

### III. FOREIGN INVESTMENT AND TRADE

#### (1) Introduction

1. Since 1991, in the context of the opening of the economy (*Apertura* programme, Chapters I, II, IV and V), Colombia has liberalized its foreign investment régime. A new legislative framework eliminated certain investment barriers and facilitated capital inflows. Foreign investment has been promoted through fiscal and foreign exchange reforms as well as by privatization efforts. As a result, the foreign direct investment (FDI) stock has almost doubled and diversified. The United States remains the major foreign investor in Colombia.

#### (2) Framework for Foreign Direct Investment

2. In the 1990s Colombia's policy objective has been to liberalize foreign investment and stimulate an inflow of foreign capital and technology. Under the 1994 National Development Plan (Chapter I), foreign investment is considered to be an important instrument for the modernization of industry. The need to maintain an open régime and to sign new foreign investment protection agreements is also stressed in the plan.

3. The basic legal framework for the treatment of foreign investment was modified in 1991. New domestic<sup>1</sup> and Andean Group<sup>2</sup> legislation was introduced. Foreign companies were put on an equal footing with local investors, including on matters relating to access to domestic credit facilities. In general, foreigners can now acquire 100 per cent of a Colombian firm, except for those involved in national defence or security, or the processing or disposal of toxic, hazardous or radioactive waste produced abroad and certain real estate activities (e.g., purchase, sale, lease).<sup>3</sup> Special conditions affect foreign investment in hydrocarbons and mining, the financial sector and portfolio investment.<sup>4</sup>

4. In July 1996, new regulations were adopted to introduce more flexibility to the FDI framework. These mainly include: a new definition of the FDI, based in international standards, allowing for the improvement of the registration procedure and reducing foreign exchange risks; the elimination of the prior authorization requirement (*permiso*) which was previously required for investments in public service, oil, mining, energy and portfolio; the suppression of some restrictions in real estate investment authorizing the purchase and sale of bonds by foreign funds; the easing of the additional capital concept (*capital suplementario*) and a decision to encourage portfolio investment by redefining certain concepts

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<sup>1</sup>Law 9 of January 1991; CONPES Resolution 51, 22 October 1991.

<sup>2</sup>Andean Group Decision 291 (Common Régime for the Treatment of Foreign Capital and of Trademarks, Patents, Licences and Royalties, 29 March 1991) replaced Decision 220 of 1987. Previous Andean Group Decisions on foreign investment in the subregion have been restrictive for investors from third countries. Decision 24 of 1971 introduced conditions for the transfer of foreign ownership to locals and limitations on the remittance of earnings; these conditions had to be observed in order to benefit from the preferential trade arrangements. The Decision forbade the access of foreign investors in a number of sectors (public utilities, transport, banking, insurance) as well as those adequately covered by local firms. The subsequent Decision 220 of 1987 maintained similar features but allowed individual Governments to decide which would be the closed sectors and the period required for the transfer of ownership (Europa Publications Limited, 1995, p.683).

<sup>3</sup>Other sector-specific access restraints are discussed below and in Chapter V.

<sup>4</sup>These are contained in CONPES Resolution 51.

such as the institutional and omnibus funds.<sup>5</sup> Reportedly, existing investment-related administrative procedures are generally routine and non-discriminatory. Investment screening and the prior authorization requirement are no longer in force.

5. Constitutional guarantees are now provided to private sector investors.<sup>6</sup> Stability against legislative changes in the area of remittance of capital and earnings is also assured; limitations on the amounts that may be repatriated were eliminated in 1992. The régime now allows the repatriation of profits and does not stipulate that majority share-holding must be transferred to local investors.<sup>7</sup> To guarantee foreign exchange rights, all foreign investment must be registered with the Central Bank.

6. Fiscal obligations on the remittances of foreign investors were modified in the tax reform of 1992.<sup>8</sup> Between 1992 and 1996 the tax on remittances of earnings (*impuesto de remesas*) from foreign investments has been gradually reduced: (i) from 12 to 7 per cent for existing non-oil investments and (ii) from 15 to 12 per cent for existing investment in the oil sector.<sup>9</sup> The rate of the tax on remittances of earnings from foreign investment in the oil sector is to be further cut to 10 per cent in 1997 and 7 per cent in 1998. If earnings are reinvested in Colombia for not less than 5 years, the tax on remittances is waived.

7. As a result of the December 1995 tax reform, ten-year fiscal stability contracts (*contratos de estabilidad tributaria*) can be signed between the Government and the investor (domestic or foreign).<sup>10</sup> These guarantee stability of fiscal treatment by adding 2 percentage points to the general rates of the income and complementary taxes (*impuesto de renta y complementarios*) in force at the time of signing; by opting to pay this higher ceiling rate, the investor is assured that future increases will not affect him. However, if tax rates are lowered, the investor benefits from the reduced rate plus 2 percentage points. At present, both foreign and national private companies are subject to a revenue tax of 35 per cent.

8. All foreign investment in petroleum exploration and development must be carried out by means of an association contract between the investor and ECOPETROL (*Empresa Colombiana de Petróleos*), the State oil company. Apart from other tax liabilities, production is subject to a "war tax" of US\$1 per barrel (Chapter V).<sup>11</sup> Under the tax reform of late 1995, this tax is to be eliminated by the end of 1997 and 2000, respectively, for production and discoveries from 30 June 1992 to 31 December 1994; discoveries made after January 1995 are not subject to the tax. In January 1995

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<sup>5</sup>Centro de Información de Colombia (CIC) (1996). *Informe Económico*, bulletin No. 22, July.

<sup>6</sup>Court ordered expropriation can take place for reasons defined in the legislation and only after indemnity is settled. Article 58 of the 1991 Constitution (Chapter II).

<sup>7</sup>Previously Colombia allowed the repatriation of earnings corresponding to only 25 per cent of the value of the direct foreign investment (GATT, 1990, August, p.116).

<sup>8</sup>Law 6a of 1992.

<sup>9</sup>IMF (1995), p.116; COINVERTIR (1996).

<sup>10</sup>Article 169 of Law 223, 20 December 1995.

<sup>11</sup>The "war tax" on oil companies, introduced as a temporary (until 1997) emergency measure in 1992, was originally levied to finance the defence of pipeline, production and exploration facilities from *guerilla* attacks.

it was announced that the State would contribute by 50 per cent to exploration costs in zones previously reserved for direct exploration by ECOPETROL.<sup>12</sup> In other areas, ECOPETROL re-imburses 50 per cent of these costs after the field is declared commercially viable.

9. In the agro-industrial and automotive sectors, Colombia maintains measures concerning local or regional content that were notified to the WTO Committee on Trade-Related Investment Measures (see also Chapters IV and V) and are to be eliminated by the year 2000.<sup>13</sup>

10. Specific conditions affect the access of foreign investors in a number of services areas, including tourism (establishment in the free zones), marine insurance (no access), consultancy on international law (requirement to be also licensed in Colombian law), franchising, data processing and audiovisual services (50 per cent of each television commercial to be produced locally). Under the Labour Code (*Código Sustantivo del Trabajo*), the movement of persons is also restricted in the transport sector and a number of professional services (e.g., architecture, engineering, construction); for example, in firms with more than 10 employees, up to 20 per cent of the skilled and 10 per cent of unskilled workers may be foreign nationals.

11. In November 1992, the Invest in Colombia Corporation (*Corporación Invertir en Colombia*, COINVERTIR), a mixed-ownership institution, was created to promote, facilitate and diversify FDI inflows. To foster specialization and an equitable distribution of investment in the sub-region, the Andean Development Corporation (*Corporación Andina de Fomento*, CAF), which was established in 1968, conducts research to identify investment opportunities and prepares proposals for investment projects. It also provides technical and financial assistance by attracting internal and external credit.

12. The régime governing the establishment of Andean Multinational Enterprises (*Empresas Multinacionales Andinas*, EMAs) was last modified in March 1991.<sup>14</sup> EMAs must be owned by at least two investors from Andean Group countries (including the host country) each with a minimum capital share of 15 per cent; provided this condition is fulfilled, investors from outside the subregion can also participate. These enterprises may participate in sectors reserved for national enterprises and enjoy national treatment as far as taxation and export regulations are concerned.

13. Since 1986, Colombia has been a member of the Inter-American Investment Corporation of the Inter-American Development Bank and, since 1995, of the Multilateral Investment Guarantee Agency (MIGA) of the World Bank.<sup>15</sup>

14. To improve the framework of guarantees covering foreign investors, Colombia signed the International Convention on the Settlement of Investment Disputes between States and Nationals of other States in 1993. Bilateral investment protection agreements (*tratados bilaterales de fomento y protección de la inversión*) were concluded with Cuba (1994), Peru (1994), Spain (1995), and the United Kingdom (1993). Negotiations to establish agreements with Argentina, Canada, Chile, Germany,

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<sup>12</sup>EIU (1995c), p.16.

<sup>13</sup>Article 5, para. (2) of the Agreement on TRIMs.

<sup>14</sup>Andean Group Decision 292 of March 1991 replaced Decision 169 in force from 1982. More information on the EMAs can be found in the TPR report of Venezuela (WTO, 1996).

<sup>15</sup>MIGA, created in 1985 to provide non-commercial risk insurance to private foreign investors in developing member countries, also provides promotional and advisory services on how to improve the ability to attract FDI.

the Netherlands and Switzerland are to be launched.<sup>16</sup> In 1985, an investment guarantee agreement was signed with the United States Overseas Private Investment Corporation (OPIC) which provides qualified U.S. investors with insurance against political risks (inconvertibility, expropriation, war, revolution, insurrection) as well as financial aid and advice.

(3) Trends and Patterns in Foreign Direct Investment

15. In the 1990s the improvements introduced by the new legal framework, the conclusion of investment protection treaties, privatization plans<sup>17</sup>, and the new opportunities in portfolio investment, reduced uncertainty and are credited with having contributed to the consequent increase in foreign direct and portfolio investment inflows (Chart III.1). In 1993, Colombia was the ninth largest host developing economy to FDI flows. In September 1995, Moody's upgraded Colombia's rating to investment grade in line with Standard and Poor's index, increasing the scope for market diversification and enhancing access to institutional investors.

16. As a result of the improved legal framework and investment opportunities, the stock of FDI has grown and become more diversified. According to COINVERTIR's estimates, by September 1995 inward FDI flows, excluding in oil and portfolio investment, had grown by more than US\$1 billion, or twice the amount recorded for the same period in 1994, an election year.<sup>18</sup> Of this increase, 78 per cent took the form of capital inflows, mostly in foreign exchange.<sup>19</sup> Between 1990 and 1994, the foreign investment stock, excluding oil and portfolio, almost doubled to US\$5.8 billion (Chart III.1).

17. Since 1991, foreign direct investment has been mainly directed to the manufacturing sector. In 1994 manufacturing, mining, and financial services accounted for more than 88 per cent of the stock of FDI. In 1995, 302 parent corporations and 2,220 foreign affiliates of transnational corporations were located in Colombia; since 1987 the number of foreign affiliates has more than doubled.<sup>20</sup> However, since 1991 there has also been a marked acceleration of investment in financial services, including insurance, as well as transport and telecommunication services. Mining (non-oil), which had received most foreign investment in the 1980s, recorded the slowest growth in FDI in this period.

18. While investments from other sources have increased in recent years, the United States remains the source of about two-thirds of the stock of all foreign investment in Colombia (Chart III.1).

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<sup>16</sup>Departamento Nacional de Planeación (1995a), p. 10.

<sup>17</sup>Privatization opened public works to foreign investors for infrastructure projects and sectors previously reserved for the State (e.g., electricity, oil refining, telecommunications, airport services).

<sup>18</sup>The figure includes inflows (in the form of foreign exchange, technology transfer, machinery, debt conversion to capital) and re-investment of profits minus capital reimbursement (*El Tiempo*, 8 February 1996).

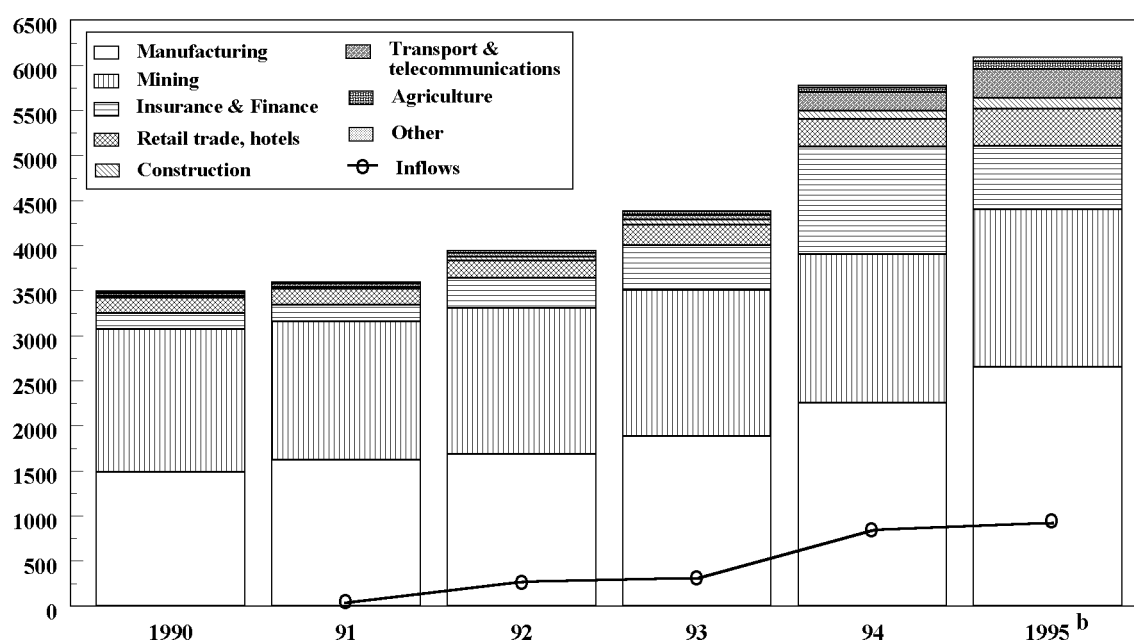
<sup>19</sup>As stated in Chapter I, private capital inflows in the form of FDI constituted one element for financing the current-account deficit in 1993 and 1995 as well as for bringing a surplus to the overall balance in 1994 (EIU, 1995c), p.18; EIU (1995d), pp.19-20; EIU (1995b), July, p.6).

<sup>20</sup>UN (1995); UN (1994), Vol. IV.

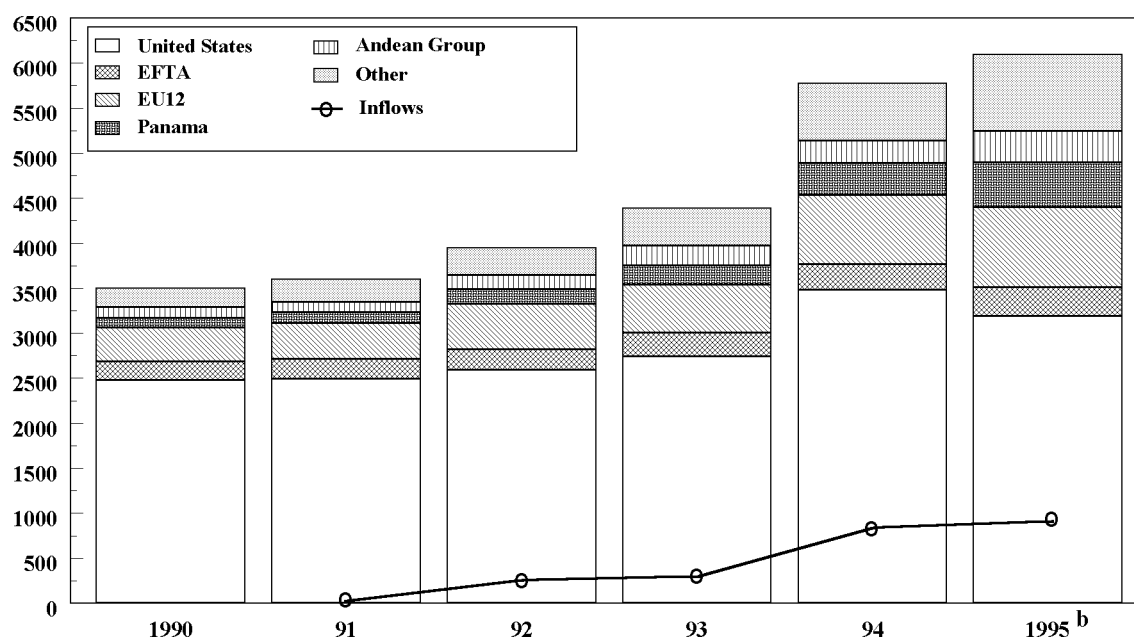
**Chart III.1**  
**Inward stock and net inflows of foreign direct investment, 1990-95<sup>a</sup>**

US\$ million

(a) By sector



(b) By origin



<sup>a</sup> Excluding oil and portfolio investment.

<sup>b</sup> 1995 data correspond to the period January-September.

Source: Banco de la República; and COINVERTIR.

19. Foreign portfolio investment is of minor importance, although it has risen strongly in recent years; more than 90 per cent originated in the United States.<sup>21</sup> Between 1993 and 1995 the stock increased by a factor of 17 (to US\$851 million) and inflows of this type of foreign investment for the period 1992-1994 increased by a factor of 50. The limited extent of foreign portfolio investment reduces Colombia's exposure to capital flight.

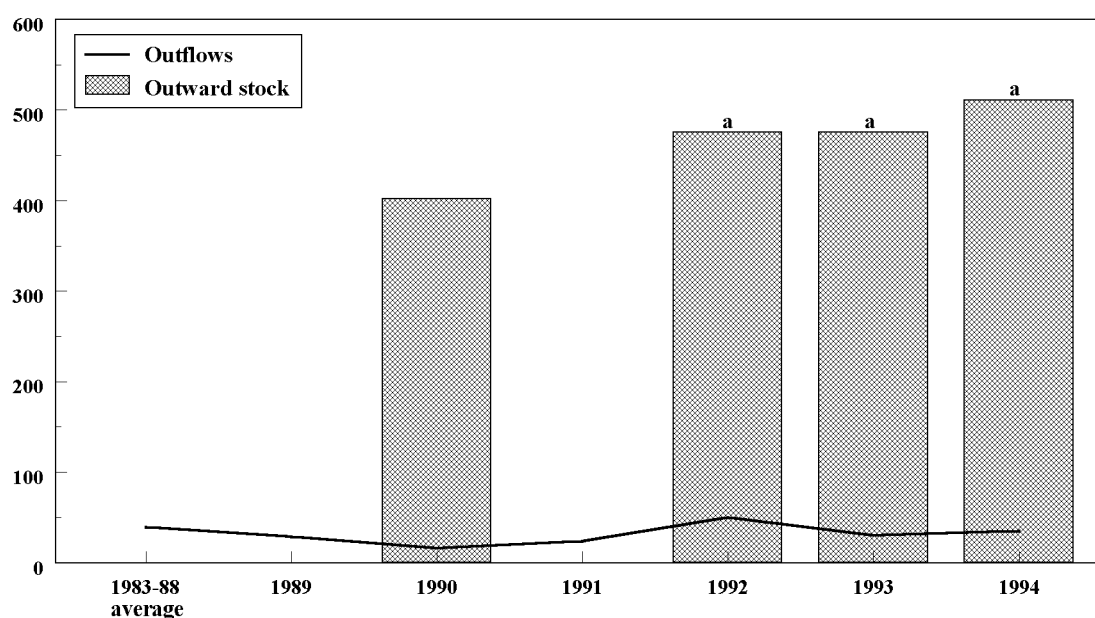
20. The Government expects an increase in the share of all FDI inflows, including oil industry and portfolio investment, from 1 per cent of GDP in 1991 to about 3 per cent in 1995. It is estimated that between 1996 and 1998 total FDI inflows will reach some US\$5 billion.<sup>22</sup>

21. Colombia's outflows of foreign direct investment have been irregular in recent years (Chart III.2); the annual average amount from 1989 to 1994 was about US\$31 million or 20 per cent less than the previous five-year period.<sup>23</sup> According to the Central Bank, the total outward stock grew by 52 per cent to US\$421 million between 1992 and 1994. In 1990, the largest transnational Colombian corporations abroad were in the area of finance, where four banks held total assets of US\$2.7 billion.

### Chart III.2

#### FDI outflows and outward stock, 1983-94

(US\$ million)



a UNCTAD estimates by adding flows to the stock of 1990.

Source: UN (1994 and 1995), *World Investment Report - Transnational Corporation and Competitiveness*.

<sup>21</sup>Data supplied by COINVERTIR.

<sup>22</sup>EIU (1995c), *Country Report 3rd quarter 1995*, July, p. 19; *Departamento Nacional de Planeación* (1995), *Balance Macroeconómico 1995 y Perspectivas para 1996*, CONPES document 2829, December, p. 10.

<sup>23</sup>Investment abroad by Colombians is freely allowed for amounts up to US\$500,000. As stated in Chapter I, to avoid the "dollarization" of the economy Colombians are prohibited from holding foreign currency accounts within the country. As of January 1992 they can hold foreign stocks and other portfolio investments abroad.