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GMS Flash Alert

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Colombia - Tax Reform Law Brings Considerable Changes to Taxation of Individuals

Colombia's Law 1819, part of the government's tax reform plan[1], contains provisions on:

- new methods for assessing individual income tax for residents;
- a new income tax structure.

From FY 2017 (returns which will be filed in 2018), income received by individuals should be separated into "baskets" depending on the type of income.

In addition, new progressive tax rates apply for the groups of baskets that differ from the labor income basket.

Moreover, limitations are being imposed upon the amount of deductions and exempt income.

WHY THIS MATTERS

The new provisions will significantly affect the taxation of individuals in Colombia. Global mobility tax professionals, international assignment program managers, and individuals rendering services in the country should take note of the changes, as they will affect individuals' tax burdens and could result in employers experiencing higher international assignment costs.

Consequently, companies that have employees who work in Colombia or that are considering locating staff there will have to take into consideration the potential increased cost of assigning those employees – modifications will need to be made to cost projection systems, and, where employees are sent to or from Colombia, to hypothetical tax calculations as well. Furthermore, where appropriate, payroll administrators should make the appropriate adjustments to payroll withholdings.

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Baskets of Income

From FY 2017 (returns which will be filed in 2018), tax resident individuals' income should be separated into "baskets," depending on the type of income:

(I) Labor income;

(II) Pensions;

(III) Capital income (interests or financial yields, rentals, royalties, etc.);

(IV) Non-labor income (residual basket); and

(V) Dividends.

It is important to mention that the system for taxing capital gains remains – understood as the gain obtained from selling assets owned for two or more years. In this case, a tax rate of 10 percent applies to the gain.

Law 1819 of 2016 eliminates the alternative minimum income tax (*Impuesto Mínimo Alternativo Nacional*, IMAN) and the simplified alternative minimum tax (*Impuesto Mínimo Alternativo Simple*, IMAS).

KPMG NOTE

The taxable base for each basket takes into account the deductions, tax benefits, costs, and expenses allowable for that specific basket. A "net income" will be calculated for each basket, which will be added to net income relating to the other categories (labor + pensions and capital income + non-labor income; and the taxable base for dividends will be only such type of income) in order to determine the income tax liability for each basket.

For the labor income basket, all remuneration, fees, and allowances paid under an employment contract or to an independent worker are treated as taxable income, whether received in cash or in-kind.

Limitation of Tax Reliefs

Although prior tax reliefs were not repealed, a limitation to such reliefs has been introduced. Thus, for example, for the labor income basket, exempt income and deductions cannot exceed 40 percent of net taxable income, and cannot exceed UVT 5,040 (Tax Unit Value, which equals to COP 31,859 for FY17).

On the other hand, under the new rules, the limitation to the reliefs, consisting of deductions and exempt income applicable to the different baskets, cannot exceed 10 percent of the result of subtracting from the total value of income, including deductions, with a limit of UVT 1,000 (see equation below) – the sum of deductions and exempt income cannot exceed 10 percent of the gross income minus costs and deductions.

Exempt income + Deductions = less than 10% * (Gross income – costs and deductions)

There is a problem with the redaction of the provision as it includes deductions as part of the limitation and part of the base to calculate the 10 percent, which we further explain below. This applies for baskets different than labor income.

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KPMG NOTE

There is an inconsistency in the law as redacted; it includes the provision that exempt income and deductions should not exceed 10 percent of net income. The terms could not be not be applied as written, as deductions were already excluded from the taxable base, hence we believe that the limitation could be applied only to exempt income.

Criteria for Determining Liability to File a Colombian Income Tax Return

One of the criteria to determine if a tax resident is required to file a Colombian income tax return is the amount of his purchases by credit card, and the amount of deposits to personal bank accounts. The limit was reduced from UVT 2,800 to UVT 1,400 (each UVT equals to COP 31,859). A taxpayer who exceeds this amount will be liable to file a return.

Tax Rates

The net **labor income** of a person resident in Colombia will be taxed at the same progressive rates applicable before the tax reform, ranging from 0 percent to 33 percent. This is currently the maximum tax rate for residents and is applied on income earned over COP 130,621,900 for the 2017 tax year. Nonresidents are liable to income tax at a flat rate of 35 percent.

Labor Income Tax Table for 2017

Taxable income bracket		Total tax on income below bracket	Tax rate on income in bracket
From COP	**To COP**	**COP**	**Percent**
0	34,726,310	0	0
> 34,726,310	54,160,300	(Taxable base – 34,726,310) x 19%	19
> 54,160,300	130,621,900	(Taxable base – 54,160,300) x 28% + 3,695,644	28
> 130,621,900	Onwards	(Taxable base – 130,621,900) x 33% + 25,104,892	33

It is important to mention that if the income received is classified as **capital income or non-labor**, the following rates will apply:

Capital Income or Non-Labor Income Tax Table for 2017		
From COP	**To**	**Tax rate**
19,115,400	31,859,000	(Taxable base – 19,115,400) x 10%
> 31,859,000	63,718,000	(Taxable base – 31,859,000) x 20% + 1,274,360
> 63,718,000	95,577,000	(Taxable base – 63,718,000) x 30% + 7,646,160
> 95,577,000	127,436,000	(Taxable base – 95,577,000) x 33% + 17,203,860
> 127,436,000	Onwards	(Taxable base – 127,436,000) x 35% + 27,717,330

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However, if the income received is **investment income** (in this event, it is considered as a "dividend"), the tax regime applied would be as indicated below.

First it should be noted who is receiving the dividend, and then how it is distributed (taxed or non-taxed). Below is an illustrative chart:

Beneficiary	**Dividends distributed by Colombian entities as non-taxed**			**Dividends distributed by Colombian entities as taxed**
	From (COP)	**To (COP)**	**Rate**	
Residents for tax purposes	**0**	19,115,400	0%	35% of the amount received, and a 0%, 5%, or 10 % of the remaining amount (*)
	19,115,400	31,859,000	Dividends less COP 19,115,400 * 5%	
	31,859,000		Dividends less COP 31,859,000 * 10% + COP 637,180	
Nonresidents for tax purposes	5% of the payment			35% of the amount received, and 5% of the remaining amount (*)

(*) First the tax of 35% should be paid on the dividends as this is the tax that the entity did not pay, and then the progressive rates should be applied upon the remaining amount.

[COP 1 = EUR 0.00032 | COP 1 = USD 0.000344 | COP 1 = GBP 0.000276 | COP 1 = CNY 0.00237]

FOOTNOTE:

1 Law 1819, *Reforma Tributaria Estructural*, was published on 29 December 2016. See the text of the law (in Spanish) published on the website for Colombia's president.

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