Hispanic Latino Team Blog
Legal Issues Affecting the Hispanic Latino Market & Hispanic Latino Companies

SHEPPARD MULLIN
SHEPPARD MULLIN RICHTER & HAMPTON LLP
ATTORNEYS AT LAW

Hispanic Latino Team Blog

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U.S. Treasury Department Signs New Treaty with Chile

By Keith Gercken and *Dawn Mayer*

On February 4, 2010, the Department of Treasury signed a new income tax treaty with Chile, signifying a milestone for both countries. The treaty has not yet been ratified, but if approved by the U.S. Senate, would become the first income tax treaty between the U.S. and Chile and only the second U.S. income tax treaty with a South American country (a treaty with Venezuela was signed in 1999).

The proposed U.S.-Chile treaty would provide some certainty and stability for U.S. and Chilean cross-border investors and would provide for reduced withholding rates on cross-border payments of dividends, interest and royalties. The current rate is generally 30% on the gross amount of U.S.-source payments under applicable U.S. domestic law.

The maximum withholding rate on dividends would generally be 15%, reduced to 5% where the beneficial owner of the dividend is a company that holds directly at least 10% of the voting power of the company paying the dividend. Further, dividends paid to pension funds would be exempt from withholding tax.

Interest payments would be subject to a maximum withholding tax of 4% if the payment is made to certain financial institutions or insurance companies; or to enterprises selling machinery or equipment if the interest is paid in connection with the sale on credit of such machinery or equipment. In all other cases, the maximum withholding rate would be 15% for a period of five years from the date the interest withholding provisions take effect, dropping to 10% after that.

Royalty payments would be subject to a maximum withholding tax of 2%, if payments are made for the use, or right to use, industrial, commercial, or scientific equipment (other than ships, aircraft or containers). A maximum withholding rate of 10% would apply to payments for the use of, or right to use, any copyright, patent, or other intangible property.

The new tax treaty contains other significant provisions, including rules to determine when an individual or enterprise of one country is subject to tax on business activities in the other country and rules to enhance the mobility of labor by coordinating the tax aspects of the U.S. and Chilean pension systems. Notably, the treaty's permanent establishment ("PE") article includes a "services PE" provision under which a PE will be deemed to arise if an enterprise performs services in the other country for a period exceeding 183 days in the aggregate. As a matter of policy, the U.S. has generally opposed services PE provisions, but has made exceptions for some treaties.

If ratified, the treaty's withholding provisions would take effect for amounts paid or credited on or after the first day of the second month following the date on which the treaty enters into force. All other provisions would take effect in January following the date on which the treaty enters into force.

Companies and individuals resident in the U.S. or Chile who hold investments or conduct operations in the other country may want to reconsider their particular tax planning in light of the provisions contained in this new treaty.

For further information, please contact Keith Gercken at (415) 774 -3207 or Dawn Mayer at (415) 774-2941.