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# Global Tax Alert

News from EY Americas Tax

## Colombia issues regulation on deferring income from private equity or collective investment funds, as well as rules on permanent establishments

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In Decree 1054 (the Decree), issued 19 July 2020, the Colombian Government establishes the requirements that private equity funds, collective investment funds and foreign portfolio investments (hereinafter, Fund or Funds) must meet to qualify for special tax treatment. The Decree also includes rules on Colombian permanent establishments (PEs), particularly profit distributions.

Decree 1054 replaces Decree 1973 of 2019, which was effectively voided when the law underlying it (Law 1943 of 2018) was declared unconstitutional due to procedural flaws.

#### Income deferral benefit

Article 23-1 of the Colombian Tax Code (CTC) permits Funds to defer the taxation of income they receive. To qualify for deferral, Funds must meet one of the following requirements:

- ▶ The Fund's shares are traded on a stock exchange regulated by the Financial Superintendence (Superfinanciera)
- or
- ▶ No more than 50% of the Fund is owned (direct or indirectly) by the same beneficial owner (including its economic related parties and family members), and none of the Fund's beneficial owners have any decision power over their distributions

Under the Decree, deferral begins the moment the Fund's shares are listed on the stock exchange (the Fund must be previously registered with the National Registry of Securities and Issuers – “RNVE” per its Spanish acronym). Deferral will continue as long as the underlying listing obligations are fulfilled and the shares are traded on the stock exchange.

For Funds not listed on a stock exchange, deferral applies from the date on which the withholding agent confirms the fulfillment of the beneficial-owner requirements. The confirmation must be certified annually by the withholding agent within three months of the following fiscal year.

The Decree contains several definitions that must be considered when deferring taxation of income received by Funds, under Articles 18-1 and 23-1 of the CTC. These include a definition for “innovative entrepreneurships.” Unlike other Funds, innovative entrepreneurships with a controlling beneficial owner may generally qualify for deferral as long as the owner's investment is less than 600,000 tax units (COP21,364,200,000, approx. US\$5,934,500 for 2020).

If deferral does not apply, the withholding agent must apply the withholding tax as specified in the mercantile trust rules.

### **Anti-abuse rules and joint liability of the withholding agent**

The Decree prohibits income deferral for Funds listed on the stock exchange when the listed shares lack economic or commercial reason or purpose. Shares lack this reason or purpose, among other reasons, when the Fund fails to fulfill its disclosure, registration and/or other obligations under the RNVE and/or stock market.

The Decree also prohibits deferral of a Fund's income when the Fund's main purpose is to defer income (e.g., structuring a Fund for the private sale of one or more assets).

Finally, the Decree imposes joint and several responsibility on Fund administrators, as withholding agents, to pay withholdings when they knowingly administer the Fund or its assets for purposes of tax avoidance or abuse.

### **PEs and their distributions**

Decree 1054 adjusts various regulations on PE taxation (and taxation of nonresidents) to match Article 66 of Law 2010, which imposes income tax on a PE's attributed worldwide income (national and foreign source).

Additionally, the Decree notes that dividend tax applies to a PE's attributed profits in Colombia, both national and foreign, that are transferred to a foreign related party under the rules established by Articles 48 and 49 of the CTC. This provision could be debatable, as the definition of dividends (Article 30 E.T.) only references PE distributions of Colombian-source income (not foreign).

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