax Treatment

1.1 Corporate Structures and Tax Treatment

Corporate Structures and Tax Treatment

Businesses generally adopt a corporate form in Colombia. Colombian commercial legislation currently establishes different types of legal entities and classifies them into general partnerships (*sociedades de personas*) and capital companies (*sociedades de capital*). The main difference between the types of legal entities in Colombia is the requirements and procedures that must be fulfilled to incorporate each type of corporation, with certain restrictions for some types – eg, only *sociedad anónima* (SA) companies can be offered in stock exchange markets.

Partnerships are conceived as closed legal entities, where the intuito personae element is the most important. In addition, in these types of companies the management is assumed jointly and directly by the partners, whose liability to third parties is subsidiary.

In contrast, in capital companies the administration is often delegated to a board of directors. In addition, the associates or shareholders are released from any direct liability to third parties, so creditors cannot pursue their personal assets. Nonetheless, the corporate veil may be pierced under certain circumstances (eg, tax abuse, fraud against the law or the detriment of third parties).

In general, legal entities are taxed as separate entities from their shareholders.

In some particular cases, foreign entities opt to operate in Colombia through branches. In this scenario, branches are taxed in Colombia over their attributable income.

Reasons for the Adoption of a Corporate Form in Colombia

The corporate form most frequently used in Colombia is the simplified joint stock company (*sociedad por acciones simplificada* or SAS), which is a capital company that allows shareholders to:

- incorporate the entity in an expeditious manner – the SAS can be incorporated by private document without the need to notarise the act by public deed;
- limit their liability – the liability of the partners and shareholders in an SAS is limited to their contributions;
- set the rules that will govern the operation of the company with flexibility; and
- defer the payment of capital contributions for up to two years.

1.2 Transparent Entities

As a general rule, all entities are considered independent corporate income taxpayers, so the income obtained is not attributed to their members, partners, shareholders or beneficiaries. As an exception, the Colombian CFC regime (*régimen ECE*) treats passive income derived by foreign companies controlled by Colombian residents as transparent.

There are specific transparent entities arrangements that are commonly used in the construction sector and for the development of infrastructure projects, such as:

- *fideicomisos* (fiduciary arrangements); and
- *contratos de colaboración empresarial*, *consorcios* and *uniones temporales* (joint ventures or JVs).

These are not regarded as corporate income taxpayers, and the partners, participants and/or beneficiaries are obliged to report income derived by the entities under certain specific rules, depending on the kind of JV or arrangement.

Private equity funds and collective funds are also transparent for Colombian tax purposes. If certain requirements are fulfilled, the beneficiaries of the funds can defer their income to the moment when the profits are distributed.

Generally, Colombia's biggest financial investors are retirement funds that invest through private equities and other types of funds, which are transparent for tax purposes.

1.3 Determining Residence of Incorporated Businesses

Colombian rules for the determination of the tax residence of legal entities follow OECD standards. Corporations and legal entities are deemed resident for Colombia tax purposes when:

- they have been incorporated in Colombia;
- they have their principal domicile in Colombia; or
- their place of effective management is located in Colombia.

Cases of dual tax residence of incorporated businesses can be solved whenever a tax treaty concluded by Colombia is applicable.

1.4 Tax Rates

Corporate Rates

The general statutory Corporate Income Tax (CIT) rate applicable to Colombian companies and to foreign corporate entities receiving Colombian source income, regardless of whether or not it is attributable to a permanent establishment in Colombia, is 35%. From 2023, a 15% minimum tax is also applicable to Colombian companies.

A reduced 20% CIT rate is applicable to eligible companies in free trade zones, and a special 15% CIT rate is applicable to certain activities, such as hotel services, tourism services and book publishing.

From 2023 to 2027, a 5% surcharge is levied on financial entities, insurance companies and stockbrokers with a taxable income equal to COP508 million (approximately). Non-renewable extractive industries are subject to a surcharge of up to 15%, depending on the price of the commodities. From 2023 to 2026, hydroelectric power generators are subject to a 3% surcharge.

Individual Rates

Resident individuals doing businesses directly or through transparent entities are subject to income tax at progressive marginal rates of up to 39%; non-resident individuals are subject to a 35% flat rate. However, compared to companies, individuals doing business directly have limited deductions (depreciation, amortisation, etc) so their taxable bases are usually higher.

Simple Tax Regime

Small and medium-sized enterprises with an annual turnover of (approximately) COP4.2 million maximum can be eligible for the simple tax regime, which replaces CIT, local turnover tax and consumption tax. The simple tax establishes fixed rates applicable to the gross income, which vary depending on the economic sector and the annual gross income, and may range between 1.2% and 8.3%. Both incorporated and unincorporated businesses can opt-in to this regime.

2. Key General Features of the Tax Regime Applicable to Incorporated Businesses

2.1 Calculation for Taxable Profits

In general terms, taxable profits are calculated based on the accounting profits, based on the financial information deriving from the accounting records kept in accordance with International Financial Reporting Standards (IFRS). Adjustments should be made to avoid the taxpayer being obliged to pay tax on theoretical income or being allowed to deduct theoretical expenses. Other adjustments include items of exempted and untaxable income, statutory allowances such as depreciation and amortisation (among other fiscal incentives), transfer pricing limitations, thin capitalisation restrictions and certain other limitations on the deductions of expenses incurred abroad.

Taxable profits for corporations are calculated on an accrual basis, whereas taxable profits for individuals are generally calculated on a receipt basis.

The taxable profits of incorporated businesses are calculated as follows: gross income–excluded items of income = gross taxable income; gross taxable income–allowed reductions = net taxable income.

2.2 Special Incentives for Technology Investments

Research and Technological Investment Special Deduction and Tax credit

Taxpayers are granted an income tax credit equivalent to 30% of the amount invested in research, technological development and innovation projects approved by the government.

Until 2022, taxpayers were also allowed to deduct their investments in research and technological projects, but this incentive was abolished by the 2022 tax reform.

Selected VAT Incentives

The equipment imported by research or technological development centres recognised by Colciencias (the National Department of Science, Technology and Innovation) and by institutions of basic primary, secondary, middle or higher education recognised by the Colombian Ministry of Education, which is intended for the development of scientific, technological or innovation projects according to the criteria and conditions defined by the National Council of Tax Benefits in Science, Technology and Innovation, is exempt from VAT.

2.3 Other Special Incentives

Certain Exempt Items of Income

Subject to eligibility and compliance with the statutory requirements by the taxpayer, available CIT exemptions include a 15-year exemption on income from power-generation activities based on wind, biomass and agricultural waste technologies, and on certain types of income related to projects for the construction of social interest and priority interest housing.

The 2022 tax reform abolished CIT exemptions, including a five-year income tax exemption for “orange” businesses (ie, those developing creative and technological value-added industries) and a ten-year exemption for income derived from investments that increase productivity in the agricultural sector.

Mega Investments Regime

For a term of 20 years, mega investments that generate at least 400 direct workplaces and make new investments of at least COP1.14 bil-

lion can benefit from a reduced 27% CIT rate and a reduced two-year depreciation term, among other benefits. This beneficial treatment is applicable to investments that were approved by the Ministry of Commerce before the end of 2022. Investments related to the evaluation and exploration of non-renewable natural resources are not eligible for this regime.

Selected VAT Incentives

The Colombian legal framework provides for several VAT incentives that are applicable to specific industry sectors, such as:

- VAT exemption on the temporary importation of "heavy" machinery and equipment not produced in Colombia and effectively used in a "basic industry" in Colombia;
- VAT exemption on certain services (not all) rendered in Colombia or abroad, as well as the purchase of certain goods, equipment and merchandise, related to investment and pre-investment in projects aimed at the generation or utilisation of renewable energy;
- VAT exclusion on imported machinery and equipment not produced in Colombia used in the treatment of atmospheric emissions; and
- VAT exclusion on the sale of machinery and equipment for the development of projects or activities that are registered in the National Registry for the Reduction of Greenhouse Gas Emissions (RENARE).

2.4 Basic Rules on Loss Relief

From 2017 onwards, the tax loss carry-forward is limited to the 12 fiscal years following the year in which the tax loss is accrued.

Tax loss carry-back is not available.

The cross-offsetting of regular tax losses against capital gains and vice versa is not possible.

Tax losses are not transferrable to share or quota holders, nor to other taxpayers, except as provided for reorganisations.

2.5 Imposed Limits on Deduction of Interest

As a general rule, interest paid is deductible if it is related, proportional and necessary to the taxpayer's income-producing activity. A thin capitalisation set of rules is enforced, under which only interest derived from indebtedness between related parties with an average value not exceeding two times the entity's net equity is deductible. This limitation does not apply to cases when the debtor is a financial entity or when the loan is obtained in order to finance infrastructure projects related to activities that are considered to be of public interest.

2.6 Basic Rules on Consolidated Tax Grouping

Group taxation or group consolidation is not permitted for the purposes of CIT. Therefore, the usage of tax losses from a company that is part of a group can only be done through a reorganisation process (usually M&A). However, this usually represents a haircut over the losses that can be used.

2.7 Capital Gains Taxation

Starting in 2023, corporations are taxed on capital gains at a general statutory rate of 15% (previously 10%).

The costs related to such gains can be offset.

Short-term capital gains (assets held for less than two years) are deemed a regular item of income subject to income tax.

Certain adjustments to the costs can be made as a relief, and certain capital gains may not be

taxable (eg, gains from the sale of shares of listed corporations). The sale of shares in Colombian holding companies (CHC) is exempted from capital gains, as is the sale of shares of foreign companies by a CHC.

2.8 Other Taxes Payable by an Incorporated Business

In addition to CIT, there are other taxes payable by incorporated businesses on transactions, as explained below.

VAT

The sale and importation of movable tangible property, the sale and licensing of intangible assets associated with industrial property (eg, trade marks, industrial designs and patents for inventions) and the provision of services in Colombia or from abroad are subject to VAT. As a general rule, the sale of fixed assets does not levy VAT. Certain public entities on a national and local territorial level are not subject to VAT.

The general rate of VAT is 19%. A reduced 5% rate applies for certain goods and services.

A reverse charge applies for most services provided to a Colombian party from abroad, so it is the Colombian party that is obliged to perform VAT back-up withholdings and pay 100% of the accrued VAT directly to the tax authorities.

Certain goods and services are exempted (zero-rated with the right to credit paid VAT and ask for a refund) or are not taxable with VAT ("excluded").

Consumption Tax

Certain economic activities are subject to a non-creditable consumption tax at a general statutory rate of 8%, and not to VAT.

Services taxed at the general 8% consumption tax rate include restaurant services, bars, grills, pubs and franchised restaurant sales. Franchisees opting out of consumption tax will be subject to VAT.

Mobile internet services provided by the carriers are subject to consumption tax at a reduced rate of 4%.

Bank Debits Tax

The bank debits tax levies any withdrawal or transfer of funds from a bank account at a rate of 0.4%. Colombian banks (and other savings institutions) must withhold the tax at source. There are very limited exemptions to this tax.

Local Turnover Tax on Industrial, Commercial and Service Activities

This is a municipal (local) level tax applicable to income deriving from all industrial, commercial and services activities performed in the territory of a district or municipality. The taxable base is the sum of the taxpayer's gross revenue from the activity carried out in the relevant municipality. The tax rates vary from one district or municipality to the next, and range from 0.2% to 1.38%. This tax is usually paid and a return is filed annually, with the exception of some municipalities that have adopted a two-month taxable period (eg, Bogotá). Incentives for this tax are created and regulated by each district or municipality.

2.9 Incorporated Businesses and Notable Taxes

Property Taxes

There are municipal (local) level taxes on real estate and vehicles. Each district or municipality adopts the applicable tax rates, so they vary from one municipality to the next. Real estate tax rates usually range between 0.5% and 1.6%, although certain exceptions may apply. Motor

vehicles tax rates range between 1.5% and 3.5%.

Registration Taxes

This tax applies to taxpayers registering acts and documents with the cadastral registry or merchants' registry offices. Depending on the type of act or document, the tax rate ranges from 0.5% to 1% when the registration is with the cadastral registry office, and from 0.1% to 0.7% when the registration is with the merchants' registry office.

National Stamp Tax

The 2022 tax reform reintroduced a national stamp tax levied on public deeds for the transfer of immovable property with a price of more than (approximately) COP848 million. A progressive tax rate of up to 3% is applicable, depending on the price of the sale of the property.

Local Stamp Taxes

Certain laws authorise departments to enact local stamp taxes to support investments in hospitals, universities and other public entities and activities. Such local stamp taxes are usually levied at a rate of 1% on the gross income attached to the taxable event.

3. Division of Tax Base Between Corporations and Non-corporate Businesses

3.1 Closely Held Local Businesses

Most closely held local businesses operate in a corporate form.

3.2 Individual Rates and Corporate Rates

While the CIT rate is flat (35%) and distributions are taxed with dividend tax, individual income tax rates vary from 0% to 39%, depending on the annual income, but with severely limited deductions. Individual income over around COP50 million a month is taxed at a marginal tax rate that may oscillate from 35% to 39% (ie, a greater tax burden than corporate taxation).

In spite of the distortions created by the two regimes, the Colombian legal system does not contemplate specific mechanisms to prevent the situation whereby individual professionals earn income through companies.

3.3 Accumulating Earnings for Investment Purposes

As a general rule, the Colombian tax system does not differentiate between active and passive income, and does not contain mechanisms to prevent closely held legal entities from accumulating earnings for investment purposes. However, the Colombian CFC regime (*régimen ECE*), which is applicable to foreign companies controlled by Colombian tax residents, taxes passive income derived by the controlled foreign company as if it was directly derived by the Colombian tax resident, preventing the tax deferral in Colombia.

3.4 Sales of Shares by Individuals in Closely Held Corporations

Dividends Tax

Starting in 2023, dividends distributed to residents are subject to dividends tax at an effective rate of up to 20%, depending on the annual income of the individual. The previous applicable rate was 10%.

Dividends paid out of profits that were not taxed at the corporate level are subject to dividends tax, at a rate that recaptures the tax not paid at the corporate level plus the dividends tax rate.

Capital Gains Tax

The sale of shares in closely held legal entities is taxed in the same manner as all other companies. Therefore, if shares were held for a period of two years or more, a 15% capital gains tax is accrued. The applicable tax rate was 10% until 2022.

On the contrary, if shares were held for a period of less than two years, income derived therefrom will be taxed at the general income tax rate applicable to individuals (marginal rates oscillate between 0% and 39%).

3.5 Sales of Shares by Individuals in Publicly Traded Corporations

Dividends Tax

Individuals are taxed on dividends distributed by publicly traded corporations in the same way that they would be taxed if the dividend was paid by a closely held company.

Capital Gains Tax

The sale of shares of publicly held companies registered in the Colombian stock exchange is not taxable, provided that the sale does not exceed 10% of the outstanding shares of the company.

4. Key Features of Taxation of Inbound Investments

4.1 Withholding Taxes

When Colombian-sourced income is remitted abroad to a beneficiary that is a non-resident individual or entity, the payment should be subject to a withholding tax. The applicable rates for interest, dividends and royalties are as follows:

- interest – 20%, unless the term of the agreement is longer than a year, in which case the rate is 15%;
- dividends – 10% if profits were taxed at the corporate level, and 41.5% withholding if profits were untaxed at the corporate level; and
- royalties – 20%.

Double tax treaties (DTTs) generally bring reliefs to the above treatment.

Considering that technical services rendered from abroad are subject to a 20% withholding tax as they produce Colombian-sourced income, the tax authorities tend to discuss the nature of services rendered to Colombian taxpayers in order to determine whether a withholding tax is mandatory in these cases.

4.2 Primary Tax Treaty Countries

Colombia's belated development of a network of OECD-like treaties has led to the execution of income tax treaties with:

- most countries of Western Europe, with the notable exception of Germany (UK, Spain, France, Italy, Switzerland, the Netherlands, Portugal, the Czech Republic and Luxembourg);
- some Latin American countries (such as Brazil, Chile, Mexico and Uruguay); and
- other countries around the globe (Canada, India, South Korea, Japan and the United Arab Emirates).

All these treaties are already enforceable, except those with Brazil, the Netherlands, Luxembourg, Uruguay, the United Arab Emirates and Japan.

Colombia is also a member of the Andean Pact, so benefits from the Andean Pact Tax Directive

578 to avoid double income taxation, enacted in 2004. With isolated exceptions, this Tax Directive provides for exclusive source taxation among member countries (Colombia, Peru, Ecuador and Bolivia).

The treaty employed is determined according to the fiscal residence and main place of business of the respective parties of the operation (OECD-like tax treaties) or to the origin of the investment resources (Andean Pact Tax Directive 578/2004), which should be studied on a case-by-case basis.

Foreign investors often seek to invest in local companies through debt instruments rather than stock.

4.3 Use of Treaty Country Entities by Non-treaty Country Residents

In spite of the fact that Colombia has a set of tax provisions to challenge the use of treaty country entities by non-treaty country residents (such as the domestic GAAR and the MLI, which limit treaty shopping), there is currently no substantial precedent of local tax authorities challenging such use of treaties.

4.4 Transfer Pricing Issues

In general terms, the biggest transfer pricing issues presented for inbound investors operating through a local corporation are those regarding services and royalties derived from rights of use and the exploitation of intangible assets paid to parent legal entities and foreign affiliates.

Transfer pricing disputes have recently arisen relating to medium-range adjustments made by Colombian taxpayers for services rendered by related parties abroad and the comparability analysis.

4.5 Related-Party Limited Risk Distribution Arrangements

At present, the Colombian tax authorities do not challenge related-party limited risk distribution agreements for the sale of goods or the provision of services locally. In fact, the Colombian tax system does not have specific provisions to challenge limited risk distributions arrangements locally. However, the use of such arrangements could be challenged using the domestic GAAR.

4.6 Comparing Local Transfer Pricing Rules and/or Enforcement and OECD Standards

Colombia's transfer pricing rules do not vary significantly from the OECD set of rules.

4.7 International Transfer Pricing Disputes

International transfer pricing disputes are not frequently resolved through DTTs and mutual agreement procedures (MAPs). In fact, very few cases have been subject to the MAP process.

Currently, the DIAN (the National Directorate of Taxes and Customs) supports the use of the MAP process and in 2020 issued the first provisions to establish a proceeding to request assistance from the DIAN in relation to a MAP. However, it requires taxpayers to withdraw domestic administrative and judicial remedies to solve MAP cases. It also stops MAP discussions if the taxpayer does not reimburse extraordinary expenses during the process.

5. Key Features of Taxation of Non-local Corporations

5.1 Compensating Adjustments When Transfer Pricing Claims Are Settled

Adjustments should be made if a difference with comparables must be amended. Decisions issued under the MAP are mandatory.

5.2 Taxation Differences Between Local Branches and Local Subsidiaries of Non-local Corporations

While local branches of foreign corporations are taxed on their attributable income, local subsidiaries are taxed on their global-sourced income.

From 2020, permanent establishments including branches of foreign companies shall be taxed on their attributable income, regardless of whether such income is sourced in Colombia or abroad.

5.3 Capital Gains of Non-residents

Non-residents' capital gains on the sale of shares in local companies are subject to capital gains tax in Colombia.

Indirect sales or transfers in any form of shares in local companies through the sale of shares of foreign companies are also subject to tax in Colombia, as if the sale of the underlying asset had been done directly.

Certain DTTs limit the capital gains for non-residents selling stocks of a Colombian company, subject to conditions.

5.4 Change of Control Provisions

There are currently no change of control provisions that could apply to trigger tax or duty charges in Colombia.

5.5 Formulas Used to Determine Income of Foreign-Owned Local Affiliates

Formulas are not used to determine the income of foreign-owned local affiliates selling goods or providing services.

5.6 Deductions for Payments by Local Affiliates

The deduction of payments by local affiliates for management and administrative expenses incurred by a non-local affiliate is permitted, given the corresponding income tax withholding is applied over the gross payment. The transaction must comply with the arm's-length principle and the overall transfer pricing regime.

5.7 Constraints on Related-Party Borrowing

Related-party borrowing by foreign-owned local affiliates paid to non-local affiliates must comply with the thin capitalisation provisions, as stated in **2.5 Imposed Limits on Deduction of Interest**.

6. Key Features of Taxation of Foreign Income of Local Corporations

6.1 Foreign Income of Local Corporations

The foreign income of local legal entities is taxed. A foreign tax credit is applicable to taxes paid abroad on non-Colombian-sourced income, provided that the amount to be credited does not exceed the CIT liability in Colombia.

Income tax treaties signed by Colombia contemplate additional tax credit provisions.

6.2 Non-deductible Local Expenses

As a general rule, foreign income is not exempt. Local expenses are deductible if they are relat-

ed, proportional and necessary to the taxpayer's income producing activity.

In the very few cases where foreign income is exempt (not because of its source but because of other tax benefits), attributable expenses are not deductible.

6.3 Taxation on Dividends From Foreign Subsidiaries

Dividends distributed to local legal entities from foreign subsidiaries are deemed to be a regular item of income subject to income tax. However, direct and indirect foreign tax credits are available, and certain DTTs may restrict Colombia's taxation of such dividends.

In exceptional cases, dividend distributions from foreign companies to CHCs are exempted, provided that the income out of which the dividends were distributed is attributable to activities carried out by foreign entities and that certain other requirements are met.

6.4 Use of Intangibles by Non-local Subsidiaries

Local transfer pricing rules oblige the Colombian company and owner of the intangible to determine an arm's-length remuneration for income tax purposes.

6.5 Taxation of Income of Non-local Subsidiaries Under Controlled Foreign Corporation-Type Rules

Local legal entities can be taxed on the income of their non-local subsidiaries under the Colombia CFC rules. Therefore, income, costs and deductions relating to passive income obtained by the CFC (non-local corporation) are deemed to be accrued at the level of the local corporation that directly or indirectly controls the non-local subsidiary, in the same taxable year in which such income, costs and deductions accrued in the CFC. Income received by non-local branches of local legal entities is also taxed under these regulations.

6.6 Rules Related to the Substance of Non-local Affiliates

Non-local affiliates are deemed to be national tax residents if their effective seat of management is located in Colombia.

The passive income of controlled foreign companies is taxable in Colombia as if it was directly derived from the Colombian tax resident.

Payments made to beneficiaries located in tax havens are subject to an increased withholding tax.

6.7 Taxation on Gain on the Sale of Shares in Non-local Affiliates

Gains on the sale of shares in non-local affiliates by local corporations are taxed as foreign-sourced income taxable in Colombia, but benefit from foreign tax credits and limitations set by DTTs.

Gains on the sale of shares in non-local affiliates by CHC are exempted.

7. Anti-avoidance

7.1 Overarching Anti-avoidance Provisions

Colombia enforces a GAAR that allows the tax administration to recharacterise, for tax purposes, transactions that lack an apparent economic or commercial purpose and are carried out to obtain a tax benefit.

8. Audit Cycles

8.1 Regular Routine Audit Cycle

The only routine audits made in Colombia are those conducted by the administration when a taxpayer requests tax refunds. Audits are usually triggered by mismatches between the information reported by third parties and the figures reported by the taxpayer, or by audit programmes implemented by the tax authority based on data that evidences repetitive tax inconsistencies on one issue.

9. BEPS

9.1 Recommended Changes

Mainly due to its process of accession to the OECD, Colombia has taken an active role in implementing several BEPS Actions. The following measures were adopted in accordance with the BEPS Actions:

- BEPS Action 3 – CFC regime and norms regarding international tax transparency (including the declaration of assets held abroad and the regularisation of tax rules);
- BEPS Action 4 – thin capitalisation rules;
- BEPS Action 6 – GAAR rules and anti-abuse provisions in some tax treaties signed by Colombia, and beneficial ownership rules;
- BEPS Action 7 – permanent establishment legal framework;
- BEPS Actions 8–11 – transfer pricing rules (regarding commodity transactions, country-by-country reports, preferential tax regimes, tax havens and intangibles) and corporate restructuring rules;
- BEPS Action 13 – country-by-country reporting and transfer pricing regime documentation; and
- BEPS Action 14 – MAPs.

9.2 Government Attitudes

Colombia has played an active role in the implementation of BEPS. So far, it has sought to be perceived as a country that is interested in following the OECD recommendations in several fields, including tax matters. The 2022 tax reform implemented provisions that somehow reflect the current global discussions related to Pillar 1 and Pillar 2, although there is not yet any intention to implement both pillars.

On the one hand, a 15% minimum CIT is established for local companies. On the other hand, the concept of Significant Economic Presence has been introduced, seeking to tax foreign taxpayers that have a deliberate and systematic presence in the country or that render digital services to the Colombian market without a physical nexus with the country.

Both pillars are likely to be given effect in Colombia. Considering the thresholds for the application of Pillar 1, no Colombian business is likely to be affected by the new rules on nexus, and the tax revenue of the country can increase.

The implementation of Pillar 2 (global anti-base erosion – GloBE) should not have a major economic impact in Colombia. Considering that the country does not have a very large number of MNEs that meet the threshold for the application of the minimum tax under GloBE, the fiscal impact in Colombia would not be substantial. However, the Colombian MNEs that would be covered by this new provision would probably have to incur higher tax compliance costs.

9.3 Profile of International Tax

While taxation traditionally has a high public profile in Colombia, international tax has attracted substantial attention in recent years due to the expansion of the Colombia DTT network, the

adoption of BEPS actions and, in particular, the international exchange of information.

There is currently significant political consensus in Colombia on the convenience of following OECD policies, including international tax measures. Therefore, it is expected that most or all of the BEPS recommendations will continue to be implemented.

9.4 Competitive Tax Policy Objective

Colombia currently faces more pressures to raise revenue due to the increase in public spending caused by the pandemic than pressures to seek a competitive tax policy in terms of lowering the corporate tax burden. Therefore, there is currently very little incentive to boost tax competitiveness by disregarding BEPS recommendations.

One of the major problems of the Colombian tax system is tax evasion, which artificially reduces the number of taxpayers and elevates pressures on their tax burden. Therefore, a competitive tax policy is triggered partly by the implementation of efficient tax evasion rules that allow for the reduction of the effective tax burden for taxpayers. Fostering international tax transparency that allows local tax administrations to increase tax collection and fiscal resources may contribute to reducing the overall tax burden for taxpayers in the long run, balancing the pressures that BEPS will bring in its trail.

9.5 Features of the Competitive Tax System

The Colombian corporate tax system faces two problems that harm its competitiveness:

- the capacity to raise revenue relies disproportionately on corporate income tax; and
- several tax benefits lack coherency and justification, propitiating tax inefficiencies.

To enhance the tax system's efficiency, it is necessary for the tax authority to increase its capacity to audit individuals, so the system does not rely heavily on CIT. Regarding tax benefits, a special commission issued a Tax Expenditures Report in 2021. It is expected that the government and Congress will follow the recommendations of this commission.

9.6 Proposals for Dealing With Hybrid Instruments

BEPS Action 2, which seeks to neutralise the effects of hybrid mechanisms, has not yet been implemented in Colombia. There is no substantial progress on the discussions related to this matter. However, if the country starts to implement domestic provisions to adopt Action 2, it is foreseeable that one of the first measures to be implemented will be the limitation of the deduction of interest generated by operations that, due to a mismatch, are not taxable in another jurisdiction.

9.7 Territorial Tax Regime

The Colombian corporate tax regime taxes corporations on their worldwide income, while it relieves foreign-sourced income by providing a tax credit on taxes paid abroad associated with non-Colombian-sourced income.

Interest is deductible, if the corresponding withholding tax is made and with the limitations imposed by the thin capitalisation rule.

9.8 Controlled Foreign Corporation Proposals

The CFC regime implemented in Colombia is consistent with the taxation of Colombian residents on their worldwide income, as it is intend-

ed to make transparent the passive income derived by Colombian residents through CFCs.

9.9 Anti-avoidance Rules

DTT limitations of benefits (typically PPT) and general and targeted anti-avoidance rules are not likely to adversely impact inbound and outbound investments.

9.10 Transfer Pricing Changes

The 2016 tax reform introduced changes to the transfer pricing regime that are respondent to BEPS, but it did not radically alter the existing regime. The most notable changes are related to the introduction of new formal obligations, such as the country-by-country report.

BEPS recommendations related to the value creation and the method to determine the value of intangibles have not yet been adopted in the Colombian legislation, resulting in a source of potential controversy.

9.11 Transparency and Country-by-Country Reporting

The introduction of the country-by-country report enhances transparency and aligns Colombian reporting obligations with international standards.

9.12 Taxation of Digital Economy Businesses

Initially, Colombia did not adopt digital services taxes but reformed the VAT regime to tax services rendered from abroad, including digital services.

In 2021, the government proposed the implementation of a withholding tax on marketing and advertisement services that are rendered abroad but consumed in the local market. Although this proposal was not expressly directed at digital economy businesses, it would have affected internet platforms and other related services. However, the proposal was rejected.

The 2022 tax reform introduced the concept of "significant economic presence" (SEP) to the legislation, seeking to tax foreign enterprises that have deliberate and systematic interaction with the Colombian market or that provide digital services to clients in the country.

9.13 Digital Taxation

Although Colombia introduced the SEP concept into its legislation in 2022, the taxation of foreign enterprises with SEP in Colombia will not enter into force until 2024.

It is notable that the provisions that establish the SEP concept expressly state that the SEP legislation will cease to be applicable if an international agreement that prohibits this type of taxation is approved and signed by Colombia.

9.14 Taxation of Offshore IP

Royalty payments related to IP directed to non-Colombian tax residents are subject to a 20% income tax withholding. Special tax withholding rates may apply to outbound royalty payments on certain DTTs signed by Colombia. Royalty payments directed to a tax haven beneficiary, corresponding to items of income deemed from a Colombian source, are subject to withholding tax at a rate of 35%.

Lewin & Wills is a boutique firm with international reach and more than 40 years of experience in the Colombian market. The firm's corporate tax practice focuses on international and domestic transactions and tax litigation. Lewin & Wills is a member and founder of Lataxnet, a network that covers more than 17 jurisdictions in Latin America; it is also a member of WTS, a specialised tax global network. These alliances enable the firm to offer co-ordinated advice in multi-jurisdictional matters, and to keep its practice updated on trending international tax topics.

Authors

Federico Lewin is a partner at Lewin & Wills, whose practice focuses mainly on tax disputes, cross-border taxation and corporate tax law. He has an MSc in taxation from the University of Oxford and a Master of Law and Business from the Bucerius Law School.

Juan Andrés Palacios is a partner at Lewin & Wills, where he has worked for over a decade. His practice focuses on both domestic and international taxation. Juan also has broad experience in tax litigation before the Colombian tax courts in various tax-related matters, including transfer pricing controversies. He holds a postgraduate advanced taxation degree and an International Taxation LLM from King's College London.

Lewin & Wills

Calle 72A 4-03
Bogotá
Colombia

Tel: +57 601 312 5577
Fax: +57 601 2117626
Email: lyw@lewinywills.com
Web: www.lewinywills.com

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