

Chilean Congress approves new tax reform

October 11, 2024

In brief

What happened?

On September 25, the Chilean Congress approved the bill that had been submitted by the Chilean Executive Branch (the 'Tax Reform' or 'Bill'). The Tax Reform is now under Constitutional review by the Chilean Constitutional Court, and once such process is finalized, the Tax Reform will be ready for the President's signature and publication in the Chilean Official Gazette and enacted as law.

Why is it relevant?

The Tax Reform adopts measures aimed at addressing tax evasion and avoidance and modernizing the Chilean tax administration. The Bill proposes changes to the Chilean Income Tax Law, Value Added Tax Law, and Tax Code, among others.

Action to consider:

Multinational companies with operations or presence in Chile should assess whether the approved changes in the current tax system could impact their current or future structures and transactions.

Included below is a summary of some aspects of the Tax Reform. Note that certain other important tax modifications included in the Tax Reform are not covered in this Insight, e.g., transfer pricing.

In detail

Selected modifications to Chilean Tax Code

General anti-avoidance rule (GAAR)

The Tax Reform modifies the definition of 'abuse' and 'simulation' currently included in Chilean GAAR, emphasizing that the key feature of an 'abuse' is obtaining tax benefits in an 'improper' way, i.e., when the legal form of a transaction does not align with the economic effect sought by the taxpayer when entering into the transaction.

One of the most significant highlights is that the Tax Reform's initial proposal of replacing the current judicial procedure with a purely administrative procedure was not approved by the Chilean Congress. Accordingly, the current procedure rules remain applicable, meaning that the Chilean tax authority will still need to initiate a judicial procedure before the Chilean tax courts to pursue a GAAR case.

Chilean tax authority assessment power

As a general principle, the Chilean Tax Code allows the Chilean tax authority to challenge transactions executed at a value that significantly differs from 'normal market value.'

The Tax Reform defines 'normal market value' as the value that third parties would have agreed in comparable transactions and circumstances, considering the relevant characteristics of the industry, sectors, functions, assets and risks, etc.

Under the original wording of the Tax Reform, taxpayers would have been required to follow specific valuation methods to support that a relevant transaction had 'normal market value.' However, this valuation methodology requirement was not approved by the Chilean Congress, and under the approved wording taxpayers may submit, upon request of the Chilean tax authorities, a valuation report that supports the 'normal market value' without any obligation of applying a specific valuation method.

Business reorganizations

Under the Tax Reform, mergers and de-mergers, whether domestic or international, will be tax neutral provided that (1) the tax basis in the transferred assets carries forward to the receiving entity and (2) there is no cash consideration.

It is worth noting that in the initial wording of the Tax Reform it was suggested that mergers and de-mergers would need to have a legitimate business reason to qualify as tax neutral. However, such a requirement was not included in the approved Tax Reform.

Finally, the Tax Reform rules that an international reorganization (different from a merger and de-merger) that produces effects in goods, shares, or rights located in Chile will be tax neutral provided that the following requirements are met:

- It has a legitimate business reason;
- The transaction does not entail a cash consideration for the transferor entity;
- The tax basis in the transferred, assigned, or contributed assets is carried over to the acquiring entity;
- Legal requirements of other jurisdictions involved in the transaction have been met; and

- Chile's taxing rights are kept or not impacted (i.e., Chile is still able to impose taxes in a subsequent transfer of the reorganized assets).

Selected modifications to Chilean income tax law

Chilean indirect transfer rules

The Chilean indirect transfer rules include a 'Tax Haven Test,' under which the capital gain derived from the transfer of interests in an entity domiciled or incorporated in a jurisdiction deemed to be a tax haven for Chilean tax purposes, which indirectly holds Chilean assets, is subject to Chilean nonresident withholding tax at a 35% rate. This test applies regardless of the value of the Chilean company indirectly transferred and the participation transferred.

Under current law, the Tax Haven Test does not apply if (1) a Chilean tax resident neither holds 5% or more of the equity, nor has the right to 5% or more of the profits of the transferred foreign entity and (2) a person resident in a tax haven neither holds, directly or indirectly, 50% or more of the equity, nor has the right to 50% or more of the profits of the transferred foreign entity.

The Tax Reform clarifies that for the 5% requirement under prong (1) of the test discussed in the previous paragraph, the holding requirement also must be tested on an indirect basis.

Selected modifications to Chilean VAT law

VAT on the transfer of assets located abroad

Under current VAT law, generally the sale of goods located outside of Chilean territory is not subject to VAT. The Tax Reform provides that goods located abroad will be deemed to be located in Chile, and therefore their sale will be subject to VAT, when such goods are remotely acquired from a non-Chilean resident, by a person that is not considered a VAT taxpayer for Chilean purposes, provided that the goods are destined to Chilean territory and the sales price does not exceed USD 500.

Broadly speaking, the tax compliance procedure currently in place for digital services would apply in these cases, and thus, the operator of a digital platform would be considered the VAT taxpayer. The Tax Reform applies the simplified registration procedure (simplified registration process that allows foreign taxpayers to register in Chile to comply with VAT filings and payments) currently in place for digital services to the case of these transfers of assets (simplified registration process that allows foreign taxpayers to register in Chile to comply with VAT filings and payments for specific digital transactions). Alternatively, credit card issuers or payment processors could be appointed as withholding agents.

VAT anti-avoidance rules

The Tax Reform includes two special anti-avoidance rules regarding assets and real estate.

Currently, the transfer of fixed assets and real estate is subject to VAT, but when the transfer occurs as part of a business reorganization VAT is generally not applicable. Pursuant to the Tax Reform VAT would be levied on those transfers even if they take place as part of a business reorganization if the main purpose of the reorganization is to avoid VAT.

Tax amnesty

The Tax Reform provides for two tax amnesty programs that would allow:

- Reporting unreported foreign assets and income, which would be subject to a 12% substitute tax on the value of the assets and income, and
- Opting for an early termination of an ongoing tax litigation (excluding cases involving tax crimes) with an abatement of accrued interest and fines.

Let's talk

For a deeper discussion of how the tax reform could affect your business, please contact:

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