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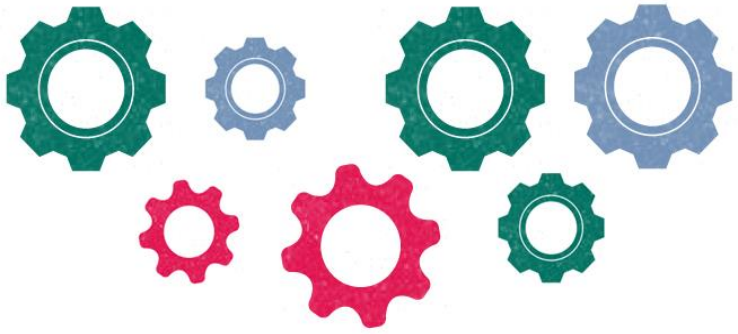
Foreign Workers In Colombia

August 2016 - Newsletter
Number 292



Ministry of Labor - Concept No. 161586, September 19, 2014

Given the recent concerns on this issue, we raise the opinion of the Labor Ministry regarding the requirements to be met by foreigners who want to work in our country, and the related obligations regarding affiliation with the social security system. It is based on the National Constitution, whose Section 4(2) sets out: "*All nationals and aliens in Colombia must comply with the Constitution and the Law, and respect and obey the authorities*", in line with Section 2 of the Substantive Labor Code (S.L.C.) "*Territorial Application: This Code is in force in the entire territory of the Republic and applies to all inhabitants, regardless their nationality*".

The regulations mentioned specify that the law's territorial principle also applies to labor regulations, that is to say, all labor contracts executed in the country, with one or both parties being foreigners, shall be ruled by the Substantive Labor Code despite of the fact that the labor relation begins in Colombia and the worker is later transferred abroad, since "*it will be governed by the legal regulations in force in the country where the contract became legally valid*" (we underline). This means that if the contract became valid under Colombian laws, it will remain as such, for months or years. Likewise, the effects of the termination of a labor relationship will be decided by Colombian Labor Courts. If the contract is executed in another country, then such labor contract shall be ruled by the laws of said country.

Consequently, the applicable social security regime, social benefits and indemnifications when the contract is executed abroad shall be those of the relevant country, and vice versa. In exceptional cases, if the contract is executed in Colombia, there must exist a covenant or treaty that allows application of a foreign law should the service be rendered in a different country, provided the minimum guarantees offered by domestic legislation are maintained. (Ruling T-1021/2008).

It must be taken into consideration that a labor relationship is established between the parties from the very moment a worker begins to develop a personal, continuous, subordinate and paid activity, with all obligations arising from a labor contract; and further, that the hiring of a foreign worker shall be subject to Colombian laws, in other words, to all requirements for the issuance of visas that the Colombian government grants to aliens who enter the country as workers.

Bonuses Paid on a Regular Basis – Non Salary Agreement

Council of State - Rulings 20687 of March 2, 2016 and 21519 of March 17,

The ruling includes the term "regular" to emphasize that the law allows the parties to freely agree on the compensation items do not deemed to be part of the salary. Such "regular" bonuses have been rejected by tax auditors during several particular audit procedures, evidencing an undue and erroneous understanding of the labor laws, which interpretation should have been left to officers well versed in labor matters or following jurisprudence that accepts the fact, like the one we are here presenting.

In this case, the Council of State rules on the items not deemed to be part of the salary; it must be taken into consideration that labor legislation is explicit and clear in this regard, as foreseen in Section 128 S.L.C. - Payments not Deemed Salary (amended by section 15 of Law 50 of 1990): "*Amounts occasionally and paid to workers merely on the will of the employer, such as bonuses or occasional rewards, (...) or regular benefits or allowances agreed upon under collective bargaining or the contract, or those granted voluntarily by the employer, when the parties have explicitly defined that they are not part of the salary in cash or in kind, such as meals, housing or clothing, voluntary bonuses, vacation bonus, half-yearly bonus or Christmas bonus, are not part of the salary*" (we underline).

To construe the mentioned section it is necessary to link it to section 17 of Law 344 of 1996, that allows employers to agree with their workers on such payment items not deemed salary in their relationship; for that purpose "*it is enough to evidence the existence of a covenant, whether under a bargaining agreement or under a contract, wherein the parties have explicitly agreed that certain payments are not part of the salary, for them to be excluded from the base to calculate the contributions and not required to claim for deduction thereof*" (brings as reference Ruling under Dossier No. 17329, July 8, 2010, see **Bulletin No. 241**; text underlined).

Mention is also made that "*based on the same legal regulation and on section 17 of Law 344 of 1996,* ***the bonuses or benefits -whether occasional or regular- are not salary either, provided they are not mandatory and the parties explicitly agree that they are not part of the salary***. *... making it clear that the so called non-mandatory regular bonuses are not part of the salary if employer and employee have so agreed, which, as mentioned, means that, just like occasional bonuses paid on the mere will of the employer, they can be excluded from the salary*" (in reference to Dossier No. 20030, August 6, 2014, see **Bulletin No. 282**; text highlighted).

All employers as well as government-owned and private entities must contribute 3% of the monthly payroll as payroll taxes (Law 89 of 1998). For the purposes of estimating such contribution, monthly payroll means all payments made of the various comprehensive salary elements pursuant to the Labor Law, specifically Sections 127 and 128 of the S.L.C.: "*regular or occasional non-mandatory benefits or bonuses agreed upon as non-salary, are not to be included in the base to calculate payroll taxes, since they are not salary*" (we underline).

An additional consideration is that regardless of the covenant that has effect only for labor purposes, all of bonuses or allowances, as general rule and for tax purposes, are levied with the income tax and subject to tax withholdings (See DIAN concept No. 0026, filing 0002, of January 15, 2016).

Practical Effects of The Tax Book

As you are probably aware, under International Financial Reporting Standards, given that accounting figures may vary, the Tax Administration has designed two systems based on which taxpayers will be in a position to control such differences (between amounts carried and taxable bases): the mandatory recording system foreseen in Section 3 of Decree 2548 of 2014, and the tax book pursuant to Section 4 ibidem. We must remember that the Tax Book is a subsidiary ledger for tax purposes only, where economic events having an effect on the estimation of taxable bases are to be recorded.

Tax Administration has pointed out that the Tax Book is to be kept pursuant to Decrees 2649 and 2650 of 1993, which for this purpose are in force. Also, it has stated that there is no legal obligation to register such book before any authority (section 175 of Decree-Law 019 of 2012) nor there is a model to be followed regarding how to keep it, and that taxpayers may keep the book manually or electronically at the option of taxpayers mandated to carry books of accounts, provided the authenticity, truthfulness and integrity of the information therein contained are guaranteed, in a manner that the records allow identifying, among other: (a) voucher, (b) date of the document and the register, (c) transaction amount, (d) identification of the third party involved, (e) accounting account affected, (f) "*the development of the recording, that is to say, debits and credits as well as the balances of the economic events therein recorded*", as well as "*a summary explanation of the differences between amounts recorded in the books and those recorded in the difference recording system*"

On the other hand and consistent with the matter, the DIAN has stated that Certified Public Accountants are not responsible of certifying the Tax Book, since not only such book lacks an accounting nature, but such formality is not required by legal regulations in force. However, a Public Accountant must participate in the preparation thereof, since, as accepted by jurisprudence of the Constitutional Court "*A Certified Public Accountant collaborates and advises individuals in the compliance with their accounting and tax-related obligations*" (Ruling C-645 of 2002).

Migrant Workers Taxation

DIAN Concept 10479 of April 29, 2016

At this time the Tax Administration analyzes the situation for tax purposes of foreign workers deemed to be "migrant workers" in the light of the Convention on the Protection of the Rights of All Migrant Workers - Law 146 of 1994.

Tax regulations in Colombia set out that it is an individual's residence for tax purposes what is relevant for assigning tax liabilities and not the individual's nationality. Based on the above, the DIAN states that taxation of foreign workers with labor contract in Colombia must be analyzed considering the following aspects:

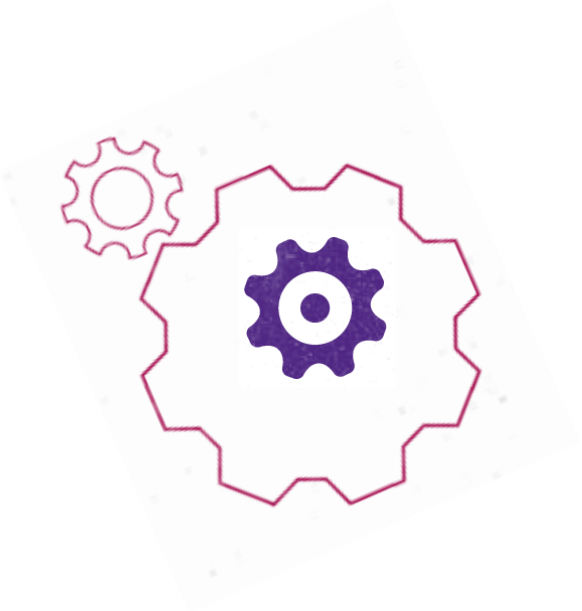
i. To qualify a foreign worker as a "migrant worker" and apply the provisions contained in the International Convention, the worker must come from one of the countries that are part to such Convention, since from the text thereof in line with the Vienna Convention, international treaties only take effect among signatory Countries that have agreed to it; for this reason, no obligations can be imposed on or bind third Countries that have not expressed their agreement to bind themselves and reciprocally comply with the provisions of a convention.

ii. Analyze whether or not the migrant worker is a resident of Colombia for tax purposes, since the following scenarios are possible depending on the actual situation:

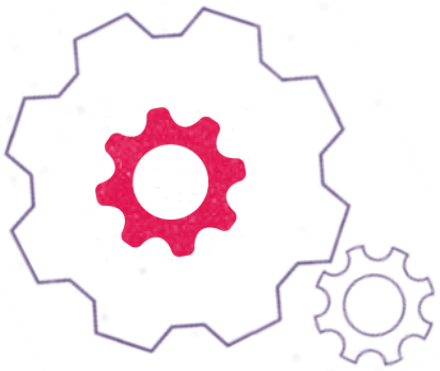
- A migrant foreign worker not deemed a resident for tax purposes: is levied a 33% tax pursuant to Section 247 of the Tax Code, applicable only on revenues obtained in the country.
- A migrant foreign worker deemed a resident for tax purposes: is levied at the tax rates set out in Section 241 of the Tax Code (according to the gradation in the chart) with the exemptions applicable to revenues from domestic and foreign source
- A Colombian worker deemed a resident for tax purposes: is levied at the tax rates set out in Section 241 of the Tax Code (according to the gradation in the chart) with the exemptions applicable to revenues from domestic and foreign source.
- A Colombian worker not deemed a resident for tax purposes: is levied a 33% tax pursuant to Section 247 of the Tax Code, applicable only on revenues obtained in the country.

From the above it is clear that the DIAN's view is that under the International Convention the tax treatment applicable to a migrant foreign worker is identical to that of a Colombian worker who is under similar circumstances regarding **residence (but not nationality)**, following a change in legislation implemented in 2013 that prioritizes residence over nationality, event in which the income tax shall be levied at the rate applicable to a Colombian resident (Section 241 Tax Code).

A foreign worker in Colombia coming from a country that is a party to the Convention on the Protection of the Rights of All Migrant Workers shall be treated equally under similar circumstances regarding the rights and levies he is subject to, and entitled to the same deductions and exemptions. Nevertheless, the criterion to determine the applicable income tax rate and the taxable base to apply such rate, is that of ***"residence"***; consequently, a foreign worker who does not meet the requirements to be deemed a resident of Colombia for tax purposes shall assess his tax at therate applicable to non-residents (Section 247 Tax Code).



Such position is debatable and not shared consistently, given that the Convention is aimed towards non-resident foreigners to be treated on an equal footing with Colombian residents, as mentioned in the same doctrine, reason why such doctrinal restrictions regarding to whom the Convention is to be applied to based on nationality, residence and signatory country, do not match the contents thereof. Further, such restrictions turn its application meaningless since the same tax treatment and differences intended to be applied would result from the application of domestic laws without the need for a Convention; the effects arising from a convention or without a convention are none. Its scope is to benefit and give equal treatment to those who migrate to Colombia seeking to provide a service without the intended discrimination arising from factors forbidden by the Convention.



Verification Of Contributions To Apply The Deduction For Provision Of Services

DIAN's concept No. 12361, May 19, 2016

In response to the request for clarification of Communication 12887 of 2015 (see **Bulletin No. 285**, which sets out that a contractor is required to pay contributions regardless the term of the relevant service agreement (it repealed the requirement of contracts with a term of more than three months), and reaffirms that "*regardless the term of the service agreement, the contracting party shall verify the affiliation and payment of contributions*".

It is supported on the Communication dated December 23, 2014 from the Legal Department of the Ministry of Health and Social Protection on the obligation to contribute to a pension system regardless the term thereof applicable to the health system, Concept No. 966871 of July 6, 2014 from the same Legal Department that regarding services provided by an individual states that not only the contractor is mandated to be affiliated with such social security systems, but that "*the contracting party shall verify the affiliation and payment of contributions regardless the term of the contract*". Summarizing, it mentions that "*there is no legal exception regarding amounts, term or nature of the contracts that limit the enforceability of the obligation of verifying the affiliation of the contracting parties with the General Social Security System for Health and Pensions, and payment of contributions thereto*".

Among others, it quotes Communication 082702 of 2013 (only payments to the contributive system are accepted, not to the subsidized system; see **Bulletin No. 276**).

Withholdings Certificate VS. Accounting Records

Dossier No. 18250, May 31, 2012

Even if not recent, on the grounds of certain particular cases identified regarding the matching of information with third parties on any issue where there is legal discussion, it is worth mentioning situations similar to this one related with the evidence supporting reported taxes withheld. In these cases it is obvious that priority is given to information from third parties over the information of the taxpayer under investigation. However, it is noted that when the same taxpayer provides information in his capacity as third party as part of an investigation against another taxpayer, then his information is credible, what denotes a certain conflicting position in jurisprudence of this type.

In this particular case, it mentions that the differences identified between the figures in the taxpayer's books of account and withholding certificates issued by third parties were not explained by the taxpayer, even rejecting his own accounting records, as compared to the certificate issued by a third party (where it is noticed that the adequacy of such third party's accounting records was not verified, and despite it is also accepted that "*they made accounting mistakes*". We should think about what would happen if such taxpayer in turn in a different proceeding certifies withholdings under a tax audit conducted on a different taxpayer; under this jurisprudential position his certificate would have been more credible (with or without proper accounting support), what did not happen when he himself was the subject of the audit.

This ruling sets out that the tax withholding certificate is special evidence to recognize withholdings, yet "*it is not the only evidence to that purpose*", since it can be replaced with another evidence. In the particular case, even if various pieces of accounting evidence and certificates by the statutory auditor were provided, it was considered that on the whole they were inadequate to supersede the withholding certificate in the belief that such pieces of evidence did not meet the requirements of Section 381 of the Tax Code.

And even if the details of the proceeding are unknown, even having provided all of the accounting records (which we assume contain all invoices issued as well as all payment vouchers evidencing all deductions including the withholdings under discussion) and having issued the company's statutory auditor certificates, one cannot understand that in addition to all other pieces of evidence conviction is reached that the certificate should have been supported by invoices or equivalent documents, as suggesting that the taxpayer did not issue such invoices or that he should have attached them all despite the certificate (apparently he is not being prosecuted or penalized on the grounds of such deficiency).

Yet the Court Room believes that such evidence must challenge "*the certainty arising from the document issued by the withholding agent*" without evidence in the proceedings of any investigation on the feasibility, reliability and proper support of the accounting records of the party issuing and endorsing such certification.

Even if the ruling clarifies that it is not that "*more credibility was given to the certificates issued by the withholding agents, but that being such documents adequate to evidence the withholdings at the source and, consequently, the revenues that were taken as the base thereof, the detail, amount, taxable year, etc.*" they must prevail over the certificates issued by the statutory auditor, and by the way we can affirm, over the taxpayer's accounting records since those are taken from such records.

Finally, the message is that even if the certificates or information requested are not available, to replace them the taxpayer must gather together all documents and supporting evidence at hand in order for them to jointly comply with each and every requirement to be met by the main proof or special proof as set out by the jurisprudence, to compensate the lack thereof, since during a tax audit it is always a trend to prioritize the information provided by third parties regardless of the manner in which such information is obtained or supported, for the audited is not the third party but the charged taxpayer.

Sincerely,

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