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Global Tax Alert

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Colombia enacts new tax reform law

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Executive summary

On 27 December 2019, Colombia enacted a new tax reform (Law 2010, so-called Economic Growth Law). This tax reform replaces the 2018 tax reform (Law 1943), which was declared unconstitutional by the Constitutional Court due to procedural flaws but was allowed to be in force until the end of 2019 (see EY Global Tax Alert, [Colombian Constitutional Court declares the 2018 tax reform unconstitutional](#), dated 17 October 2019). The new tax reform will generally apply from 2020, keeping many of the provisions introduced by the 2018 tax reform (see EY Global Tax Alert, [Colombia enacts tax reform](#), dated 3 January 2019 for details about the 2018 reform). However, certain changes and new provisions were introduced during the legislative discussion and are outlined below.

Detailed discussion

Business taxation

The tax reform increases the dividend withholding tax rate applicable to foreign nonresidents (individuals and companies) from 7.5% to 10%. The tax reform reduces the presumptive income tax rate for 2020 from 1% to 0.5%. For 2021 and onward, the rate will be 0%. Presumptive income is an alternative taxable income based on a percentage of net equity as of December 31 of the preceding year.

The tax reform also reenacts the surtax applicable to financial institutions with taxable income exceeding approximately US\$1.2 million. The surtax will be (i) four percentage points for 2020 (for a total corporate income tax rate of 36%); and (ii) three percentage points for 2021 and 2022 (for total corporate income tax rates of 34% and 33%, respectively). The tax reform establishes an advance collection mechanism for the surtax to allow financial institutions to pay the surtax in advance. The advance payment is made on the tax return for the preceding year and calculated on the preceding year's income tax base.

Additionally, the tax reform clarifies the definition of effective beneficiary and establishes a registration requirement for effective, final or real beneficiaries.

For indirect transfers of Colombian assets, the tax reform establishes that the value paid in the acquisition of the shares of the foreign entity, which is attributed to the underlying Colombian assets, will be considered as tax basis in a subsequent indirect disposal. In addition, the tax reform clarifies that indirect transfers conducted through mergers or demergers between foreign companies will be subject to Article 319-8 of the Tax Code and, therefore, will be nontaxable, to the extent certain requirements are met.

In addition, the tax reform increases the number of jobs a company must create to qualify for mega investment benefits from 250 to 400. For investments in high technological industries, however, the tax reform maintains the employment requirement at 250. The tax reform also clarifies that mega investment projects may occur in free trade zones.

Additionally, the tax reform:

- ▶ Establishes a deduction equivalent to 120% of wages paid to employees under 28 years old who are being employed for the first time (monthly maximum deduction of approximately US\$1,250 per employee)
- ▶ Clarifies the income tax exemption for agricultural activities, such as the number of employees required based on the investment and income required, and the moment at which the company would have to be incorporated to access the benefit
- ▶ Modifies certain rules on extractive companies and ports so they may make in-kind tax payments (i.e., performing projects for the community in lieu of paying taxes), provided that, in these cases, the investments are not related to their income-generating activity

- ▶ Extends, until June 2021, the period for investment funds to adjust to the new requirements to apply the income-recognition deferral regime for their investors (under which investors would recognize income when the funds distribute profits)

Individual taxation

The tax reform decreases the dividend withholding tax rate applicable to individual residents from 15% to 10%. It also allows individuals to recognize the inflationary component of financial yields as non-taxed income.

Individuals who receive income from sources outside of their employment may reduce their taxable basis with costs and expenses related to their income-producing activities. In addition, the tax reform progressively reduces the health contributions made by certain low-income retirees.

Equity tax and normalization tax

The tax reform maintains the equity tax for 2020 and 2021 at a rate of 1%. For this tax to apply, the net equity of the taxpayer must be at least COP5,000 million (approximately US\$1.5 million) as of 1 January 2020. For nonresidents, the net equity only includes assets located in Colombia. For nonresident entities, the tax reform maintains that the equity tax will not apply to shares in Colombian companies, accounts receivable from Colombian debtors, certain portfolio investments and financial lease agreements.

In addition, the tax reform establishes a new normalization tax with a 15% rate for year 2020. A reduced 7.5% rate may apply in certain cases.

Value added tax (VAT)

The tax reform clarifies the way in which the taxable basis for the VAT should be determined when importing goods from free trade zones. The tax reform also excludes from VAT brokerage services for reinsurance contracts and commissions paid to investment management companies.

Medicines are generally included in the VAT-exempt goods list (0% rated). The tax reform charges the National Commission for the Prices of Medicines and Medical Devices with reviewing the effective reduction of medicine prices of as a result of this exemption.

In addition, the tax reform:

- ▶ Adds a VAT exclusion for cosmetic surgeries, as well as for certain bicycles under 50 tax units (approximately US\$520)

- ▶ Reintroduces Article 491 of the Colombian Tax Code, which expressly indicates that VAT paid on the acquisition of fixed assets generally cannot be treated as creditable input VAT
- ▶ Provides that foreign nonresident providers of digital services are not required to issue Colombian invoices or equivalent documents
- ▶ Establishes three days per year in which there will be a VAT exemption for some products, provided the value does not exceed certain amounts
- ▶ Requires a fixed amount to be paid to low-income families to reimburse them for VAT paid
- ▶ Increases from two to three years the period for voluntarily amending tax returns to reduce the refund or increase the amount due
- ▶ Modifies the criminal law provisions on tax matters and their applicability
- ▶ Establishes payment provisions for (i) mutual agreement terminations in administrative procedures and (ii) conciliations at the judicial stage
- ▶ Requires tax authorities to apply the most favorable application of the law at the collections stage

Procedural rules

Taxpayers must file the report for assets owned abroad if their value exceeds 2,000 tax units (approximately US\$20,000). The tax reform also:

- ▶ Extends the audit benefit to tax year 2021
- ▶ Reduces the statute of limitations to five years for tax returns in which losses have been accrued or offset (the previous statute of limitations was 12 years), as well as those filed by taxpayers to which the transfer pricing regime applies (the previous statute of limitations was six years)

Other provisions

The tax reform:

- ▶ Eliminates the consumption tax applicable to the sale of immovable property
- ▶ Creates a fee for reporting business integrations to the Superintendence of Industry and Commerce
- ▶ Creates an expert commission to study existing tax benefits
- ▶ Requires the Colombian Executive Power to deliver to the Congress a report on the effect of eliminating the VAT and replacing it with an 8% national consumption tax

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