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# Colombia

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zilian company.

AN 64/83 is more incisive on this point and specifically provides that this investment must be equivalent to the sum that the Brazilian company will have to remit abroad in payment for the technology and that the investment must be made before the respective remittance. It is important to note that this rule applies only to purchases of technology owned by companies other than those of the same economic group as the company controlling the Brazilian company. In fact, the INPI has not permitted any companies to provide any remuneration where such foreign controlling companies have supplied technology to their affiliates in Brazil.

Furthermore, in choosing among the various concepts that exist to determine "control", the INPI has adopted the definition contained in the Foreign Capital Law. Accordingly, AN 64/83 would extend to all legal entities established in Brazil in which at least 50% of the voting capital is directly or indirectly held by the company which has its head office abroad. In applying the provisions of AN 64/83, the INPI is seeking to increase the technological capacity of Brazilian industry and to, at the same time, counterbalance the remittance of foreign exchange out of Brazil. Parallel thereto, the requirement for an equivalent investment will make production contracts more expensive thus inevitably resulting in an increase of the cost of products manufactured with foreign technology.

PINHEIRO NETO - ADVOGADOS  
SAO PAULO, BRAZIL

## COLOMBIA

*The following is a brief summary of recent legislation and judicial decisions affecting the activity of foreign enterprises and individuals in Colombia.*

### I. NEW INCOME TAX LAW

Law 009/83, adopted by Congress in June 1983 together with Decree 2579 of September 12, 1983, has amended the income tax law in several important ways. Some of the changes enacted by Congress confirm measures adopted by the government at the end of 1982 and in the beginning of 1983 as part of its economic emergency program.

*Income from Foreign Investment*

a) Where dividends are paid by Colombian “*sociedades anonimas*” (S.A.) to non-resident shareholders, a 40% withholding tax is due and the withholding must be made by the Colombian entity (ss.47(a) and 48).

b) The rate of withholding on such dividends is 20% where the tax rate on dividends received in the foreign investor’s home country is at least 70% of the income tax rate applicable to Colombian *sociedades anonimas* (s.48).

c) Where the foreign investor receives income as a result of his interest in a *sociedad de responsabilidad limitada* or similar enterprise, such income is subject to a withholding tax, in the hands of the Colombian entity, of 40% (s.47 (b)).

d) In all cases where income or capital gains are transferred abroad to a foreign investor, a remittance tax is payable. Two exceptions exist; one for dividends from *sociedades anonimas*; and, another for interest payments on certain foreign loans which, in accord with Law 74 of 1981 and Decree 231 of 1983, are not considered to be national source income. This tax is fixed at 20% on profits made in Colombia by branches of foreign firms and 12% on income generated from an interest in a *sociedad de responsabilidad limitada* or other similar enterprise held by a foreign investor. Where a withholding tax is payable on the same income, the remittance tax is calculated on the net value of income after subtracting the withholding tax (s.46 (a) (b) and 2). This “netting” applies to income received from *sociedades de responsabilidad limitada* but not to profits received by the foreign investor from branch operations.

e) The base for calculating the remittance tax does not include reinvested or retained earnings of a branch of a foreign enterprise. However, when retained earnings are transferred to a non-capital account, deferred remittance tax becomes payable (art. 2 of Decree 2579/83).

*Royalties, Technical Services and Similar Items*

a) Royalties arising from technology or “know-how” transfer arrangements and payments made as consideration for technical services are subject both to a withholding tax of 40% (s.47 (c)) and a remittance tax of 12% of the net value after the withholding tax

is subtracted (s.46 (c) and 2) bringing the total tax liability to 47.2% of the gross amount.

b) Where payments are made to lease movies or use computer programs, the withholding and remittances taxes are calculated on 60% and 80% respectively of the gross value and net value after withholding tax of such payments (ss. 46 (d) and 47 (d) for movies and ss. 46 (e) and 47 (e) for computer programs).

Certain categories of income are deemed not to be national source income and are not subject to tax. These include income from loans made abroad to Colombian *corporaciones financieras*, loans to finance trade made through banks and *corporaciones financieras*, loans made abroad to Colombian, foreign or mixed enterprises whose activities are considered to be of significance for the economic and social development of the country according to criteria adopted by the National Council on Economic and Social Policy (CONPES) and loans obtained by foreign, national or mixed enterprises whose activities are related to energy, water and sewage supply, telecommunications, public health, education, mining and petroleum exploration and development. Technical services performed outside Colombia are also exempt, provided the Royalties Committee has certified that they could not be performed in Colombia and the foreign supplier of services has no branch in Colombia (ss. 49 and 50). Decree 2579 (art. 16) also exempts income from technical services performed abroad consisting of either repairs and maintenance of equipment or the training of personnel from the Colombian public sector abroad.

## II. DECREE 222/1983 - ADMINISTRATIVE CONTRACTS

This Decree was adopted by the government in virtue of powers delegated by Law 19 of 1982. It replaces Decree 150 of 1976 as the instrument governing contracts made by the public sector. The new Decree is very complex and parts of it are quite controversial.

### *Types of Contract Covered:*

The Decree covers the following types of contracts when made with either the national government or its agencies, departments, public utility enterprises, state commercial and industrial enterprises and *sociedades de economia mixta* in which the state has at least 90% interest:

- i) public works contracts

- ii) purchase and use of real estate
- iii) consultancy contracts
- iv) supply contracts
- v) sale and transfer of personal property and real estate
- vi) rental agreements
- vii) contracts for provision of services
- viii) telecommunications, postal service, and provision of notes and coins
- ix) loan agreements
- x) insurance contracts.

#### *Who May Contract:*

With the exception of certain types of activities such as radio and television broadcasting, foreign entities may contract with the Colombian public sector on much the same terms as national entities. In order to be able to bid on public works contracts, a company must be registered with the particular entity which will award the contract. In all cases, a foreign private entity which seeks to participate in public works contracts must have a branch office in Colombia if the contract is "permanent" (i.e. for more than 1 year). Where the contract is temporary, it must have at least a legal representative domiciled in Colombia. Joint bids may be made only with the permission of the entity awarding a contract. Where such bids are possible, the joint bidders will be considered to be in consortium and will be severally responsible for the execution and fulfillment of the contract if it is awarded to them.

#### *Obligatory Contractual Terms:*

All public sector contracts must provide for certain types of clauses. Among the most important are:

- i) unilateral termination by the public contracting entity
- ii) unilateral modification by the public contracting entity
- iii) unilateral interpretation by the public contracting entity
- iv) Colombian governing law and jurisdiction and waiver of claims by diplomatic channels ("Calvo clause")
- v) obligatory guarantees by the private sector contracting party such as bonds or insurance policies, according to norms established by the Auditor-General's office
- vi) the right of the public sector contracting party to impose fines for non-performance
- vii) a monetary penalty clause

viii) obligatory termination clause.

Obligatory clauses i, ii, v, vi, vii, and viii do not apply to loan agreements or financing arrangements with foreign or international public sector agencies.

*Engineering and Consulting Contracts:*

The Decree provides special protection for Colombian engineers and consultants. Consulting contracts can only be awarded to foreign entities where the *Fondo Nacional de Proyectos de Desarrollo* (FONADE) certifies that no Colombian consultants are available for the work involved. Any foreign entity chosen as a consultant must associate itself with a Colombian entity either as an advisor to the Colombian entity or in consortium with it. The association between the Colombian and foreign consultants must be structured so as to ensure adequate technology transfer.

Similar rules apply to engineering contracts. Where a foreign engineering firm is chosen it must have Colombian associates on the project participating in at least 40% of the project. This association can either be through a consortium, a mixed company or simply subcontracting. All the provisions of Law 64 of 1978 regulating the practice of engineering and protecting local engineers are applicable to public sector contracts.

*Loan Agreements:*

Decree 222 governs the procedure for obtaining foreign loans, though not for obtaining credit lines or similar services from publicly owned banks (s.221). Where foreign loans are directly contracted for by the national government, the National Council on Economic and Social Policy must approve the project to be financed. Further, the Department of Finance must give its approval of the negotiations with a foreign lender, based on a prior favorable opinion of the Interparliamentary Commission on Foreign Credit regarding the particular lender. Where loans are contracted for by the "decentralized agencies", such as utilities, the Department of Finance must give its permission for such negotiations based, in part, on a favorable opinion by the National Planning Department concerning the project to be financed. The contract may only be signed when an executive resolution is adopted by the government. Further, such resolutions will only be adopted on the recommendation of the General Directorate of Public

**Credit.** A simplified procedure is provided for where the credits are for less than US\$ 5 million. Where the guarantee of the national government is sought, the approval of such a guarantee must be obtained from the National Council of Economic and Social Policy.

Decree 222 maintains the requirement that foreign loan agreements are governed by both Colombian law and courts. This rule applies not only to contracts signed in Colombia but also to those signed elsewhere whose execution will take place in Colombia. Section 239 has an important nuance: contracts which are to be "verified" abroad can be governed by foreign law. It is not clear what "verified" means. According to one of the authors of the decree, the expression covers loans such as Eurobond transactions where the bonds are issued abroad. If this is indeed the meaning of the term "verified", then the scope of any potential application of foreign law will be narrow as Eurobond transactions are extremely rare for Colombian entities. However, as a matter of practice, foreign law may continue to be stipulated in fixed-rate subsidized interest transactions.

The Decree contains several provisions which limit "tied credits." For example, where the credit is conditioned on the purchase of equipment originating in a particular country. As a general rule, loan agreements made directly with public sector entities cannot provide for "tied credits." This principle does not apply to supplier credits and doesn't appear to apply to credits provided by public international or governmental credit agencies. The Public Credit Directorate (Ministry of Finance) interprets section 286 of the Decree to refer only to lines of credit extended by such agencies to the Colombian government with the understanding that such lines would be available if and when suppliers met national content or other similar conditions.

Decree 222 was designed exclusively to cover project financing to public entities. In a recent policy statement, the government affirmed that foreign loans would be sought only to finance investment.<sup>1</sup> However, several influential economic advisory groups are urging the government to consider recourse to foreign borrowing as a means of helping to finance its own deficit without "crowding out" private borrowers in the domestic capital market.

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1. El Tiempo (Bogotá), Mar. 31, 1983.

### III. LIMITS ON LENDING AND GUARANTEES BY BANKS

In an effort to avoid banks being over-exposed to particular clients by either loans or guarantees, Decree 3363 of 1982 requires them to limit unsecured loans and guarantees to any single entity to 7% of their paid-up capital and reserved assets. This limit is raised to 15% where the loans or guarantees are secured by charges on real estate, provided the value of the property so charged is at least 20% greater than the amount of the loans or guarantees it secures.

Foreign medium and long-term credits for development purposes are not subject to the constraints imposed by the Decrees. There is no definition of "development lending" but it is believed that the term covers at least investment in infrastructure and public services. The above-mentioned limits can be raised to 10% for unsecured transactions and 25% for secured transactions where the project to be financed or guaranteed is considered to be significant for national economic and social development according to criteria established by the National Council on Economic and Social Policy and where the particular financing has been approved by the Monetary Board (*Junta Monetaria*).

The financial institutions covered by the Decree have until December 21, 1984 to comply with its requirements. The decree applies to publicly-owned banks as well as private sector institutions, but does not apply to *corporaciones de ahorro y vivienda* (similar to savings and loan associations in the United States).

### IV. CHANGES IN FOREIGN INVESTMENT RULES

In March of 1983, the Colombian government announced its intention to derogate from Andean Pact norms concerning foreign investment in order to make such investment more attractive in certain sectors of the economy. The government hopes that increased investment in these sectors will have positive effects both on employment and on improving the balance of payments. Resolution 036 of the National Council on Economic and Social Policy (CONPES), issued on August 19, 1983, has given effect to that intention.

The most important provision of the Resolution provides that the annual rate of profit remittance as a percentage of registered capital now available to foreign investors in the favored sectors will be equivalent to 20% plus the average prime rate in New York for



the year as determined by the Bank of the Republic. This favored treatment, which compares with the 20% remittance rate allowed for by Decision 24 of the Andean Pact, applies to investments made *after* August 19, 1983 in a wide range of industrial, agricultural and service sectors including tourism, aircraft manufacture, smelting and even fish processing.

Where investments were made before August 19, 1983 in the favored sectors, the new improved remittance rate will be available for both 1983 and subsequent years where the Colombian enterprise can demonstrate to the National Planning Department (DNP) that more than 50% of its sales were in export markets.

#### V. FOREIGN BORROWING AUTHORIZED FOR PRIVATE ENTERPRISE

One of the primary objectives of government industrial policy is to increase the capitalization of private enterprises. With an extremely tight and somewhat limited domestic capital market, the government decided to permit private enterprises to borrow abroad.

Resolution 87/83 of the Monetary Board (*Junta Monetaria*), issued on September 7, 1983, permits private borrowings by entities involved in agriculture, manufacturing, mining and service-oriented activities provided the loan contracted for is of at least 3 years duration with a minimum of a 1-year grace period and with repayment of principal in equal semi-annual installments. Interest can be fixed up to a maximum of either the prime rate or Libor plus 2.5%. Any loans so contracted must be registered with the Exchange Office of the Bank of the Republic. Any extension or assignment of registered agreements must be approved by the Exchange Office.

The benefits of Resolution 87/83 do not extend to the distribution and housing sectors. These sectors have been specifically excluded by virtue of s.8 of the Resolution.

#### VI. FOREIGN ARBITRATION AND THE CORELCA CASE

In its recent decision in *CORELCA v. Westinghouse International Corporation*, the Council of State, Colombia's highest administrative law court, invalidated a clause in an agreement between a public utility and a private U.S. supplier providing for foreign arbitration. The arbitration in question would have been carried out by Colombian arbitrators, in Colombia, according to

the rules of the International Chamber of Commerce. Having affirmed that such arbitration was indeed "foreign", the Council held that it was not in conformity with Colombian constitutional requirements.

According to the Constitution, only courts established by the State can render binding decisions. While the law does recognize arbitration clauses, it requires that all arbitration be carried out according to the terms of the Code of Civil Procedure. As far as the Council of State was concerned, the ICC arbitration did not fall within that category even though the arbitrators would be qualified to so act under Colombian law. It is important to note that, though invited to do so by Westinghouse, the Council of State did not discuss what effect Colombia's ratification of the 1958 New York Convention on International Arbitration would have on the "no foreign arbitration" rule. The Council decided that the Convention could not apply to contracts, such as the one at issue, which were entered into before September 26, 1979, the date upon which Colombia ratified the Convention.

By implication, this may mean that the Convention is applicable to agreements made after that date and that foreign arbitration could thus be stipulated. In practice, the agencies whose approval is required for licensing and technology transfer arrangements (Royalties Committee) technical services agreements (Exchange Office) and loan agreements (the General Directorate of Public Credit) still insist that where arbitration is provided for, it must be governed exclusively by Colombian law.

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