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LATIN AMERICAN TAX UPDATE

JOHN W. SCHMITZ*

Recent Legislation in Bolivia and Chile

Bolivia

The General Directorate of Internal Revenue was appointed as the agency responsible for the system of enforcement of revenue stamps and stamped paper. The General Directorate of the Treasury was designated as the only State institution permitted to issue fiscal papers. Additional regulations were established for the enforcement of revenue stamps and stamped paper.¹

Regulations were also established to govern the obligation of some commercial and industrial firms to present an independent auditor's certificate together with their financial statements.²

A unified tax on public shows was enacted and is to be applied by municipal authorities throughout the country.³

The tax on urban real estate was also placed under the exclusive jurisdiction of municipal authorities.⁴

Companies were required to make a revaluation of their fixed assets as of December 31, 1976. A single tax of five percent is to be payable upon the value ascertained by the revaluation. The method of revaluation is explained by the General Directorate of Internal Revenue in Circular Letter 05-74/77.⁵

Brazil

Fixed dividends, attributed to preferred shares resulting from foreign loan conversion, will be deductible for a maximum period of ten years, provided that the loan is registered with the Central Bank of Brazil by December 31, 1977 and the conversion is requested by December 31, 1978. The Central Bank will establish the procedure for this conversion, especially in relation to the amortization period of the shares, the aggregate sum of the fixed dividend and all other privileges attributed to the shares.

Joint taxation is now allowed at the rate of 32 percent applicable to the actual consolidated profit of a Group of Companies (Grupos de Sociedades" as defined in the Corporation Law) and to a group of com-

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1. Decree Law 14280 of December 31, 1976.
2. Decree Law 14310, regulating Decree Law 1335 of 1976.
3. Decree Law 14374 of February 21, 1977.
4. Decree Law 14375 of February 21, 1977.
5. Supreme Decree 14460 of March 25, 1977.

panies ("con junto de sociedades") in which one directly or indirectly controls the other(s) by holding 80 percent or more of the voting capital.

The obligation to make monetary corrections of the fixed assets and net worth has been extended to all legal entities. The counterentries registered in a "monetary correction" account will result in a debit balance (deductible from the actual profit) or a credit balance (inflationary profit taxed to the extent that it is realized).

"Sociedades Anonimas" with relevant investments in associated and controlled companies will register these assets according to the net worth. The acquisition differences will receive special treatment by way of premium or discount. While the investment is held, the differences verified in each balance sheet will constitute a profit or loss which may be deferred in certain cases.

Losses resulting from the merger, consolidation or split of companies may be deferred for up to ten years, up to the market value of the net worth of the extinguished company. Profits from these operations may be deferred until the fixed assets representing said profits are realized.

Besides the commercial bookkeeping books, a Book of Ascertainment of Actual Profit was introduced for the registration and control of the differences between the net profit of the fiscal year and the actual profit. An Auxiliary General Ledger was also introduced, in ORTN's, for the registration of the monetary correction of the balance sheet and the control of the fluctuations in the accounts which are subject to this correction.

The compulsory financial statements will be the Statement of Assets and Liabilities, the Statement of Fiscal Year Results and the Statement of Accrued Profits and Losses, prepared according to commercial legislation, and the Statement of Actual Profit, prepared according to the tax law.

The following regulations were more clearly defined: *Voluntary revaluation of assets* (allowing deference of taxation in certain cases); *disguised profit distribution* (which only occurs between a legal entity and the individual beneficiaries); registration of *bonus quotas or shares* (only in quantity without mention of value); *compensation of losses* (in four years, regardless of the application of the book loss); *sale on credit of fixed assets* (allowing the acknowledgement of profit in the same proportion of the receipt of the price); *capitalization of profits or reserves* (maintaining tax exemption, except when made during the five years following a former capital reduction or if a reduction or extinguishment is effected during the following five years); taxation of *capital reserve surplus* (limited to "sociedades anonimas", if the profits or profit reserves exceed the corporate capital); *establishment of exempt or reduced profit* for companies receiving SUDENE, SUDAM or Tourism incentives (excluding the proceeds from eventual transactions, among other things).

The 5 percent Income Tax levied on the profits distributed to individuals residing in Brazil or individuals or legal entities residing or domiciled abroad was revoked as from the fiscal year of 1979.

In general, the changes described will affect only the assessment of the Income Tax of the fiscal year of 1979, base-year 1978. The tax of the fiscal year of 1978, base-year 1977, will be calculated according to the regulations effective up to the issuance of Decree-Law No. 1.598, with some of its changes.

Chile

The statutes governing foreign investment in Chile were amended in several important respects. Terms of contract were eliminated and a minimum period of three years for the permanence of capital was established. The power to grant exemptions from custom duties was revoked. In addition the invariability of taxation (at a 49½ percent rate) was limited to ten years. Investors were granted the right to claim the non-applicability of a discriminatory legal provision. Furthermore, foreign investors subject to the prior law governing foreign investment (Decree Law 600) were permitted to elect, prior to March 18, 1978, to be governed by the new statutes. However, the Committee on Foreign Investment was empowered to enter into contracts concerning foreign investment under conditions different from those stipulated by the new statutes, whenever the Committee determined that prior commitments made such a contract necessary for the Chilean government.⁶

The income tax rate applicable to first category income was amended.⁷

The stamp tax applicable to the transfer of real property was reduced from eight percent to four percent. In addition, the President was authorized to decrease the four percent rate still further or eliminate the stamp tax entirely within one year.⁸

The new valuation of real property, resulting from the new general assessments adopted under Supreme Decree 1350 of 1975 was established as being in force as of July 1, 1977.⁹

A permanent system for accelerated depreciation of fixed assets was adopted. A taxpayer may elect either the normal depreciation system or the new system, and may change the election at any time.¹⁰

Taxpayers were authorized to apply value added tax credits against any taxes that they were obligated to pay, providing that they make estimated tax payments on a bimonthly basis.¹¹

6. Decree Law 1748 of March 18, 1977.

7. Decree Law 1754 of March 22, 1977.

8. *Id.*

9. *Id.*

10. Decree Law 1859 of July 20, 1977.

11. Supreme Decree 585 of July 23, 1977.

Amendments to the regulations to the Act on the tax on sales and services, were introduced.¹²

Recent Developments in Tax Administration

The Exchange of Information under Tax Treaties

On August 28 through September 3, 1977, in Curacao, Netherlands Antilles, the Inter-American Center of Tax Administrators (CIAT) held its 19th Technical Conference on "Exchange of Information under Tax Treaties." Seventy experts participated in the Conference, including delegates from each of the twenty-six CIAT member countries and observers from six non-member countries and from several specialized agencies. Among the speakers were Dr. Max Croes, the Minister of Finance of the Netherlands Antilles, Dr. Jose Rafael Marquez, President of the CIAT Executive Council, and Mr. Argaban Amarilla of Paraguay.

The Conference focused on recent developments in the field of tax treaties, on problems involved in the exchange of information, and on studies and recommendations issued by the United Nations Group of Experts and LAFTA (Latin American Free Trade Association). Included in the topics covered were: The current status of studies and work in the field of tax treaties; the criteria for the allocation of the power of taxation among tax jurisdictions according to different types of income, assets and taxable items; the structure and parts of a tax treaty; the procedures and limitations on exchange of information; case studies on the exchange of information concerning auditing of multinational companies, related companies, and international operations; the impact of exchange of information on tax administration; and the stages and formal procedures for the negotiation of tax treaties.

In the Final Report of the Conference, the CIAT summarized the basic objectives of a tax treaty as being threefold. First, a tax treaty should be designed to mitigate or avoid the distorting effects of double taxation by establishing the allocation of the power of taxation of the Contracting States. Second, it should promote trade and investment between the Contracting States through clauses permitting the establishment of a tax burden which does not hamper the normal flow of capital. And third, it should, through an exchange of information, prevent tax evasion and avoidance on the part of taxpayers subject to the provisions of the tax treaty.

The CIAT noted various model treaties, comparing the Model of the Organization for Economic Cooperation and Development (OECD), the Andean Pact Models, the United Nations "Guidelines", the United States Model, and the recommendations of the LAFTA Group of Experts. The CIAT stated that the concept of "permanent establishment," which deter-

¹² Supreme Decree of Finance No. 600 of July 27, 1977.

mines the power of taxation according to the main purpose and function of the company engaged in business activities, is favored by the models of the OECD and the United States, but not by those of the Andean Pact or LAFTA, which instead assert the concept of exclusivity of taxation by the country where the source of income is located. The CIAT reported that the U.N. "Guidelines" offer "a conciliatory formula by admitting the possibility for Contracting Parties to share taxation, on the basis of taking into consideration the power of taxation of the country of origin of the capital or of the license when applicable and, likewise, that of the country of source in the production of the income." However, the CIAT did not recommend which of these models was preferable in the determination of tax jurisdiction. Instead, the CIAT simply stated that the number of treaties subscribed in recent years and the flexibility exhibited by the U.N. Group of Experts may indicate that the developed and developing countries may come to greater agreement on tax jurisdiction in forthcoming years. Yet the failure of developed countries to recognize the concept of having the country of residence afford a tax credit for foreign taxes not paid as a result of an exemption or exoneration of the source country, discounts the possibility of prompt agreement on the related issue of tax jurisdiction.

Agreement on the primary subject of the Conference, the exchange of information under tax treaties, does appear more likely. In its Report, the CIAT explained that the exchange of information may be of two types: Either (a) automatic (and perhaps periodic), including, for example, information on dividends, rentals, and royalties, or (b) on the basis of a specific request. The Report, with respect to the latter type, stated that the State requesting information must indicate a valid tax interest in making a request, and the information must concern a specific and identified taxpayer. If the request is a valid one, the State receiving the request must provide the information, unless doing so would necessitate exceeding the scope of its regular administrative activities or cause the disclosure of business, industrial, or professional secrets. To avoid disputes over the scope of a particular tax administration's regular administrative activities, the Report noted that it may be well for future treaties to specify the concrete types of information to be exchanged on the basis of a specific request. The Report also stated that, in order to deal with the problems arising from bank secrecy, future treaties might be more carefully drafted with regard to the exchange of information, and that the concept of "the prevention of tax fraud" might be better defined. The Report expressed concern that the workload involved in an exchange of information may outweigh the benefits of the exchange, principally for the developing countries. However, the CIAT Report did note that the determination of actual transfer prices of companies engaged in business activity in several tax jurisdictions is generally made possible by a system of information exchange, and that the exchange of information may also be helpful in avoiding double taxation.

Future Conferences and Training Courses

The 20th Technical Conference of the Inter-American Center of Tax Administrators (CIAT), to be held in Buenos Aires, Argentina, on March 26 through April 1, 1978, will focus on various aspects of tax collection. Work groups will discuss the legal constraints on tax collection, organizational and staffing constraints, and constraints derived from public attitudes toward compliance. In addition, papers presented by the Organization of American States, the Internal Revenue Service, the Agency for International Development, and the Inter-American Center of Tax Administrators will examine technical assistance programs implemented by international agencies in the field of tax collection.

The XII General Assembly of the CIAT, to be held in Port-of-Spain, Trinidad and Tobago, on May 21 through May 27, 1978, will be devoted to the study of major legal issues involved in tax administration activities. The XII Assembly will also consist of discussion of the report of the 20th Technical Conference on "Tax Collection," and of the reports of the Technical Conferences held in Montevideo and Curacao in 1977, concerning "Taxation of Multinational Companies" and "Exchange of Information under Tax Treaties."

The German Foundation for International Development, the Institute for the Technical Development of Public Finance of Mexico, and CIAT will offer an intensive course, conducted in Spanish, on the "Negotiation of Tax Treaties." The course, intended for the Ministries of Finance and tax administration officials of the Spanish-speaking CIAT member countries, will be held from February 20 through March 17, 1978, at Ajijic, a conference center located near Guadalajara, Mexico. The course will cover the following topics: tax jurisdiction; international economic relations and the fiscal factor; tax policy and foreign investment; fundamental principles and institutes of international tax law; criteria for tax allocation; international double taxation; the objectives, structure, parts, and negotiation of tax treaties, the solutions offered by model treaties and groups of experts for the allocation of tax jurisdiction; the exchange of information under tax treaties; the tax measures of developed countries to promote investment in developing countries; and the tax measures of developing countries to promote foreign investment and the crediting of exempt taxes. Stanley Surrey, Milka Casanegra, Roque García Mullin, and experts of the Institute for Fiscal Studies of Madrid and of the Federal Republic of Germany are scheduled to offer lectures as part of the course.

The Internal Revenue Service will offer a training course on "Middle Management Development in Tax Administration" for foreign tax officials from April 3 through May 19, 1978. The course is designed to convey an understanding of the organization and functions of the IRS. Total cost of the program for each participant, apart from travel cost, is approximately \$4,000.