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Corporate Tax

Chile – Law & Practice

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CHILE

LAW & PRACTICE:

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The 'Law & Practice' sections provide easily accessible information on navigating the legal system when conducting business in the jurisdiction. Leading lawyers explain local law and practice at key transactional stages and for crucial aspects of doing business.

Law & Practice

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Carey is Chile's largest law firm, with over 200 legal professionals. A full-service firm, the various corporate, litigation and regulatory groups include highly specialised attorneys and practice areas covering all areas of law. Carey's Tax Group has positioned itself as the largest tax practice amongst law firms and a leading competitor in the field, along with the large auditing firms in Chile. Currently, the tax team is comprised of 29 members: three partners, 18 associates, six certified accountants and two law clerks. Carey is the only large law firm in Chile that has in-house certified accountants, which allow the department to provide the client with comprehensive tax advice. The firm has been actively involved in assisting clients to deal with the changes rolling out from the Chilean tax reform of 2014.

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1. Types of Business Entity, Residence and Basic Tax Treatment

1.1 Corporate Structures and Tax Treatment

Businesses generally adopt a corporate form, and Chile allows for three main types of legal entities to be used as business vehicles, all of which grant limited liability to their shareholders or partners: corporations ("sociedades anónimas"), limited liability companies ("sociedades de responsabilidad limitada" or "SRL"), and stock companies ("sociedades por acciones" or "SpA").

- The SRL requires a minimum of two partners and allows a maximum of 50 partners. SRLs generally require unanimous consent to amend their by-laws in any respect, to accept new members or to allow existing partners to assign their interest. The partners have complete freedom to designate the type of management of the company (such as a board or administrator, for example).
- A corporation requires at least two shareholders, and can be publicly held or closely held. A public corporation is one that has issued equity shares registered with the Chilean Securities and Exchange Commission ("SVS"). Registration is voluntary, except where the corporation has 500 or more shareholders, or if at least 10% of its capital stock is held by at least 100 shareholders. Public corporations are supervised by the SVS. All other corporations are closely held and as such are not subject to the supervision of the SVS unless they are issuers of publicly traded debt securities or if otherwise required by a special regulatory framework (for example, insurance companies).

Corporations are managed by a board of directors appointed by the shareholders, with certain specified decisions reserved to the shareholders. The board has the broadest authority over the corporation and its affairs. Closely held corporations must have at least three board members, public corporations at least five, and, under certain market capitalisation and ownership dispersion thresholds, at least seven. Shareholders' resolutions taken in shareholders' meetings are required for certain corporate actions, such as selling more than 50% of the assets, amendments of the corporation's by-laws, merger, transformation (ie to a SRL or SpA) or dissolution. Also, their vote is required during the first four months of the fiscal year (typically set to the calendar year) to approve the corporation's annual accounts, the distribution of dividends and to appoint and revoke the board of directors.

Corporations are generally prohibited from acquiring their own shares and must distribute minimum statutory dividends (30% of net earnings). There are statutory withdrawal rights for shareholders, pursuant to which a shareholder can sell its shares back to the corporation upon certain actions being approved.

- The SpA combines attributes of a corporation (free assignability of equity interests) with the contractual flexibility of the SRL (the SpA does not require unanimous consent for amendments of its by-laws, for example). The SpA can be formed by one or more persons (individuals or legal entities), and allows for any type of corporate agreement, with the exception of a few mandatory rules.

If the SpA, however, reaches the number of equity holders that would render a corporation a publicly held corporation, it will automatically become a public corporation.

Unlike corporations, there are no statutory pre-emptive rights for the SpA (again, except as contemplated by the organisational documents). The organisational documents may indicate minimum or maximum percentages or amounts of capital that are to be directly or indirectly controlled by one or more shareholders. The repurchase of their own equity interests is allowed for SpAs. Furthermore, the SpA may issue preferred shares accruing fixed or variable dividends. Features such as preferred dividends accruing from specific businesses or assets are also permitted.

All these entities are taxed in Chile as separate legal entities. Currently there are no significant tax differences whether the local businesses are operated through an SRL, corporation or SPA.

1.2 Transparent Entities
There are no transparent entities under Chilean tax law.

1.3 Determining Residence
In Chile the residence of incorporated businesses is determined by the place of incorporation.

1.4 Tax Rates
Chilean incorporated businesses are currently subject to a 24% corporate tax on their annual net taxable income.

The Chilean income tax system is considered an "integrated system", because the corporate tax may be credited towards final taxes on dividends. As corporate profits flow from incorporated businesses to the owners, the corporate tax that was previously paid works as a form of advanced tax payment, being creditable against the final taxes of the owners. The final taxes are the global complementary tax, which levies income of Chilean resident individuals with a progressive tax rate from 0% to 40%, and the withholding tax, which levies the income of non-resident individuals or entities with a general tax rate of 35% (hereinafter, jointly the "final taxes"). Therefore, under the Chilean tax integrated system, ordinary income of local entities is subject to corporate tax and final taxes upon distribution (hereinafter, the "ordinary tax regime").

Profits distributions between Chilean incorporated businesses are not subject to taxes.

As a consequence of an extensive tax reform enacted on 29 September 2014 (the "Tax Reform") some cornerstones of the current Chilean tax system were changed. Amongst these changes, the Tax Reform established two different tax regimes that will replace the current regime from 2017 onwards.

The Tax Reform has established, on one hand, an attribution regime that levies with a 25% corporate tax the income obtained by Chilean incorporated businesses each year, which will be immediately allocated to their owners, being the corporate tax fully creditable against final taxes ("Regime A"). Under this regime, the owners of incorporated businesses will pay taxes every year based on the annual results of the company, regardless of actual distributions. Therefore, under this regime the total tax burden of foreign owners of Chilean incorporated businesses will be 35%. Regime A is only available for companies other than corporations, whose partners are Chilean resident individuals, and/or non-Chilean resident taxpayers.

On the other hand, there will be a partially integrated regime that levies with a 27% corporate tax the income obtained by Chilean incorporated businesses in each tax year ("Regime B"). Under Regime B, owners of Chilean incorporated businesses are allowed to defer final taxes until such profits are effectively distributed, but it only allows the use of 65% of the corporate tax paid by the relevant Chilean incorporated business as a credit against final taxes. However, if the owners are resident in a tax treaty country, they are allowed to use 100% of the corporate tax paid by the Chilean incorporated business as a credit against withholding tax. Consequently, under this regime the payment of final taxes is triggered only upon effective distribution of profits. The total tax burden upon distribution of profits will be 35% or 44.45%, depending on whether the foreign owner is or is not a resident of a tax treaty jurisdiction.

In addition, from 2017 onwards the Tax Reform reduces the top tranche of the global complementary tax to 35%.

2. Key Features of The Tax Regime

2.1 Calculation of Taxable Profits

As a general rule, the corporate tax is assessed on the net taxable income determined under full accounting records. For these purposes, income is defined as gross income minus the costs and expenses required to produce that income. In addition, the corporate tax is applied on an annual and accrual basis.

When calculating the corporate tax's tax basis, the following adjustments should be considered:

- In general, assets and liabilities are adjusted by domestic inflation.
- Expenses should be deducted from gross income, provided that:

  (a) they are related to the entity's business (ordinary expenses);
  (b) they are necessary to produce taxable income, considering its nature and amount;
  (c) they have not been previously deducted as a direct cost of goods or services;
  (d) they are incurred in the relevant taxable period, whether paid or accrued; and
  (e) they are supported by appropriate documentation.

- Imported or new fixed tangible assets may, under certain conditions, be depreciated in one third of the normal useful life.

2.2 Special Incentives for Technology Investments

There is no specific patent box regime in Chilean legislation; however, there are some incentives for investments in intellectual property.

In general, expenses incurred in scientific and technological research activities that are developed for the benefit of the company are deductible as a tax expense. These kinds of expenses may be deducted in the same year that they are incurred (whether paid or accrued), or at the taxpayer's option, for up to six consecutive business years.

There are certain special incentives for private investments in R&D. Subject to certain conditions, 35% of the investment in R&D is deemed a tax credit against corporate tax, and 65% is deductible as a tax expense. Under this special regime up to 50% of the R&D activity may be developed in a foreign country. The 35% tax credit is capped at approximately USD950,000 per year.

Capital gains derived from the transfer of intellectual property are subject to corporate tax as a sole tax, provided the transfer is executed by its author or inventor. As a consequence of the Tax Reform, from 2017 onwards gains derived from the transfer of intellectual property executed by a company will be generally subject to the ordinary tax regime.

2.3 Other Special Incentives

VAT cash-refund for investment in fixed assets

Under VAT Law, companies are entitled to request a cash refund for the VAT-credit borne in the acquisition of fixed assets, provided that the following conditions are met:

- The VAT borne must qualify to be a VAT-credit under general rules (ie the company must be engaged in activities subject to VAT, and the VAT borne must be related to those activities).
- The VAT-credit must be related to the acquisition of tangible personal property or real estate destined to be part of the fixed assets of the taxpayer, or to services that are needed to integrate its cost value.
- The VAT-credit must have accumulated for at least six or more consecutive monthly periods.

The amounts refunded through this mechanism must be repaid to the Chilean Treasury if the company does not carry out activities that are subject to VAT after the refund is obtained.

Special regime for Small and Medium Enterprises ("SME")

The Tax Reform established a new preferential framework for taxation of SME. In order to benefit from this special regime, amongst other conditions, the annual average sales of the SME should not exceed approximately USD1.8 million in the last three fiscal years, limited annually to approximately USD2.2 million.

The main benefits of this special regime are:

- Taxation on a cash basis. SME are allowed to use a simplified accounting procedure based on income and disbursements, paying taxes only on the positive difference. In the event that the SME shareholders are all Chilean resident individuals, their income will not be subject to corporate tax, and they will be subject to final taxes only.
- Withholding tax exemptions for certain services provided by non-residents.

- An extended term to pay VAT to the Treasury.

Companies located in the Southernmost and Northernmost Regions
Subject to certain conditions, companies located in the Southernmost and Northernmost regions of Chile are entitled to tax credit for investments used to produce goods or provide services in these regions. The tax credit may be up to 40% of the investment, provided that certain specific conditions are met.

2.4 Basic Rules on Loss Relief
There are no time limits on carry-back or carry-forward of tax losses. However, tax losses may not be deducted from earnings obtained after a change in control occurring during a calendar year if, in addition, any of the following conditions is met:

- As a consequence of the change in control or in the twelve-month period immediately preceding it, the company changed or expanded its main line of business, unless it keeps its original line of business;
- Upon the ownership change, the company does not own capital assets or other assets related to its trade or business that allow the continuation of the same trade or business or the value of which is not related to the acquisition value of the company; or
- Following the ownership change, the company solely obtains passive income from investments in other companies or as a recipient of profit reinvestments.

For these purposes, a change in control is deemed to occur in the calendar year when the new shareholders or owners acquire or end up acquiring directly or indirectly at least 50% of the capital or participation in Chilean incorporated businesses.

An exception to this limitation on the use of losses exists when the change of ownership occurs between companies belonging to the same corporate group.

Income subject to the ordinary tax regime cannot be offset against losses derived from special tax regimes.

As a consequence of the Tax Reform, from 2017 onwards only carry-forward of tax losses will be available in Chile. The carry-back of tax losses will no longer exist.

2.5 Limits on Deduction of Interest
Interest expenses are generally deductible. However, an interest expense may not be deducted if the loans are used to acquire or exploit assets that will not create ordinary income in Chile. The ability to use debt to finance the acquisition of a target company by a local holding company is specifically allowed by Chilean tax legislation.

Interests paid abroad by a Chilean corporation to a related party can be deducted only on a cash basis, provided the applicable withholding tax, if any, is paid.

2.6 Basic Rules on Consolidated Tax Grouping
Chilean tax rules do not provide a tax consolidation regime. However, an indirect tax consolidation may be achieved between a Chilean holding company and its subsidiary through a dividend distribution. The holding company is allowed to offset losses against profits received from its subsidiary, and is entitled to request a refund of the corporate tax paid on the underlying profits distributed by the subsidiary company.

In addition, under the attribution regime enacted by the Tax Reform, a de-facto tax consolidation occurs.

2.7 Capital Gains Taxation
Capital gains derived by corporations are generally subject to corporate tax and final taxes (ie the ordinary tax regime as described under **1.4**). However, subject to some conditions, capital gains on certain assets may be exempted or subject to corporate tax as a sole tax (ie subject to a special tax regime).

Currently, a qualified long-term capital gain derived from the sale of shares is subject to corporate tax as a sole tax. For this purpose, a qualified long-term capital gain requires a one-year holding period, the seller to be non-habitual on the sale of shares, and the purchaser to be unrelated to the seller. As a consequence of the Tax Reform, from 2017 onwards this special tax regime will be eliminated, and capital gains derived from the sale of shares will be subject to the ordinary tax regime.

In addition, the sale of regularly traded and publicly listed stock is not subject to taxes provided some specific conditions are met. This special tax regime was not modify by the Tax Reform.

Capital gain taxes may be reduced if the beneficiary of the income is a resident of a tax treaty country.

2.8 Other Notable Taxes
As a general rule there are no transactions taxes in Chile.

Chilean incorporated businesses could be subject to the following taxes when doing business in Chile:

Value Added Tax (“VAT")
A 19% VAT applies as a general rule, on the price of the following goods and services, amongst others:

- Sales and transfers of tangible goods located in Chile and on real estate also located in Chile and owned by a construction company, provided such operations are performed on a recurrent basis. The Chilean VAT law presumes that all

sales made within an entity's ordinary course of business are recurrent.
- Commercial, financial and intermediation services are subject to VAT when either rendered or consumed in Chile. Professional, consulting and technical services are generally not subject to VAT.
- Import operations, whether customary or not. Exports are exempted from VAT.

The VAT levied on the acquisition of goods or services gives the VAT taxpayer the right for a VAT fiscal credit. This fiscal credit equals the VAT charged in the invoices supporting acquisitions of goods, utilisation of services, imports operations and other VAT-taxable operations.

When the taxpayer sells goods or renders services subject to VAT, the VAT so charged becomes a VAT fiscal debit, which may be offset with the carried-forward VAT fiscal credit. The positive difference between the fiscal debit and the fiscal credit represents the VAT payable by the VAT taxpayer. If the VAT fiscal credit exceeds the VAT fiscal debit, the excess can be carried forward indefinitely.

The VAT Law also establishes certain relief mechanisms that may either exempt certain operations from VAT or allow the taxpayer to request a cash refund for its carried-forward VAT fiscal credit.

Mining tax

Also known as a mining royalty, this tax is structured as an income tax on "mining operational taxable income" (ie the net income determined for corporate tax purposes, with some adjustments) obtained by a "mining exploiter" (ie an individual or entity that extracts a mineral substance and sells it at any stage of production).

The rate is progressive, pursuant to the value of the annual sale of mining products, expressed in metric tons of fine copper (MTFC), determined according to the average price of copper on the London Metal Exchange. Thus, mining exploiters whose annual sales exceed the value of 50,000 MTFC are subject to progressive rates ranging from 5% to 14%, depending on their operational margin. Exploiters whose annual sales are valued between 12,000 and 50,000 MTFC are subject to progressive rates ranging from 0.5% to 4.5%. Finally, mining exploiters with annual sales less than 12,000 MTFC are exempt.

Stamp tax

The Chilean stamp tax is applicable mainly on documents evidencing indebtedness for borrowed money, including loans (national or cross-border), notes and bond issuances.

Current rates are the lesser of (a) 0.066% multiplied by the number of months or fraction of a month to maturity; and (b) 0.8%. For loans payable on demand, the stamp tax rate is 0.332%. The stamp tax in each case is applied over the principal amount of the debt.

Municipal licence tax

Commercial investments, industrial and any lucrative activities are generally subject to the municipal licence tax at rates ranging from 0.25% to 0.5%, applied over the tax-adjusted equity, and capped at approximately USD505,000 per year.

Primary industry and extractive activities are also subject to this tax when they include product elaboration processes or when such products are directly sold to the public.

3. Division of Tax Base Between Corporations and Non-Corporate Business

3.1 Closely Held Local Businesses

Most closely held local businesses operate in an incorporated form in Chile. Local businesses are held through legal entities in order to benefit from a deferral of final taxes, amongst other reasons. Moreover, foreign investments are usually structured through a Chilean holding company which allows the foreign investor to (a) achieve an indirect consolidation (the taxable profits of the subsidiary company can be offset against the holding company's losses, as explained in **2.6**), and (b) distribute profits from the subsidiaries to the holding company and reinvest them in Chile without triggering taxation.

3.2 Corporate Rates and Individual Rates

The current corporate tax rate is 24%, whilst individual or final tax rates are (a) a progressive rate from 0% to 40% for Chilean resident individuals (ie the global complementary tax), and (b) a 15% withholding tax rate for foreign individuals who provide professional services (this withholding tax rate is increased to 20% in the case of payments to related companies or when the beneficiary is resident in a tax haven jurisdiction).

There are no specific rules that prevent individual professionals from earning income at corporate rates. Chilean tax legislation allows professional companies (companies incorporated by individual professionals to render professional services) to be taxed at corporate rates in the same way as any other company in Chile. In such a case, the distribution of profits from the professional company to the individual professionals will trigger final taxes as described under **1.4**.

From 2017 onwards, the top tranche of the global complementary tax will be reduced to 35%. In addition, the corporate tax will increase progressively until 2018. The final corporate tax rate in 2018 under the Tax Regime A will be 25% and under the Tax Regime B will be 27%.

3.3 Accumulating Earnings for Investment Purposes

There are no rules that prevent closely held corporations from accumulating earnings for investment purposes.

3.4 Sale of Shares in Closely Held Corporations

Dividends received by individuals from closely held corporations are subject to final taxes where a tax credit for the corporate tax has been paid by the entity over those profits, as per the ordinary tax regime.

The gain derived on the sale of shares in closely held corporations will be taxed in a similar way to the sale of shares in corporations, as explained under **2.7**.

3.5 Sale of Shares in Publicly Traded Corporations

Dividends received by individuals from publicly held corporations are taxed similarly to dividends received from closely held corporations.

As mentioned under **2.7**, capital gains on shares of publicly held corporations are not subject to taxes if the stock is regularly traded, the corporation is publicly listed, and certain other specific conditions are met. Otherwise, the gain is subject to the same taxation as closely held corporations.

4. Key Features of Taxation of Inbound Investments

4.1 Withholding Taxes

Interest

Interest payments made to a foreign lender are generally subject to a 35% withholding tax. A reduced withholding tax rate of 4% may be available for interest payments made on loans obtained from a foreign bank or registered financial entity. However, a foreign loan from a related party financial entity would be subject to thin capitalisation rules.

According to the Chilean thin capitalisation rules, interests, commissions and fees, amongst others, for services corresponding to 'Excessive Indebtedness' determined at the end of the tax year, are subject to a 35% sole tax, with a tax credit for the withholding tax already paid for those concepts. For these purposes, "Excessive Indebtedness" is defined as that which exceeds three times the debtor's adjusted tax equity at the end of the business year. This 3:1 debt-to-equity limit is tested every year in which payments are made abroad on the aggregate of:

- Related-party and third-party debt,
- Local and foreign debt and
- Debt of a permanent establishment abroad.

Reduced rates may be also available for interest payments made to a beneficiary resident in a tax treaty-country.

Dividends

Dividend payments from a Chilean entity to a foreign shareholder are subject to a 35% withholding tax. As a consequence of the corporate tax integration mechanism explained in **1.4**, currently the effective rate of withholding on net dividends is 14.47%, assuming that the underlying profits were subject to a 24% corporate tax.

Item	Amount
Corporate tax basis	100
Corporate tax	(24)
Dividend payment to foreign shareholder	76
Withholding tax basis (dividend payment + corporate tax)	100
Withholding tax	(35)
Corporate tax credit	24
Payable additional withholding tax	(11)
Available to foreign shareholder	65

Chile has negotiated with all its tax treaty partners that this dividend taxation would not be limited by the dividends' article of the treaties as long as the corporate tax can be used as a credit against the dividend withholding tax.

Dividends paid between Chilean resident companies are not subject to taxation.

Royalties

Royalty payments for:

- The use of trademarks, patents, formulas and similar are subject to 30% withholding tax.
- The use of patents or utility models and other industrial designs are subject to 15% withholding tax.
- Tailor-made software is subject to 15% withholding tax.
- Standard software is not subject to withholding tax.

These tax rates may be reduced if the beneficiary of the royalties is resident in a tax treaty country.

4.2 Primary Tax Treaty Countries

Spain is one of the main tax treaty countries used by foreign investors to make investments in Chile.

Currently, Chile has tax treaties in force with Australia, Austria, Belgium, Brazil, Canada, Colombia, Croatia, Denmark, Ecuador, France, Ireland, Malaysia, Mexico, New Zealand, Norway, Paraguay, Peru, Poland, Portugal, Russia, South Korea, Spain, Sweden, Switzerland, Thailand and the United Kingdom. Also, tax treaties have been signed with Argentina, China, Czech Republic, Italy, Japan, the USA and South Africa, but they are not yet in force.

4.3 Use of Treaty Country Entities by Non-Treaty Country Residents

There are no specific provisions in Chilean legislation restraining the use of treaty country entities by non-treaty country residents. However, recent treaties have incorporated different versions of a limitation of benefits clause. In addition, a recently enacted general anti-avoidance rule may be used to prevent treaty-shopping.

It should be noted that the Chilean tax authority has recently confirmed the possibility that a foreign investor may change residence from a non-treaty country to a treaty country, provided that the investor meets the definition of resident of the tax treaty subscribed with the relevant tax treaty partner (Ruling No 1,985 of 2015).

4.4 Transfer Pricing Issues

In general, the biggest transfer pricing issues for inbound investors operating through a Chilean corporation are related to intra-group financing structures and inter-company service agreements.

4.5 Related Party Limited Risk Distribution Arrangements

Under Chilean transfer pricing rules, related party arrangements should be executed on an arm's-length basis. In this regard, the Chilean tax authority generally follows the principles endorsed by the OECD Transfer Pricing Guidelines. Although there is no clear guidance or precedent, it is expected that the Chilean tax authority will endorse BEPS guidelines.

4.6 Variation from OECD Standards

Not in theory, but in practice it has been observed that the Chilean tax authority is using transfer pricing rules to challenge not only prices, but also legitimate business decisions (ie choice of financing with debt or equity).

5. Key Features of Taxation of Non-Local Corporations

5.1 Taxation of Non-Local Corporations Versus Local Subsidiaries

From an income tax perspective, there are no significant differences between the taxation of Chilean subsidiaries and branches of foreign entities. As a general rule, both are subject to corporate tax and withholding when profits are distributed to the foreign owner or parent entity.

From the VAT perspective, there may be a difference in connection with transactions carried out between a Chilean branch and its foreign head office. Since the branch and its head office are legally the same entity, the Chilean tax authority has stated that services provided by the parent to the branch are not subject to VAT, as the VAT's taxable event requires the provision of services from one entity or individual to another (Ruling No 1,794/2011). However, services provided by the foreign corporation to its Chilean subsidiary could achieve the same result, as they will be VAT exempt if the services are subject to withholding tax.

5.2 Capital Gains of Non-Residents

Capital gains of non-residents on the sale of stock in Chilean corporations are generally taxable in Chile, subject to the tax regimes explained under **2.7**.

Capital gains of non-residents derived from the indirect sale of Chilean assets could also be subject to taxation in Chile.

Chilean indirect transfer rules apply to foreign transactions involving underlying Chilean assets, provided that the following conditions are met:

- Chilean underlying assets represent at least 20% of the fair market value of the interest of the foreign holding entity being sold; and
- The interest of the foreign holding company being transferred corresponds to at least 10% of that foreign entity.

If the first of these conditions is not met, the indirect transfer rules could also be applicable if the fair market value of the Chilean underlying asset being indirectly transferred is higher than approximately USD160 million. In addition, the indirect transfer rules will also be triggered if the transferred entity is resident in a jurisdiction listed as a tax haven by the Chilean Treasury Department.

The rate applicable to indirect transfer rules is 35%, although the seller may opt to be taxed as if the Chilean business had been directly sold.

Indirect transfer rules do not apply when the Chilean underlying assets are transferred, due to a corporate reorganisation process of the foreign company.

5.3 Change of Control Provisions

There is no special provision as regards of change of control. However, Chilean indirect transfer rules may apply to any transfer involving significant Chilean underlying assets, regardless of how many tiers may be interposed between the Chilean underlying assets and the foreign entity.

5.4 Determining the Income of Foreign-owned Local Affiliates
No formulas are used in Chile. OECD principles are generally applied.

5.5 Deductions for Payments by Local Affiliates
Payments by Chilean affiliates for management and administrative expenses incurred by a non-local affiliate will be subject to the general scrutiny of tax expenses. In this regard, the management and administrative expenses should meet the following conditions:

- They are related to the entity's business;
- They are necessary to produce taxable income, considering its nature and amount;
- They have not been previously deducted as a direct cost of goods or services;
- They are incurred in the relevant taxable period, whether paid or accrued; and
- They are supported by appropriate documentation.

The materiality of the services and the benefits caused to the Chilean affiliate should be clearly identifiable and verifiable in order to deduct these management and administrative payments as per the Chilean tax authority position.

5.6 Constraints on Related Party Borrowing
Interest payments are generally deductible, as explained under **2.5**. The deductibility restrictions do not depend on whether the lender is foreign, a related party or both, although under transfer-pricing rules the Chilean tax authority is entitled to challenge excessive interest charges made to a Chilean borrower by a foreign related party.

Related party borrowing by foreign-owned Chilean affiliates paid to non-local affiliates is subject to thin capitalisation rules in order to apply the reduced 4% withholding tax rate as described under **9.1**.

6. Key Features of Taxation of Foreign Income of Local Corporations

6.1 Foreign Income of Local Corporations
Foreign income of Chilean corporations is not exempt from corporate tax in Chile.

Chilean corporations are subject to taxation based on their worldwide income. As a general rule, the foreign income of Chilean corporations is taxed on a cash basis unless such income is derived from a foreign branch or CFC rules are triggered (in which case the foreign income is taxed on an accrual basis).

Subject to certain restrictions, a foreign tax credit may be available to the Chilean corporation. However, in the case of non-treaty countries the foreign tax credit will be limited to taxes paid for:

- Dividends or profits distributions,
- Income from a foreign branch, permanent establishment or CFC entities, and
- Income derived from trademarks, patents or technical services.

The foreign tax credit is capped at 32% for non-treaty countries, and at 35% for treaty countries.

6.2 Non-Deductible Local Expenses
There are no attribution rules of local expenses to exempt foreign income. The Chilean tax law only establishes the general principle where expenses linked to exempt income are not deductible against ordinary income (ie income subject to ordinary taxation).

6.3 Taxation of Dividends from Foreign Subsidiaries
Dividends received by a Chilean corporation from a foreign subsidiary are deemed ordinary income, subject to corporate tax and final taxes.

6.4 Use of Intangibles
Intangibles developed by Chilean corporations can be used by foreign subsidiaries in their business to the extent that a licence agreement has been agreed.

The royalty to be received by the Chilean corporation from its non-local subsidiary derived from the licence agreement will be deemed to be ordinary income, subject to corporate tax and final taxes. Under transfer pricing rules the royalty should be determined following the arm's-length principle.

6.5 Taxation of Income of Non-Local Subsidiaries Under CFC-Type Rules
The Tax Reform introduced Controlled Foreign Corporation ("CFC") rules for the first time in the history of Chilean legislation. As per the new CFC rules, passive income of a foreign subsidiary is taxed in Chile on an accrual basis equivalent to that controlling Chilean resident taxpayers.

Passive income includes dividends, interest (except for banking or financing entities), royalties, certain capital gains, income for lease of real estate (except for entities for whom the real estate lease is their main business) and income generated in specific operations with Chilean related parties.

A foreign entity is deemed to be controlled by a taxpayer if the taxpayer:

- Holds 50% or more of its equity, profits or voting rights;
- Has the authority to appoint the majority of its board; or
- Is entitled to amend its bylaws unilaterally. In addition, entities located in a low-tax jurisdiction are deemed controlled by each Chilean-resident taxpayer, unless otherwise shown by the taxpayer.

For these purposes, low-tax jurisdictions are those that meet any two of the following conditions:

- It taxes foreign-source income at a lower than 17.5% rate (in the case of progressive rates, the test is made on the "average tax rate");
- It has not entered into an information exchange agreement with Chile;
- It lacks substantive transfer-pricing rules;
- Its law limits the information that can be requested by its tax authority or limits the ability to share that information with third-countries;
- It is identified as a preferential tax regime by the OECD; or
- It taxes local source income only. OECD jurisdictions are exempted per se from the low-tax test.

Income derived from foreign branches of Chilean corporations is also taxed on an accrual basis.

6.6 Rules Related to the Substance of Non-Local Affiliates

Other than CFC rules and transfer pricing principles, there are no specific rules related to the substance of foreign affiliates.

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6.7 Taxation on Gain on the Sale of Shares in Non-Local Affiliates

The gain of a Chilean corporation derived from the sale of shares in non-local affiliates will be deemed ordinary income subject to corporate tax and final taxes.

7. Anti-Avoidance

The Tax Reform has enacted, for the first time in the history of Chilean legislation, an overreaching general anti-avoidance rule ("GAAR"). According to the GAAR, tax obligations are triggered and are payable based on the legal nature of the business or acts carried out by taxpayers, regardless of their form, denomination or validity.

The Chilean GAAR also recognises the principle of good faith of taxpayers, requiring the Chilean tax authority to disregard the form only to the extent that taxable events are avoided by means of abuse or simulation. "Abuse" is defined as the total or partial avoidance, reduction or deferral of a tax by means of one or more actions or dealings that do not have any relevant legal or economic effects other than tax effects. "Simulation" is defined as actions or dealings that conceal the existence or the elements of a taxable event, or the taxable event's true amount or triggering date.

The existence of abuse or simulation must be declared, by a tax court, upon the requirement of the national director of the Chilean tax authority. In the proceeding, the Chilean tax authority has the burden of proof of abuse or simulation. Individuals and entities that are shown to have designed or planned abusive actions or dealings may be liable to pay a penalty that is capped at approximately USD76,000. In the case of legal entities, the penalty must be imposed on its directors or representatives, if they have failed in their oversight duties.

8. Audit Cycle

Chilean law has not established a regular routine audit cycle.