

Setting up your Business in Chile

Issues to consider



Chile is the best evaluated economy in Latin America and, indeed, one of the best evaluated among emerging economies worldwide. Its sustained economic growth and social progress have been highlighted by different international organizations and, in 2010, it became the first South American country to join the Organization for Economic Co-operation and Development (OECD).

Fiscal discipline is one of the pillars of Chile's solid economy. Its fiscal accounts have shown sustained stability.

However there are a number of issues which you must consider when you are looking to set up your business in Chile. This document takes you through some of the common questions we come across and gives you practical information about the issues you need to consider.

What type of Business Structure should we use?

There are advantages and disadvantages to all of them, and there is no one correct answer, it's all dependent on your specific business circumstances and needs. A brief overview of the main structures is below:

- **Forming a Foreign Corporation's Subsidiary in Chile**

In the first place, a foreign corporation (parent company) may establish a subsidiary in the country as the foreign parent company's legal entity.

For this, a resident and duly empowered agent or representative shall be appointed. It is not required that this agent or representative be a partner, shareholder, or owner of the company. He/she may be a company's employee. The company may be formed with a given, but not minimum, capital.

- **Forming a Company in Chile**

Alternatively, it is possible to form a Chilean partnership (limited liability partnership – Ltda.) or a corporation (S.A.) receiving the investment, in which case a foreign corporation participates as partner or shareholder, with no limitations regarding capital ownership. However, the partnership shall have at least two partners or shareholders, and the second partner could have a merely formal ownership (1% or less capital contribution). The exception is the Society for Action (SpA), a simplified corporation that does not require the participation of a third party.

- **Legal Formalities**

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Forming a Chilean partnership and a foreign corporation's subsidiary is subject to similar legal formalities regarding the granting of a public deed, publishing of its by-laws abstract in the Official Gazette, and registration in the Register of Commerce.

- The investor foreign company shall authenticate its articles of incorporation and by-laws and its legal representative's power of representation before the Chilean Consul in its country of origin, and later in Chile before the Ministry of Foreign Affairs.
- The tax residence of the member, and where the profits in the LLP originated will determine in what jurisdiction and how these profits are taxed

How much Corporation Tax will the business pay?

Current Corporation Tax rates in Chile are:

Tax rate (%)	
2015	22,5 %
2016	24 %
2017	25 – 25,5 %
2018	25 – 27 %

First category tax with a proportional rate applied on the earned base of income from industry, trade, mining, real estate, movable capital, corporate or commercial service provision, and other activities involving capital use. This tax is a deductible credit or advancement regarding payable global taxes on the base effective at the withdrawal or profit distribution moment.

The law will provide for two options, since 2017, namely attributed income or semi integrated income. In the case of attributed income the taxpayer must pay tax on the income he is entitled to, whether paid or not. In the case of semi integrated income, the taxpayer will only pay personal income tax or additional tax assessed on partners or shareholders not domiciled nor resident in Chile when actually paid. In the case of semi integrated income, the First Category Tax will be 27% in lieu of 25% but personal income taxes or additional tax will only be paid once the profit has been received.

Deducting the fiscal year's and previous years' company losses from the gross earnings is accepted, except in the case of companies undergoing changes in their corporate ownership, as long as they have changed their line of business, have no capital assets, or other assets to develop their line of business, or have earnings from their participation in other companies only.

What if we use Chile to set up our holding company?

The advanced foreign investment regime regulations in force in Chile (tariff liberalization, tax

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stability, national treatment, and trade openness), and deducting carry-forward losses with no time or amount limit, has a positive effect for the investor, the same as its option to accelerate depreciation considering one third of the asset useful life.

Highlight tax impact of disposals of group companies.

Comment on treatment of dividends paid and received including the impact of withholding tax.

Chile has signed agreements with 24 countries to avoid double taxing, and 59 Free-Trade Agreements (TLC) with the most important economies in the world, such as European Union (called Association), Canada, Mexico, European Union, EFTA, Korea, New Zealand, Singapore, Brunei (P4), China, Australia, etc. These agreements eliminate customs tariffs between the signing countries for the terms established in the said agreements.

Earnings generated by corporations with non-resident partners or shareholders are subject to 35% tax when the said earnings are withdrawn, distributed as dividends, or remitted abroad, except in the case of agreements to avoid double taxation.

What if we make cross-border transactions between group companies?

Chile follows internationally recognized **Transfer Pricing** (TP) rules where cross-border trading and financial transactions between affiliated entities have to be conducted on an arm's length basis. The price and terms should be the same as if the transactions had been between completely independent parties.

Typical transactions between affiliated entities that are covered by TP regulations are:

- Sale and purchase of goods
- Provision of management services
- Property rental charges
- Transfer of intangible assets e.g. trademarks, patents
- Sharing of knowledge, expertise, business contacts etc.
- Provision of financial support e.g. inter-group loans and charging a "market" interest on loans

Entities with annual incomes over \$ 500.000.000 (US\$ 994.000) will need to prepare an annual Transfer Pricing Affidavit proving the arm's length basis of transactions. The affidavit will include a detail of all the operations between related parties: date, amount, type of operation, transfer pricing method used to determine the price of the transaction, etc., and it must send to the tax authorities every June 30.

However even if an entity is exempt from the Chile's transfer pricing regime it may fall under the scrutiny of the other international tax jurisdictions where it transacts. There may also be other tax regulations which ensure transactions are undertaken at a commercial value.

What Employment Taxes and Social Security will need to be paid?

If an individual is resident in Chile then they are subject to Chile tax laws. As a general rule, taxpayers domiciled or residing in Chile are subject to taxation on income of any source. Non domiciled and non-resident taxpayers are taxed only on income from Chilean sources. As an exception to the above, foreigners who establish their domicile or residence in Chile will only be subject to taxes on income from Chilean sources for the first three years (this term may be extended by the IRS National Commissioner).

We would advise any new entrant to Chile or person who spends time working in Chile to take professional advice to determine whether they are Chilean tax resident.

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- **Second Category Tax** applied to income from dependant workers' personal services in progressive rates as single income tax, at rates ranging from 0% to 40%. (It will be 0% to 35% since January 2017). It is calculated on total salary and remuneration for work, less social security payments. The tax is withheld and paid monthly by the employer. Independent workers' and professionals' income and that of professionals' partnerships are considered second category income with a 0% rate, as they are only subject to the complementary lump-sum tax (The withholding monthly tax in these cases is 10% rate).

- **Complementary Lump-sum Tax** applied to resident individuals' total income from both categories.

A person is deemed to be domiciled or resident in Chile if:

- It may be assumed from the activities that he/she wishes to stay in the country on a permanent basis (domicile); or
- If he/she spends more than six months in the country in a given calendar year or over a period of two years (resident).

Employers and employees also have to pay Chile social security, over base salaries:

Current Social Security rates are:

	Insurance	Rate (%)
Employer	Unemployment	2, 4
	Life and Disability	1, 26
	Labour Accident	0, 95 Minimum
Employee	Health	7, 0 Minimum
	Social Security (Retirement)	10, 77 to 12.36
	Unemployment	0, 6

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Note: Social security in Chile is a private system. The rates depend on each Institution.

It is the employers' legal responsibility to pay over employee's tax and social security deductions to the Chile tax authorities.

Chile has in force International Social Security Agreements with Germany, Argentina, Australia, Austria, Belgium, Brazil, Canada, Colombia, Denmark, Ecuador, Spain, United States, Finland, France, Netherlands, Luxembourg, Norway, Peru, Portugal, Quebec, Czech Republic, Sweden, Switzerland and Uruguay. These International instruments are entered into between two or more States, and are intended to meet the needs of migrant workers in social security, which have put their work in one or more countries in a Convention.

What is Value Added Tax (VAT) and should the business be registered?

VAT is a "goods and services tax" on supplies made, the standard rate of which is 19%. on the sales of goods and services, with a few exemptions for some services, and on sales of real estate by a construction company if it was built completely by the firm or was partially built on its behalf by a third party. This tax also applies to fiscal institutions, semi-fiscal institutions, autonomous state institutions, local councils, and the companies that belong to these entities, or in which they have a stake.

There are two types of supply

- Taxable – must charge VAT on supplies, can reclaim input VAT
- Exempt – cannot charge VAT nor reclaim input VAT

The same general rate applies to imports, habitual or otherwise, made by any individual or legal entity.

Exporters are exempt from VAT and are entitled to reimbursement of VAT on purchases of goods and services that they use as part of their export activity.

Special sales taxes apply to alcoholic and non-alcoholic beverages, and luxury goods. These taxes are charged in addition to VAT, and are applied on the same tax base as VAT. They are levied on the sale and/or import of specific goods.

As a general rule, the seller of goods or services is responsible for the payment of the tax. The amount of VAT, however, is added to the price of the goods or services. Consequently, it is actually the buyer who bears the economic impact of the tax.

Exceptionally, when the seller is not domiciled in Chile or for other reasons is difficult to control by the IRS, the buyer has to withhold and pay VAT.

The tax is payable monthly, except for special situations such as imports.

VAT charged by a company on sales of goods or services is called "VAT debit". VAT borne by a company on purchases of goods or services is called "VAT credit". The tax borne on the

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acquisition of related physical assets, including buildings and constructions, may also be credited.

VAT credits are deducted from VAT debits and the difference has to be paid to the Chilean Treasury.

If in any given month credits exceed debits, the difference may be carried forward and added to the credits of the following month.

VAT credits incurred in the purchase of fixed assets that remain outstanding for more than six months will be refunded in cash by the Treasury.

Can we provide Share option plans to our staff?

Many companies see Share Option plans as being an important way of attracting, motivating and retaining key staff.

An Open Corporation may consider that up to 10% of the amount is allocated to compensation plans of its employees or its subsidiaries, as well as preferred shares if shareholders not exercise their right (Stock Options), whereupon may give the following situations:

1. The Open Corporation delivery actions arising from the capital increase and the worker acquires its own resources. In this situation there is no effect of taxes. Later, in the event that the employee disposes of the shares and greater value originates, it may subject to tax under the Income Tax Law.
2. If Open Corporation delivery actions arising from the capital increase in return for remuneration, should, in this case, the single tax levied on Second Category, as part of the Worker's Compensation, with rates from 0% to 40%.

How else can we compensate our employees?

Employers have no legal obligation to provide fringe benefits, other than benefits which may be voluntarily agreed upon in individual or collective contracts or agreements. Pension and sickness benefits are covered by the Social Security system. There is no legal obligation to provide catering facilities and meals.

- I. Short-term benefits
 - i. Vacation

Also known as annual holiday is a duty payable to workers with more than one year of service to make use of an annual vacation of fifteen working days, with full pay, which is awarded according to the rules laid down in the Labor Code.

- ii. Gratification

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Is that part of the profits that legally, the employer must distribute to all employees of the company (mandatory minimum bonus: 30%)

II. Termination Benefits

i. Compensation for years of service

The employer who shall term to a Labor Contract that has been in place for one or more years, must pay the worker compensation equivalent to 30 days of the last monthly salary paid for each year of service and amounts above 6 months for the same employer continuously provided.

Pensions, private medical insurance, life and disability cover are now commonplace benefits provided by many Chile businesses to their workforce.

To discuss your requirements please contact the International Office on +44 (0) 1245 449266 or [email](#) us directly.

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