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# Colombia

## International Estate Planning Guide Individual Tax and Private Client Committee

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## I. Wills and disability planning documents

### A. Will formalities and enforceability of foreign wills

In Colombia, a testament is a solemn act that must comply with the formal requirements established to be valid and binding by civil law.

A will, like any other legal act, must fulfil the essential requirements for validity, which are that the testator has legal capacity to grant the will; that his or her consent is not impaired by vices such as error, duress or fraud; and that the act has a lawful purpose and cause.

Depending on the type of will, legislation has established certain specific formalities for its validity.

Under Colombian legislation, wills are classified as solemn or privileged. In turn, solemn wills may be open or sealed and privileged wills are classified as verbal, military or maritime wills.

A solemn will must always be recorded in writing and executed before competent witnesses. At least two of the witnesses must be domiciled at the place where the will is granted, and they must be able to read and write.

In an open will, also known as a nuncupative or public will, the testator makes his or her dispositions public before three witnesses and a notary, when the latter is present. The witnesses must copy the words of the testator verbatim and, at the end of the proceeding, read and sign the will. In a sealed will, on the other hand, the witnesses and notary are not required to know the content of the dispositions contained in the will. However, the sealed deed must be presented before a notary and five witnesses, declaring *viva voce* that the deed contains the will.

Privileged wills, however, may omit some of the formalities by reason of specific circumstances expressly determined by law.<sup>1</sup> Nevertheless, a privileged will must meet three requirements: (1) the *viva voce* statement of the testator regarding his or her desire to make a will must be unequivocally declared; (2) the persons whose presence is necessary in the granting of the will appear before the testator; and (3) the act is continuous in such a way that it may only be interrupted exceptionally for brief intervals when required by reason of an accident. The validity of this type of will is provisional and, therefore, once the exceptional situation is overcome, the requirements of a solemn will must be complied with.<sup>2</sup>

In relation to the content of a will, legislation provides that it must indicate the full name, place of birth, nationality, domicile and age of the testator, as well as the circumstance of being of sound mind, and the names of the testator's spouse and children, together with information on each of the witnesses and the notary, indicating the place, day, month and year of execution of the will. Errors in content do not imply the nullity of the testament, provided there is no uncertainty regarding the identity of the testator, notary or witnesses.

The allocations to be made must be determined or determinable, underlining the fact that the will of the testator is limited by the forced allocations established by Colombian law. These allocations are mandatory for the testator, and therefore, even if they contradict what is expressly provided in the will, they will be observed when they have not been applied.

Forced allocations include alimony due by law to certain persons: the marital share, that is, the portion of the assets of the decedent that the law assigns to the surviving spouse who lacks the necessary means for a decent subsistence; and the legitimes, which are the compulsory portions assigned to certain persons known as legatees.<sup>3</sup>

Law 1934, 2018 excluded the quarter portion of the estate for accretions to the inheritance of legitimate heirs, which was compulsory prior to 2 August 2018.

In accordance with the above, the testator may dispose freely of the entire estate only as of the third order of inheritance, that is, if no descendants or ascendants survive the testator; otherwise, the testator may make allocations at his or her discretion on a percentage equalling 50 per cent of his or her assets and must transfer 50 per cent of his or her estate to the legitimes in equal parts.

The validity of wills granted abroad is subject to them having been made in compliance with the laws of the state where they were executed, with evidence thereof, proof of their authenticity and their legal translation, where applicable.

If the will is granted abroad in compliance with Colombian regulations, the following requirements must be met for its validity: (1) the testator is a Colombian national or a foreigner domiciled in Colombia; (2) the will is authorised before a Colombian consulate; (3) the witnesses are Colombians or foreigners domiciled in the city where the will is executed; and (4) the rules of a solemn will are observed.

#### *B. Will substitutes (revocable trust or entities)*

It is important to point out that while Colombian law does not contemplate a common law trust, there is an institution with similar characteristics, known as a civil law trust or *fiducia*.

The establishment of a civil law trust implies the imposition of an encumbrance on all or part of the estate of the trustor. When this ownership is retained by the trustor or transferred to another person, this is done on the condition that it will be passed on to a third party upon the occurrence of a specific event.

As a substitute for the testament, a civil trust is useful for transferring the assets of a future *de cujus* through the designation of the spouse and other heirs as beneficiaries of the trust, once a condition is met, which in this specific case is the death of the trustor.

Therefore, a civil trust involves three parties: the trustor, trustee and beneficiary or beneficiaries. The trustor is the person who delivers the assets by way of a trust to the trustee; the trustee is the person to whom the property is entrusted until the condition is fulfilled, with the charge of transferring it to the beneficiary; and the beneficiary is the person in whose favour restitution is to be made once the condition is fulfilled.

The trustee holds the full right of ownership and usufruct of the assets for the duration of the trust, except as otherwise stipulated, bearing in mind that trust ownership may be established on the bare title, reserving the proceeds for the beneficiaries. When the person dies, the ownership of his or her assets passes to the beneficiaries in the proportion established in the document constituting trust ownership, without the need for a probate hearing.

From a tax point of view, this mechanism is taxable given that if the trust is gratuitous, at the time of occurrence of the condition, in every case, it generates a taxable occasional gain for the beneficiary.

On the other hand, even if this mechanism does not constitute will substitutes as such, in order to minimise the tax burden at the time of succession and as an instrument for the administration of the estate of the decedent during his or her lifetime and after his or her death, certain corporate schemes may be used both in Colombia and abroad through corporate forms contemplated in Colombian law, such as limited partnerships and simplified stock companies.

The establishment of a limited partnership allows the testator to have control of the company in the form of an administrative or managing partner, and to structure the assignment of his or her assets with new capitalisations, through which the heirs will gradually increase their rights or shares in the capital of the company.

Likewise, simplified stock companies (SAS) have a flexible and dynamic regulatory framework in which the autonomy of the shareholders prevails. This corporate form enables the establishment of types of shares that assign the control of the company to one of the shareholders through multiple votes or fractioning of vote stipulations for the election of boards of directors or other collegiate bodies of the company. In addition, SAS offer the possibility of establishing minimum or maximum amounts of corporate capital that may be controlled by a specific shareholder and special restrictions for the negotiation of shares issued by the company.

The implementation of foreign companies also allows a testator to manage his or her wealth in the jurisdiction he or she considers most favourable for tax and corporate purposes. The transfer of funds abroad in order to make investments in assets is permitted in the country, provided that the funds allocated for such purposes are channelled through the exchange market.

As in the case of Colombian companies, these offshore schemes allow the transfer of the title to assets that represent the estate of the testator to the beneficiaries. The testator retains the power to manage the estate and receive profits thereof until his or her death.

#### *C. Powers of attorney, directives and similar disability documents*

Under Colombian civil law, all persons have legal capacity to acquire rights and contract obligations, except for those who the law declares disabled, that is, those who, despite their status as legally capable persons, cannot govern themselves or manage their affairs.<sup>4</sup> These persons must act through a representative.

Legal disabilities have been established to protect the interests of certain persons who, for one reason or another, do not have full discernment or lack the necessary experience to be able to express their will, acquire rights and bind themselves in a sufficiently clear manner, and are therefore disqualified from executing legal acts.

Disabilities may be general or specific. General disabilities refer to all types of legal transactions, while specific disabilities only refer to certain acts and are expressly stipulated by law. In accordance with the Civil Code, said general disabilities may in turn be absolute or relative. Thus, individuals with absolute mental disability,<sup>5</sup> children who have not reached puberty and deaf-dumb individuals who cannot make themselves understood are considered to have absolute disabilities and their acts are subject to absolute nullity; on the other hand, adult minors and squanderers who are under judicial interdiction are considered to be relatively incapable, given that their acts may be admissible under certain circumstances and, in certain specific cases, determined by law. This disability results in relative nullity.

To protect the interests of disabled persons, legislation has created guardianships, which include tutorships and curatorships. A tutorship is exercised over children who have not reached puberty and is always of a general nature, whereas a curatorship may be general or special. The latter refers to a specific act or a particular transaction.

On the other hand, Law 1306 of 2009 provides that, when the value of the productive assets of an individual with absolute mental disability or of a minor exceed 500 legal monthly minimum wages, or even if these do not exceed 500 legal monthly minimum wages but the judge deems it necessary, the administration of the assets will be turned over to a trustee.

Likewise, Law 1306 of 2009 created the measure of disability for persons suffering from behavioural deficiencies, prodigality or business immaturity, and who, as a consequence, may place their wealth at serious risk. These individuals may be disqualified to enter into certain legal transactions, at the request of their spouse, relatives up to the third degree of consanguinity and even by the individual him or herself. This may also be imposed as an accessory measure at the request of creditors or ex officio by a judge in estate liquidation proceedings and in cases of payment through the assignment of the assets of individuals.

## **II. Estate administration**

### *A. Overview of administration procedures*

In Colombia, succession may be testate, intestate or mixed, that is, it may be governed by testamentary dispositions and, in all matters not provided for by the decedent, by Civil law.

When the testator dies, an unsettled succession arises and its settlement may be carried out through a judicial proceeding or be processed before a notary public. Unsettled succession only disappears from the legal world when the judgment approving the partition or the public deed is executed or when it is recorded in the case of the allocation of real property.

The following persons may take part in probate proceedings:<sup>6</sup>

- the surviving spouse or domestic partner for the purposes of the liquidation of community property or the community estate;
- the heirs in matters related to inheritance rights;
- legatees for a testamentary disposition in their favour;
- assignees of the inheritance right;
- creditors, who may come forward until the inventory and appraisal hearing, as their legal interest to become a party is exhausted upon its occurrence;
- an executor, who is not entitled to a portion of the inheritance; his or her legitimation to intervene derives from his or her capacity as the executor of the will by the testator; and
- the National Tax and Customs' Authority (Dirección de Impuestos y Aduanas Nacionales or DIAN), who will intervene in the proceedings when the amount of the assets exceeds 700 Unidad de Valor Tributario (UVT),<sup>7</sup> that is, COP 26,688,400 (approximately US\$7,550.38) for the year 2023.

Considering the existence by law of forced allocations that limit the will of the testator, in testate, intestate and mixed successions, the estate (assessed after the liquidation of community property, if any) is reduced by these allocations. Therefore, hereditary credits, any taxes that may be incurred, allocations for support and the marital share are deducted from the decedent's estate. The result is the net estate available for partitioning, which must be completed subject to the legitimes.

Generally, the stages of succession proceedings are as follows:

1. an order is issued declaring the liquidation proceedings open and recognising the parties interested therein. Notwithstanding the order, there may be future recognitions;<sup>8</sup>
2. the request for the acceptance of the inheritance is formalised. It seeks to generate an act of acceptance or renunciation by the heir. At this stage, the spouse may opt for the conjugal share or for the property acquired during the marriage, as explained in the section on marital property below;

3. the inventory, and appraisal of assets and liabilities may be lengthy, considering that objections to appraisals by the intervening parties are permitted; and
4. once the assets of the decedent have been cleared, partitioning takes place, through which the distributions corresponding to each heir are made in accordance with the will or law. The executor may be designated by the parties by joint agreement, by the judge or by the testator him or herself when there is a will. The judge must validate the partition and, if appropriate, issue a judgment approving it.

In the case in which there is a single heir, the inheritance will be allotted to him or her. This allotment substitutes the partition.

After the succession proceedings have been concluded, if new assets of the testator that were not included in the inventory, or new assets of community property or the estate, are found, or if the executor failed to distribute certain inventoried assets, there may be additional partitioning if there are several interested legatees. At this stage, a discussion may arise regarding the existence of persons with equal or better rights who did not come forward in the succession proceeding. In this case, they must file an action to claim their inheritance right against whoever holds it through a proceeding known as a demand for probate of the decedent's estate.

The other procedure for the liquidation of succession, that is, the formalisation of liquidation before a notary public, may be carried out in all cases, provided the heirs, legatees, surviving spouse or assignees are fully capable and act by joint agreement.

#### *B. Intestate succession and forced heirship*

In cases in which there is no testament, or if there is a will, when it is invalid, intestate succession occurs, in which the assets of the decedent are allocated to the persons who the law has established as holders of the right to inherit in the order prescribed by Civil law.

As previously mentioned, Colombian law establishes forced heirship in relation to alimony support, the marital share and the legitimes. The law establishes the legatees, that is, the descendants, or if there are none, the ascendants of the deceased, as forced heirs.

The legatees are entitled to 50 per cent of the decedent's estate.

The order of succession is made up of descendants in first place, ascendants in second place, siblings in third place, followed by their children in fourth place, the surviving spouse in fifth place and finally, in the absence of all the foregoing, the state through the Colombian Family Welfare Institute (Instituto Colombiano de Bienestar Familiar or ICBF).

#### *C. Marital property*

In Colombia, there is a community property system. Community property exists from the moment of the marriage or declaration of domestic community,<sup>9</sup> and is dissolved by reason of death, divorce and/or mutual agreement. However, if there is a legal tie, community property is not visible, that is, the civil, commercial and tax obligations of the spouses operate individually.

As provided in Article 1781 of the Civil Code, community property assets include the salaries and emoluments of every nature arising from office or employment obtained during the marriage by each of the spouses, as well as all proceeds, yields, pensions, interest and profits of any kind derived either from community property or the assets belonging to each of the spouses that were earned during the marriage.

In addition to the foregoing, community property includes:

- money that either spouse or domestic partner brings to the marriage, or is acquired during it, which must be restored in the same amount from community property;
- fungible goods or movable property that either spouse or domestic partner brings to the marriage, or are acquired during it, which must be restored from community property according to the value they had at the time of the contribution or acquisition; and
- all assets that are acquired by either the spouses or domestic partners during the duration of the marriage or relationship for valuable consideration.

Assets acquired before the marriage or domestic partnership, and those subsequently received by donation, inheritance or legacy, do not become part of community property and are deemed to belong to each of the spouses or domestic partners. However, the proceeds, income, profits or value increases produced by these assets during the marriage or domestic partnership are part of community property.

On the other hand, the liabilities of community property include external liabilities consisting of obligations chargeable to the unsettled estate and in favour of third parties, and internal liabilities, in turn, consist of obligations chargeable to the unsettled estate for the benefit of one of the spouses.

The spouses may exclude any assets that are part of their own wealth from community property by establishing specific provisions in the marriage articles (prenuptial agreements).

Likewise, community property may be liquidated without affecting the marital relationship or domestic partnership as a result of partitioning the assets as the parties decide by mutual agreement. Third parties, who do not intervene in this process, are protected through the establishment of the joint and several liability of the spouses or domestic partners, with respect to obligations vis-à-vis third parties.

On the death of one of the spouses or domestic partners, if there is community property, the surviving spouse may choose whether to participate in the succession proceedings as a spouse or heir. The decision must be communicated before the inventory and appraisal stage by the spouse indicating whether he or she opts for a portion of the decedent's estate as a legatee or for the marital property. If he or she opts for the marital share, the unsettled assets of the inheritance and community property are merged into a single unit.

In the case in which the surviving spouse opts for the marital property, he or she may carry on the administration of the assets of the community property until partitioning is complete.

Within the same succession proceedings there may be a combination of liquidations, that is, the liquidation of the succession and that of community property or the community estate between domestic partners. However, inventories and appraisals must be completed separately in order to identify the assets and liabilities corresponding to each of the estates.

Community property assets must be distributed among the parties in equal shares, as established in civil law, or as stipulated in the prenuptial agreement, if one exists.

#### *D. Tenancies, survivorship accounts and payable on death accounts*

As of the moment of death, the assets of the decedent become part of the estate. The administration of said estate may be carried out through different procedures, depending on whether succession is testate or intestate, or whether the assets belong to community property.

In the first case, the administration and tenancy of the assets of the decedent's estate correspond to the executor, or if there is no executor, to the heirs who have accepted the inheritance.<sup>10</sup>

The executor may only refuse the designation for a justified cause; otherwise, the person designated as the executor will give ground for disqualification from inheritance. This designation cannot be delegated, except in cases in which the testator has so provided, and it is not transferable to the heirs of the executor.<sup>11</sup> It should be pointed out that the executor is liable with respect to his or her administration up to ordinary negligence, and the heirs or legatees are likewise entitled to demand guarantees from the executor regarding the security of the assets when the executor has possession.

In intestate succession, the heirs acquire the possession of the inheritance from the moment of its denouncement,<sup>12</sup> this legal fiction is known as lawful possession of the inheritance. The purpose of lawful possession is that the inheritance is not considered heirless or with no apparent owner, as well as to allow the heirs to exercise their option right (inventory benefit), that is, their right to accept or renounce the inheritance or legacy, or to accept it only up to the value of the liabilities, and to exercise the joint administration of the estate.<sup>13</sup>

Where there is community property, assets that are included are administered jointly by the surviving spouse and executor.<sup>14</sup>

Before the formal inventory is taken and completed, the administrators of the estate are required to hold the assets representing the decedent's estate under deposit (the law indicates that any personal property must be kept under lock and key). When the inventory and appraisals become final, the administrators may dispose of the assets in order to pay the liabilities of the decedent, and if the available funds are insufficient to cover the liabilities of the inheritance or legacy, the spouse, executor or any one of the heirs may request the sale of certain assets in a public auction or at a stock exchange, where applicable. If there is real estate property, any of the heirs may ask the judge to issue the decree of effective possession in favour of all the heirs, and to order its recording in the Registry of Public Instruments. This recording grants the heirs the power to dispose of the real estate.

Likewise, considering the fact that, under tax law, an unsettled estate is subject to income taxes from the date of death until the execution of the decision approving the partition, or of the issuance of the public deed, the executor or heirs who have accepted the inheritance must act as the representative of the succession before the state in order to comply with formal tax obligations, such as the filing of tax returns, and to make corresponding payments at the estate's expense.

Certain regulations in Colombia are similar to the tenancy systems in other countries. Among them is that contemplated in Law 258 of 1996, known as encumbrance as a family dwelling. This encumbrance applies to real estate property acquired in full by one or both spouses, either before or after the marriage, and intended as a place of abode for the family. The main consequences of the encumbrance as a family dwelling are, on the one hand, the non-attachability of the property designated as such,<sup>15</sup> and on the other hand, that, in order to sell the property, the encumbrance must be lifted through a public deed signed by both spouses.

On the death of one of the spouses or domestic partners, the encumbrance as a family dwelling is extinguished, unless the under-aged heirs that are inhabiting the property request that the judge, for justified cause, maintains the encumbrance for as long as necessary, although this term may not extend beyond the date on which the under-aged heirs reach the age of 18 or become emancipated.

Likewise, Law 70 of 1931 consecrates the institution named Unattachable Family Property, which may be established in favour of designated beneficiaries on the full ownership of a real estate property that is not held jointly and severally, is not subject to encumbrance by mortgage, subject to security for the payment of an annuity or to antichresis, and whose



value at the time of the imposition of the family property restriction is not greater than 250 monthly minimum wages (ie, COP 290m (US\$73,753.06) for 2023). In the event of the settler's death, the family property subsists in favour of the surviving spouse. In the event of the death of both spouses, the family property restriction subsists in favour of the children until they reach the age of 18.

Regarding *survivorship accounts* and *payable on death accounts*, under Colombian legislation, for the decedent to designate the individuals he or she chooses as beneficiaries of his or her bank deposits, a collective deposit must be set up.

Although it is feasible for bank deposits (checking or savings) to have multiple holders through collective or joint accounts, in the case of joint accounts, that is, those held in the name of two or more individuals acting jointly to dispose of the funds deposited in them, the concurrence of the signatures of all holders is necessary in order to make withdrawals and, therefore, on the death of one of the holders, no withdrawals may be made and the portion of the funds corresponding to the deceased holder must be determined in the inventory during the appraisal stage of succession.

In collective deposits, on the other hand, when one of the holders of a savings or checking account dies, the balance may be reimbursed to the other holders. The same applies to time deposit certificates established in favour of several persons containing the clause 'and/or'. When the principal dies, and at the time of the maturity of the certificate, the financial institution may pay its amount to the other beneficiaries.

Regarding funds held by the *de cujus* in financial institutions, there is a special benefit that allows banking institutions to release, up to a specified amount, the balances of funds deposited in savings accounts and checking accounts, and amounts represented in time deposits and cashier's checks, without demanding proof of succession proceedings. The maximum amount that may be released by banks without requiring a succession proceeding is published annually by the Financial Superintendency and equals the sum of COP 74,358,288 (approximately US\$18,910.87) for the period between 1 October 2022 and 30 September 2023.

The Colombian pension system provides for the extension of the pension of the decedent to the heirs. Under pertinent legislation, the spouse or domestic partner of a deceased pensioner or affiliate to the pension system is entitled to receive the survivor's pension, until death.<sup>15</sup> Children under the age of 25 who are financially dependent on the deceased at the time of death are also considered beneficiaries, provided they are unable to work by reason of their studies, as well as any disabled children of any age, if there is economic dependency, for as long as their disability conditions subsist. If the pension is assigned only to the spouse, the spouse will be entitled to the full amount, but if there are also children that are entitled, the pension will be distributed: 50 per cent to the spouse and 50 per cent to the children.

In the absence of a spouse, domestic partner and entitled children, the parents of the deceased or any disabled siblings may be the beneficiaries, but only if they depended economically on the deceased.

### **III. Trusts, foundations and other planning structures**

#### **A. Common techniques**

As mentioned above, the most widely used mechanisms for family estate planning purposes consist of corporate structures in Colombia and abroad, and the use of civil and commercial trusts. Foreign trusts are not commonly used by Colombian nationals, except in the case of persons who own assets and/or businesses abroad. Likewise, nationals who own assets abroad frequently establish private foundations. Despite that, as discussed below, these

foundations are treated as limited liability companies for Colombian income tax purposes, and founders and beneficiaries, as partners in commercial companies; or as fiduciary agreements for equity tax purposes and beneficiaries as fiduciae beneficiaries. In the case in which the beneficiaries have not been determined, the settler will be deemed liable for income and equity tax.

B. *Fiduciary duties (trustees, board members, directors, etc)*

It is important to mention that, in addition to the civil trust described above, Colombian law regulates commercial or mercantile trusts and escrow accounts (*encargos fiduciarios*).

A commercial trust agreement implies the transfer of assets allocated to the fulfilment of a specific purpose to a free-standing trust fund separate from the rest of the assets of the trustee and assigned to said purpose.<sup>16</sup> Only banking institutions and trust companies specially authorised by the Financial Superintendence may act as trustees.

Regarding the duties of the trustee, it should be noted that, as long as a commercial trust agreement is in force, the trustee may not assign the assets to any purpose other than that provided in the constitutive document, except if the settler so decides, when the trust is not irrevocable. Therefore, the purpose established by the settler in the trust agreement is the basis for determining the main tasks that the trustee is required to perform.

Article 1234 of the Commercial Code imposes the duty to fulfil certain non-transferable obligations on the trustee, namely, to:

- diligently perform all necessary acts to attain the purpose of the trust;
- hold the legal capacity for the protection and defence of the assets assigned to the trust against the acts of third parties of the beneficiaries and even of the settler him or herself;
- invest the earnings obtained from the trust in the manner and according to the requirements established in the constitutive documents;
- seek the highest profitability from the assets destined to the fiduciary business, except for a determination to the contrary in the constitutive document; and
- render verified management accounts every six months and transfer the assets to the appropriate person according to the constitutive documents or the law on the expiry of the term of duration.

According to commercial legislation, the trustee shall be liable up to ordinary negligence in the fulfilment of its duties.

In this respect, the Colombian Financial Superintendency has ruled<sup>17</sup> that a trustee is required 'to act diligently and prudently, always seeking to fulfil the purpose established in the constitutive document, being required, in order to attain said purpose, to observe the non-assignable duties imposed both by the law and by the trust agreement, a duty that must correspond to that required from every professional in relation to the administration of third-party affairs'.

Furthermore, in the matter of taxes applying on the funds of the trust, trustees must pay any value added and withholding taxes that may be incurred because of the transactions of the trust, as well as the corresponding default interest, penalties and indexation, where applicable.

In the matter of income taxes, trust companies are authorised to file a single return for all the free-standing trust funds they manage.<sup>18</sup> The National Government will specify which individual trusts are to be discriminated, in which case, the trustee will be required to file a separate tax return for the specific trust.

The trust company will keep a disaggregated listing in case the tax administration requires specific information.

When it is not possible to identify the beneficiary of a trust because, for instance, the trust is subject to certain conditions precedent or subsequent, earnings must be declared by the settler for income tax purposes.

Beneficiaries or trustors, on the other hand, must report the earnings obtained during the same tax year in which they accrue in favour of the free-standing trust fund, retaining their nature as taxable or non-taxable, and with the same description and tax conditions they would have if they were received directly by the beneficiary or the trustor, for income tax purposes.

Escrow, however, is characterised by the delivery of the assets without the transfer of ownership by the settler to the trustee to fulfil the purpose established for the benefit of a third party or the settler him or herself. In this regard, the Financial Superintendence (formerly the Banking Superintendence) in the Basic Legal Circular Communication, distinguished between a commercial trust and escrow, covering the latter with the rules of a mandate agreement.

In accordance with the foregoing, from a tax point of view, the trustee in escrow complies with the duties of an agent and therefore must identify any income received on behalf of the principal and the payments made in his or her name in its accounts, and must perform all tax withholdings derived from the transactions carried out under the trustor's instructions, but it will be the latter, in his or her capacity as principal, who is required to declare the income and apply for the respective costs, deductions and deductible taxes according to the information provided by the trustee.

In the case of a civil trust, the law provides that the trustee will have free management of the assets, given that until the condition is met, he or she is the owner of the assets in the trust. Nevertheless, the trustee is responsible for any impairments or deteriorations derived from acts or negligence. For tax purposes, bearing in mind that the trustee holds the ownership and possession of the assets until the condition occurs, the obligation to declare the assets and revenue of a civil trust applies to the trustee, unless it is provided that the proceeds of the assets belong to the trustor. In this case, these must be reported by the latter.

#### *C. Exchange control treatment of foreign trusts and foundations*

Pursuant to Colombian exchange regulations, Colombian residents may set up trusts abroad, which shall be regarded as capital investments in the financial sector.

The amounts to be contributed to said trusts must be channelled through the exchange market in the form of foreign currency and amounts entitled to reimbursement. The investment is deemed to be registered on the filing of the pertinent exchange declaration with the Banco de la República, in accordance with the regulations of said entity.<sup>19</sup>

### **IV. Taxation**

#### *A. Domicile and residency*

As provided in Articles 9, 12 and 20 of the Tax Code, individuals, both national and foreign, who qualify as non-Colombian residents are only subject to income and complementary taxes on income or capital gains from a national source. In the case of foreign investors holding a permanent establishment (PE) in Colombia, Article 66 Law 2010, 2019 establishes that income tax is assessed on the national and foreign income that is attributable to the PE.

Colombian residents are subject to taxes on global source income, so Colombian residents must report earnings on a worldwide basis. Foreigners residing in Colombia are only subject to taxation on their domestic and foreign income after 183 days of continuous or discontinuous permanence in Colombia including days of arrival and departure during any 365 consecutive calendar day period.

In the case of foreign individuals residing in Colombia, net worth taxes on a global basis will be applicable as of the first year of residence within the country.

Likewise, nationals who meet one of the following conditions are considered residents, even if they themselves remain abroad:

- when the spouse or domestic partner or minor dependent children have tax residence in Colombia;
- when 50 per cent or more of their income is from a national source;
- when 50 per cent or more of their assets are managed in the country;
- when 50 per cent or more of their assets are deemed to be possessed in the country;
- when having been required by the tax authorities, they do not prove their residency status abroad for tax purposes; or
- when the individual is a tax resident in a country qualified by the National Government as a low-tax jurisdiction, non-cooperative jurisdiction or preferential tax regime.<sup>20</sup>

Nevertheless, nationals who meet any of the conditions referred to above are not considered Colombian tax residents if, and when, they comply with one of the following requirements:

- 50 per cent or more of their annual income has its source in the jurisdiction of their domicile; or
- 50 per cent or more of the national assets are located in the jurisdiction of their domicile.

As previously noted, Colombian law establishes that an unsettled succession is subject to income tax, and therefore earnings, revenue and assets previously belonging to the decedent that are part of the succession must be declared in the succession. Likewise, for an unsettled succession, deceased persons who were not residing in the country at the time of their death do not qualify as Colombian residents and are only subject to income tax on revenue and capital gains from a local source, and to equity tax with respect to the assets held in the country.

Inheritance, legacies and donations, and funds received as the marital share will be considered as earnings subject to inheritance tax, regardless of the location of the assets that are part of the estate in the case of Colombian succession.<sup>21</sup>

Tax accrues on the date of the execution of the partition or distribution decision. The amount of capital gains received by reason of inheritance, legacies, donations and marital shares is the value of the property and rights on 31 December of the year immediately preceding the date of the settlement of the estate, or on execution of the donation or the legal act *inter vivos* whereby assets are transferred gratuitously, as applicable.

In the case of the following goods and rights, the succession value is determined as follows:

- the value of cash deposits will be assessed at a nominal value;
- the value of gold and other precious metals will be assessed at market value;
- the value of vehicles shall equal the annual commercial assessment by the Ministry of Transport;

- the value of shares, contributions and other rights in companies will be determined at cost value;
- the value of credits will be a nominal value;
- the value of assets and loans in foreign currencies will be market value, expressed in the national currency;
- the value of securities, bonds, certificates and other negotiable instruments that generate interest and financial income will be cost plus discounts or returns accrued and not paid on the last day of the taxable period;
- the value of trust rights shall be 80 per cent of the net worth value;
- the net worth value of the rights in the trusts for the beneficiaries is that corresponding to their participation in the liquid assets of the trust at the end of the year or on the date of the statement of account. For the beneficiaries, the assets retain the condition of mobilised or immobilised, or monetary or non-monetary assets that they have in the trust;
- the value of real estate shall be the higher value between the acquisition cost and fiscal cost;
- the value of income or periodical payments from trusts, private foundations and other similar vehicles, established in Colombia or abroad, to individuals residing in the country will be the total value of the respective income or periodical payments; and
- the value of a temporary usufruct must be determined in proportion to the total value of the asset given in usufruct at a rate of five per cent of the value for each year of the usufruct without exceeding 70 per cent of the value of the asset. The value of a life usufruct is 70 per cent of the total value of the asset given in usufruct. If the assets were acquired by the decedent during the year of death, the value of the asset may not be assessed for less than cost.

Current legislation determines that the transfer of marital property does not constitute income generating a net increase in the amount of net worth, and consequently is not taxed.

The assets listed below are exempt from tax on capital gains in the following amounts:

1. the first 13,000 UVT (COP 551,356,000/US\$140,221.36) of the value of the real estate of a dwelling owned by the taxpayer;
2. the first 6,500 UVT (COP 275,678,000/US\$70,110.68) of real property other than the dwelling owned by the taxpayer;
3. 3,250 UVT (COP 137,839,000/US\$35,055.34) of the value of the allocations received by the surviving spouse and each one of the heirs or legatees, as the case may be, on account of a marital portion, inheritance or legacy;
4. 20 per cent of the value of the goods and rights received by persons other than the legitimates and/or the surviving spouse on account of inheritances and legacies; and
5. 20 per cent of the goods and rights received on account of donations and other *inter vivos* legal acts celebrated free of charge, without such sum exceeding the equivalent of 1,625 UVT.

#### B. Equity tax

Law 2277 of 2022, section 35, consecrated a permanent equity tax (previously, this tax was established on a temporary basis), which is generated by the possession of equity as of 1 January of each year, that is valued equal or higher than 72,000 UVT (COP 3,053,664,000/US\$776,610.61).

For tax purposes, the concept of equity is equivalent to the net assets assessed on the total gross equity of the taxpayer owned on the mentioned date minus the debts payable by the taxpayer in force on the same day.

The following are subject to equity tax:

1. individuals and unsettled successions that are taxpayers of income tax or income tax substitute regimes;
2. individuals, national or foreign, *who do not have residence in the country*, with respect to their *assets owned directly in the country*, with exceptions provided for in international treaties and domestic law;
3. individuals, national or foreign, who do not have residence in the country, with respect to their *assets held indirectly* through *PEs* in the country, with exceptions provided for in international treaties and domestic law;
4. unsettled successions of deceased persons without residence in the country at the time of death with respect to their patrimony owned in the country; and
5. foreign companies or entities that are not income tax payers in the country and that own assets located in Colombia, other than shares, accounts receivable and/or portfolio investments in accordance with section 2.17.2.2.1.2 of Decree 1068 of 2015 and section 18-1 of the Colombian Tax Statute, such as real estate, yachts, boats, motorboats, works of art, aircrafts or mining or oil rights. Equity tax does not apply to foreign companies or entities that are not income tax payers in the country that enter into financial leasing contracts with entities or persons who are resident in Colombia.

Equity tax rates are progressive and apply as follows:

UVT ranges		Marginal rate (%)	Tax
From	To		
>0	72,000	0.00	0
>72,000	122,000	0.50	(Taxable base in UVT - 72,000 UVT) × 0.5%
>122,000	239,000	1.00	(Taxable base in UVT - 122,000 UVT) × 1.0% + 250 UVT
>239,000	Onwards	1.50*	(Taxable base in UVT - 239,000 UVT) × 1.5% + 1,420 UVT

\*The rate of 1.5 per cent will only apply on a temporary basis during the years 2023, 2024, 2025 and 2026.

#### 1. RULES TO ADJUST THE TAXABLE BASIS

- In the case of individuals, the first 12,000 UVT (COP 508,944,000/US\$129,435.10) of the net value of their home or apartment is excluded. This exclusion applies only with respect to the house or apartment where the individual lives most of the time; therefore, recreational property, second homes and any other property that does not meet the condition of being the place where the individual lives are not covered by this exclusion.
- The value of the shares in national companies or entities that are not listed in the Colombian Stock Exchange or one of recognised international standing as determined by DIAN *corresponds to the fiscal cost* determined according to the provisions of the Colombian Tax Statute. The shares purchase cost may be updated annually under the terms of Article 73 of the Colombian Tax Statute as of the year of acquisition. The shares or quotas of corporate interest acquired before 1 January 2006 shall be deemed to have been acquired in the year 2006.

If the value of the *updated fiscal cost* is greater than the *intrinsic value* of the shares, the latter shall be taken.

The intrinsic value shall be calculated by dividing the book value of the net assets of the company as of 1 January of each year by the number of outstanding shares or quotas of corporate interest.

- In the case of shares or quotas of corporate interest in national companies or entities *listed* on the Colombian Stock Exchange or one of recognised international standing as determined by DIAN, the value of the shares shall correspond to the average market quotation for the year or fraction of year immediately prior to the date of taxation.

The rules above shall be applicable to assessing the equity value of rights in *investment vehicles* such as mercantile trusts or collective investment funds holding shares or quotas of social interest of national companies or entities in accordance with Article 271-1 of the Colombian Tax Statute, as far as these do not contradict the following paragraph:

- Participation in private interest foundations, trusts, insurance with a material savings component, investment funds or any other fiduciary business abroad shall be assimilated into fiduciary rights and, in this case, the provisions of sections 271-1 (patrimonial value of fiduciary rights) and 288 (difference in exchange rate) of the Colombian Tax Statute shall be applied.

The fiscal cost of shares in national companies shall not be adjusted provided the company issuing the shares fulfils the following requirements:

- the company is an innovative emerging company, meaning that its incorporation was not prior to four years and its purpose is the development

of an innovative and scalable business, and involves the intensive use of digital technologies within its main economic activity;

- the company has received at least 105,000 UVT (COP 4,453,260,000/US\$1,132,557.14) of capital investment during the current taxable year or in the four immediately preceding taxable years in exchange for at least five per cent of participation in the capital of the company;
- the company had no taxable net income as of 31 December of the immediately preceding taxable year; and
- the fiscal cost of the shares of one or more of the non-founding or initial shareholders of the corporation is at least three times the intrinsic value based on the net worth of the corporation as of 31 December of the immediately preceding taxable year.

### C. *Taxes on income and capital*

Income deriving from an increase in the value of the taxpayer's net worth is subject to income tax in Colombia. Income may be in the form of cash or kind, ordinary or extraordinary, and from a domestic or foreign source. As mentioned, individuals who qualify as Colombian residents are subject to tax on earnings from both domestic and foreign sources. Non-residents are subject to tax only on their income from a domestic source.

Income from a domestic source is considered to include earnings derived from the exploitation of both tangible and intangible assets in the country and from the provision of services in Colombia, either permanently or transitorily, with or without a commercial establishment. The following, among others, are deemed to be income from a domestic source:

- capital income derived from real estate property located in the country, such as rentals or encumbrances to secure the payment of annuities;
- profits derived from the sale of real estate property located within the country;
- earnings derived from real estate property exploited within the country; and
- interest derived from credit held in the country or economically related to it. Exempt from income tax is interest derived from transitory credit that originated from both the import of goods and bank overdrafts.

Ordinarily, the income tax basis is assessed by subtracting from the sum of all ordinary and extraordinary income realised during the tax period, the costs attributable to such income and pertinent deductions, thereby obtaining the net income which, except for applicable exemptions, will be taxable income.

Income tax is generally assessed on the ordinary net income and, as an exception, on the increase in the value of the net worth from one year to the other, when such increase is not justified by valorisations or capital gains.

Applicable income tax for individuals is established progressively, with the maximum income tax rate for individuals being 39 per cent.<sup>22</sup> Any unsettled successions will be taxed on the aforementioned basis.

Under income tax regulations currently in force, trust agreements will be governed by the rules of the country where the agreement is entered into and performed.

Settlers of foreign trusts will only be required to report the investment abroad as long as they keep their share in the trust.



For income and complementary tax purposes, any Colombian residents receiving periodical rentals from foreign trusts or private foundations, are subject to capital gains taxes at 15 per cent.

Private interest foundations are equated to limited liability companies and subject to income tax. Under that qualification, these entities are taxed on their Colombian source income at the general rate of 35 per cent.<sup>23</sup>

Founders are required to report the value of their contribution as an investment abroad for the purposes of Colombian income tax. Assets will also be part of the basis for the net worth tax.

It should be noted that, in Colombia, non-profit foundations and associations are subject to a special tax system.<sup>24</sup> For such a purpose, Decree 2150 of 2017 consecrated the conditions that must be met by an entity to qualify as a non-profit corporation, foundation or association under the special tax regulations:

1. the main corporate purpose of the entity and any funds raised by the entity must be invested in health, sports, formal education, cultural, scientific or technological research, ecological or environmental protection activities. or social development programmes;
2. the said activities must be of general interest; and
3. their surplus must be totally reinvested in activities that correspond to the corporate purpose. Non-profit entities may not distribute earnings to the founders, managers, directors and so on. If they do, the entity will be excluded from the special tax system and taxed as a commercial entity.<sup>25</sup>

This system applies to foreign entities that comply with the three requirements established in the regulation, as stated by the Council of State in Decision 16467 of 2010.

To be admitted within the special tax system, entities must file a request to the tax authority demonstrating their compliance with all the substantial and formal requirements stated above.

## Notes

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<sup>1</sup> A verbal will only occurs in cases of imminent danger to the life of the testator. Similarly, to make a military will, the testator must be in a war expedition or campaign against the enemy or at a garrison in a territory under siege. A maritime will may only be granted on board a Colombian warship at sea.

<sup>2</sup> A verbal will has no value if the testator dies after 30 days following its execution or, if having died before, the will was not set down in writing within 30 days following the death. In the case of a military will, if the testator dies within 90 days following the date on which the circumstances of war that enabled him or her to grant a military will have ceased, his or her will is valid, but if the testator survives this term, then the will becomes invalid. A maritime will is not valid unless the testator has died before disembarking or during a period of 90 days following disembarkation.

<sup>3</sup> The following are legitimes: descendants and ascendants.

<sup>4</sup> According to Art 1502 of the Civil Code, capacity may refer to enjoyment or action. The former consists of the general legal competence of every individual or legal entity to hold rights and assume obligations. The capacity to act consists in the ability recognised by law to a person to bind him or herself, without the intervention or authorisation of another person.

<sup>5</sup> Persons suffering from a severe or profound learning or behavioural condition or pathology, or mental impairment are considered to suffer from absolute mental disability.

<sup>6</sup> Whoever requests recognition as a party must fully evidence such capacity through documentary proof.

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<sup>7</sup> A UVT is a Tax Value Unit. The value of a UVT for the year 2023 is COP 42,412 (approximately US\$10.78) at the rate of exchange in force on 28 July 2023, ie, US\$1 = COP 3,932.04.

<sup>8</sup> The request for intervention may be filed until the decision approving the partition is issued.

<sup>9</sup> The law presumes the existence of community property when there is a de facto marital union in a period of no less than two years. It should be highlighted that the Constitutional Court, in decision C-029 of 2009, stated that the expressions 'singular, permanent and continuous union', 'domestic partner' and 'domestic partnership' contained in Colombian positive law must be read and interpreted in the sense that they all refer, all conditions being equal, to same-sex couples.

<sup>10</sup> One or several executors may be appointed, in which case, the judge may divide the administrative powers corresponding to each at the request of the executors themselves or of a party with an interest in the succession proceedings. If there are any executors with common powers, they must all authorise all acts and contracts related to the administration of the decedent's estate. All executors are jointly and severally liable, except when the testator has divided their powers or exempted them from such joint and several liability, or when the judge segments the functions.

<sup>11</sup> The prohibition to delegate does not prevent the executor from entering into mandate agreements for the proper administration of the decedent's estate.

<sup>12</sup> The denouncement of an inheritance is a call made by law to an heir or legatee to state his or her acceptance or renunciation at the time of the death of the deceased.

<sup>13</sup> In the case of discrepancies regarding the administration of the estate, receivership, that is, the judicial administration of the assets, may be ordered at the request of any interested party. If there is no request for receivership, the judge may settle any conflicts between the spouse, heirs and executors through an incidental proceeding or a simple judiciary order. Once the performance of his or her duties has ended, the administrator of the succession must hand over the assets as appropriate, according to the relevant partition judgment or public deed and submit a report on his or her administration by presenting the relevant accounts to the judge for approval under penalty of the commencement of a separate proceeding for the rendering of accounts.

<sup>14</sup> Art 496 of the Colombian Code of Civil Procedure.

<sup>15</sup> The attachment is enforceable if the asset was mortgaged prior to the date of the recording of the encumbrance as a family dwelling, or after said date if a mortgage was created in order to acquire, build or improve the dwelling subject to family encumbrance. Additionally, members of the family group of an old or disabled beneficiary of a common risk pension who dies and members of the family group of a person affiliated to the system (not yet pensioned) who dies, are entitled to the survivors' pension, provided the deceased has contributed to the system for 50 weeks during the last three years immediately preceding the death.

<sup>16</sup> Art 1227 of the Commercial Code provides: '[t]he assets subject to the trust are not part of the general security of the creditors of the trustee and only secure obligations contracted in furtherance of the intended purpose'.

<sup>17</sup> Opinion No 2003018295-1, 23 May 2003.

<sup>18</sup> It is provided for this purpose that the Tax Administration must assign a Tax Identification Number (Numero De Identificacion Tributaria or NIT) different from that of the trust company that identifies all trusts administered as a whole.

<sup>19</sup> Exchange registration is not necessary when transactions are carried out abroad with foreign currency that need not be channelled through the exchange market.

<sup>20</sup> It is worth noting that, since Law 1819 of 2016, the Colombian tax system has substituted the notion of 'tax havens' for low-tax and non-cooperative jurisdictions, as well as preferential tax regimes. The government has the task of listing the jurisdictions that fall within the above categories. However, the Tax Office has stated that, regarding preferential tax regimes, the taxpayer is required to verify whether the estate where the relevant economic activities take place meets the conditions to qualify as a preferential tax regime as per Art 260-7.

<sup>21</sup> From the tax compliance perspective, it is worth noting that Colombia has entered into agreements with different countries for the automatic exchange of information following the Common Reporting Standard (CRS). Colombia has also executed an exchange of information agreement with the United States under the Foreign Account Tax Compliance Act (FATCA).

<sup>22</sup> S 241 of the Colombian Tax Code establishes the progressive marginal rates for income tax applying to individuals residing in Colombia. S 247 of the same statute includes the income tax rate applying to non-resident individuals.

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<sup>23</sup> For 2023, the statutory income tax rate is 35 per cent, according to s 10, Law 2277 of 2022.

<sup>24</sup> Entities belonging to this system are subject to income tax, but have the benefit of assessing the tax at the special rate of 20 per cent on the net profit or surplus, which shall be exempt in the portion reinvested for the fulfilment of their corporate purpose. Likewise, they will not be required to calculate the tax on the presumptive income system (minimum alternate income tax system) nor will they be subject to withholding taxes, except for income obtained from financial yields or industrial and marketing activities.

<sup>25</sup> Art 1.2.1.5.1.41 of Decree 2516 of 2016 consecrates the events where there is a deemed indirect distribution of earnings by entities covered by the Special Tax Regime:

- (i) when the remuneration to individuals in managing positions exceeds 30 per cent of the annual expenditure of the entity;
- (ii) when payments for services, rentals, fees, commissions, interest, special bonus and similar do not meet the market standards;
- (iii) when any type of reimbursement for the founder contributing the funds upon incorporating the non-profit organisation or for other donors contributing funds is generated;
- (iv) when the entity is dissolved and liquidated without distributing the surplus in accordance with Art 649 of the Colombian Civil Code;
- (v) when the Colombian tax authorities determine that any agreements or onerous transactions with founders, contributors, donors, legal representatives and administrators, spouses and relatives within the fourth consanguinity or affinity grade or within the only civil grade, or with legal entities where the mentioned individuals possess more than a 30 per cent share, constitute indirect distributions of the earnings in the non-profit entity under Art 356.1 of the Colombian entity; and
- (vi) when the provisions in para 3, Art 356-1 of the Colombian Tax Code on indirect distributions of excess profits and excess remuneration to directors and other managing positions are not complied with.