



the global voice of
the legal profession[®]



Doing Business in Latin America
IBA Latin American Regional Forum
October 2018

Colombia



V. Colombia

A. Foreign investment in Latin American countries

i. Authorisations versus limitations or prohibitions

A. GENERAL ABSENCE OF RESTRICTIONS

According to Decree No 1,068 of 2015 ('Decree No 1,068'), foreign investments are allowed in all sectors of the economy, except for the following activities:

- defence and national security; and
- processing and disposal of hazardous or radioactive products not produced in Colombia.

The Colombian FX regime is divided into two markets: (1) the FX market; and (2) the free market.

The FX market consists of all FX transactions that must be completed through: (1) authorised FX intermediaries; or (2) compensation accounts (foreign bank accounts registered with the Colombian Central Bank and subject to periodic reports). Because FX transactions must be completed entirely through the FX market, they cannot be offset or condoned, in principle.

Pursuant to Regulation 1 of 2018 issued by the Colombian Central Bank ('Regulation 1'), the following transactions are deemed regulated FX transactions and thus must be registered in a timely manner before the Colombian Central Bank: (1) import and export of goods; (2) foreign indebtedness operations; (3) foreign investments; (4) guarantees and collateral in foreign currency; and (5) derivatives transactions.

The FX market is strictly regulated by the Colombian Central Bank, and its compliance is jointly supervised by the Superintendence of Companies, the Finance Superintendence and the Tax Authority. Failure to duly conduct FX transactions through the FX market is a violation to applicable regulations and may result in the imposition of fines.

Please note that foreign investments that are duly registered with the Colombian Central Bank confer foreign investors the right to: (1) remit abroad or repatriate proven net profits generated by the relevant investment; (2) reinvest profits or retain them as surplus undistributed profits; (3) capitalise amounts with remittance rights and finally, to remit them abroad; and (4) remit any income received from purchasing the investment in Colombia, from liquidating the company receiving the investment, or from reducing its capital.

Moreover, investment repatriation conditions are those in force on the date on which investments are registered and may not be modified in any way that may be detrimental to the foreign investor, except on a temporary basis when Colombia's international reserves fall below the equivalent of three months' worth of imports.

B. DEFINITION OF FOREIGN INVESTMENT

Article 2.17.2.2.1.2. of Decree No 1,068 defines direct foreign investment as: (1) any contributions and/or participation in the capital of a Colombian company; (2) investments in trusts; (3) acquisition of real estate; (4) contributions in kind, subject to specific restrictions and registration procedures; (5) initial or supplementary investment in the assigned capital of a local branch of a foreign company; and (6) investment in private equity funds.

Furthermore, portfolio investment is defined as any investment in securities registered in the National Securities and Issuers Registry (Registro Nacional de Valores y Emisores).

C. NATIONAL, FAIR AND EQUITABLE TREATMENT

Pursuant to Decree No 1,068, foreign investors shall be treated equally vis-à-vis Colombian investors. This represents a guiding principle set forth in Colombian FX regulations.

D. FREE CHOICE OF LAW AND JURISDICTION

As a general rule, Colombia's legal system adopts the principle of International Private Law of *lex loci solutionis*. This principle states that the applicable law to any contract is the law of the place of its performance. Particularly, Article 869 of the Code of Commerce, states that agreements executed abroad but performed in Colombia are governed by Colombian law. Also, it is generally accepted that *dépeçage* operates under Colombian law, therefore if the obligations under a contract are to be performed in different places, each obligation shall be governed by the law of the place of its performance.

Consequently, there is no private free will regarding the applicable law to contracts performed in Colombia, considering that the *lex loci solutionis* principle is mandatory. Nonetheless, it has been generally accepted that, exceptionally, the parties may choose a different substantive law if they have validly agreed to international arbitration, regardless of the place of performance of the agreement.

Pursuant to international arbitration, Law No 1,563 of 2012 ('Law No 1,563') states that the parties to a contract that provides for disputes arising thereunder to be resolved by international arbitration are entitled to choose a foreign law as the governing law of the contract. Therefore, the parties to a contract may agree on a foreign substantive governing law, provided the agreement is included in an international arbitration clause.

According to said law, arbitration is considered to be 'international' when there is an international element. If the parties, at the time of entering into the arbitration agreement, are domiciled in different countries or if the place of performance of the substantial part of the contractual obligations directly related to the subject matter of the controversy is located outside the country in which the parties have their principal domicile, it is understood that the international element is met.

Therefore, parties may agree to international arbitration with a foreign choice of law if one of the following conditions has been met: (1) the parties to have their domiciles in different countries; (2) a substantial part of the obligations of the agreement is to be performed outside of the country in which the parties have their principal domicile; or (3) the dispute affects international commerce or trade interests.

As previously mentioned, foreign investments in Colombia are generally permitted in all sectors of the local economy (except for those referred to above), and no additional permits are required from the FX perspective.

Notwithstanding, foreign investment in Colombian financial institutions is subject to the prior authorisation of the Financial Superintendent of Colombia.

ii. Treatment of foreign investment in infrastructure initiatives and PPP projects

During recent years, there has been a significant development in infrastructure matters in Colombia, particularly due to the enactment of the PPP legal framework, that is, Law No 1508 of 2012, Law No 1682 of 2013, Law No 1882 of 2018 and all their regulatory decrees. These laws seek to attract foreign investors in the infrastructure field, in order to contribute to the development of the country in areas where it is urgently needed.

During 2012, the Colombian Government launched an ambitious infrastructure project called the fourth-generation of road concession contracts ('4G'), which comprises 42 projects aiming to build roads of approximately 8,000 kilometres (4,970 miles) long and requires investment in the order of US\$24.4bn. The 4G roads are now in the construction phase and facing environmental, social and financial challenges that may prove the strength of certain Colombian institutions (eg, the Attorney General's Office and the Superintendence of Industry and Commerce), and may also test the suitability of the legal framework in order to achieve the successful completion of current and future projects.

In this regard, for the purpose of attracting first-tier international contractors and investors to the 4G projects, the Colombian Government developed a series of incentive policies or measures, which are summarised as follows:

On 10 January 2012, the Colombian Congress enacted Law No 1508 (the 'PPP Law'). This law comprises a series of elements that are typical in traditional project financing arrangements that are intended to establish basic principles to contribute to the bankability of those infrastructure projects that are to be developed under a PPP model.

The PPP Law includes elements typical in traditional project financing structures that are intended to provide comfort for lenders. As an example, this law requires that the project's resources must be administered through a trust fund, to which all assets and liabilities of the project must be transferred. This requirement provides greater reassurance to lenders with respect to outstanding payments and enforceability of any security interests. Likewise, the PPP Law expressly confers project lenders step-in rights in the event of default under the applicable loan agreement. Additionally, the PPP Law requires that any PPP contract must include an early termination payment that should be determined by a formula, which serves as additional security for lenders as an instrument to effectively cover the debt service obligations of the concessionaire under the financing agreements if the contract is terminated early. These provisions constitute important legislative developments that significantly improve lenders' comfort and encourage them to finance projects to an internationally commercial standard and in a cost-efficient manner.

In addition to the foregoing, during 2013, the Colombian Congress enacted Law No 1,682 (the 'Infrastructure Law'). This law provides mechanisms to solve the major bottlenecks that infrastructure projects in Colombia have encountered in the past, which are those related to the acquisition of legal rights over the land required to develop the project, obtaining environmental licences, and the removal and/or relocation of utilities networks and related infrastructure affected by the construction of the works.

For the purposes of dimensioning the impact of the aforementioned bottlenecks and highlighting the importance of Law No 1682 of 2013, a survey undertaken by the Colombian National Planning Department (Departamento de Planeación Nacional) concluded that 53 strategic national infrastructure projects have issues related to said bottlenecks as follows: 80 per cent have issues regarding environmental permits and 23 per cent are encountering problems pertaining to land acquisition.

According to the Colombian Government, with the enactment of Law No 1682 of 2013, the time to complete land acquisition activities required by an infrastructure project is expected to have a 50 per cent reduction by the implementation of, among others, the following measures: (1) setting out the obligation of the court to force the tenant or owner to deliver the land required to execute the infrastructure project as from the filing of the corresponding expropriation law suit and not at the end of the expropriation process when the indemnification to the tenant or owner is established; (2) providing a clear set of rules regarding land appraisal; and (3) reducing the timeframes set forth to exhaust the steps and requirements in the land acquisition process from the direct negotiation to the expropriation ruling.

On the other hand, aiming to expedite the process for obtaining an environmental licence for an infrastructure project, Law No 1682 of 2013 provides different mechanisms, such as establishing that environmental authorities are to be held liable for the damages suffered by third parties if the authority fails to comply with the term to issue environmental licences as set forth by environmental law; establishing that projects that entail maintenance, improvement and rehabilitation works do not require an environmental licence; and providing that minor modifications to the project during the execution of the works do not require a modification to the environmental licence previously approved for the project.

Finally, with respect to the relocation of public utility networks, Law No 1682 of 2013 includes a clear set of rules regarding which party (ie, project company or owner of the network) is responsible to bear the removal or relocation costs, and provides that, in the event the owner of the networks fails to initiate the relocation works in a given period of time, the Concessionaire is entitled to directly undertake the relocation works. In line with the foregoing, the Colombian Government has amended the specific regulation dealing with the proceeding for obtaining environmental licences, which is expected to have a positive impact on project development in general.

The significant number of PPP projects that have been awarded and structured indicates that Colombia will significantly increase its investment in infrastructure. This scenario entails an opportunity to reinforce and improve the new but solid legal framework in this field, as well as the capabilities of Colombia's public institutions to supervise the projects while managing potential crises.

In this regard, the enactment of Law No 1882 of 2018 represents an improvement in the Colombian public procurement system, introducing mandatory provisions regarding transparency, competition,

efficiency and specific rules of procedure for events whose regulation was unclear until now. Moreover, Law No 1882 provides further solutions and regulation for issues that are considered to cause bottlenecks for projects currently underway regarding land management and environmental permits. The new law also seeks to overcome the standstill in project financing as a result of corruption scandals by means of adopting provisions to assure investors that their investments are safe in the event of unlawful conduct of the other agents involved in the projects.

In addition, the recently enacted Law No 1882 of 2018 provides the option to pay the concessionaire with real estate rights over properties that are not necessary in the provision of the utility associated with the infrastructure. Furthermore, Law No 1882 broadens the projects in which it is possible to set functional units, including airports, water treatment facilities, tunnels and railways, hence facilitating the remuneration of the works performed therein. Regarding territorial entities, Law No 1882 repeals the restriction that prevented districts and capital cities of the departments from executing PPP agreements in the respective local government's last year of administration. This provision will allow local administrations to move forward with several projects that are currently being structured.

A. PARTICIPATION OF FOREIGN BIDDERS

In order to determine the role that the foreign investors play and the status that the Colombian legal framework gives to these investors in comparison with Colombian investors, it is important to establish that Colombian public procurement law sets forth a reciprocity principle that allows foreign bidders to participate in public procurement to execute contracts with state entities in Colombia under the same conditions as a Colombian bidder may participate in procurement procedures in the foreign bidder's origin country. Additionally, the requirements in terms of experience, financial and legal capacity are included in the terms of reference or requests for proposals issued by the contracting entity, creating a scenario where both types of investors participate under the same conditions.

The Public Procurement Statute provides many possibilities for participating in public procurement in Colombia. Both national and foreign individuals and companies, with or without domicile or a branch in Colombia, are allowed to participate in these bidding processes, provided they comply with the particular requirements set forth in the corresponding request for proposal. Pursuant to Law No 816 of 2003 and its regulatory decrees, foreign entities are allowed to participate in government bidding proceedings on equal basis with offers submitted by Colombian nationals when:

- a free-trade agreement so provides;
- Colombian offers are treated as national in foreign jurisdictions; and
- the corresponding bidder is a member of the Andean Community of Nations.

Furthermore, it is important to establish the modalities by which foreign companies or individuals may participate in Colombian procurement procedures, as follows:

1. Direct participation

Foreign individuals or companies that do not have a branch in Colombia are allowed to participate directly in the public entities' procurement procedures by submitting the documentation required

by the terms of reference. In this case, if the foreign bidder is awarded with the contract and its contractual obligations entail the development of permanent activities in Colombia, the bidder must open a branch before beginning to perform its obligations under the awarded contract.

2. Through a branch

Foreign bidders are able to participate in procurement procedures through a branch registered in Colombia. Bearing in mind that the branch is not a separate legal entity, it is possible for it to credit the experience, financial capacity, technical capacity and organisational capacity of the parent company.

3. Through a subsidiary

Foreign bidders may already have a Colombian subsidiary of their companies, usually with the purpose of participating in public procurement through a special purpose vehicle, which allows them to separate liabilities. However, by adopting this method, and depending on the terms of reference of each particular procurement procedure, they may or may not be allowed to credit their experience, technical capacity and/or organisation capacity with the experience of their parent companies, given that a subsidiary is a different legal person from its parent company.

Additionally, the Public Procurement Statute has provided various ways for investors to associate and present a joint proposal by using one of the following associative forms: (1) consortiums; (2) temporary unions (*uniones temporales*); and (3) promises of establishment of future companies. A distinctive feature of these associative forms is that all the members thereof shall be jointly liable with respect to the liabilities arising from the submitted offer and the contract, if awarded. In the case of consortiums and temporary unions, once awarded with the contract, no separate legal entity is incorporated, while when the selected form of association is the promise to incorporate a company, the company must be incorporated prior to the execution of the awarded contract.

iii. Treatment of foreign investment in oil and gas and mining activities

In accordance with Article 332 of the Colombian Constitution, in Colombia, ownership of the subsoil and non-renewable natural resources belongs to the state. The said disposition sets forth that all natural hydrocarbons and mineral reservoirs in existence within the Colombian territory, whatever their nature may be, including those inside national boundaries and under the territorial seabed, the continental platform and in the exclusive economic zone belong exclusively to the Republic of Colombia.

In that sense, the exploration and exploitation of minerals require the awarding of a mining title, materialised through the execution of a concession contract granting the contractor the right to explore the subsoil seeking for particular minerals and exploit them for a certain period of time. Concession contracts are granted by the Mining National Agency (Agencia Nacional de Minería (ANM)), the entity in charge of the management of mineral resources. The concession contract shall be registered at the National Mining Registry (Registro Minero Nacional) to be valid and enforceable.

On the other hand, as from 1 January 2004, pursuant to Decree No 1,760 of 2003 (as amended by Decree Nos 2,394 of 2003, 409 of 2006 and 4,137 of 2011), in order to carry out the exploration and

exploitation of hydrocarbons in Colombia, both onshore and offshore, a contract shall be executed with the National Hydrocarbons Agency (Agencia Nacional de Hidrocarburos (ANH)) in the form of an exploration and production (E&P) contract or technical evaluation agreement (TEA).

According to Decree No 381 of 2012 (as amended by Decree Nos 1,617 and 2,881 of 2013), the MME is vested with the power and authority to administer the non-renewable resources belonging to the state. Notwithstanding the above, the MME has delegated such power for the management of mining matters to the ANM, as well as to certain territorial entities, and for the management of oil and gas matters to the ANH. Both agencies are national public entities ascribed to the MME having its main seat in the city of Bogotá, DC.

A. REGULATORY BODIES

1. National Hydrocarbons Agency (ANH)

The ANH is the regulatory body responsible for the Colombian crude oil industry. In particular, the ANH is responsible for managing hydrocarbons resources and defining the contracting policy for the exploration and exploitation of hydrocarbons.

By means of Decree No 1,760 of 2003 (as amended by Decree Nos 2,394 of 2003, 409 of 2006 and 4,137 of 2011) the management and control of Colombian hydrocarbon resources were transferred from the state-owned company, Ecopetrol, to the ANH. Ecopetrol conducted its E&P business through several types of contractual forms with the Colombian Government or third parties, where the most significant is the association contract, whose purpose is the E&P of hydrocarbons.

2. National Mining Agency (ANM)

The ANM is the regulatory body responsible for the Colombian mining industry. The ANM is responsible for managing Colombian mining resources and defining the contracting policy for its exploration and exploitation.

Decree No 4,134 of 2011 establishes the faculties, responsibilities and duties in charge of the ANM, as the governmental entity in charge of managing Colombia's mining resources.

It is important to note that certain territorial entities in Colombia have been vested in the past with the authority to grant mining titles (ie, Antioquia, Bolívar, Boyacá, Caldas, Cesar and Norte de Santander). Nevertheless, currently, the only department that still holds the power to grant and monitor mining titles is the department of Antioquia through its Secretary of Mines.

3. The Ministry of Mines and Energy (MME)

The MME is the governmental entity responsible for the management and regulation of mines and the energy economic sector (including hydrocarbons and mining sector). This entity is empowered to adopt and execute policies, guidelines and technical regulations related to hydrocarbons and mining activities.

4. The Ministry of Environment and Sustainable Development (the 'Ministry of Environment')

The Ministry of Environment is a branch of the executive power in charge of managing the environment and renewable natural resources, and is responsible for guiding and issuing environmental planning and development policies and regulations.

5. National Authority of Environmental Licensing (Autoridad Nacional de Licencias Ambientales (ANLA))

The ANLA is a specialised administrative unit in charge of granting environmental licences to large-scale projects, including those of the oil and gas, and mining sector. The ANLA is in charge of granting environmental licences to the activities listed in Article 2.2.2.3.2.2 of Decree No 1,076 of 2015 on environmental licensing (projects that are considered of national importance or may cause severe environmental impact due to their magnitude). The ANLA also surveils projects, works or activities subject to environmental licences in order to ensure that said projects effectively comply with the environmental regulation currently in force.

B. DEVELOPMENT OF OIL AND GAS ACTIVITIES

Oil and gas activities are mainly regulated in the Colombian Petroleum Code set forth in Decree No 1,056 of 1953 (as amended), which declares the petroleum industry and its activities of exploration, exploitation, refinement and transport as of public utility (*utilidad pública e interés social*); Decree No 1,073 of 2015; and the administrative regulations issued by the MME and ANH, including a set of agreements (*acuerdos*) issued by the ANH to regulate the execution of activities by contractors and the process to allocated areas for the execution of said activities.

Under Colombian laws: (1) E&P contracts shall be governed by Colombian law and subject to the jurisdiction of Colombian courts; and (2) foreign companies must establish a Colombian branch domiciled in Bogotá, DC in order to enter into contracts in the hydrocarbons sector and perform exploration and exploitation activities in Colombia.

1. Contractual regime

In accordance with the existent regulations (ANH Agreement 2 of 2017), the exploration and exploitation of hydrocarbons owned by the state can be carried out by private investors through one of the following contractual structures:

The purpose of a technical evaluation agreement (TEA) is to allow the investor to evaluate an area of interest in order to determine its production potential. Said contract consists of evaluation activities related to geology, geophysics, geochemical, cartography, phonology, surface exploration activities and stratigraphic well drilling, among others, excluding exploration drilling. Part of the areas covered by TEA may be converted into an E&P contract upon the contractor's request to ANH.

The purpose of an E&P agreement is to grant the contractor the right to explore the subsoil seeking hydrocarbon reserves and exploit them for a determined period of time. The E&P contract consists

of four² phases: preliminary, exploration, evaluation and exploitation. The preliminary phase has a term of 24 months, and its purpose is to confirm the presence of ethnic communities in the area of the project and, if applicable, perform prior consultation processes. The exploration phase has a term of six years and is normally divided into yearly exploratory phases. Once a discovery is made, the area enters into a two-year evaluation programme to determine the commercial potential of the discovery. After said evaluation, the contractor shall inform the ANH of its decision on whether to commercially exploit the discovery. The production phase is usually of up to 24 years and is extendable for a similar term or up to the commercial economic limit of the field. Special terms have been set for the development of activities in unconventional reservoirs and offshore activities, including increasing the exploration and production periods as follows: the exploration period increased to nine years and the production period increased to 30 years.

Special agreements are exploration and/or exploitation agreements with special characteristics set forth by the Board of Directors of the ANH depending on the technological advancements and new developments of the sector with respect to exploration, operation, production, incremental production, shared production and utilities.

2. Awarding of areas

The terms of the allocation of areas for exploration and exploitation of hydrocarbons through E&P contracts are regulated by means of Agreement 2 of 2017 of the ANH. In this respect, the awarding of areas for the exploration and exploitation of hydrocarbons shall be made through one of the following processes:

- i. Open competitive bidding process (generally named rounds (*rondas*)): Pursuant to an open competitive process, ANH awards based on certain capacity requirements set out in the relevant Terms of Reference issued for each open competitive bidding process. Currently, open competitive bidding processes are the most common processes for awarding hydrocarbon areas. Several rounds have taken place since 2004, totaling 262 E&P contracts and 14 TEA currently in force as of December 2017. Among those are the Ronda Caribe 2007 with nine contracts, MiniRonda 2007 with 12 contracts, Heavy Oil process with eight contracts, Ronda Colombia 2008 with 22 contracts, Mini Ronda 2008 with 41 contracts, Ronda Colombia 2010 with 68 contracts, Ronda Colombia 2012 with 50 contracts allocated and finally, Ronda Colombia 2014 with 26 contracts allocated (see Resultados, Retos y Estrategias de Crecimiento del Sector de Hidrocarburos, ANH 2015). In 2017, the ANH launched a competitive bidding process for 15 areas located in the Sinu San Jacinto sedimentary basin for which six companies qualified. The process is ongoing.

The qualification criteria are determined in each open competitive process in accordance with the provisions of Agreement 2 of 2017.

The particular steps and requirements for the participation in the corresponding open competitive processes are provided in the relevant Terms of Reference issued by the ANH for each process.

² As of May 2017, ANH included a preliminary phase in E&P contracts. Some contracts executed as a result of Ronda Colombia 2014 also include a preliminary phase.

- ii. Permanent competitive bidding process: ANH Agreement 2 of 2017 introduced a permanent competitive bidding process by means of which the ANH will select areas over which proposals will be received at any time, without the need of launching specific bidding procedures for their allocation. Once the ANH receives a proposal over a selected area, it will make public such proposal and invite the public to compete for its allocation.
- iii. Closed competitive bidding process or invitation: In the closed competitive process, the ANH will invite a pre-established group of companies that meet certain capacity requirements to submit a proposal. Then the ANH will initiate the negotiation process with the bidder that has a satisfactory contracting proposal.
- iv. Direct assignment: Finally, for the direct assignment of the corresponding contract for hydrocarbon exploration and exploitation, prior authorisation from the board of directors of the ANH is required. Please note that the ANH will exceptionally allocate areas that have been specially selected for said purpose in accordance with the following conditions:
 - special nature and geographical localisation;
 - social and/or environmental restraints of the area;
 - limited technical information about the subsoil or required exploratory study;
 - for purposes of public interest, national security or public order; and
 - special considerations on energy and economic policies.

Stakeholders Registry: ANH Agreement 2 of 2017 also created a Stakeholders Registry (Registro de Interesados) as a prequalification tool of companies willing to participate and develop oil and gas activities in Colombia. Companies will have to accredit their technical, financial, corporate social responsibility, environmental and legal capacity based on the terms of ANH Agreement 2 in order to be registered in the Stakeholders Registry and update the registry annually.

3. Obligations of the contractor

Once the corresponding contract is granted, the contractor shall comply with the obligations resulting from the contracts and the relevant regulations. The following are the main obligations applicable to E&P contracts:

Payment of surface fees: The contractor shall pay an annual fee for the exclusive right to use the subsoil for evaluation, exploration and production of the relevant hydrocarbon deposit under the corresponding E&P contract or TEA. In the exploration period and during the evaluation period, the fee is based on US dollar fee per hectare, which varies depending on the location of the area (onshore, offshore with less than 1,000 metres in depth and offshore with more than 1,000 metres in depth). During the production period, the fee is based on a US dollar fee per barrel of crude oil or cubic fee of natural gas.

Payment of royalties: The contractor shall pay royalties consisting of between eight per cent and 25 per cent of the daily gross production based on the monthly average of hydrocarbon production

under the relevant E&P contract. The royalty is reduced by 20 per cent for onshore gas fields and offshore gas fields at depths less than or equal to 1,000 ft, and by 40 per cent for offshore gas fields at depths greater than 1,000 ft and for unconventional hydrocarbon deposits.

High prices fee (windfall profit): Under certain E&P contracts, the contractor must pay to the ANH a fee for 'high prices', when a certain production level is reached and the international prices exceed a base price, which represents between 30 per cent and 50 per cent of the production calculated in accordance with a set formula.

Environmental and labour bonds and guarantees: Under the corresponding E&P contract, the contractor is obliged to grant guarantees to cover labour and environmental liabilities in the execution of activities.

Proper performance guarantee: Under the corresponding E&P contract, the contractor shall grant a guarantee for the performance of each phase of the corresponding contract.

Civil liability guarantee: Under the corresponding E&P contract, the contractor shall grant a guarantee to cover contractual damages arising out of the execution of activities.

Creation of the abandonment fund: Under the corresponding E&P contract, the contractor must establish a fund to guarantee the financing of the required activities to perform the abandonment programme of the wells and the environmental restitution of the assigned areas for the production at the end of the production period.

Transfer of technology: Under the corresponding E&P contract, the contractor agrees to perform certain scientific and technological activities, whose objectives, terms, conditions and beneficiaries are determined by the ANH during the term of the contract.

Interest over production (X factor): If an E&P contract is awarded through a bid process, the contractor must pay to the ANH, in cash or in kind, the so-called X-factor, which is the percentage of gross production after royalties offered by the contractor during the bidding process.

Additional interest over production: In the event of extensions to the production phase, the contractor is obliged to pay to the ANH, in cash or in kind, a percentage of gross production after royalties equivalent to ten per cent of the base production of conventional hydrocarbons or five per cent of the base production of unconventional hydrocarbons, natural gas, heavy crude oil and offshore reservoirs.

C. DEVELOPMENT OF MINING ACTIVITIES

Law No 685 of 2001 (the 'Mining Code'), the law currently in force for the awarding of mining areas and mining titles, establishes the concession contract as the only valid mining title.

However, said new form of contracting through the concession agreement does not impact preexisting mining titles (licences, *aportes* and concessions), which shall continue to be in force until their expiration.

The term for concession contracts is 30 years counted from their registration in the National Mining Registry, divided into the following phases:

- exploration: three years (extendable for additional periods of two years up to 11 years);
- construction and assembly: three years (extendable for one additional year); and
- exploitation: 24 years (extendable for 30 additional years).

As per Colombian law, foreign individuals and corporations that are mining concessionaires have the same rights as Colombian individuals and corporations. Thus, Colombian Governmental regulatory bodies shall not request any additional or different requirements from such foreign parties.

The sole particular requirement, specifically established for foreign companies, is to incorporate a branch, subsidiary or affiliate in Colombia to be the titleholder of the mining concession.

In general terms, to protect and preserve the rights of applicants in accordance with the time and date of the application for the concession contract before the mining authority, Colombian mining law applies the principle 'first in time, first in right'. Nevertheless, there are certain areas that can be temporarily or permanently excluded from the areas to be granted in concession. These areas are:

- special reserve areas: areas where informal and traditional mining activities are developed or areas for the development of a high-scale mining project;
- national security areas: areas with respect to which the Colombian Government determines that mining activities are not permitted for security reasons;
- excluded areas: areas that have been legally declared and bordered as protected zones for the development and protection of renewable natural resources and the environment;
- restricted mining zones: areas that allow mining activities under certain restrictions; and
- areas reserved for formalisation purposes: areas that are reserved for the formalisation of small mines.

However, Law Nos 1450 of 2011 and 1753 of 2015 created Strategic Mining Reserve Areas and Areas for Mining-energy Development, which are areas that must be granted through competitive bidding procedures after their delimitation and declaration. These are areas with a high potential for strategic minerals³ that are reserved in order to allow an organised management of non-renewable natural resources.

Therefore, in Colombia, mining titles may be acquired through three main mechanisms:

- concession contracts granted by the mining authority prior to the request of the interested party;
- concession contracts for strategic mining areas through public bidding; and
- total or partial transfer of concession rights, which requires prior approval from the ANM.

Once the concession contract is granted, duly executed and registered in the National Mining Registry, the concessionaire shall comply with all the obligations derived from Mining Code and the relevant concession contract. Particularly, it is important to indicate that said obligations depend on each stage or phase of the concession contract. Below are the main obligations that shall be complied with by the concessionaire under corresponding mining concession contracts:

³ Resolution 180,102 of 2012 of the MME. The following are the strategic minerals for Colombia: (1) gold; (2) platinum; (3) copper; (4) phosphates; (5) potassium; (6) magnesium; (7) coal; (8) uranium; (9) iron; and (10) niobium and tantalum (also known as coltan) and/or black or industrial sands.

1. Mining environmental insurance policy

The concessionaire shall obtain a mining environmental insurance policy that covers compliance with environmental mining obligations, the payment of potential fines and the consequences of an eventual early termination by the ANM of the mining title.

2. Payment of a surface fee

The concessionaire must pay a surface fee in order to undertake exploration activities in the concession area during the exploration, assembling, construction and exploitation periods.

3. Payments of royalties

The concessionaire shall pay royalties, which consist of a percentage, fixed or progressive, of the exploited gross product, and its sub-products, calculated or measured on the mine head, payable in currency or in kind, as established in the relevant law.

4. Recent developments

It is also important to mention two recent developments that have impacted the development of mining activities in Colombia.

Per recent rulings of the Constitutional Court and the Council of State, the ANM must *reach agreements* through consultation processes with local governments on the execution of mining activities in the territory prior to the granting of any mining title. Such consultation agreements shall consider the protection of the environment and the economic, social and cultural development of citizens.

Through the consultation, the ANM and local governments jointly determine areas of the territory that are compatible with mining activities based on an analysis of the following items: (1) overlap in areas in which mining is excluded by law; (2) overlap in areas in which mining is restricted by law; (3) overlaps with other environmental limitations; (4) overlaps with other mining areas; (5) overlaps with different uses of land set forth by the land planning instrument currently in force; and (6) mining potential in the area.

After an agreement has been reached, the ANM and the mayor of the municipality execute consultation minutes summarising the commitments of both the ANM and the local government. The minutes are then included in all concession agreements granted in the territory of the municipality as an obligation and guideline for grantees of those concessions.

On the other hand, and pursuant to Article 259⁴ of the Mining Code, the ANM has devised a process of public hearings with local communities to take place before a mining title is granted, and after the consultation process with local governments has taken place and a consultation agreement has been reached. The purpose of this process is to provide information to citizens, community leaders and concerned groups in a given territory about existing mining title proposals in their territory, and to guarantee the exercise of effective participation rights in the process of granting a mining title.

⁴ See Article 259. When the participation of third parties, community representatives and social groups in the concession agreement granting procedure is required, the invitation to participate shall be sent in an effective way, within the terms set forth by law and through appropriate means.

As a result of this public hearing, minutes are recorded and become part of the concession contract, with the purpose of being the first initiative of the Social Management Plan (Plan de Gestión Social) of the mining contract. In this sense, the public hearing reaffirms the proponents' commitment to work with the community and contribute to its development through mining activity.

As of the end of June 2018, 38 public hearings have been held by the ANM in nine departments.

D. COLOMBIAN SOCIO-ENVIRONMENTAL REGIME

In Colombia, any project, work and/or activity that involves the use of natural renewable resources and/or that may affect the environment, will require the interested individual/company (the 'beneficiary') to request and obtain before environmental authorities (either national, regional or district) the environmental licences, concessions, permits and/or authorisations (the 'control instruments'), prior to the execution of the corresponding project.

Moreover, the Colombian Constitution defines Colombia as a multicultural state in which several ethnicities coexist. Particularly important are indigenous and afro-descendant communities because they have special protection according to Colombian legislation currently in force, and the right to prior consultation. Apart from ethnically differentiated communities, other social actors are also entitled to actively participate in the environmental procedures aimed at granting environmental permits and licences, and shall also be considered as an integral part of any mining, and oil and gas projects.

In Colombia, the key administrative instrument for the preservation of the environment and for controlling the use and exploitation of natural resources (the control instrument) is the Environmental Licence. This control instrument is regulated essentially by Law No 99 of 1993 and Decree No 1,076 of 2015.

The Environmental Licence shall only be applicable to those projects or activities that may imply serious deterioration of natural renewable resources, or that have the capacity to introduce considerable modifications to the landscape. Please note that in Colombia, said activities are limited and clearly defined in Articles 2.2.2.3.2.2 and 2.2.2.3.2.3 of Decree No 1,076 of 2015, which means that the Environmental Licence shall only apply to those activities that are effectively listed.

iv. Treatment of foreign investment in real estate (rural and urban properties)

When acquiring real estate property in Colombia, a foreign investor must consider that: (1) Colombia protects private property, considering that by means of the Constitution, legally acquired ownership rights cannot be affected by ulterior laws; (2) both nationals and foreigners have, in principle, equal rights concerning the acquisition of real estate property; and (3) the use for a specific activity must be in compliance with the corresponding zoning dispositions. Therefore, all regulations regarding foreign investment in real estate property is subject to the dispositions and procedures set forth in Section C below.

v. *Treatment of foreign investment in the rendering of public services*

A. A GENERAL LEGAL FRAMEWORK

From the enactment of the Constitution of 1991, the privatisation of public utilities started in Colombia, allowing private parties to initiate the provision of public utilities under a free market scheme, subject to strict regulation.

Under the Constitution, the Colombian Government, although responsible for ensuring the provision of domiciliary public utilities, was instated with the power to supervise and regulate public utilities rather than operate the provision of such services. Prior to 1991, the Colombian Government either provided public utilities directly through specialised providers or granted concessions to private parties to provide such services.

In this regard, the Colombian Government has significant powers to dictate policy, and monitor and regulate public utility companies in order to ensure the continued availability of public utilities.

In Colombia, unlike several other jurisdictions, the telecommunications sector and public utility provision sectors differ in several ways. Therefore, for the purpose of the present document, it is important to bear in mind that we will address the following public utility services: electricity, gas, water, sewage and solid waste management.

There are two main structural laws that compose the public utility sector. The first, Law No 142 of 1994, established the overall general market structure defined by Congress for the provision of public utilities. In addition, Law No 143 of 1994, a special law regulating the electricity and gas sectors, established additional rules and incorporated additional regulations solely applicable for the previously mentioned sectors. In this regard, Law No 143 of 1994 is specially applied – compared with Law No 142 of 1994 – when analysing matters applicable to the electricity and gas sectors.

Under the aforementioned laws, utilities providers, consumers and other market participants operate under a uniform set of rules guided by principles of efficiency, quality, improved service coverage, financial sustainability, and fair and equitable participation regardless of government affiliation.

The current legal and regulatory regime promotes competition for the benefit of consumers in areas such as pricing, quality and coverage. Government entities and government-owned entities that provide public utility services must ensure that they remain competitive in these areas, without solely relying on their dominant position.

B. FOREIGN INVESTMENT IN PUBLIC UTILITIES

Colombia's public utility sector provides multiple business opportunities for local and foreign investors. Although it is a strongly regulated sector, our strong legal and administrative structure facilitates the incorporation of public utility companies by any agent – either foreign or national – in the sector. There are no restrictions for foreign investors to participate in the provision of public utilities as shareholders of public utility companies.

C. GOVERNMENTAL PARTICIPATION AND RESTRICTION IN PUBLIC UTILITIES

As we have mentioned above, the Colombian Government was the primary responsible party to provide public utilities before the enactment of the 1991 Constitution. Currently, the Colombian Government owns and has equity participation in different utility companies at the national, regional and local levels.

Nonetheless, under current regulations, the Colombian Government's participation in new projects is subsidiary to the participation of private individuals in the provision of public utilities. Therefore, as a rule of law established pursuant to Articles 6 (for the local level), 7 (for the department level) and 8 (for the national level) of Law No 142 of 1994, the Colombian Government will enter directly in the market and provide the public utilities itself only in such circumstances where private agents are not willing to provide the utilities themselves.

D. WATER, SEWAGE AND WASTE MANAGEMENT

The Colombian Government has recently pursued a high standard in the provision of water, sewage and waste management public utilities. Because of this, major governmental programmes have been enacted to meet such shortcomings in water, sewage and waste management infrastructure.

Among others, in matters pertaining to water and sewage, the Colombian Government has undertaken 'Water for Prosperity' programmes, where several investors, including foreign investors, participate in the construction and operation of water and sewage infrastructure. According to the latest information published by the Ministry of Housing, City and Territory, during the last years the Colombian Government constructed 1,135 water and sewage infrastructure projects, reaching an overall value of almost COP\$2.3bn (approximately US\$766m). During 2018, the Colombian Government foresees terminating the construction of 212 projects for a total value of COP\$1.03bn (approximately US\$334m). Furthermore, other important programmes have been enacted, for example, the Departmental Water Management Plans, where by joining regional efforts, different municipalities may access funding from the national government and initiate the procurement process for the construction of 76 projects to achieve, during this government, the construction of 1,623 projects in 32 departments for an overall value of COP\$3.6bn (approximately US\$1,200m). It is important to mention that there are several reservoir recovery projects and, in this regard, several municipalities and departments are publishing projects related to waste water treatment plants. The new government that took office on August 2018 announced its intention to advance the projects regarding the provision of water and sewage to rural areas to achieve coverage of 70 per cent.

In matters related to waste management, there are currently several projects related to the recovery of waste in order to make some waste productive. These projects are mainly being led by the waste management public utility companies already incorporated in Colombia's territory; nonetheless, it is a major opportunity for foreign investors to verify the possibilities to be included in this special activity in the waste management sector.

E. ELECTRICITY AND GAS

From the electricity sector perspective, the Colombian Government enacted Law No 1715 of 2014 on Renewable Energies, establishing certain tax benefits for foreign and local investors interested in advancing the constructing of renewable energy projects. Law No 1715 of 2014 promotes investment in renewable energies (mainly wind and photovoltaic) by introducing tax breaks, such as deductions in income tax, accelerated depreciation, exemption from VAT, and reduction of custom duties for equipment, machinery, supplies and services. In the same vein, the Regulatory Commission for Energy and Gas is issuing new regulations to ensure the bankability of these projects, and foster the rebalancing of Colombia's power generation portfolio. These initiatives are complemented by regional transmission line projects undertaken by the Mining and Energy Planning Unit, which are under tender, to transmit power generated in the northern part of Colombia.

In this regard, The Ministry of Mining and Energy issued Decree No 570 of 2018, which regulates public policies to implement long-term energy contracts for non-conventional renewable energy projects. In addition, the Energy and Gas Regulatory Commission has had discussions with energy market agents about new regulations regarding the awarding of firm energy obligations under the scope of the reliability charge.

In addition, Colombia is endowed with the largest coal reserves in the region, ranking second in the world in hydroelectric potential, and is one of Latin America's top five countries in terms of oil reserves. Colombia's electric and gas energy industries have undergone constant internal restructuring over the last century, mainly permuted by the innovative encroachment of the private sector and the need to promote competition in the market.

Finally, it is important to mention that the Colombian Government is structuring a project for a regasification facility on the Pacific coast, which, along with the brand new floating storage and regasification unit (FSRU) located at Cartagena, will ensure the supply to gas-fired power plants that generate power during El Niño–Southern Oscillation periods.

F. TELECOMMUNICATIONS

The current general framework applicable to information and communication technologies was established in Law No 1341 of 2009. According to this law, the provision of telecommunications networks and services, including fixed telephony, is considered a public service under the control of the state, separate from other public utility services covered by Law No 142 of 1994. Law No 1341 of 2009 also sets forth a general legal habilitation for the provision of telecommunications networks and services, which allows any private party to be part of it. This habilitation is not applicable to television and radio broadcasting services. Regarding all other networks and services, no particular restrictions or limitations are imposed over foreign investors. The general habilitation, nonetheless, does not cover the use of the spectrum. In order to use it, the Ministry of Information and Communication Technologies must authorise interested companies through a bidding process (*proceso de selección objetiva*).

The only requirement in order to operate telecommunications networks or render telecommunications services different from radio and television is to obtain registration before

the Ministry of Information and Communication Technologies. All companies that provide the mentioned networks or services, or that use the spectrum must have said registration. Additionally, telecommunications networks and services providers must pay an amount equivalent to 2.2 per cent of their gross income in the form of a consideration. Other fees applicable to the use of the spectrum are established in function of particular criteria, such as the quantity of spectrum granted, number of potential users, expansion plans of the company and availability of the spectrum (determined based on supply and demand). In some exceptional cases, for reasons related to national defence, attention to and prevention of emergencies, and public safety, the Colombian Government may establish other obligations.

Different regimes govern the provision of television and radio broadcasting services. In order to render these two types of services, a company must obtain a concession by means of a public bidding process. Only Colombian citizens or legal entities duly organised in Colombia can be granted with a concession. Moreover, foreign investment in companies that provide television services cannot be greater than 40 per cent of the share capital of the respective company. These dispositions were included among the approved non-conforming measures in the FTA between Colombia and the US.

B. Rendering domestic public services

i. Legal framework

Article 365 of the Colombian Political Constitution, establishes the constitutional framework for public services or utilities in Colombia. Under this article: (1) public services are inherent to the social purposes of the state; (2) the state must ensure that such services, including domestic public services, are made available to all Colombian citizens in an efficient manner; (3) private parties are entitled to provide such services, subject to regulation by the state.

These principles were developed by means of Law No 142 of 1994, which sets out the overall legal framework applicable to said services (ie, water and sewage, sanitation, electricity, natural gas distribution and telephone services), as well as to activities complementary to those services, such as power generation and transmission, natural gas transport and others.

The law sought to limit the involvement of the state in the provision of domestic public services in order to focus on policy-making and regulation while leveraging resources by encouraging the private sector to participate in the provision of high-quality services.

Under Law No 142: (1) Colombian Government entities of the national, departmental and municipal level have the responsibility to ensure that public services are provided efficiently to citizens by public, mixed capital or private entities; (2) citizens have the right to choose their service providers; and (3) any person (Colombian or foreign) has the right to organise and operate companies dedicated to the provision of public services.

Law No 142 specifically indicates that no concession or permit will be required to provide domestic public services or to engage in activities complementary to them, without prejudice to other permits that may be required for any economic activity, such as environmental licences and/or permits, municipal zoning and health permits.

The reform introduced by Law No 142 has achieved many of its policies. Local and domestic private investors have invested significantly in the electricity, natural gas, telecommunications (particularly in mobile telephony) and drinking water, and both the coverage and quality of services has improved.

By 2016, the electricity service reached 99.7 per cent of households in municipal capitals, while in other populated centres and the rural sector, the coverage of this service was 95.0 per cent. The coverage of domestic water supply services in municipal capitals was 97.5 per cent, although challenges remain, especially in the dispersed rural sector, where coverage is approximately 60.1 per cent.⁵

ii. Public utility companies

In order to ensure a level playing field between government-owned and privately owned providers, domestic public services may only be provided by certain types of entities, the most important being utility companies (*empresas de servicios públicos* (ESPs)), which may be owned by private (including foreign) investors or by the Colombian Government and are subject to a special legal regime whereby their acts and contracts are subject to private law, regardless of whether they are state or privately owned.

They are also required to ensure that services are provided continuously and cost-efficiently; to refrain from practices that restrict competition, when such competition is possible; to facilitate access by lower income users using subsidies provided by the Colombian Government; and to facilitate access and interconnection by other service providers to their networks and assets used for the provision of such services.

ESPs, whether private or government-owned are subject to regulations issued by national regulatory commissions (see below), and are required to meet efficiency standards established by such regulatory commissions and enforced by the Superintendency of Domestic Public Services (the ‘Superintendency’), which are updated from time to time. They must also implement systems and procedures to deal with complaints from their clients/users.

The Colombian state at the national, departmental (provincial) and municipal level may participate in public utility companies, but may not grant or receive from them subsidies or benefits other than those expressly established in Law No 142, which essentially means that government-owned ESPs must compete on market terms with private operators.

It should also be noted that ESPs are subject to a special insolvency proceeding established by Law No 142 and administered by the Superintendency applying the same rules applicable to the administrative receivership and liquidation of financial institutions.

Therefore, if an ESP is unwilling or unable to render adequate public services or becomes insolvent, the Superintendency may take over management of the ESP and appoint a fiduciary entity or new management under its authority and subject to oversight by an advisory board. At least two of the major creditors of the utility must be represented in this board. As a result of the takeover: (1) all judicial attachments over the public service company’s assets may be terminated; (2) all credit enforcement proceedings initiated prior to the takeover are terminated, and creditors may join the takeover proceedings to seek payment of their credits; and (3) the Superintendency has two months

⁵ Presidency of the Republic of Colombia Government Informative System, 2017.

to determine whether it has to liquidate the company or administer it with a view to rehabilitation for up to two years.

Liquidation will be supervised by a board of creditors, appointed by the Superintendency and consisting of five members, three of whom will represent the largest creditors and the two remaining being appointed by the Superintendency.

iii. Tariff rates

Tariff rates charged by ESPs are regulated by the relevant regulatory commission, except when they do not have a dominant position in their market, as determined by the commission.

Pursuant to Law No 142, the tariff structures for public utilities are based on several principles which include: (1) the principle of financial feasibility; (2) the principle of economic efficiency; and (3) the principle of solidarity.

Under the first principle, tariff rates must allow the service provider to recover operational costs and expenses, and a return on investment comparable to the return that would be obtained by an efficient company in a sector of comparable risk.

Under the second principle, the tariff scheme must provide for a mechanism that sets prices for such services in a manner similar to that in which prices are set in a competitive market. In addition, under such principle the service provider should share the benefits of productivity increases with its customers, as it would do in a competitive market, and may not transfer to the consumer the costs of inefficiencies in its operations. Under the principle of solidarity, higher income and commercial users, together with the Colombian Government must subsidise lower income users. For this purpose, municipalities are zoned to determine lower and higher income areas and surcharges applied to higher-income families that are used to subsidise lower-income families, along with contributions from the Colombian Government.

Regulatory commissions typically issue general methodologies to calculate various components of the tariffs and the review calculations of the actual tariffs to be charged by a particular company based on the investments made in their service infrastructure. Tariff cases are typically updated every five years for each company.

iv. Competition regime

One of the stated objectives of Law No 142 is to introduce competition in the provision of public utilities. Therefore, there are numerous provisions in the law and in the regulations issued by the Regulatory Commissions aimed at promoting a level playing field, including by ensuring adequate access to the infrastructure networks of incumbent service providers (in many cases, legacy municipal utility companies).

Pursuant to Article 2 of Law No 1,340 of 2009, all agents of the economy are bound by competition laws and regulations. No person, governmental entity, company or association, whether public or private is above or outside the regulatory scope of competition laws and regulations.

Therefore, despite being subject to a special regime, public utility providers are subject to general competition regulations, as well as specific rules for their particular sectors. Responsibility for the enforcement of these regulations lies with the Superintendence of Industry and Commerce.

v. *Institutional framework*

Colombian Government entities that play an important role in the domestic public service sectors are: (1) the MME; (2) the Ministry of Housing (responsible for water and sewage); (3) the Ministry of Information and Communications Technology; (4) the Energy and Gas Regulatory Commission (Comisión de Regulación de Energía y Gas (CREG)); (5) the Regulatory Commission for Telecommunications (Comisión de Regulación de Telecomunicaciones (CRT)); (6) the Regulatory Commission for Water, Sewage and Sanitation (Comisión de Regulación de Agua Potable y Saneamiento Básico ('CRA')); and (7) the Superintendence of Public Utilities (Superintendencia de Servicios Públicos Domiciliarios (SSPD)).

Each of the energy, water and sewage and telecommunications-information technology (IT) sectors is under the overall jurisdiction of the relevant ministry, which is responsible for adopting the Colombian Government's policies for each sector.

The regulatory commissions, CREG, CRA and CRT are administrative bodies comprised of the following members: the ministers of the relevant sectors (in the case of CRA, they include the Minister of Housing and Minister of Environment or their delegates), Minister of Mines and Energy, Minister of Finance and Public Credit, Director of the National Planning Department and a number of independent technical experts appointed by the President of Colombia.

The principal purpose of the regulatory commissions is to ensure that ESPs in the sector provide economically efficient and high-quality public services. The commissions fulfil this purpose by, among other things: (1) issuing resolutions applicable to the provision of services; (2) promoting competition through open and non-discriminatory access to and use of networks; and (3) establishing the tariff structure for the provision of services subject to its jurisdiction.

ESPs are subject to the oversight of the Superintendence of Public Utilities, which is an administrative body created by Law No 142 that is primarily responsible for: (1) inspecting, controlling and monitoring all companies providing public utility services; (2) enforcing regulations, imposing penalties and generally overseeing the financial and administrative performance of public utility service companies; (3) developing the accounting norms and rules for public utility service companies; and (4) in general, organising statistical and other information networks and databases pertaining to public utilities.

C. **Real estate**

Any person – whether an individual or a legal entity, foreign or national – is entitled to acquire real estate property in Colombia, subject to the limitations indicated below.

i. Rural properties: limitations for private parties

A. ENVIRONMENTAL RESTRICTIONS

Under Colombian law, rural properties may be classified by the environmental authorities as a so-called 'ecological area', whenever there are ecosystems or renewable resources located therein. In such cases, the property must be preserved in order to guarantee its sustainable development.

In these protected ecological areas, the development of industrial, agricultural or farming projects must respect the land use restrictions and, in some cases, these projects are entirely prohibited.

The environmental authorities adopt these protection measures by issuing Regional Development Plans, as well as the so-called Units of Rural Planning (Unidades de Planificación Rural), through which the environmental protection measures and land use restrictions are implemented.

B. SPECIAL LIMITATIONS TO THE PURCHASE OF RURAL PROPERTIES

1. Family agricultural units (*unidades agrícolas familiares*)

Colombian regulations provide for a special rural property limitation regarding family agricultural units (*unidades agrícolas familiares* (UAF)). These land units are comprised of the minimum extension of land that a single family is entitled to receive as a governmental economic grant. If a company is willing to purchase some of these land units, the competent authority (Instituto Colombiano de Desarrollo Rural ('INCODER')) must authorise the purchase, provided that the company proves that it does not own any other rural property in the country.

2. Land parcel licence (*licencias de parcelación*)

In order to divide a rural property into smaller extensions of land, the owner must obtain a land parcel licence. The licence-holder is entitled to carry out certain work within these properties.

3. Property tax (*impuesto predial*)

In Colombia, real estate properties are levied with a property tax. The owners must declare and pay this municipal tax, usually once a year, but in some municipalities on a quarterly basis. The tax basis is assessed in accordance with the cadastral record and an estimated value of the property made by the same owner. Depending on the economic use of the property, the tax rate generally oscillates between 0.3 per cent and 3.3 per cent.

4. Capital gains tax (*impuesto de plusvalía*)

Whenever the owner of a property carries out any improvement, the capital gain resulting thereto will be subject to a capital gains tax, which ranges between 30 per cent and 50 per cent of the gain. Capital gains tax is usually levied when the property is transferred, or when a construction licence for improving the property is granted.

5. Betterment tax (*impuesto de valorización*)

In the case in which the Colombian Government decrees a public betterment that would benefit the surrounding properties, the corresponding owners would be charged with the betterment tax on the basis that these betterments increase the value of their properties.

6. Urban development tax (*impuesto de delimitación urbana*)

Real estate owners in Colombia are levied with an urban tax when they create new constructions, additions or modifications of existing constructions on their properties. This particular tax applies to both urban and rural properties, despite its denomination.

ii. *Urban properties: limitations for private parties*

A. REGIONAL DEVELOPMENT PLANS (RDPs) AND PARTIAL PLANS (PPs)

Both RDPs and PPs regulate the development of construction projects, especially regarding urban properties. RDPs define the organisation of urban areas, indicating their specific land uses, while PPs develop and complement RDPs by establishing what type of construction projects can be developed in the areas determined under the RDPs.

B. BUILDING AND PLANNING PERMISSIONS

Every construction, addition or modification of built structures in urban properties must be authorised by local governments by means of a planning permission. The authorities verify land use compliance, the potential development index (*índice de edificabilidad*), accessibility and other technical key features.

C. TAXES

The following taxes: property tax, capital gains tax, betterment tax and urban development tax, also apply to urban properties, on the same terms as indicated above.

iii. *Expropriation events*

A. EXPROPRIATION FOR PUBLIC PURPOSE

The Colombian Political Constitution provides that any land expropriation must be preceded by a court proceeding, and, in any case, the owner will be entitled to a proper compensation. This judicial expropriation takes place when a governmental authority declares that a specific property must be expropriated for the sake of a public purpose or social interest.

Exceptionally, governmental authorities are entitled to carry out an administrative expropriation, which in any case will still require economic compensation for the owner. This expropriation will be subject to a judicial review aimed at protecting the rights of rural and urban property owners.

B. EXTINGUISHMENT OF OWNERSHIP

Regarding rural properties, there is a special expropriation proceeding in the case in which a rural property is not used or exploited by its owner in more than three years.

Other extinguishment proceedings also apply when the property has been acquired in violation of money laundering regulations or other illicit means.

iv. Due diligence

In addition to the aforementioned restrictions, it is important to bear in mind that prior to the acquisition of real estate in Colombia, it is advisable to review at least the following documents to have a complete status of the property at the time of the transaction: (1) the certificate of and tradition of the property (*certificado de tradición y libertad*) up to the date of the transaction; (2) the public deeds containing the acquisition titles and other legal acts that have been carried out on the property in the last 20 years (eg, mortgages, attachments and servitude); (3) certificates related to the payment of taxes affecting the property; and (4) the land use certificate.

The following aspects must be taken into consideration:

- analysis of the titles of the property: this is carried out by an expert lawyer for the purpose of determining if there is any circumstance that affects or limits, or is likely to affect or limit, the right of ownership over the real estate; this analysis is to verify mainly that there are no legal risks in the transaction, or in the chain of transactions, and verify the quality of the owners or the sellers;
- analysis of land use: this is carried out by a lawyer or an expert technician who seeks to determine what type of construction (including volumetric aspects) and activities are allowed to develop on the property object of the transaction, allowing the investor to have total certainty of the feasibility of developing the respective project according to the applicable specifications set forth for the property in which the project would be performed; and
- in relation to the acquisition of rural properties, it is important to take into account that there is a special regulation that imposes certain limitations on the acquisition and development of these properties, as occurs, for example, with the limitation established in Article 72.9 of Law No 160 of 1994, which prohibits the acquisition of vacant lots if the size of the UAF is exceeded.

v. Contracts for transferring ownership of a property

For purposes of transferring real estate in Colombia, prior to the execution of the property purchase contract, the parties execute a promise to purchase agreement. In this agreement, the buyer and seller agree the essential elements of the contract of sale (the corresponding real estate, price and terms of payment) is usually celebrated when the parties have established all the conditions of the contract, and only the legal formalities are pending.

The contract for the purchase of real estate must be granted through a public deed. The cost of this procedure is approximately 0.3 per cent of the value of the sale.

Moreover, it is important to point out that the ownership of a real estate is transferred with the registration of the public deed of sale in the Office of Registration of Public Instruments (*Oficina de Registro de Instrumentos Públicos*). The registration of the public deed generates a registration tax that can range between 0.5 per cent and one per cent of the value of the purchase agreement contained in the public deed, as well as the so-called registry rights equivalent to 0.5 per cent of the value of the price of the sale, and generally are paid by the buyer.

D. Development of ample/integrated capital markets and joint activities between Latin American countries

i. Merger of stock exchanges: attempts versus realities

The integration of the stock markets of Chile, Colombia, Peru and Mexico (the Member Countries) through MILA was structured to be implemented in two stages. The initial stage, which Member Countries of MILA have completed, consisted of the entry into operation of an order routing system allowing the sale and purchase of equity-based securities (ie, equity, participation units in funds bound to stock indices and equity, etc). Orders are placed by local residents through a local stock broker dealer to buy/sell the securities in any of the Member Countries; however, the negotiation and actual sale/purchase of such securities is conducted by the broker-dealer of the country where the securities are negotiated, and with whom the local broker-dealer has entered into an agreement. Other important aspects related to transactions conducted through MILA are still disparate in each Member Country, including clearing and settlement of transactions, fiscal, FX regulation and surveillance standards.

In the second stage of the implementation, it is expected that local broker-dealers will be authorised to sell/purchase securities in any of the Member Countries (equity based or fixed income securities) without the intermediation of broker-dealers of the countries where the securities are negotiated. In order to implement this stage, a standardisation of trading rules and definition of a model of cross-border clearing and settlement are required. To achieve the former, effort has already been made to eliminate disparities between the legislations of the Member Countries. For instance, in Colombia, important legislation in different fields has been enacted. The most important regulation is reflected in Decree No 4,087 of 2010 ('Decree No 4,087'); Decree No 1,850 of 2013 ('Decree No 1,850'); and Part I, Title II Chapter II of External Circular No 29 of 2014 issued by the Colombian Financial Superintendence ('Circular No 29'). Decree No 4,087 authorised the listing of equity-based securities in foreign securities' quotation systems (*sistemas de cotización de valores del extranjero*) administered by the BVC and negotiated in foreign stock exchanges, pursuant to agreements entered into by BVC with foreign stock exchanges (eg, the case of MILA). It was the first regulatory amendment, which opened the door to integration. Decree No 4,087, also allowed that orders placed through a local broker-dealer in Colombia to purchase/sell securities listed in foreign securities' quotation systems are registered in the electronic entry-book registry of the foreign broker-dealer of the country where the securities are negotiated, rather than in the electronic entry book of the local broker-dealer. Decree No 4,087 also made important progress by allowing foreign clearing houses to register equity-based securities transactions in accounts held in the Colombian securities depository,⁶ and also by allowing the latter to register equity-based transactions cleared and settled in foreign clearing houses. On the other hand, Decree No 1,850 authorises foreign issuers and local securities intermediaries (ie, broker-dealers and financial corporations), to promote foreign equity-based securities that make part of an IPO in Colombia. In addition, Decree No 1,850 authorised local securities intermediaries to enter into underwriting agreements for the placement of foreign equity-based securities issued in a different country and negotiated in another stock exchange (eg, those of the Member Countries of MILA). Finally, Circular No 29 establishes the minimum requirements that must be included in

⁶ The current equity-based securities depository in Colombia is Deposito Centralizado de Valores-Deceval SA.

agreements entered among stock exchanges (eg, the stock exchanges of Member Countries), as well as those entered into among broker-dealers of different countries. Today, more than 60 broker-dealers are authorised to operate in MILA.⁷

On the other hand, in other Member Countries such as Chile, the legal framework has also been evolving during recent years in order to implement an internationally integrated securities market. In January 1999, Law No 19,601 ('Law No 19,601') created an offshore market that allowed the registration of foreign securities by an issuer or its legal representative in order to trade them in Chile. In June 2007, Law No 20,190 ('Law No 20,190') authorised the registration of foreign securities, now by third parties called sponsors (*patrocinadores*) simplifying, in that sense, the trade of these securities in the offshore market. With the enactment of Law Nos 19,601 and 20,190 in November 2010, the implementation of the first stage of MILA in Chile did not require changes in law.

From the regulatory authority's point of view, the Chilean Commission for the Financial Market (Comisión para el Mercado Financiero (CMF)), which supervises, among others, corporations, insurance companies, stock exchanges and broker-dealers, has also contributed to the implementation of MILA in Chile. The CMF, through its regulatory framework, has issued a significant number of standards. First, Circular No 1,046 dated 17 December 1991 (amended by Circular No 1,371 dated 30 January 1998) authorised, as a complementary activity for broker-dealers, advice and specific commission for the purchase and sale of securities in foreign stock markets. Then, on 12 June 2008, Norma de Carácter General (NCG) No 215 (amended by NCG No 357 dated 18 December 2013) established the requirements and conditions to be met by companies in order to sponsor the registration of foreign securities in Chile. Finally, during recent years, and in order to ease the implementation of the second stage of MILA, the CMF issued NCG No 352 (21 October 2013) that established the standards for the public offering of foreign securities in Chile, and on 14 July 2014, the CMF issued NCG No 366, which provided instructions on the negotiation of those securities in Chile.⁸ As in the legal Chilean framework, some of the rules of the CMF were previously issued to MILA, and without seeking said purpose, they have facilitated its implementation in Chile.

The surveillance authorities of the Member Countries, excluding Mexico,⁹ have also entered into several cooperation agreements (*acuerdos de entendimiento* or memoranda of understanding (MOUs)) seeking to implement mechanisms for combined surveillance, an exchange of information, cross-border risk administration and cooperation during investigations, and sanctioning processes involving transactions or entities that make up part of MILA. In this regard, agreements include: (1) a cooperation agreement entered on 28 October 2009 among the Member Countries, excluding Mexico, which set forth the main tasks to be performed by regulators for the implementation of MILA; (2) a cooperation agreement entered on 15 January 2009 among the Member Countries, excluding Mexico, establishing mechanisms for the exchange of information and assistance intended to facilitate the compliance of securities regulations of each of the countries party to this agreement; and (3) an amendment to the cooperation agreement entered on 15 January 2009 among the Member Countries, excluding Mexico, and dated 15 January 2010, establishing a combined surveillance committee in charge of the following functions:

7 See <http://mercadomila.com/quienes-somos/que-hacemos> accessed 27 August 2018.

8 Furthermore, NCG No 304 dated 10 March 2011, establishes, among others, the registration procedure of debt securities issued by foreign states, international and supranational organisations and foreign entities in the Chilean securities registry.

9 The supervision authorities of the Member Countries, excluding Mexico are: (1) Comisión para el Mercado Financiero de Chile; (2) Superintendencia Financiera de Colombia; and (3) Comisión Nacional Supervisora de Empresas y Valores (Perú).

(i) creating the guidelines for the operation of the committee and the compliance of its functions; (ii) determining, in accordance with the aforementioned guidelines, the most suitable channels for the exchange of information and documentation requested by authorities of the Member Countries, and promoting their implementation; (iii) setting forth mechanisms for the recollection of evidence in any of the Member Countries required for the administrative processes conducted by the surveillance authorities of the Member Countries; (iv) enabling mechanisms to coordinate and provide support in connection with any investigation process related to transactions performed in MILA and conducted by any of the surveillance authorities of the Member Countries, excluding Mexico; (v) creating working teams to study, analyse and develop strategies to improve supervision standards related to MILA; and (vi) procuring that information is kept confidential by its members.

Despite the aforementioned advances, in the regulation to implement MILA, there are still several regulatory challenges for the full implementation of stage 2. Further regulatory amendments are required in each of the Member Countries to achieve homogenisation in clearing and settling rules, as transactions performed through MILA's platforms are cleared and settled in each of the Member Countries according to their own risk administration standards (ie, establish the characteristics of intermediated routing; and qualify the activity for broker-dealers and mechanisms for the exercise of political and economic rights of investors, subscriptions of MOUs between local authorities and the supervisory authorities of other participants in MILA, etc).

Homogenisation is additionally required in tax regulations pertaining to transactions performed through MILA's platforms. For example, taxes on dividends are different in each of the Member Countries: in Colombia, dividends from profits generated before fiscal year 2017 paid to non-resident holders of securities will be subject to a withholding tax of 33 per cent if such profits were not taxed at the corporate level. Dividends generated out of profits as of fiscal year 2017 on investments registered as FDI will be subject to a withholding tax of five per cent if profits generated by the corporation have been previously subject to income tax at the corporate level or 38.25 per cent rate (35 per cent plus five per cent on the balance that results after applying the initial 35 per cent withholding tax) if dividends are paid out of profits not subject to tax at the corporate level. In addition, dividends generated out of profits as of fiscal year 2017 on a foreign portfolio investment will not be subject to withholding tax if profits generated by the corporate have been previously subject to income taxes at the corporate level, or at a 25 per cent rate if they are paid out of profits not subject to tax at the corporate level: in Chile, there is a withholding tax of 35 per cent over dividends for non-residents; in Peru, there is a withholding tax of 6.8 per cent for 2016, 8.0 per cent for 2017 and 2018, and 9.3 per cent for 2019¹⁰ (applying to non-residents); and in Mexico, there is a withholding tax of ten per cent,¹¹ which generates regulatory arbitrage, which can cause a disincentive for investors. As another example, while in Colombia capital gains are not taxed if resulting in a sale of shares of a publicly listed company provided that they do not exceed ten per cent of the total capital of the company, in Mexico non-residents are taxed differently (zero per cent¹² depending on treaties subscribed with different countries or ten per cent if there is no treaty). In addition, the standardisation of rules for the negotiation of securities in the stock exchange of each Member Country will allow local broker-dealers not only to place, but also to negotiate transactions over securities in a foreign stock market without the intermediation of their

10 See http://mercadomila.com/wp-content/uploads/2018/04/MILA_Info_Tributaria.pdf accessed 27 August 2018.

11 *Ibid.*

12 *Ibid.*

fellow counterparties. Moreover, in order to reach the standardisation of regulation, further efforts are required for the implementation of combined surveillance by the authorities of the Member Countries. For example, combined surveillance is necessary in connection with risk administration of transactions conducted through MILA, including the assessment of risk derived from the implementation of new financial products and instruments (ie, fixed income securities and derivatives); the transfer of risk from one market to another, including systemic risk; continuity plans derived from operational failures in the negotiation platforms of MILA; and crisis situation management. Furthermore, regulatory changes are essential to permit that a single authorisation by any of the authorities of the Member Countries allows issuers to perform IPOs in the Member Countries without further authorisation. To achieve the former, the standardisation of information presented to investors and authorities by issuers is required (ie, offering memoranda and public information on the web pages of issuers and authorities).

On the other hand, it is important to point out that, currently, MILA limits negotiations to equity-based securities. It is expected that fixed-income securities are authorised to be negotiated within the MILA platforms, including corporate bonds and public debt (ie, TES (Colombia), CKD (Mexico) and *títulos emitidos por la Tesorería General de la República de Chile* (Chile). Other financial instruments, such as derivatives and structured products, shall be gradually included to attract the interest of more investors.

As a public policy to develop capital markets in the Latin American region, and specifically in the Pacific Alliance, at the end of 2017, the regulator issued the Decree No 1,756 of 2017 ('Decree No 1,756') known as the funds passport (*pasaporte de fondos*).

Pursuant to Decree No 1,756, any Colombian investor can invest in a foreign investment fund or vehicle ('FIF') if: (1) the FIF is a collective investment fund that has been authorised in its local jurisdiction; and (2) its local regulator and the Superintendencia Financiera de Colombia (SFC) have signed supervision and information exchange agreements.

Any Colombian investor, either retail or institutional, can invest in a FIF provided the investment is not restricted or forbidden according to its local investment regime.

A FIF distribution must be done using a mutual funds special distributor (*distribuidor especializado*), such local commercial banks (*establecimientos bancarios*), broker-dealers (*sociedades comisionistas de bolsa*), trust companies (*sociedades fiduciarias*) or investment management companies (*sociedades administradoras de inversión*) through omnibus accounts.

With respect to the interest of investors and issuers in MILA, it is believed that a more aggressive and educational campaign has to be conducted by MILA among them to show the potential benefits of conducting business through MILA (see the next section for information on the objectives of MILA). As will be explained in the next section, numbers show that the current results for the volume of negotiations and liquidity in MILA has not reached the desired levels. This is explained in part because of the regulatory challenges pending to implement stage 2 of MILA described above, but also the lack of knowledge of investors and issuers of the benefits of negotiating securities through MILA.

ii. MILA: current results and expectations

Since the commencement of the operations of MILA on 30 May 2011, its Member Countries have pursued seven main objectives: (1) to promote a higher level of integration between the economies of the region;

(2) to provide investors with diversified investment opportunities by granting access to a combined stock exchange market with a market value of US\$991,416bn and 657 issuers as of 1 September 2017;¹³ (3) as a consequence of the latter, to increase the volume of negotiations carried out in the combined stock market using MILA's order routing systems, which as of April 2018 reached a volume of negotiations of US\$16,105,249,990;¹⁴ (4) to provide liquidity to the stock markets of the Member Countries to obtain growth in the sources of financing of issuers on the combined stock markets; (5) for broker-dealers, to increase the range of products to distribute to their customers; (6) the creation of new investment vehicles; and (7) to obtain a technological strengthening and adoption of international standards.

The above objectives have been partially achieved. Even though investors currently have access to the combined stock markets of the Member Countries, now the second largest after BOVESPA of Brazil, the volume of negotiations using MILA's platforms and the liquidity of the combined stock markets have not reached the desired levels. This is for two main reasons: (1) the regulatory challenges pending to implement stage 2 of MILA (see section D(i) above); and (2) the lack of knowledge of investors and issuers of the benefits of negotiating securities through MILA. A more aggressive and educational campaign on MILA has to be conducted – mainly by the authorities of each of the Member Countries – to show the potential benefits of business conducted through MILA, which were described at the beginning of this section.

iii. Pacific Alliances: governmental action and proposed treatment and agreements

The Pacific Alliance is a regional and economic integration initiative whose members are the same Member Countries of MILA, and it was created in 2011. The objective of this alliance is to build an area of deep economic integration to achieve the free circulation of goods, services, capital and persons. Furthermore, it was created as a platform for trade integration, among other objectives, to foster economic development and growth.

Taking into consideration the above, MILA has an important role in this integration process. Allowing the Member Countries to have a free trade of their securities with equal regulatory standards will enhance the economic growth of the Member Countries and development of their corporate sectors.

iv. IPOs of companies in MILA

During 2017, several companies performed IPOs through the stock exchange markets that integrate MILA.¹⁵ Among the issuers were companies such as Cencosud SA, Clínica Las Condes SA, Parque Arauco SA, COFACE Seguro de Crédito Perú SA, Colegios Peruanos SA and HDI Seguros SA. However, and as mentioned before, current regulations do not allow performing IPOs without the joint authorisation of each of the authorities of the Member Countries that integrate MILA. We believe that allowing issuers to file a single authorisation request with any of the authorities to perform an IPO in any of the Member Countries would substantially increase the number of IPOs in MILA because fewer regulatory obstacles would make the process faster and less costly.

13 See <http://mercadomila.com/datos-del-mercado/capitalizacion> accessed 27 August 2018.

14 See <http://mercadomila.com/datos-del-mercado/volumenes> accessed 27 August 2018.

15 According to MILA.



International Bar Association

4th Floor, 10 St Bride Street
London EC4A 4AD, United Kingdom

Tel: +44 (0)20 7842 0090

Fax: +44 (0)20 7842 0091

Email: member@int-bar.org

www.ibanet.org