

Transfer Pricing and Tax Havens

Obligation to file an informative return, to prepare support documentation and possibility to enter into an Anticipated Price Agreement with the Colombian Tax Authorities (DIAN)

- Fiscal Year 2004 -

Decrees 4345 and 4349 of 2004

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By means of Decree 4345 of 2004, the Colombian Government established which persons or entities are obliged to file an informative return, individual or consolidated, in connection with transactions with economically related parties (transfer pricing) or with entities located in tax havens. In addition, the Government also regulated the content of the informative return and of the support documentation, as well as the Anticipated Price Agreements (APAs), through Decree 4349 of 2004.

1. Terms for the filing of the informative tax return, for preparing the support documentation and to request the execution of an APA

Informative return

Taxpayers who carry out transactions with foreign entities to which they are economically linked or related must file with DIAN an informative tax return containing information regarding said transactions evidencing due compliance with the regulations on transfer pricing.

As per article 23 of Decree 4345 of 2004, taxpayers who carried out transactions with entities to which they are economically linked and/or with related parties from abroad and/or with entities located in tax havens during 2004 must file an informative return using the form set forth by DIAN to that effect (please refer to section 3 below for more details).

The form of the return must be submitted to entities authorised to collect taxes within the terms listed below, which depend on the last digit of the company's tax ID number (NIT):

Last Digit of NIT:	Deadline
9 or 0	June 17, 2005
7 or 8	June 20, 2005
5 or 6	June 21, 2005
3 or 4	June 22, 2005
1 or 2	June 23, 2005

Support Documentation

Taxpayers liable for the filing of informative returns must prepare and keep the relevant support documentation on which the return is based. This documentation must be prepared and be available for DIAN on 30 June 2005, at the latest (please refer to section 5 below for more information in this connection).

Anticipated Price Agreements (APA)

Entities to which the transfer pricing regime is applicable may request, in writing and within the first quarter of the relevant year, the entry into with DIAN of an APA.

Notwithstanding, it is important to note that the provisions regarding APAs contained in Decree 4349 of 2004 will only become effective as from 1 January 2006 (please refer to section 6 below for more information in this connection).

2. Transactions with economically related parties and with entities located in tax havens

With respect to the topic subject matter of this document, it seems to us pertinent to note some basic aspects of the regulation regarding transactions with (1) economically linked or related parties from abroad (transfer pricing) and/or (2) entities located in tax havens.

2.1. Transactions with economically linked or related parties from abroad (transfer pricing)

2.1.1. Transfer Pricing

If a Colombian company has an economical relationship or is linked with foreign entities and carries out transactions with them, it must apply the regulations on transfer pricing. The provisions of these regulations mainly require that transactions amongst economically linked or related parties are carried out in the same terms and conditions that would apply should the negotiation involved completely independent entities.

These limitations must be taken into account for determining income, costs, deductions, assets and debt for purposes of income and complementary taxes.

2.1.2. Anticipated Price Agreements (APA)

For purposes of complying with the regulation on transfer pricing, taxpayers may enter into APAs with DIAN in which the criteria and methodology for fixing prices, economic consideration amounts or return margins applicable to the transactions with economically linked or related parties from abroad are established (please refer to section 6 below for more information in this connection).

2.1.3. Informative return

Taxpayers who carry out transactions with foreign entities to which they are economically linked or related must file with DIAN an informative tax return containing information regarding said transactions evidencing due compliance with the regulations on transfer pricing.

In case the information regarding the transactions with economically linked or related parties does not comply with the requirements established by DIAN, said entity may impose sanctions and fines upon the taxpayer liable for the submittal of the return.

2.1.4. Economically linked or related parties

For purposes of the application of transfer pricing, there is an economic link when:

- The decision making power of affiliated or subordinated entities is subject to the will of the parent company (article 260 of the Commercial Code).
- The parent company (i) owns, directly or indirectly, more than 50% of the entity's capital; (ii) may, directly or indirectly, cast enough votes to constitute a majority; or (iii) exercises a dominant position (article 261 of the Commercial Code).
- One of the entities is the Colombian branch of the other (article 263 of the Commercial Code).

- There is an agency agreement between the relevant entities (article 264 of the Code of Commerce).
- There is entrepreneurial group (article 28 of Law 222 of 1995).
- In general, when there is a predominant relationship with respect to the corporate capital of the companies carrying out transactions (articles 450 and 452 of the Tax Statute).

2.2. Transactions with companies located in tax havens

2.2.1. Payments to companies located in tax havens

Payments to persons or entities located in countries qualified by the Colombian Government as tax havens may not be treated as expenses or costs by the Colombian entity, unless they have been subject to an income and remittance tax withholding at source.

2.2.2. Legal presumption regarding payments to related parties

There is a legal presumption pursuant to which, unless it can be evidenced that it is not the case, payments made to persons or entities located in tax havens are deemed to be made to economically linked or related parties. Therefore, the provisions regarding transfer pricing are applicable in the case of payments to entities located in tax havens.

2.2.3. Withholding rates

Payments for any concept constituting taxable income for its beneficiary are subject to 35% and 7% withholdings for income and remittance taxes, respectively, when said beneficiary is located in a tax haven.

These rates are not applicable when the payments are made under financial transactions registered with the Colombian Central Bank.

2.2.4. List of tax havens

The Colombian Government must determine the countries considered to be tax havens by means of a Decree. Notwithstanding, this Decree has not yet been issued.

3. Taxpayers responsible for the filing of informative returns

Articles 21 and 22 of Decree 4345 of 2004 establish which taxpayers are responsible for the filing of an informative return, either individual or consolidated.

3.1. Taxpayers who must file an individual informative return

The following taxpayers must file an individual informative return regarding transfer pricing for fiscal year 2004:

- i) Taxpayers having carried out transactions with economically linked or related parties domiciled or residing abroad and:
 - which gross patrimony as of 31st December 2004 is equal or greater than the equivalent of 5,000 minimum monthly legal wages (US\$779,000 approx.); or
 - which gross income as of 31st December 2004 is equal or greater than the equivalent of 3,000 minimum monthly legal wages (US\$467,000 approx.)
- ii) Taxpayers resident or domiciled in Colombia who:
 - Carried out transactions with entities residing or domiciled in tax havens, regardless of whether or not i) above applies.

There is no obligation to file an informative return if there is evidence against the legal presumption contained in paragraph 2 of article 260-6 of the Tax Statute to which reference was made in Section 2.2.2 above.

3.2. Taxpayers who must file a consolidated informative return

The following taxpayers must file a consolidated informative return regarding pricing transfer for fiscal year 2004:

- The parent or controlling entity in the case of subordination, control or entrepreneurial group.

The obligation to file a consolidated informative return must be complied with without prejudice to the obligation in charge of each of the subordinated or controlled entities to file their own individual informative returns.

- All controlling entities, in the case of joint control.

The informative return may be filed by the member of the group designated to that effect, in which case DIAN must be informed of such designation by means of a written document addressed to the Pricing Transfer Group of DIAN.

- The Colombian branch, when the foreign controlling or parent entity has a branch and one or more subsidiaries within Colombian territory.
- The subordinate company with the highest networth as of 31 December 2004, when the foreign controlling or parent entity does not have a branch in Colombia.

These rules will apply in the cases foreseen under Colombian Law as constituting a control situation or an entrepreneurial group.

4. Content of the informative return

4.1. Individual informative return

As per article 2 of Decree 4349 of 2004, the individual informative return must contain the following:

- i) The form set forth by DIAN duly filled in.
- ii) The information necessary for identifying and locating the taxpayer.
- iii) The information necessary for the identification of the economically linked or related parties abroad and/or the persons or entities domiciled or residing in tax havens with which transactions were carried out.
- iv) The information necessary for the identification of the transactions between the taxpayer and the economically linked or related parties and/or the persons or entities domiciled or residing in tax havens during 2004.

- v) The information regarding the methodology used and other factors necessary for determining the prices or return margins.
- vi) The information necessary for determining the situations of economic linkage.
- vii) The liquidation of sanctions, when applicable.
- viii) The signature of the individual complying with the formal requirement of filing the return.

4.2. Consolidated informative return

As per article 4 of Decree 4339 of 2004, the informative return must include a consolidation of all the transactions carried out by the Colombian subordinated or controlled entities with economically linked or related parties from abroad or entities located in tax havens, and must contain the following:

- i) The form set forth by DIAN duly filled in.
- ii) The information necessary for identifying and locating the consolidating taxpayer.
- iii) The information necessary for the identification of the economically linked and related parties abroad and/or the persons or entities domiciled or residing in tax havens with which transactions were carried out.
- iv) The consolidation, by type of transaction, of all the transactions carried out by the entities in a situation of control or of entrepreneurial group with foreign economically linked or related parties and/or entities located in tax havens.
- v) The information necessary for determining the situations of economic linkage.
- vi) The liquidation of sanctions, when applicable.
- vii) The signature of the individual complying with the formal requirement of filing the return.

5. Support documentation

Taxpayers responsible for filing informative returns must:

- Prepare the support documentation necessary for evidencing the adequate application of the regulation on transfer pricing; and
- keep said documentation for a term of 5 years.

Content

This support documentation, which must be prepared in Spanish, must contain the studies, documents and other elements that serve to evidence that the income, costs, deductions and assets and debt involving transactions with economically linked or related parties and/or entities located in tax havens were determined taking into account the prices, economic consideration and return margins that would have applied should the transaction have been carried out between unrelated parties.

In view of the above, the support documentation must contain general and specific information regarding (i) the type of relationship between the parties involved, (ii) the economic aspects and analysis of the transactions, and (iii) the establishment of the agreed prices and margins.

In addition, it must also contain (i) the financial statements, (ii) the agreements and contracts entered into by and between the taxpayer and the economically linked or related parties from abroad and/or entities located in tax havens, and (iii) the market and financial studies and reports, and budgets and forecasts prepared for the relevant fiscal year when there are special situations affecting the transactions subject matter of pricing transfer.

Term

The support documentation corresponding to the transactions carried out during 2004 must be prepared on 30 June 2005, at the latest, and made available to DIAN, when it request so, within the 15 calendar days following the date on which notice of the request is served upon the taxpayer.

Obligation to keep information

The above-mentioned support documentation must be kept for a term of 5 years counted as from the 1st of January of the following fiscal year. This means that the documentation corresponding to transactions carried out during fiscal year 2004 must be kept until 31 December 2009.

6. Anticipated price agreements (APA)

For income tax purposes and, in particular, for the application of regulations on transfer pricing, Colombian taxpayers may enter into APAs with DIAN, including the criteria and methodology to fix the prices, economic consideration and return margins for the transactions carried out with foreign economically linked or related parties.

6.1. Term for requesting the entry into an APA

Interested parties may ask DIAN to execute an APA by submitting to said entity a written request within the first quarter of the relevant year.

6.2. Content of the request

The request for an APA must contain the following information:

- a) Name, tax ID number, country of residence, domicile and address of the taxpayer and of the foreign economically linked or related parties, who would be covered by the APA.
- b) General description of the economic activities performed by the taxpayer filing the request and of its foreign economically linked or related parties with whom the taxpayer will carry out transactions to be included in the purpose of the APA.
- c) Local and international corporate structure, corporate capital and main agreements entered into by and between the related parties involved in the transactions showing the impact thereof on their financial statements.
- d) Description of the content of the proposed APA, including references to each type of transaction to be covered therein, indicating the currency that would be used in the transactions.
- e) Description and justification of the main aspects of the APA.

- f) Detailed explanation of the proposed methodology for transfer pricing, showing its application during the last 3 fiscal years.

6.3. Acceptance or rejection of the request for an APA and effects

Once the request for an APA has been filed, DIAN will have a 9 month term to carry out any necessary analysis and to ask for and receive the relevant amendments and clarifications needed for accepting or rejecting the request.

The APA may become effective for the fiscal year in which it is requested and for the 3 subsequent years, as agreed by the parties.

6.4. Reports regarding compliance with the terms and conditions of the APA

Taxpayers who have entered into an APA with DIAN must submit a report evidencing the compliance of their transfer pricing with the terms and conditions of the APA, simultaneously with the filing of the relevant informative return.

6.5. Term of the application of the legal provisions

The legal provisions regarding APAs contained in Decree 4349 of 2004 will only become effective on 1 January 2006.

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