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Santiago – Chile

TTN Conference

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Major International Tax Aspects
of the
Chilean Tax Reform

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Outline

1. New source rules on Chilean debt instruments & interest
2. Obligation to report investments made abroad
3. Obligation to report trusts & other fiduciary structures
4. New restrictions on thin cap rules
5. Anti-deferral rules on passive income (CFC regime)
6. Low tax jurisdictions list (added to tax havens list)
7. Elimination of the Foreign Investment Statute (DL 600)
8. Tax Amnesty

1. Source Rules on Debt Instruments

- Basic Rules:
  - Assets located in Chile & Services performed in Chile
- Traditional source rule on equity instruments:
  - Shares in Chilean corporations & interests in Chilean companies are deemed to be located in Chile
  - Problem: no similar rule on debt instruments
  - **2014 Tax Reform**: debt instruments issued in Chile by entities domiciled, resident or incorporated in Chile are deemed to be located in Chile
- Specific (and traditional) Rule on interest: domicile of debtor
  - Practice of issuing debt through a foreign Branch
  - **2014 Tax Reform**: interest of Branch or PE = Chilean source income.

2. Reporting Investments made Abroad

- Chile's tradition as a destination of FDI under reconsideration
- Detailed report required on or before June 30 of each year
- Corporate Tax Provision or Private Wealth Provision?
  - 2015 Tax Amnesty
- Non filers are subject to Article 21 Penalty Tax
- More specific info required from Low Tax Jurisdictions & Tax Havens
- Deliberate incomplete filing or non filing = Tax Fraud

3. Reporting Trusts & Similar Structures

- Administrative Precedent
- Obligation affects only "taxpayers or entities" domiciled, resident or incorporated in Chile (unlike the previous case)
- Obligation affects settlors, trustees, beneficiaries <u>and</u> "managers".
- Fiduciary structures (very broadly defined) also qualify as trusts
  - What about single premium life insurance?
- Non reporting = tax abuse
- False reporting = tax fraud

4. New Thin Cap Rules

- **Traditional Chilean Thin Cap Rule**: Focused on potential related party abuse of 4% reduced income tax on cross border interest.
  - Only Related Party Foreign Debt on preferred 4% Tax Regime was relevant for 3:1 ratio
- **2014 Tax Reform**
  - New extended concept of interest paid to a related party ("any other conventional surcharge")
  - Foreign debt with unrelated parties subject to 4% regime and all Chilean debt are relevant for 3:1
  - Debt issued by foreign Branches & PEs is relevant for 3:1
  - 35% tax only applies to interest payments made to a related party
  - Broader related party definition + Specific Anti Avoidance Rules
  - Regulated Financial Entities maintain their exclusion

5. New CFC Regime on Passive Income

- Definition of Control:
  - 50% or more of the equity ("capital"), rights to profits, **OR** political rights
  - Ability to appoint or dismiss management or to amend by-laws
  - <u>Legal presumptions of control</u>: low tax entities & call options
- **Passive income** generally includes dividends, interest, royalties, capital gains on passive assets, certain real estate income and certain operations with low tax or tax haven entities
- Additional reporting requirements
- Special tax credit for "circular structures"
- De minimis: UF 2,400 per year (approx. USD 100k)
- <u>Problem</u>: Double Tax Treaties?

6. Low Tax Jurisdictions

- **Definition**: Meets two or more of following requirements:
  - Effective tax on foreign source income less than 17.5%
  - No tax treaty with Chile in force
  - No transfer pricing audit in line with OECD or UN recommendations
  - No exchange of tax information allowed
  - Defined as preferred tax jurisdictions by OECD or UN
  - Territorial source jurisdictions
- OECD jurisdictions excluded.
- Chilean IRS must publish the list of low tax jurisdictions

7. Elimination of DL 600

- DL 600 of 1974 as a key element for FDI since 1974
- Other similar mechanisms existed decades before DL 600
- The tax Invariability issue
  - Mining Royalty Discussions
- DL 600 as a unilateral concession v/s Investment Protection Treaties
- New Foreign Investment Regime should replace DL 600

8. Tax Amnesty on Foreign Assets

- Basic Requirements:
  - Taxpayers resident in Chile before January 1, 2014
  - Assets and income located abroad acquired before Jan 1, 2014
  - Assets and income located in FATF/GAFI high risk or uncooperative jurisdictions do not qualify
  - Persons subject to AML procedures or convicted for certain AML figures, tax fraud, etc or subject to tax audits on those assets
- 8% sole tax (income, estate tax, VAT, etc)
- No repatriation required
- Risks?
- Alternatives?

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