

3. Foreign Trade and Customs Rules

Colombia enjoys a strategic geographic location and a privileged position to access international markets through commercial agreements and tariff preferences that guarantee the best conditions for the sale of Colombian products in foreign markets. Additionally, Colombia has customs procedures that are agile, efficient and modern, in accordance with current international trade standards.

3.1 Foreign Trade Procedures

Colombian legislation has concentrated on facilitating customs operations for imports, exports and transit of goods by regulating the application of various forms of foreign trade, conforming to the guidelines of the World Trade Organization Treaty ("WTO") (approved by Law 170 of 1994), aimed at promoting and supporting different benefits for the companies associated with this sector in Colombia.

Since 2005, Colombia implemented the Single Window for Foreign Trade ("VUCE"), managed by the Ministry of Commerce, Industry and Tourism. This Window, based on electronic and Internet media, has the purpose of consolidating all the government procedures related to foreign trade operations. To these ends, it has three independent sections: Imports, Exports and the Single Foreign Trade Form ("FUCE"), that allow on-line transactions such as electronic payment, aiming to speed up the procedures. More information on VUCE may be obtained at the website www.vuce.gov.co

3.1.1 Imports

Imports, according to customs rules, consist of the entry of goods to the "national customs territory" from the rest of the world, or from a Free Zone, with the purpose of remaining permanently or temporarily in it for the achievement of a specific purpose.

The importation processes before the DIAN [the Colombian Internal Revenue and Customs Service] can only be carried out by users registered in the Customs Information System, either Customs Agencies (previously called Customs Intermediation Companies) or Permanent Customs Users ("UAPs"). The latter may file their own customs declarations, as long as the value of the imported goods exceeds the sum of US \$1,000; otherwise, they must do it through the Customs Agencies.

3.1.1.1 Ordinary importation

This is the most widely used mode of importation. With it, the importer in Colombia receives the goods for his free disposal, once he has completed all customs procedures. The obligations include the declaration of the goods, in the formats established by the customs authorities, the payment of all applicable customs duties, including tariffs and value added taxes ("VAT"), and obtaining the final release order.

The valuation of the goods is done according to the methods established by the General Agreement on Tariffs and Trade (GATT).

The importation declarations have a standing term of three (3) years.

3.1.1.2 Temporary importations

3.1.1.2.1 Temporary importation for re-exportation in the same condition

Temporary importation is defined as the importation with suspension of customs duties (tariffs and VAT) for certain goods that, at the end of the specified period, must be exported in the same condition as they came in to the national customs territory, that is, without having experienced any modification, except for the normal depreciation originated by their use. The sale of the goods will be restricted. These importations may be of two classes:

Short Term

Applies when the goods are imported to attend to a specific need that determines their brief stay in the country. The maximum importation term will be six (6) months, which may be extended up to three (3) additional months and in exceptional cases for up to three (3) more months with prior customs authorization. The customs duties on this type of temporary importation are permanently suspended, unless the importer decides that the goods will stay permanently in Colombia.

Long term

Applies to the importation of capital goods, their accessories, parts and spares, as long as they constitute one single shipment. The maximum term for this importation is five years. Customs duties will be deferred in semi-annual payments, which in any case must be paid during the time that the goods stay in the national customs territory.

3.1.1.2.2 Temporary importation for active perfecting

The kinds of temporary importation for active perfecting allowed in the customs statutes are:

Temporary importation for active perfecting of capital goods

This type allows the temporary importation with suspension of customs duties, of capital goods destined to be re-exported after being subjected to repairs and reconditioning in a term no longer than six (6) months, which can be extended for an equal period. The disposition of the goods will be restricted.

Temporary importation for industrial processing

This type allows the temporary importation of raw materials and supplies that are going to be subjected to transformation, processing or industrial manufacture by industries recognized as "Highly Exporting Users" ("ALTEX"), and authorized by the customs authority (DIAN). The sale of the goods will be restricted

3.1.1.3 International leasing

The concept of international leasing may be applied to long term financing of temporary importations of capital assets, which may remain in the National Customs Territory for more than five (5) years. Under this concept, a foreign company (foreign supplier, foreign financial institution or leasing company) grants the right of use of imported capital assets in Colombia to a Colombian resident in exchange for periodic payments by the latter. Payments must be made through the mechanisms authorized by the foreign currency exchange regulations and following the procedure established for passive external debt operations, because the operation is considered to be a financed importation. In this case, the customs duties are caused bi-annually. The maximum term for deferment is 5 years, regardless of the fact that their actual stay in the country may be higher than this period.

This system has the following advantages:

- a. Payment of customs duties (tariffs and VAT) are carried out in semi-annual payments within a maximum period of five (5) years.
- b. Operative leasing is not subject to "integral inflation adjustments" on the part of the lessee, since it is not registered as an asset.
- c. In the case of operative leasing, the lessee may deduct on his income tax statement 100% of the payments transferred abroad (until 2012).
- d. The payments made to the leasing company when it is a foreign leasing company without registered offices in Colombia are not subject to income tax withholding in the country (as they are not domestic income).
- e. There is a 40% income tax deduction on investments effectively made through financial leasing with an irrevocable purchase option.

3.1.2 Exports

Exports, according to their legal definition, are foreign trade operations consisting in the exit of goods from the National Customs Territory with destination to the rest of the world or to a Free-Trade Zone.

In Colombia, exports do not cause customs duties and are privileged by a large amount of mechanisms, such as, among others:

- a. Special export and import programs – Vallejo Plan.
- b. International Marketing Agents (*Comercializadoras Internacionales*), which are businesses specifically established to purchase national products for export, granting the manufacturers and the suppliers all the benefits as if they were exporters.
- c. Special export programs ("PEX") of tax reimbursements.

Furthermore, exports are benefited by a large number of international agreements granting tax preferences.

3.1.2.1 Special export programs – PEX –

These programs allow the treatment as exports of sales made by a domestic producer to a foreign company, even though the products are not exported directly by him, but delivered to another domestic company to be transformed and exported as a finished product.

Through these PEX operations an agreement is made under which a foreign resident purchases raw materials, supplies, intermediate goods, packaging material or bottling from a Colombian company and arranges its delivery to another Colombian producer who in turn, commits to manufacture and export the products manufactured from the goods received.

PEX programs must be approved by the DIAN and allows the direct or indirect exporter to have access to the tax benefits granted to exporters, VAT exemption, and the exclusion of Industry and Commerce Tax and of the Stamp Tax at the moment of export of the finished goods.

3.1.3 Special Import and Export Programs – Vallejo Plan

In order to promote foreign trade operations, Colombia has included in its customs legislation special importation - exportation programs through which goods or equipment may be imported with tax benefits as long as the exportation agreements of finished goods or services are fulfilled.

The following are among the current types of Plan Vallejo:

3.1.3.1 Exportation – Vallejo Plan for raw materials

This type allows the receipt, within the National Customs Territory, under Decree Law 444 of 1967 and Order 1860 of 1999, with total or partial suspension of customs duties, of specific goods destined to be totally or partially exported within a certain period of time, after having undergone transformation, manufacture or repair, including the materials needed for these operations.

Under this type, machinery, equipment and spare parts may also be imported, to be used partially or entirely in the production and sale, of goods and services destined for export. The goods so imported remain under restrictions of sale.

Starting on January 1, 2007, customs duty exemptions for the importation of capital goods, spare parts and intermediate goods were eliminated, except for products for the agricultural sector not related with subsidies (Order 11 of 2003, Ministry of Commerce).

Plan Vallejo benefits are granted by direct operation to the importer of goods, raw materials or supplies, who produces and exports the finished goods, or by indirect operation to the importer or producer of intermediate goods sold to the exporter, or to whoever provides the associated services with the production of the goods to the exporter.

3.1.3.2 Vallejo Plan for exportation of services

This type, applicable to the exports of companies whose main activities are lodging services, human health, air transportation of passengers, research and development, consulting and management, architecture and design, engineering, special design services, value-added telecommunications and software exports, allows the temporary importation of capital goods listed in Decree 2331 of 2001, with total or partial suspension of duties and deferment of payment of Sales Tax. In addition, it allows the temporary importation of spare parts for the aviation industry.

Those having access to this program must export services, as a minimum, for an amount equivalent to 150% of the FOB value of the imported capital goods and spare parts, guaranteeing the authorized use of the capital goods and spare parts temporarily imported and not to sell them or give them a use different from that authorized while the goods are under restrictions as to disposition.

3.1.3.3 Replacement or junior Vallejo Plan

This type grants the exporter of goods the right to replace, through a new importation exempted of duties, the raw materials or supplies that have been used in the production of such goods, when the all customs duties were originally paid (tariffs and VAT) upon importation (art.183 of Decree 2685 of 1999). This reposition right must be requested within the 12 months following the shipment of the exported products.

3.1.4 Free-Trade Zones

In order to promote commerce, investment and the creation of sources of employment in the country, in Colombia there are Special Permanent Free-Trade Zones or “Single-Company Free-Trade Zones” and Permanent Free-Trade Zones, which depart from the general guidelines applied in the rest of the national territory.

In essence, these Free-Trade Zones are geographic areas of the national customs territory with boundaries established by the national customs authority, within which customs duties do not apply and in most cases where reduced rates in income taxes apply.

Following are the levels of investment required to access the benefits of a Free-Trade Zone. The amounts, by law, are calculated in Current Minimum Legal Monthly Wages (“SMMLV”), however they are expressed in Dollars at an exchange rate equivalent to Col\$2,500 per US Dollar. The Minimum Monthly Wage for 2008 was Col\$481,500. Both the SMMLV as well as the exchange rate may vary.

3.1.4.1 Types of Free-Trade Zones

3.1.4.1.1 Special Permanent Free-Trade Zone or “Single-Company Free-Trade Zone” – ZFPE or ZFU –

With this special type a single company may request the establishment of a Free-Trade zone in order to develop a new investment project. Depending on the economic sector in which the project will take place, the following requirement must be met:

Special Permanent Free-Trade Zone or ZFU of Goods

For its establishment a minimum new investment of US \$ 29.8 million must be made and 150 new direct jobs must be created. For each US\$4.6 million over the minimum required investment, the number of jobs to be created can be reduced by 15. In any case the project may use fewer than 50 employees.

Special Permanent Free-Trade Zone or ZFU of Services

For its establishment any of the following levels of investment and employment job creation must be met:

| Investment Range (in Millions) | Jobs Directly Created |
|--------------------------------|-----------------------|
| Between US\$ 2 and US\$ 9.1 | 500 |
| Between US\$ 9.1 and US\$ 18.3 | 350 |
| Higher than US\$ 18.3 | 150 |

If the project is developed in different geographic areas, exceptionally the establishment of a ZFE may be requested for each.

Special Permanent Free-Trade Zone or ZFU for Agro-industry

For its establishment a minimum new investment of US \$14.9 million must be made or 500 direct or related jobs must be created. The projects must certify their connection with the areas farmed and domestic raw materials.

Special Permanent Free-Trade Zone or ZFU of Ports Company

For its establishment a minimum new investment of US \$29.8 million must be made and twenty (20) new direct and fifty (50) related jobs must be created.

Special Permanent Free-Trade Zone or ZFU for pre-existing investments

For its establishment, the investor must meet the following 3 requirements:

- a. Net assets of more than 150,000 SMMLV (US \$29.8 million)
- b. Make new investment within 5 years following the declaration of more than 692,000 SMMLV (US \$137.5 million)
- c. Double the net taxable income calculated as of December 31 of the year before the date of the declaration

This type of Free-Trade Zone may be chosen by companies that were favored with the Special Tax System under the Paez Law, for whom the requirements are less.

3.1.4.1.2 Permanent Free-Trade Zone – ZFP –

It is an area within the national territory in which multiple companies are organized, enjoying a special tax and customs treatment, managed by a “User Operator”.

For the creation of a new ZFP the User Operators must meet the following requirements:

- a. The project to be developed must have a minimum area of 20 hectares

- b. The User Operator must have net assets of more than US \$ 4.6 million for a ZFP and US \$457.000 for a ZFPE.

Within five (5) years following the declaration, the ZFP must have installed at least five (5) users that make new investments of more than US \$9.1 million.

3.1.4.2 Kinds of Users

Every Free-Trade Zone, Special Permanent, or Permanent must have a User Operator. Within its perimeter, commercial (only in Permanent Free-Trade Zone - ZFP) or industrial users may operate and among the latter, there can be industrial users of goods and/or of services.

To be qualified as a user in a ZFP, the interested party must request authorization from the User Operator.

To be qualified as user in a Special Free-Trade Zone, the interested party must obtain the recognition (statement) from the customs authority (DIAN).

In order to produce goods, render services or carry out commercial activities within the ZFP, industrial users must meet the following requirements, depending on the total assets of the company:

| Total asset range of the company | Minimum amount of the new investment to be made | Minimum amount of direct jobs to be created |
|--|---|---|
| Between US\$ 0 and US\$ 99,000 | US\$ 0 | 0 |
| Between US\$ 99,001 and US\$ 1 million | US\$ 0 | 20 |
| Between US\$ 1 million and US\$ 6 millions | US\$ 1 million | 30 |
| More than US\$ 6 millions | US\$ 2,3 millions | 50 |

3.1.4.2.1 User operator

The User Operator is a company dedicated to the management and control of customs matters. In the ZFP the User Operator is also in charge of promoting its creation and development and of qualifying to each commercial or industrial user who requests to operate inside the same.

3.1.4.2.2 Industrial users of goods

These are users that manufacture, produce, transform or assemble goods inside the Free-Trade Zone.

3.1.4.2.3 Industrial users of services

These are users that that render services within or from the area of the Free-Trade Zone , to develop, among others, the following activities: Logistics, transportation, distribution, telecommunications, scientific and technological research, medical assistance, dental and medical health in general, tourism, technical support, ship and airplane equipment, consulting or similar.

3.1.4.2.4 Commercial users

These are users that store, market, preserve and sell within the corresponding Free-Trade Zone. They may occupy up to 5% of the total area of the ZFP. They cannot be located in a ZFPE or a ZFU.

3.1.4.3 Incentives

Free-Trade Zones offer the following incentives to their users:

3.1.4.3.1 Tax and Customs

- Single flat 15% income tax rate for all users of the Free-Trade Zones, except for Commercial Users with general income tax rate.
- Exemption of customs taxes (VAT and tariffs) for the introduction of goods from abroad, while the goods remain in the Free-Trade Zone. Taxes are caused when the goods are permanently introduced into the national territory.

- c. Possibility of nationalizing the goods manufactured in the Free-Trade Zone, using the tariff sub-item of the finished product and paying taxes on the added value of the foreign supplies, or nationalizing the raw materials before entering the production process, with their own tax entry.

3.1.4.3.2 Procedural

- a. Quick and simplified introduction procedures.
- b. Possibility of introducing foreign goods, nationalized goods and domestic goods for temporary storage, in general with the sole authorization of the User Operator of the Free-Trade Zone, without having to go through national customs procedures.
- c. Possibility of temporary removal of raw materials for partial processing outside of the Free-Trade Zone for a period of up to 9 months.
- d. Ease of handling of inventories and logistics operations between Border Free-Trade Port Zones and Interior Port Free-Trade Zones.

3.1.4.4 Introduction of products to Free-Trade Zones

Sales made from the rest of the national territory to users of the Free-Trade Zones are treated as sales tax (VAT) exempt when referring to finished products, raw materials and supplies that are inside the Colombian territory, as long as these goods are going to be used in production processes related to the activities of the industrial users of the Free-Trade Zone in which they are going to be introduced or are destined for export.

These benefits do not apply when the goods are introduced to the Free-Trade Zone for temporary processes of passive perfecting.

3.1.5 Highly Exporting Users – ALTEX –

Companies recognized as “Highly Exporting Users –ALTEX” by the DIAN, enjoy a series of tax and administrative benefits. For their recognition they must meet the following requirements:

- a. Have exported during the 12 months prior to the filing of the request, an amount equal or higher than US \$ 2,000,000
- b. That the value of exports, directly or through an International Marketing Agent , represents at least 30% of the amount of its domestic sales in the same period.
- c. When not meeting the previous conditions, certify, prior to the request, directly or indirectly exported FOB amounts equal or higher than US \$21,000,000 regardless of the sales percentage to the export markets.

Among the tax benefits for ALTEX are:

- a. No levy of VAT in ordinary importation of industrial machinery that is not produced in the country, destined for the transformation of raw materials.
- b. Possibility of obtaining the authorization, on the part of DIAN, of an industrial processing warehouse that allows the importation of supplies and raw materials with suspension of customs duties and of VAT, as long as they are used in the production of exportation products.

3.1.6 Authorized Customs Warehouses

Authorized Customs Warehouses are public or privately-owned spaces approved by the customs authority for the storage of goods under customs control. The goods may remain temporarily stored in the authorized customs warehouses, without payment of customs duties (VAT and tariffs) applicable to their importation or nationalization, for the duration established in the law, while their customs situation is defined.

Among the privately-owned customs warehouses are:

- a. Private warehouses for transformation or assembly.
- b. Private warehouses for industrial processing.
- c. Private warehouses for international distribution.
- d. Private warehouses for aviation.
- e. Transitory private warehouses.
- f. Warehouses for urgent deliveries.

The authorized warehouses cannot carry out activities of cargo consolidation or de-consolidation, transport or customs intermediation, with the exceptions established by law.

In order to apply this concept, the company must certify that it has the minimum technical and administrative infrastructure required by the DIAN, that it does not have previous customs, exchange or foreign trade violations and that it meets the rest of the legal requirements.

3.2 Colombia and the World Trade Organization – WTO –

The WTO agreement came in force for Colombia on April 30, 1995 and since that moment, the country meets all the commitments as full member of this organization. Colombia is a beneficiary of all the rights derived from the principle of Most Favored Nation, from the principle of National Treatment and of all the guarantees established in the Agreement. Among the benefits, there is the protection provided by the WTO mechanism for dispute resolution, to which the member states may have recourse when they consider that the commitments and the agreements ratified in the WTO framework have been infringed by another member.

3.3 Tariff Preferences

3.3.1 The United States – ATPDEA –

Initially the Andean Trade Preference Act –ATPA was a unilateral preferential tariff program granted by the United States in year 1992 to favor economic growth and support the fight against drugs in the Andean countries (Colombia, Bolivia, Ecuador and Peru).

In October 2002, the United States Congress enacted a law by which it extended ATPA and expanded the preferences to products of great importance that were previously excluded. This new law, which is known as ATPDEA (Andean Trade Preference and Drug Eradication Act), allows the entry to the United States without tariffs of certain products that are grown, produced or manufactured in a beneficiary country in the initially approved sectors, including chemical, agricultural, metalworking, plastics, craftsmanship, wood and furniture, paper and lithography, shoes and leather manufactures, oil and its derivatives, among others.

The ATPDEA preferences will be in effect until December 31, 2009 for Colombia, thanks to the latest extension granted by the United States Congress in September 2008.

3.3.2 Generalized Preference System with the European Union – GPS Plus –

At the end of the year 2005, the system called GPS Plus was approved, having as its purpose to stimulate economic and social development and the insertion of the developing countries into the world economy. The system went into effect on January 1, 2006, with a duration of 10 years from that date. Colombia is among the beneficiaries of the System, together with other countries such as Bolivia, Ecuador, Peru and Venezuela.

On July 22, 2008, the Council of the European Union approved the Generalized Tariffs Preferences System for the period between January 1, 2009 and December 31, 2011. Colombia will be a beneficiary of the tariff preferences granted by the European Union as a special stimulus for sustainable development.

3.3.3 Commercial Agreements

In addition to the commercial preferences mentioned above, Colombia has been structuring a policy of open integration, thanks to which it enjoys free markets in the Latin American arena, within the Latin American Integration Association – ALADI.

Among the different agreements signed by Colombia, the most relevant are:

3.3.3.1 Andean Community of Nations – CAN –

One of the strategic integration plans for Colombia is the Andean Community of Nations that works under the auspices of ALADI. By virtue of this agreement, Colombia has exemption of duties and restrictions becoming a Free-Trade Zone with Bolivia, Ecuador, Peru and Venezuela until 2011, after the withdrawal from the agreement by this country in 2006. Additionally, in September 2006, the Council of Ministers of Foreign Relations of the

Andean Nations granted the condition of associated member country to Chile, reaffirming the economic commitments established with that country and expanding the integration framework in the region.

The main objective of the CAN is to deepen the integration through a common market, in which agreements are reached, by consensus and with a supranational character, on monetary, fiscal, currency exchange, environmental and public services policies.

Mexico – Colombia Free Trade Agreement – FTAs (TLCs) – G2 –

This treaty went into effect in 1995, with the participation of Colombia, Mexico and Venezuela. At present, it includes only Colombia and Mexico, since Venezuela withdrew in November, 2006. The agreement includes a schedule of asymmetric elimination of tariffs from the entire set of tariffs that aims to equalize, within a period of 10 years, the tariffs of the 3 countries, giving special treatment to the agricultural and automotive sectors.

The treaty establishes mechanisms to prevent the application of internal protective measures to health and human, animal and vegetal life, to the environment and to the consumer.

3.3.3.2 Economic Complementation Agreement (ACE) with Chile and Colombia – Chile TLC

Through the ACE, a Free-Trade Zone between Colombia and Chile is created, with the gradual elimination of customs duties and non-tariff barriers, eliminating 95% of the duties in bilateral trade, corresponding to 96% of all Colombian tariffs. The remaining percentage will be totally freed, with zero tariffs in year 2012.

Based on the depth reached by the ACE with Chile, both countries decided to initiate the negotiation of a Free Trade Agreement. As a consequence of such negotiations, on November 27, 2006, The final text of the TLC was signed and is presently under review by the Constitutional Court.

3.3.3.3 Free Trade Agreement – FTAs (TLCs) – signed and under Negotiation.

At present, Colombia has signed Free Trade Agreements with the US (2006), Chile (2006), “Northern Triangle” – El Salvador, Guatemala, Honduras (2007), Canada (November 2008) and The European Free Trade Association (EFTA) Switzerland, Norway, Iceland and Liechtenstein (November 2008). The Agreement with the European Union is under negotiation.

3.3.3.4 Economic Complementation Agreement with CAN and Mercosur

On October 18, 2004, the Economic Complementation Agreement was signed between Argentina, Brazil, Paraguay and Uruguay, the countries that make up MERCOSUR, and Colombia, Ecuador, and Venezuela member countries of the Andean Community of Nations - CAN. The Agreement, with an unlimited duration, takes into account the asymmetries derived from the different levels of economic development of the parties, and as a consequence, it determined sub-items for immediate tariff elimination and periods for tariff elimination of between 6 and 15 years for sensitive products such as vehicles, auto parts and electric appliances.

The Agreement includes topics such as dispute resolution, health and plant safety standards, technical regulations and safeguards.

3.3.3.5 Caribbean Community – Caricom –

Caricom is a trade liberalization program that went into effect on January 1, 1995. For its application it takes into account the differences in relative economic development levels of the member countries. The agreement lets Colombia have access to the 4 million consumers of Caricom.

In the framework of the Agreement, Colombia grants tariff preferences to member countries in 1,128 sub-items of products and receives a reduction in tariffs on 1,074 sub-items from Trinidad and Tobago, Jamaica, Barbados and Guyana. The levels of tariff preferences for negotiated products are 100%.

3.3.3.6 Colombia and the Pacific Basin

Moving closer and strengthening the ties with the Pacific basin countries is a priority of Colombian foreign policy. To this end, the Colombian Council of Cooperation with the Pacific (COLPECC) was created.

At present, Colombia belongs to the Pacific Basin Economic Council – PBEC, also called the Pacific Club. This is a non-governmental association made up by the most important entrepreneurs of countries with coasts on the Pacific, whose purpose is to increase mutual knowledge, business and investment flow, economic cooperation, transfer of technology and tourism, among others.

The Asia Pacific Economic Cooperation Forum - APEC is a governmental organization of great economic importance, whose purpose is creating a free trade zone among its members by 2010 at the latest, for the developed countries, and by 2020 for the less developed ones. Presently, Colombia has the position of an observer and participates in the different work groups of this organization. In the future, the country hopes to participate as a full member.

Likewise, Colombia is a full member of the Pacific Economic Cooperation Council – CCEP, a three party non-government organization, made up of the governmental sector, private enterprise and academia.