# New Tax Agreement between the Chilean Executive Branch and the Senate's Finance Commission

*November 11, 2019*

## *In brief*

*On November 8, 2019, the Chilean government reached an agreement with the Senate's Finance Commission regarding the 2018 Modernization Tax Bill (currently being discussed in the Senate) and future amendments to the Chilean Tax Law, in order to strengthen the government's social agenda, mainly towards:*

1. *Increasing tax revenues, in order to face a more challenging social agenda.*
2. *Helping the senior population from a tax perspective.*
3. *Supporting the Small and Medium Enterprises (SMEs) from a tax perspective.*

*The aim of the agreement would be encouraging growth, investment, entrepreneurships, savings and employment.*

*This agreement contains measures that will result in amendments to the Tax Modernization Bill, while other measures will be the subject of a long-term finished study, which would be based mainly on an analysis of the tax expenditure of the Government, that is, the analysis of exemptions from the Income Tax and VAT legislation which could be translated in a future Tax Bill.*

*This new agreement is intended to collect USD 2 billion more.*

## *In detail*

### *Full integration of Corporate-level tax and Final Taxes:*

The 2018 Modernization Tax Bill proposed repealing both the Attribution and the Partially Integrated methods and introduce a single regime of taxation where the corporate-level tax (so called "First Category Tax") should be fully creditable against final taxes and shareholders´ should, accordingly, be subject to tax on a cash basis only.

However, according to the agreement, the full integration of Corporate-level tax and final taxes proposed in the 2018 Modernization Tax Bill for all companies, will be limited only to SMEs whose sales does not exceed USD $ 2,8 million annually app. The Partially Integrated method would remain for the companies exceeding such threshold.

### *New Real Estate Tax:*

A new real estate tax would be incorporated. Real estate whose fiscal value is worth USD 600.000 app. or more should be subject to tax.

The tax would be included as a surcharge of the current Real Estate Contributions on a progressive basis.

Real estate worth between USD 600.000 app. and USD 945.000 app. should be subject to a 0,075% rate. From USD 945.000 app. to USD 1.200.000 app. it should be subject to a 0,15% rate. From USD 1.200.000 onwards, real estate should be subject to an additional 0,275% rate.

Companies may deduct as an expense the tax paid for Corporate Income Tax (CIT) determination purposes. SMEs on the other hand would be exempted from real estate tax.

## *General Anti-Avoidance Rule (GAAR)*

According to the agreement, no amendments shall be introduced by the 2018 Modernization Tax Bill. Therefore, GAAR rules should remain the same.

## *Progressive repeal of Payments per Absorbed Profits (PPUA)*

In a Chile to Chile profit distribution, the distribution usually goes with a CIT credit attached. When the recipient entity is in a tax loss position, the profit dividend received is offset against the existing losses. In that scenario, the recipient entity is entitled to claim the refund of the CIT credit attached to the profit absorbed (PPUA).

The agreement introduces a progressive repeal of PPUA from 2020 (90%), 2021 (80%), 2022(70%) and 2023 (50%). From 2024 onwards, the PPUA would be completely repealed. It would imply a significant change in the Chilean Tax Law.

Therefore, Chilean Holding Companies may not be able to request a tax refund to the Chilean National Treasury for the taxes paid by its subsidiaries domiciled in Chile in the event the Holding Company is in a tax loss position.

According to the agreement, such repeal would not affect tax loss deduction against profits, nor the use of CIT credits against final taxes.

## *Private Investment Fund (FIP)*

The agreement introduces new requirements for quota-holders (e.g., 8 non-related parties not being able to hold a 20% ownership interest in the fund each).
In addition, some limitations are introduced regarding market makers contracts and the tax benefits arising from the disposal of fund's quotas, listed in the stock exchange market.

## *Repeal of Registration/Repatriation of assets located abroad provision*

The provision included in the 2018 Modernization Tax Bill would be repealed, and therefore no additional period for the repatriation would be considered.

## *Income tax increase for Chilean domiciled individuals*

Chilean domiciled individuals with the highest income would be taxed at a 40% rate, instead of a 35%.

Such amendment in principle would imply a 44,45% effective tax rate.

## *Construction tax credit*

New thresholds proposed in the 2018 Modernization Tax Bill would be repealed. Therefore the 65% VAT credit for the construction of homes worth USD $ 75,000 is preserved.

## *Other expected amendments*

- Investment companies would be subject to municipal license.
- Tax benefit DFL2 regarding real estate would be limited.
- The flexibility regarding tax havens introduced by the 2018 Modernization Tax Bill would be repealed.
- Instant depreciation proposed by the 2018 Modernization Tax Bill is preserved.

## *The takeaway*

Through the abovementioned measures, the Government expects to collect USD 2 billion more, in order to satisfy the social requests.

Multinationals having Chilean subsidiaries should closely monitor the measures to be included by the agreement in the 2018 Modernization Tax Bill and determine how the expected amendments may affect their operations in Chile.

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