

MEMORANDUM

REFERENCE: NEW LIST OF TAX HAVENS ISSUED BY THE GOVERNMENT OF COLOMBIA

The Government of Colombia has issued Decree 1966 dated October the 7th of 2014, through which the list of tax havens was modified. In this sense, we consider it is relevant to report some of the most significant aspects contained in this recently emitted regulation:

1. New jurisdictions considered as tax haven in Colombia:
 - 1.1. Republic of Panama.
 - 1.2. Barbados.
 - 1.3. United Arab Emirates.
 - 1.4. State of Kuwait.
 - 1.5. State of Qatar.

2. Jurisdictions that are no longer considered as tax haven in Colombia :
 - 2.1. Cayman Islands.
 - 2.2. British Virgin Islands (“BVI”).
 - 2.3. Bermuda
 - 2.4. Principality of Liechtenstein.
 - 2.5. Principality of Andorra.
 - 2.6. Republic of Cyprus.
 - 2.7. Bailiwick of Guernsey.
 - 2.8. Bailiwick of Jersey.
 - 2.9. Anguilla.
 - 2.10. Isle of Man.

MEMORANDUM

3. WITHHOLDING TAX

- 3.1 By January the 1st of 2015, outbound payments to residents in tax haven jurisdictions will be subject to withholding tax, whenever the income is characterized as Colombian-source income.
- 3.2 Import payments are not Colombian-source income. Thus, in any case these payments are not subject to withholding tax.
- 3.3 If the item of income is Colombian-source, any outbound payments made to tax havens residents will be subject to a 33% withholding tax (except for income derived from portfolio investment in Colombia, in which case a 25% withholding tax is imposed). Normally, the items of income subject to withholding tax are those related to technical services, technical assistance, consulting, credit interests, services offered in Colombia, goods sold within Colombia, among others.
- 3.4 Costs and expenses accrued in 2014 will be subject to withholding tax rates established by the Colombian tax code for each type of payment or service, regardless of the fact the outbound payments are made in 2015.
- 3.5 Colombian tax code provides that the income derived from portfolio investments made by persons located in tax havens will be subject to a 25% withholding tax rather than 33%.

4. TRANSFER PRICING

- 4.1 By January 1st of 2015, invoices originated by an entity located in a tax haven, must always be (i) reported in the transfer pricing return/study and (ii) be arm's length. In addition, the tax-haven entity must include a functional data analysis (assets, risks, costs, expenses, assigned staff and duties fulfilled) regardless of whether this entity is a related party to the Colombian payor.
- 4.2 Filing the transfer pricing return and preparing the supporting study are a legal obligation, regardless of the value of the assets, level of income or equity of the Colombian payor.
- 4.3 The non-compliance with the above-mentioned obligation may result in high tax penalties.
- 4.4 In order for a Colombian payor to tax deduct the payments made to an entity located in a tax haven, especially those payments that, like imports, are not Colombian-source income, the

MEMORANDUM

Colombian payor must comply with all the transfer pricing statutory requirements (DIAN Concept 607 of May 26th 2014).

4.5 It should be noted that, notwithstanding the transfer pricing requirements, the outbound payments of Colombian-source income must be subject to a 33% withholding tax in order for the payor to tax deduct the expense.

5. COLOMBIAN INVESTMENT OPERATIONS IN TAX HAVENS

5.1. Cash investment operations performed by Colombian enterprises or persons in companies or financial entities located in tax havens, are not considered as operations that generate costs or expenses. Thus, these transactions will not be subject to the tax-haven withholding dispositions.

5.2. Non-monetary investments will be subject to transfer pricing regime and to taxes established by Colombian law.

6. TAX HAVEN INVESTMENT OPERATIONS IN COLOMBIA

6.1. As mentioned, an item of income characterized as Colombian-source will be subject to 33% withholding tax if is paid to a tax haven resident. Pursuant to the Colombian foreign portfolio investment regime, the portfolio investment made by a resident of a tax haven will be subject to a 25% withholding tax.

7. TIMELY APPLICATION OF THE NEW REGULATION

7.1. Since this new regulation has direct effects in the computation of income tax, it is important to analyze its practical application in accordance with Colombian constitutional law.

7.2. The tax-haven regulation for the newly listed jurisdictions (such as Panamá) will enter into effect as of January 1st/ 2015. Thus, payments to tax havens resident that are or will be accrued in FY2014 should not be subject to the tax haven regulations, even though the actual outbound payment is made in FY2015. This is fully recognized by article 4 of Decree 1966 of October 7 of 2014.

MEMORANDUM

- 7.3. In this sense, the 33% withholding tax rate will be applied to those payments to be accrued and made in FY 2015, considering that the withholding tax is full tax due for tax haven residents.
- 7.4. The deductions requisites (transfer pricing requirements) only apply to those operations performed with the newly listed tax havens jurisdictions as of January 1st 2015. The latter is clearly established by article 4 of Decree 1966 of October 7 of 2014.
- 7.5. This conclusion is also supported by DIAN concept 11309 of 2014, which states: *“The balanced and complete interpretation of the dispositions transcribed, in virtue of the principle established in superior article 338, indicates that Decree 2193 of 2013 applies starting taxable year 2014 to those operations performed by the equity taxpayers with persons, companies, entities, or residents in tax havens”*.
8. Important to mention those cases involving indebtedness with financial and non-financial entities located in tax havens, since they usually comprise higher complexity and require a case by case analysis.
9. Please do not hesitate to contact us should you require further information.

POSSE HERRERA RUIZ