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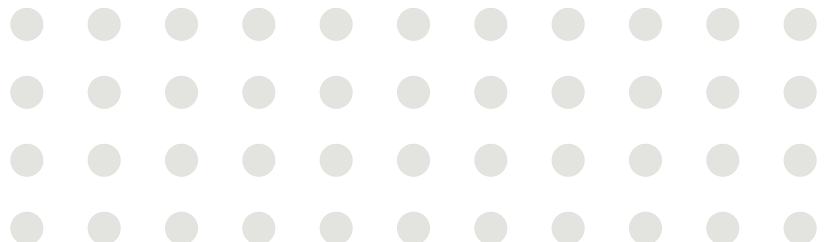
Navigating Tax Law Policies in Latin America

WSG
World Services Group



Introduction

The international community, through the OECD, has been trying for more than 15 years to implement tax policies at a global level, which would allow standardizing the tax burden of taxpayers (mainly those with multinational presence), and the exponential development of the digital economy has accelerated these efforts, generating the 15 Actions of the BEPS Plan and now Pillars 1 and 2.

However, it is entirely to be expected that any development of international tax policies should be accompanied by the parallel development of new organizational alternatives for companies with local and international presence, allowing new business alternatives and opportunities, together with greater tax efficiencies, within the legal parameters established by the different jurisdictions.

Latin America is no exception, although the different jurisdictions in the region are not fully integrated to the previous efforts of the international community, mainly due to their general situation of economic development; therefore, the mere fact of sharing the rules of the game applicable to the different actors within the region, becomes an enormously useful tool in order to coordinate and improve the opportunities of business reorganization to take advantage of the economic opportunities and the possibilities of tax efficiency applicable.

Attending the inherent multinational characteristics of WSG, the following information tries to integrate the most useful and interesting highlights of the WSG Latam Tax Group, gathering the tax rules applied in Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Venezuela. Alas, this document has not the intention being the "solution" of each single tax issue that might rise to WSG Latam Tax Group members, it wants to be the first approach to analyze the best course of action on those matters.

The contents are systematized on 4 major areas: Income Taxes, Trading Taxes/Rules, OECD/International Tax Rules and Special Promotions. Each area take care of the main aspects of each tax jurisdiction regarding each major topic, such as Corporate Income Tax or Capital Gains Tax on Income Taxes, Value Added Tax on Trading Taxes, or BEPS actions on OECD/International rules. This structure allows to create tax-jurisdiction sheets, similar as "Doing business" documents does, but this time only on tax matters. The final area (Special Promotions) seeks to highlight special concessions by industry, which any country applies to promote FDI.

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INCOME TAXES

Corporate Income Tax (CIT):

Under the general taxation regime, Chilean resident entities are subject to CIT at a 27% rate over its net taxable income, generally determined under full accounting records and on an accrual basis. Entities are entitled to deduct from their gross income the expenses incurred in the corresponding tax period to the extent such expenses meet the requirements of the Income Tax Law ("ITL").

The Chilean income tax is an integrated system in which the CIT annually paid by Chilean companies may be totally or partially credited against "final income taxes" payable at the owners' level (i.e., Personal Income Tax ["PIT"] applicable to Chilean resident individuals or Withholding Tax ["WHT"] applicable to non-Chilean residents).

Under a special regime, the CIT rate applicable to SMEs is 25%, provided the requirements established in the ITL are met. It should be noted that these entities are subject to a CIT rate of 10% for commercial year 2023, which increases to 12,5% and 25% in commercial years 2024 and 2025, respectively.

Dividend Tax (DT):

A distinction must be done between dividend distributions made to Chilean residents and those made to non-residents.

Regarding dividends distribution between Chilean resident taxpayers, it is important to differentiate between distributions made to entities and those made to individuals. Dividend distribution between Chilean entities is not subject to DT (but the distributed profits are registered in the Chilean shareholder's register with the associated CIT tax credit), whereas individuals must include the amount received in their PIT taxable base, and generally have the right to credit 65% of the CIT paid against the determined PIT.

Dividend distributions paid abroad are typically subject to a 35% WHT applied over the grossed-up dividend on a cash basis, with a full (100%) or partial (65%) credit for the CIT paid by the Chilean entities distributing the dividend. This full or partial credit will generally depend on the existence of a Tax Conventions for Avoiding Double Taxation ("TCADT") in force between Chile and the country where the taxpayer receiving the dividend resides.

Capital Gains Tax (CGT):

Capital gains obtained by Chilean resident entities are deemed ordinary income, and thus subject to CIT at a rate of 27% under the general taxation regime.

Capital gains obtained by Chilean resident individuals are generally subject to PIT, on a cash basis. If obtained from the sale of shares and the gains does not exceed USD 9,500 approx., it may qualify as non-taxable income. If obtained from the sale of real estate located in Chile (acquired post 2004), there is cap of USD 360,000 approx. that may qualify as non-taxable income.

Capital gains obtained by non-residents are generally subject to a 35% WHT on a cash basis. TCADT may provide relief or a reduced limitation on this rate. Benefits described in the paragraph above for individuals also apply to non-resident capital gains obtained from the sale of shares and real estate, respectively.

Special rules (i.e., 10% sole tax) may apply to capital gains obtained in the sale of Chilean shares that are regularly and substantially traded on a stock exchange, as outlined in Article 107 of the ITL.

Withholding Tax (WHT):

Generally, Chilean-source income (i.e., income arising from goods located in Chile or activities developed in the country) earned by non-Chilean residents is subject to WHT at a 35% rate on a cash basis. Additionally, certain payments made by Chilean residents to non-residents are subject to WHT.

The general WHT rate may be lowered by application of a TCADT or local law provisions. For example: (i) interest paid abroad arising from loans granted by foreign or international banks of financial institutions may benefit form a reduced 4% WHT; (ii) royalties paid abroad are generally subject to a WHT rate of 30%, which can be further reduced to 15% or being exempt depending on the nature of the intellectual property involved; and (iii) remuneration for services provided abroad has a special treatment (please refer to the International Services Rules below).

TRADING TAXES

Value Added Tax (VAT):

VAT is imposed at a standard rate of 19% on the habitual sale of movable assets and of real property (excluding land) located in Chile, and on services rendered or utilized in Chile that are not covered by an exemption contemplated in the law. In addition to this, VAT is applied to specific taxable events, including imports and the provision of digital services abroad. Notwithstanding, exports of goods and services and some specified transactions are VAT exempt.

The VAT levied on the acquisition of goods, utilization of services or imports gives the VAT taxpayer the right for VAT fiscal credit ("Fiscal Credit"). When said taxpayer sells goods or renders services subject to VAT, the VAT so charged becomes a VAT fiscal debit ("Fiscal Debit"), which may be offset with the carried-forward Fiscal Credit. The monthly positive difference between the Fiscal Debit minus the Fiscal Credit constitutes the VAT payable by the VAT taxpayer in cash. If the Fiscal Credit exceeds the Fiscal Debit the excess can be carried forward indefinitely.

Free-Trade Zones System (FTZ):

Certain free trade zones, specifically Iquique in the north and Punta Arenas in the south, are protected by a presumption of extraterritoriality. Goods brought into these zones are deemed located outside the country, and thus exempted from custom duties, taxes, and other charges. Users of free trade zones are exempt from VAT for specific operations carried out within the zone, such as sales and services provided to other zone users. Additionally, these users are exempt from CIT on profits derived from activities conducted within the free trade zone.

Custom Allowances:

Import operations in Chile are generally subject to the payment of a 6% customs tariff calculated over the CIF value of the goods, plus a 19% VAT, which must be collected by the National Customs Service before the goods are cleared to enter the country. Export operations are free from payment of any duties or taxes.

Preferential treatment (generally, reduced, or waived customs tariffs) may be available and claimed under applicable Free Trade Agreements or Economic Cooperation Agreements, provided that the relevant rules of origin are fulfilled.

Furthermore, the import (or sale) of specific goods including luxury products and alcoholic beverages, may be subject to additional taxes, as applicable depending on each product.

OECD/INTERNATIONAL RULES

BEPS Multilateral Instrument (MLI):

Chile has been active in implementing the BEPS recommendations. In this regard, it has already signed and deposited its Instrument of Ratification, Acceptance or Approval of the MLI, which is in force since March 2021. Furthermore, it has incorporated several changes of the 2017 OECD Model Tax Convention in its tax treaties and has made changes to internal laws in line with the said recommendations.

Tax Conventions for Avoiding Double Taxation:

Chile is party to several TCADT. Currently, there are 37 agreements in force (please refer to https://www.sii.cl/normativa_legislacion/convenios_internacionales.html for the full list). Please note that the TCADT between Chile and the US entered into force in December 2023, making Chile the second South American country (after Venezuela) to have a TCADT in force with the US. Its provisions will become effective: (i) generally, for taxable periods beginning on or after January 1, 2024; and (ii) with respect to taxes withheld at source (e.g., Chilean WHT) on February 1, 2024.

Multilateral Assistance Convention (MAC):
The MAC was signed by Chile on October 2013, and is in force since November 2016.

Common Reporting Standard (CRS):
Chile has subscribed the OECD's Common Reporting Standard rules, which are currently in force in the country. On 2017, the Ministry of Finance issued the Supreme Decree No. 418 of 2017, in which it established the Regulation to which information obligations derived from the CRS are subject. Furthermore, Article 62 ter of the Tax Code encompasses the provisions for the CRS rules. These rules empower the Chilean Tax Authority to seek annual information when specific criteria are fulfilled.

Controlled Foreign Corporation Rules (CFC):
Chilean resident individuals, companies, and equities must recognize for tax purposes the passive income directly or indirectly derived from controlled foreign entities on an accrued basis. This is an exception to the general rule of ITL under which foreign source income is recognized on a cash basis.

For the rules to apply, two cumulative requirements must be met: (i) control over a foreign entity by a local taxpayer; and (ii) such foreign entity obtaining passive income.

An entity is considered controlled by a Chilean resident taxpayer when, at the end of the fiscal year or at any time during the preceding 12 months, such taxpayer, alone or together with related persons or entities, in the proportion that corresponds, directly or indirectly own 50% or more of: i) the equity, or ii) the rights to profits, or iii) voting rights of the entity in question. Furthermore, control is presumed when the foreign entity is incorporated, domiciled, or resident in a country or territory considered as a preferential fiscal regime.

For the purposes of Chilean CFC rules, passive income include, among others: (i) Dividends, withdrawals, distributions, and any other form of profit distribution or accrual (unless coming from an entity whose line of business is not the obtention of passive income); (ii) Interests and other income arising from movable capital (unless the controlled entity is a banking or financial institution regulated as such by the authorities of the respective country); and (iii) Royalties or income from the assignment of the use, enjoyment, or exploitation of trademarks patents, formulas, computer programs and similar services.

Transfer Pricing Rules (TP):
Under Chilean TP rules, the Chilean Tax Authority is able to challenge the prices, values or profitability of transactions celebrated between a Chilean resident or domiciled taxpayer and its non-resident related parties, provided they do not conform to normal market values (i.e., those that have been or would have been agreed by independent parties in comparable operations and circumstances, considering, for example, the characteristics of the relevant markets, the functions assumed by the parties, the specific characteristics of the goods or services contracted and any other reasonably relevant circumstances).

Differences determined by the Chilean Tax Authority through a transfer pricing audit may be subject to a 40% penalty tax, with the risk of an additional 5% fine if the taxpayer does not provide the required information on time.

Thin Capitalisation Rules (TC):
Under Chilean TC rules, a 35% TC tax is applied on any portion of interest paid abroad to a foreign related party that is attributable to the Chilean borrower excessive indebtedness (i.e., the excess over the debt-to-equity ratio of 3:1).

The debt-to-equity ratio of 3:1 is assessed at the end of every year and shall be calculated considering both intercompany and third-party debt, as well as domestic and foreign debt, with the exception of loans with a maturity date of 90 days or less, all in a monthly permanence basis (e.g., if the company owed USD 1,200 at the beginning of the year and paid the debt in January, only USD 100 should be considered for the calculus). For this purpose, a company's equity means its tax-adjusted equity, which corresponds to the total assets of the company less its current liabilities, both at tax values.

The applicable WHT on interest payments abroad can be credited against the 35% TC tax (i.e., if the WHT applicable over the interest payment is applied at a 35% rate, TC tax would not be applicable). The 35% TC tax is deductible for income tax purposes by the borrower.

Hybrid Structures Rules (HS):
There are no specific Chilean HS rules.

The Chilean general anti-avoidance rule ("GAAR") recognizes the principle of good faith of taxpayers (i.e., legal forms should be in principle respected by the authority) but enables the Chilean Tax Authority to disregard the legal forms to the extent that taxable events are avoided by means of abuse or simulation. *Abuse* exists when the taxable event is avoided, or the tax liability is reduced or delayed, by means of one or more actions or dealings that do not have any relevant legal or economic effect -other than tax- (the reasonable exercise of choices of conduct contemplated by the provisions of Chilean tax legislation, which establishes that the taxpayers have the right to choose between reasonable behaviors and alternatives contemplated in the tax law, is recognized as valid). *Simulation* exists when the existence of a taxable event or the elements, true amount or triggering date of a tax liability is disguised.

International Services rules:
The payments for remuneration of services provided abroad is subject to a 35% WHT rate. However, this rate may be reduced to 15% for the remuneration of engineering or technical works and professional or technical services (or 20% if the beneficiary is resident in a country considered as a preferential tax regime). Additionally, several payments for services rendered abroad may be WHT exempted, such as mercantile commissions (i.e., commercial agency agreements that involve intermediation services). Moreover, these payments could be subject to the specific provisions of a TCADT.

SPECIAL PROMOTIONS

Tax Allowances by Industry/Market
The VAT Law includes a provision that grants a specific VAT exemption for the importation of certain capital goods. This exemption applies to goods intended for the development, exploration, or exploitation of investment projects within a range of sectors such as mining, energy, telecommunications, research, or scientific development, and only applies provided the investment project as a whole is of involves US$ 5 million or more.

Similarly, investment projects intended exclusively for the development of health, educational, scientific, research or technological development activities, and the construction of housing and offices, may be exempted from the Regional Contribution, a 1% tax applied to the acquisition value in excess of US$ 10 million of all the fixed assets comprising an investment project that is subject to the environmental assessment system.

Other Concessions by Industry/Market:
Generally, Chilean tax laws do not contemplate tax benefits by industry or market. Exceptionally, and by way of reference, there is the case of a special law applicable to Chilean commercial airlines (i.e., Decree-Law No. 2,564 of 1979). According to this law, payments made by these entities to non-resident taxpayers for technical advice, services rendered abroad, interest, or any other concept related to their ordinary line of business activities, shall be exempt from WHT.

Special Tax Regimes, Incentives or Subsidies:
Chilean laws contemplate certain specific territorial tax incentives worth mentioning.

Firstly, Navarino Law (Law No. 18,392) and Tierra del Fuego Law (Law No. 19,149) establish preferential customs and tax regimes for companies domiciled in Tierra del Fuego, in the south of the XII Region. Both contemplate similar benefits ranging from corporate tax exemptions, VAT exemptions, real estate tax exemptions, among others. These benefits are exclusive for taxpayers that conduct industrial, mining, sea resources exploitation, transportation and tourism activities in this zone, provided that their establishment and activity entails a rational use of natural resources and that they ensure the preservation of nature and the environment.

On the other hand, Austral Law (Law No. 19,606) serves as a catalyst for fostering economic growth in the regions of Aysen (XI Region) and Magallanes (XII Region), along with the province of Palena (X Region). This law grants a tax credit against the CIT that ranges between 10% and 32% of the value of the fixed assets corresponding to constructions, machinery and equipment, including real estate intended for commercial exploitation for tourism purposes acquired new or constructed in the relevant year, capped at 80,000 monthly tax units (US$ 6.3 million approx.)

Tax Exemptions:
Chilean tax laws contemplate certain tax exemptions which intend to benefit non-profit organizations, if certain conditions are met.

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Tax Group facilitates key knowledge exchange between members both globally and regionally on important industry and practice topics, expertise and trends. The Group also offers key networking opportunities throughout each year for members to build and grow business relationships.

Latin America Tax Group

World Services Group is the most prominent global network of independent firms that provides an exclusive setting and platform to connect its members to the most elite legal firms and their multinational clients worldwide. Additionally, WSG provides cross industry access to a select few investment banking and accounting firms creating more expansive opportunities to service clients.

Through seamless collaboration and continual innovation, WSG delivers authentic association of global expertise with highest quality and value for clients.

For additional questions or to schedule a call with a WSG Executive Team Member, please contact us.

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