The Netherlands and Colombia Have Signed a Tax Treaty

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On 16 February 2022, the Netherlands and Colombia signed a tax treaty for the elimination of double taxation and the prevention of tax evasion and avoidance (the Treaty). The Treaty prevents double taxation and contributes to the economic interests of both countries.

Currently, no official date has been published as to when the Treaty will take effect. However, entry into force will occur after parliamentary ratification and the exchange of ratification instruments between the contracting states.

This GT Alert summarizes the contents of the Treaty.

Contents of the Treaty

Colombia is an important partner for the Netherlands in Latin America, and the Treaty removes potential barriers that could otherwise impede economic activities in Colombia and the Netherlands. The Treaty is largely based on the Organisation for Economic Co-operation and Development (OECD) and UN model treaty.

The Treaty contains provisions to prevent tax avoidance. With these provisions, the Treaty meets the minimum standards of the so-called Base Erosion and Profit Shifting project of the OECD/G20 (BEPS) against tax avoidance.

Permanent Establishment

For purposes of the Treaty, the term “permanent establishment” means a fixed place of business through which the business of an enterprise is wholly or partly carried out.

A permanent establishment will also be deemed present if an enterprise provides services in a contracting state through employees or other engaged personnel if the activities continue for longer than 183 days within any 12-month period.

Furthermore, a building site, construction, assembly or installation project, or supervisory activities in connection therewith, but only if such site, project, or activities last more than 183 days, will be deemed a permanent establishment.

Dividends, Interest, and Royalties

The Treaty provides for the taxation of dividends, interest, and royalties to be capped in certain cases.

Dividends may be taxed in the source state, but if the beneficial owner of the dividends is a resident of the other contracting state, the tax so charged shall not exceed 5% if the beneficial owner is a company holding at least 20% of the capital of the dividend-paying company over a 365-day period that includes the day of the dividend payment. Otherwise, the tax so charged shall not exceed 15% (however, a 0% rate applies if the beneficial owner of the dividend is a recognized pension fund resident in the other contracting state).

The source state may tax interest, but if the beneficial owner of the interest is a resident of the other contracting state, the tax so charged shall not exceed 5% of the gross amount of the interest paid in connection with a loan granted by a financial institution for infrastructure projects with a term of at least three years. Otherwise, the tax so charged shall not exceed 10%.

The source state may also tax royalties arising in that state, but if the beneficial owner of the royalties is a resident of the other contracting state the tax so charged shall not exceed 5% of the gross amount of the royalties for the use of, or the right to use, industrial or scientific equipment. Otherwise, the tax so charged shall not exceed 10%. The royalty definition in the Treaty follows that of the UN Model Convention and therefore includes fees for the use or right to use industrial, commercial, or scientific equipment.

Capital Gains

According to the Treaty, gains a resident of a contracting state derives from the alienation of shares or other rights representing the capital of a company resident of the other contracting state may be taxed by that other contracting state if the resident of the first mentioned state owned, at any time within the 365 days preceding the alienation, 20% or more of the capital of that company. However, this tax charged shall not exceed 10% of the net amount of such gains.

Furthermore, gains derived by a resident of a contracting state from the alienation of shares or other rights representing the capital of a company resident of the other contracting state may be taxed (in full) by that other contracting state if, at any time within the 365 days preceding the alienation, these shares or comparable interests derived more than 50% of their value directly or indirectly from the commercial value of immovable property situated in that other state.

Exchange of Information and Arbitration

Agreements have been made about the mutual exchange of information and assistance in the collection of taxes. The Netherlands is also the first country with which Colombia has made agreements on arbitration. This ensures that if taxpayers from Colombia or the Netherlands have a dispute about double taxation, and the competent authorities of the two countries do not resolve it, they can submit their dispute to a fixed group of industry experts, who will give a binding ruling.

Anti-Abuse Provision

The Treaty includes a comprehensive anti-abuse provision in line with the BEPS project that prevents the Treaty from being used to avoid taxation. This provision allows a country to deny a taxpayer Treaty benefits if a company funnels money through the Netherlands or Colombia purely to avoid tax by using the Treaty (treaty shopping).

A resident of a contracting state will not be entitled to the benefits of the Treaty unless the resident is a qualified person as defined in the Treaty (Limitation on Benefits). Furthermore, the Treaty includes a general anti-abuse provision (Principal Purpose Test), which provides that a benefit under the Treaty shall not be granted in respect of an item of income if it is reasonable to conclude that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the Treaty.

Furthermore, the article contains a provision that implies that treaty benefits can still be granted at the request of the taxpayer if those benefits, or other benefits, would have been granted in the absence of the relevant constructions or transactions. The competent authorities to whom a request is addressed will consult with the competent authorities of the treaty partner before rejecting the request.

Multilateral Instrument

The Treaty would not be a covered tax agreement for the Multilateral Instrument because neither of the two contracting states has included it in its notification at this time. However, the language of the Treaty itself is in line with the Multilateral Instrument.

Conclusion

The Treaty will enter into force when both contracting countries have ratified it in accordance with national constitutional procedures. Subsequently, the Treaty’s provisions shall take effect on the first day of January in the calendar year following that in which the Treaty has entered into force.

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