

CHALLENGES IN DETERMINING THE TAX BASE FOR EXTRACTIVE INDUSTRIES

*The use of debt as a financing tool in the
extractive sector in Colombia*

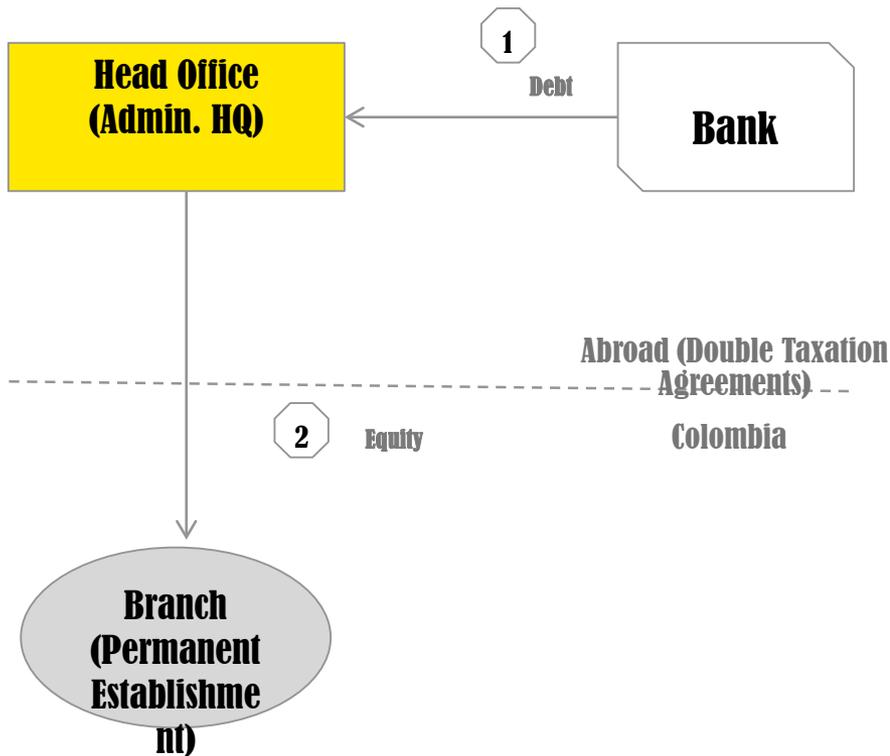
Ricardo Ruiz
Energy Market Leader
Tax Partner



Building a better
working world

Special Exchange Rate Regime (RCE) – Indebtedness acquired abroad

Structure



Accounting

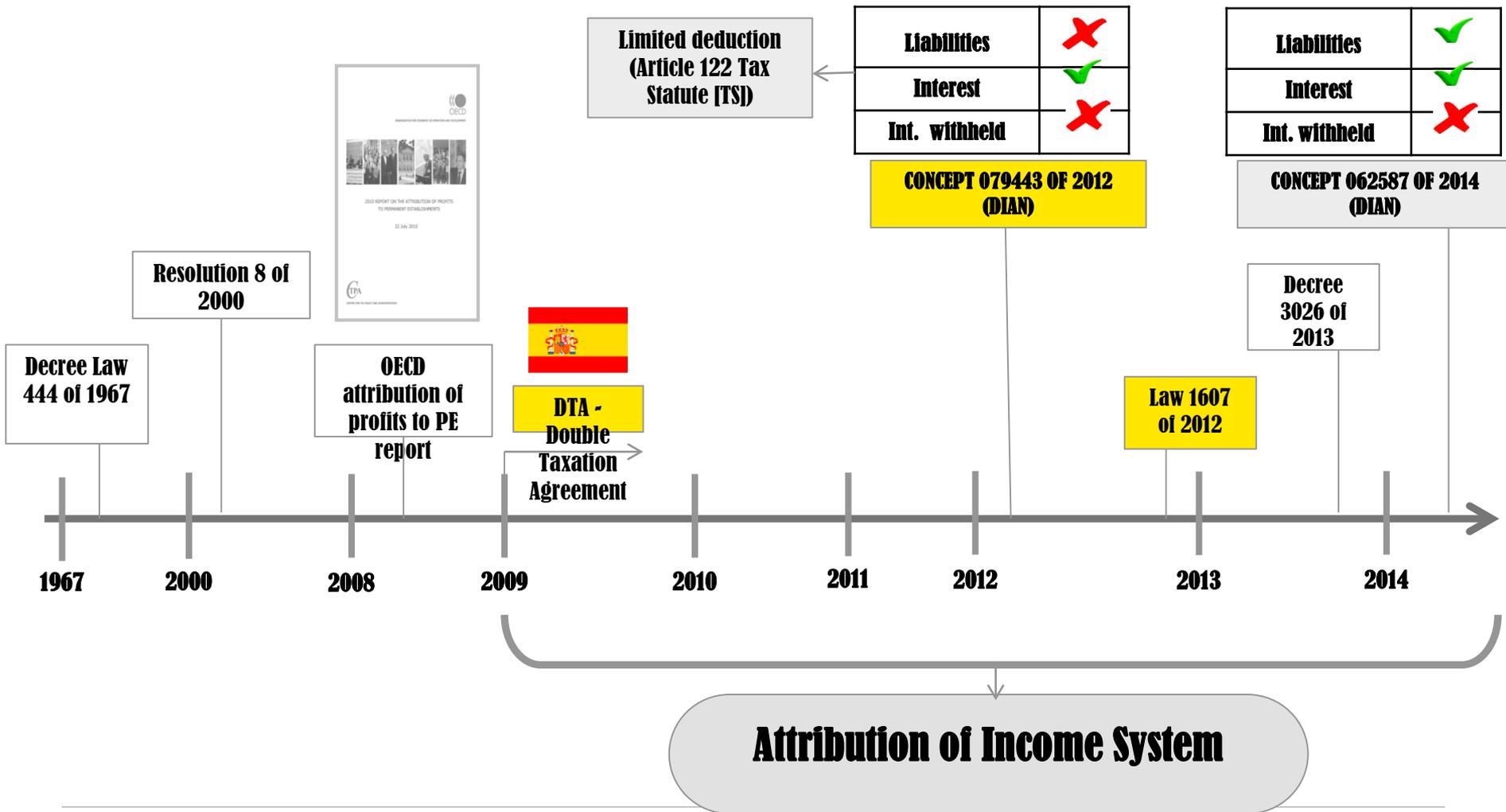
Head Office

| | |
|-----------|-------------|
| Assets | Liabilities |
| | 1000 |
| Net worth | |

Branch

| | |
|--------|--|
| Assets | Liabilities |
| | Net worth - Investment in addition to assigned capital |
| 1000 | |

Changes in indebtedness under the RCE - Milestones



Differences in indebtedness: operating in the sector as a branch v. corporation



Branches RCE - RCO (Special - Ordinary ER regime)

Corporations

- Attribution**
- Free capital**
- Transfer prices (letter a. No. 1. Article 260-4 TS)**
- Undercapitalization (Article 118-1 TS)
- Limit 15% of liquid income (R.L.) (Article 122 TS), Concept 079443/12 DIAN**
- T.P. - Anti Back to Back Rule (Letter e. No. 1. Article 260-1 TS)**
- Tax Haven Rules**

| Liabilities | Interest |
|-------------|----------|
| ✓ | ✓ |
| ✓ | ✓ |
| ✓ | ✓ |
| ✗ | ✓ |
| ✗ | ✓ |
| ✓ | ✓ |
| ✗ | ✓ |

| Liabilities | Interest |
|-------------|----------|
| ✗ | ✗ |
| ✗ | ✗ |
| ✓ | ✓ |
| ✗ | ✓ |
| ✗ | ✗ |
| ✓ | ✓ |
| ✗ | ✓ |

Conclusions and comments

- ▶ **Adoption of the OECD standard (attribution of profit to the PE) has helped ensure that extractive activity using the Special Exchange Rate Regime (RCE) can reflect the tax effects of indebtedness**
- ▶ **Domestic rules interacting with the profit attribution system generate adverse affects on tax paying capacity that need to be reviewed**
- ▶ **How the Double Taxation Agreements signed by Colombia are to be interpreted continues to pose a challenge for the Tax Authorities (with adverse consequences for taxpayers)**
- ▶ **The new standards adopted by Colombia allow plenty of control over debt abuse**