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COLOMBIA

The following is a review of recent legal and economic developments in Colombia.

I. INTRODUCTION

Colombia enters 1988 in an economic context which is at the same time more favorable and less certain than at the beginning of 1987. According to official government statistics, the rate of economic growth in 1987 was higher than five percent; the unemployment rate in the principal cities fell to eleven percent; and the level of international reserves remained generally stable, now around US\$ 3.4 billion. The signing in October 1987 of a new agreement on export quotas by the member states of the International Coffee Organization was received positively in Bogota. The Colombian authorities have, for many years, favoured a structured and organized international market for the country's principal export.

Among the negative factors, the rate of inflation is perhaps the most crucial. In 1985 inflation reached twenty-five percent, quite low in comparison with most Latin American countries, but exceeding the target set by the government. To control this rise, the Central Bank (Banco de la República) instructed six important commercial banks that they must refuse all new overdraft facilities to their clients until the end of 1987. Another source of concern arises from the international consequences of the collapse in the principal stock exchanges since October 19, 1987. Although the international stock exchange crisis has not yet affected Colombian exchanges, where the purchase and sale of shares is a negligible portion of activities and foreign investors are precluded from participation, the crisis already has produced effects on other economic sectors. The government was forced to accept a reduction of US\$ 60 million in the amount of its "Concorde" loan with international commercial banks (the loan will be for US\$ 1 billion), in part for purely Colombian reasons but, in large measure, because bankers have been more reluctant to grant new credits to Latin America under present economic circumstances. Officially, Colombia has not been seeking to restructure its foreign debt but the new

debt authorization statute permits the government, for the first time, to completely or partially restructure the external public debt. The difficult state of the petroleum market, resulting in part from the pessimistic economic outlook in 1988 for the principal industrialized countries, affects the important Colombian hydrocarbon sector, on which the government heavily relies to diversify the country's exports.

Congressional legislative activity during the session which ended on December 16, 1987 achieved less than expected. After many incidents and crises, the parliamentarians approved a new debt authorization statute and a new land reform law. Several important bills were left on the order paper, including a bill providing for new rules governing foreign investment in the financial services sector. Because of Congress' failure to adopt the bill, Colombia now has more restrictive rules in this area than it had under the old Decision 24 of the Cartagena Agreement Commission. Decision 24 contained a safeguard clause which empowered the government to authorize foreign investment in certain local banks over and above the forty-nine percent limit fixed by Law 55 of 1975. The new Decision 220 has no safeguard clause. It leaves the national government free to choose the sectors reserved for local investment. The Colombian government concluded that it was necessary to replace Law 55 of 1975 by a new legislative measure in order to liberalize the rules on foreign investment in the financial services sector, but this step has not yet been taken.

II. THE 1987 DEBT AUTHORIZATION STATUTE

Law 43 of 1987, effective November 30, 1987, increases the national government's authorized foreign indebtedness by US\$ 4 billion. This figure includes the government's direct borrowing, the issuance of securities by the government and guarantees given by the government for loans or securities issued by public sector entities. Law 43 also contains several important provisions concerning the legal aspects of Colombian public sector foreign debt.

In the future, the "special contracts" provided for in Article 247 of Decree 222 (which for the most part are made directly by the Colombian government with foreign governments for carrying out projects) must be reviewed beforehand by the National Planning Department. The financial conditions surrounding such projects must be reviewed by the Ministry of Finance and Public

Credit (General Directorate of Public Credit).

The government is authorized to seek a decision by the Council of State in connection with the issuance of securities in the same manner as for external loan agreements. Law 55 of 1985 states that the Council must, at the request of the government, decide on the legality of a loan agreement (or a guarantee given by the government for such a transaction). A favorable decision of the Council is final and not subject to appeal.

Pursuant to Law 58 of 1985, which requires the publication of official documents, once the Director-General of Public credit sends executive resolutions for publication to the official gazette, they will be deemed published. This reform expedites orders in which the government authorizes public entities to sign loan agreements and facilitates the signing of contracts by shortening the delay between the adoption of an executive resolution and its publication in the official gazette.

Law 43 adds a new procedural requirement to the already long list of those imposed on public entities for loan agreements. In the future, these entities must register their contracts with the Ministry of Finance and Public Credit (General Directorate of Public Credit) within five days of execution of the contract. The General Directorate of Public Credit has five days from the date on which the contract is presented to it to complete registration formalities. The law reaffirms that credit agreements and payments made under foreign credit agreements by Colombian public-sector entities are free of all taxes, fees and levies of any kind in Colombia.

Law 43 envisions for the first time the possibility that Colombia may seek to restructure its foreign debt. The law authorizes the government to completely or partially restructure the public sector foreign debt. The term "restructuring" is defined to include any of the following actions:

1. the reduction of interest rates;
2. the waiving of interest;
3. the capitalizing of interest;
4. the extending of delays for payment; and
5. the amending of other financial conditions.

The law provides for the possibility that, as a part of restructuring, the national government would directly assume obligations contracted to by public sector entities. Within three months of a

restructuring, the government may determine in what manner public entities will pay, in Colombian pesos, the amounts which they owed by virtue of foreign obligations subject to restructuring. The government may also determine financial mechanisms for the capitalization and maintenance of such payments.

III. TAX PROVISIONS

Some provisions of Law 43 amended the tax laws. The following amendments are significant:

1. Stamp duties are imposed only on instruments (including promises to contract and assignments), having a value of more than 1 million Colombian pesos. Cheques, bearer and registered bonds, shares of companies not listed on the stock exchange, bank guarantees and assignments of shares in companies not listed on the stock exchange are not affected by the changes. Instruments of indeterminate value continue to be subject to the stamp tax of existing legislation;

2. Taxpayers residing in Colombia must purchase "special financing bonds" in an amount up to five percent of their taxable income in 1986 for purchases in 1988, and three percent of their taxable income in 1987, for purchases in 1989. Individual taxpayers are obliged to purchase such bonds only if their taxable income for 1986 exceeds 4 million Colombian pesos. The bonds are in bearer form, have a maturity of five years and are freely negotiable. Proceeds received from the sale or reimbursement of such bonds can only be used to meet tax liability. Losses from such sales cannot be used to offset the liability. Proceeds received by the government from the issue of the special financing bonds are devoted to the needs of the armed forces, the police and the judiciary;

3. The government has until March 30, 1989 to adopt the income tax code provision in Law 75 of 1986. The first part of the code must be adopted no later than January 1988.

IV. RESOLUTION 47 OF THE MONETARY BOARD

Resolution 47 states that private enterprises contracting foreign debt are authorized to prepay certain debts or to purchase them at a discount from their creditors. The resolution covers loans registered with the Exchange Office, in accordance with Colombian legal requirements, which have been amended or extended

between April 27, 1983 and August 26, 1987. Loans which were restructured within the framework of Monetary Board Resolution 33 of 1984 may also benefit from the provisions of Resolution 47.

Debtors who desired to take advantage of this resolution were obliged to apply for approval from the Exchange Office before September 25, 1987. An overall ceiling of US\$ 75 million was fixed for these operations. A further ceiling of US\$ 12 million was fixed for individual debtors. In the case of prepayment of loans which were restructured under Resolution 33, the debtor must pay the Colombian commercial bank, which acts as intermediary, a sufficient amount in pesos to enable the bank to purchase immediately the certificates which it undertook to purchase by installments from the Central Bank as part of the restructuring operation, up to the amount to be prepaid to the foreign creditor. In the case of purchase of debts at a discount, the debtor must obtain a bank guarantee for 100% of the amount to be purchased in order to guarantee pro-rata extinction of the debt purchased within two months of the sending by the Exchange Office of the foreign currency required to make the purchase in question.

V. RESOLUTION 2 OF THE NATIONAL SECURITIES COMMISSION

On October 22, 1987 the General Chamber of the National Securities Commission resolved that all purchases and sales of shares in companies listed on the stock exchange for an amount at least equal to Col\$ 200,000, must be routed through the exchange. A series of purchases and sales made over a period not exceeding 120 days between the same parties in connection with shares in the same company, the total amount of which exceeds Col\$ 200,000, are considered a single transaction or the purposes of the resolution, even if no transaction of the series, considered individually, exceeds Col\$ 200,000.

VI. JUDICIAL DECISIONS

A. *The Telecom Case*

On October 26, 1987 the Council of State declared that the assets and revenues of public establishments (establecimientos publicos) have, in principle, complete freedom from seizure and attachment. The Council based its decision on Decree 3130 of 1968 which enables public establishments to enjoy the same privileges

as the national government. Since the government has complete immunity from execution and attachment by virtue of Article 336 of the Code of Civil Procedure, Telecom (the state-owned enterprise responsible for national and international telecommunications) and other public establishments have similar immunity.

The Council admitted that such immunity was subject to specific legal provisions and cited two examples (of which one is purely procedural) of norms which provide for execution and attachment of assets belonging to public establishments. Curiously, the Council did not mention Article 684 of the Code of Civil Procedure which provides that up to one-third of the income obtained by a public establishment, resulting from the operation of a public service, may be attached. This lapse by the Council does not affect the validity of Article 684. Many foreign lenders have relied on Article 684 in loan agreements with Colombian public establishments.

B. The Maizena Case

On July 6, 1987, the Council of State declared that Colombian corporations in which foreign investors have an interest, may not remit profit abroad during the year in which such profits are being accumulated. The local company must wait until the end of the year in question before remitting profits to its foreign investors. The Council of State interpreted the norms governing foreign investment and, in particular, exchange control regulations, so that only remittances calculated as a percentage of the registered foreign investment, as of December 31 each year, may be allowed. In the present framework of the Colombian exchange control rules, it is impossible to create a system of anticipated payments with a balancing payment made to foreign investors or returned to the local company. A system of anticipated payments is possible (and is permitted by the Commercial Code) in the case of dividends or profits payable to local shareholders or associates but exchange control requirements provide that such a system cannot be applied to foreign investors. Once foreign exchange has left Colombia, the Colombian exchange control authorities lose control over its movement. To prevent such loss of control, the Council has made it impossible to establish a remittance system based on anticipated payment of profits whose exact amount is not yet determined when such payments are made.

C. Income Tax Applicable to Foreign Companies

On September 3, 1987 the Supreme Court rejected an argument that certain paragraphs of section 1 of Law 75 of 1986 were unconstitutional. The paragraphs in question provided for higher tax rates on Colombian corporations than on foreign corporations during a transition period covering the 1987, 1988 and 1989 fiscal years. During that period, foreign companies are subject to a single tax rate of thirty percent; Colombian "sociedades anonimas" and similar entities must pay taxes of between thirty-one and thirty-three percent and must devote the savings due to the reduction in their tax burden to purposes set forth in the tax legislation itself.

The allegation stated that these provisions violate article 11 of the Constitution, which provides for equality of treatment between Colombians and foreigners, and article 26 of the Constitution, which declares that no one may be judged except by virtue of pre-existing laws. The Attorney General supported the allegation of unconstitutionality, but exclusively on the basis of article 11 of the National Constitution.

The Supreme Court held that article 11 of the Constitution, and the diplomatic protection which States accord their nationals abroad apply only to natural persons. "Moral" persons, and in particular corporations, do not possess a nationality in the strict sense, even though the law, including tax laws, distinguishes between "local" and "foreign" companies. Therefore, article 11 of the Constitution is not pertinent to analysis measures which affect corporate or "moral" persons exclusively. In any case, even though the Colombian Constitution does not expressly mention the right to equality, the implicit existence of such a right may be deduced from several constitutional provisions, including the obligation imposed on the State to protect all residents of Colombia in their life, honor and possessions and the abolition of slavery. It cannot be asserted, however, that the principle of equality before the law requires that all fiscal provisions must apply to everyone in exactly the same manner. The Constitution recognizes the government's right to regulate economic activity to attain certain objectives. This right includes the possibility of structuring the tax system in the manner provided for in the provisions reviewed in the present case. Article 26 of the Constitution was also inapplicable because the fiscal provision in question was not a judgment but a statute.

D. The Rights of Individuals Before the Andean Court: The Aluminio Reynolds Case

The Andean Court, which was established by a treaty signed in 1979 by the member states of the Cartagena Agreement (Bolivia, Colombia, Ecuador, Peru and Venezuela) and which sits in Quito, Ecuador has not been overburdened with work; in its seven years of existence, it has rendered few judgments. In its most recent decision of October 22, 1987, however, the court held that individuals do not have the right to take proceedings before it for alleged violations by member states of the Cartagena Agreement itself or of norms duly adopted by the Andean Pact Commission.

In the instant case, a Colombian company, Aluminio Reynolds Santo Domingo, S.A., desired a ruling on Section 95 of Colombian Law 75 of 1986. The law provides that a uniform tax equal to eighteen percent of the CIF value be imposed on imports from all countries without exception. Circular 984 of the Customs Directorate provides that a ruling on this tax applies to imports from member states of the Andean Pact which are not included in the "liberalization program" but which are on the reserve list or the excepted list. Aluminio Reynolds alleged that these provisions were inconsistent with the obligations assumed by Colombia through Article 54 of the Cartagena Agreement.

The Andean Court made the following points with respect to jurisdiction:

1. Individuals may take proceedings directly before the Andean Court when they challenge Andean Pact norms (decisions of the Commission, for example) on the basis of their alleged inconsistency with the Cartagena Agreement;

2. Individuals may take proceedings directly before national courts with respect to alleged violations of Andean norms by member states, if the rights of such individuals are directly affected by the alleged violations;

3. The Andean Pact Commission and the member states may take proceedings directly before the Andean Court concerning alleged violations of Andean norms by a member state. Individuals do not have this right and, in such a case, must take proceedings before national courts. These courts must request a preliminary ruling by the Andean Court when it is necessary to interpret a provision of Andean law for the purpose of the particular case.

In accordance with these principles, Aluminio Reynolds was not entitled to take proceedings in the Andean Court concerning the alleged Colombian violation of Andean norms.

E. Andean Law Before National Courts: The FEDEMETAL Case

Two weeks after the decision of the Andean Court in the Aluminio Reynolds case, the Council of State accepted an application presented by the Colombian Federation of Metal Industries (FEDEMETAL) against the same eighteen percent tax on imports imposed by Article 95 of Law 75 of 1986 on the basis that the tax (which replaced previous import taxes) was inconsistent with the obligations assumed by Colombia via Article 54 of the Cartagena Agreement. More particularly, the application concerned the same Circular 984 of the Customs Directorate which was in issue before the Andean Court in the Aluminio Reynolds case.

According to the Council of State, Article 54 of the Cartagena Agreement imposed a "standstill" obligation on member states of the Andean Pact with respect to customs duties and other taxes on imports. Subject to certain exceptions which were not relevant in the present case, Colombia was not entitled to amend its rules on customs duties or import taxes in such a manner as to burden imports from other member states of the Andean Pact with higher taxes than those existing at the time Colombia incorporated the Cartagena Agreement into its national law by means of Decree 1245 of 1969. At that time, the aggregate of the taxes on imports, which article 95 of Law 75 of 1986 was designed to replace, did not exceed three percent of the CIF value of imported merchandise. On imports from member states of the Andean Pact, Colombia is not entitled to adopt measures that impose higher taxes than in 1969. The Council therefore ordered the provisional suspension of Circular 984. Circular 984 was replaced by Circular 397 of October 15, 1987 which is the same as Circular 984 on imports from member states of the Andean Group.

F. Easing of Tax Burden on Certain Dividends

Decree 2539 of December 30, 1987 provides that dividends paid or payable to non-resident individuals or corporations on profits obtained before January 1, 1986 by a Colombian corporation are taxed at the rate of twenty percent. Such profits must

have been identified in the corporation's 1985 tax return as "undistributed profits" and the tax return must have been presented no later than June 30, 1986. If such dividends were subject to retention at source in 1987 at a higher rate than twenty percent, the excess retention may have been offset against retentions to be made in future periods.

Law 9 of 1983 provided that dividends payable to non-residents were taxed at forty percent (and in certain exceptional cases, twenty percent). Law 75 of 1986 substituted a uniform rate of thirty percent. For fiscal year 1986, however, the retention at source was that provided for in Law 9 of 1983 (Decree 823 of 1987, May 1987). In most cases, the retention at source applied to dividends paid or payable on profits obtained before January 1, 1986 is higher than twenty percent, so that Decree 2539 has eased considerably the tax burden on foreign investors with respect to such dividends.

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