# TAX TRANSFORMATION

**ANA ONATE** OUTLINES COLOMBIA'S NEW TAX REFORMS

**IN DECEMBER 2018**, Colombia's new government passed a raft of tax reforms, contained in *Law 1943 – Tax Reform* (the Law). The Law was enacted by the Congress of Colombia in order to restore the balance of the national budget, and came into effect as of 1 January 2019.

The move is designed to collect and cover the country's fiscal deficit and comes two years after the approval of the previous reform. Additionally, with Colombia being accepted as a member of the OECD, it is obliged to follow global best practices and to modify its laws accordingly. The Law achieves both.

The Law establishes important amendments on both direct and indirect taxes, as well as clarifying some aspects of the previous Bill that were uncertain, and delimiting some procedures and interpretations. It also has a major objective to attract foreign investment and to increase the national revenue. The Law is a wide-ranging tax reform; however, the following topics stand out.

## WEALTH TAX

The wealth tax and the 'normalisation special tax' (disclosure-amnesty) are still in force. Wealth tax is applicable for individuals who for fiscal years 2019 to 2022 had a net worth, as of 1 January 2019, equal to or higher than COP5 billion (approximately USD1.7 million). The applicable tax rate is 1 per cent.

Tax normalisation will be triggered by possession of non-reported assets and inexistent liabilities. Its tax rate remains at 13 per cent, giving the possibility to be reduced to a 6.5 per cent effective rate if the assets are invested in the country for at least two years. There will be no future reprisals or negative effects for those who accept the aforementioned tax, provided it is proved that the origin of the reported assets is not illegal.

## TRUSTS AND OTHER VEHICLES

Trusts, private foundations, insurance policies with a saving component, investment funds and any other type of fiduciary vehicle, including structures involving entities with substantially lower fiscal costs, should be disclosed within the normalisation tax. Regardless of their characteristics (e.g. irrevocable, discretionary, those where beneficiaries are not fully defined or determined), the founder, settlor or whoever shall have the position of creator has the obligation of reporting the vehicle in operation.

This new rule is positioned against a ruling issued by the Colombian Tax Office, according to which, in a discretionary irrevocable trust, neither the settlor nor the beneficiaries had to report it.

With regard to insurance policies, it is important to bear in mind that indemnities derived from such contracts will be taxed as from the 2019 tax year as capital gains (at a rate of 10 per cent), should the amount exceed COP450 million (approximately USD136,000). Previous to the tax reform, they were considered exempt.

## THIN CAPITALISATION

Regarding thin capitalisation rules, a requested correction was implemented. Before the introduction of the Law, the rules applied to all parties involved in the financing process; as of 2019, they will only be applicable to related parties. Additionally, the applicable ratio for these operations has been modified from 3:1 to 2:1.

## HOLDING REGIMES

A new holding regime, the Colombian Holding Company, has also been created under the Law, and, as with other holding regimes, it is aimed at attracting new investors by granting exemption status to dividends received by foreign subsidiaries and for capital gains earned from the sale of subsidiaries. For the regime to be applicable, certain substance requirements must be met, such as having three employees based in Colombia and having at least 10 per cent of the participation directly or indirectly in the subsidiary for at least 12 months.

The inclusion of new criminal offences targets the omission of assets, creation of non-existing liabilities, tax evasion and tax fraud within the scope of the tax administration that will request action to the criminal authorities.

In December 2018, after years of being discussed, taxes for indirect sale of companies will be triggered as if the sale were being directly done by the owner. Obligations for seller and buyer in these cases are mandatory.

Earlier this year, the government enacted regulatory decrees clarifying some aspects of this law. *Rule No. 874* addresses the normalisation and wealth tax and clarifies that whoever has the potential or real economic use of the assets will be obliged to declare, settle and pay the normalisation tax. It also defines those considered as beneficial owners of the above-mentioned fiduciary vehicles. If the vehicle is discretionary or subject to conditions, the settlor is deemed to have economic benefit and therefore must report; otherwise, beneficiaries must report.

The law also explained the treatment that entities with substantially lower cost will have. Those companies with no economic or real purpose presenting a substantial difference between their fiscal costs from their underlying assets must report in a complete manner, based on the value of the underlying assets.

The intention of this last clarification was to encourage taxpayers, who have reported assets in the past, regardless of their real underlying value, to proceed and report according to real value of assets. In addition, it detailed the conditions for carrying out the repatriation of the omitted assets in order to obtain the 50 per cent reduction on the taxable base of the tax. Still, some clarifications are needed and more regulatory rules will follow.

**ANA ONATE TEP** IS BRANCH DIRECTOR AT TRUSTMOORE, BOGOTÁ