Doing Business in Chile

Chile

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INTRODUCTION

As Chile continues to demonstrate economic and political stability and integrate with international markets, its treatment of foreign investment and the impact its laws and legal system may have on investment decisions are likely to be of increasing interest to overseas investors.

This Guide has been prepared with the goal of introducing the major issues likely to confront those considering investment in Chile on topics as diverse as taxes, corporate law, antitrust legislation, environmental regulation and trademark law. In the interests of preparing a Guide that was concise and usable, certain legal issues have been dealt with in summary fashion and not exhaustively analyzed. Any person planning to make an investment in Chile should carefully consult with their legal and financial advisors before making any investment.

This Guide is based on laws in effect in Chile and information applicable as of January 2003.

KEY FEATURES OF INVESTMENT IN CHILE

Foreign Investment Encouraged. Chilean laws are structured to encourage foreign investment by providing a stable and certain regulatory framework, which allows foreign investors to compete on equal terms with local businesses. With the exception of certain industries which are deemed to be in Chile's national interest, 100% foreign ownership of investments is possible and there is no maximum time that foreign investments may remain in Chile.

Repatriation of Capital & Profits. Foreign investment capital and profits may be remitted overseas at any time. Under the Foreign Investment Statute (see *Foreign Investment Legislation and Regulations*) foreign investment capital may be remitted overseas one year after entering Chile and profits may be remitted overseas at any time.

Exchange Controls. he Chilean Central Bank requires that most transactions relating to foreign investment to be effected in a "formal" currency market, i.e., by means of commercial banks or financial institutions.

Foreign Investment Statute. Normally approval of foreign investments is obtained under the Foreign Investment Statute (the "Statute") introduced in 1974. The Statute creates a modern legal framework for foreign investment embodying principles of non-discriminatory and nondiscretionary treatment of foreign investors. Approval under the Statute is rarely denied. Once a proposed investment in Chile is approved, the Chilean government and the investor execute a contract setting out their respective rights and obligations. In addition, Chile is a signatory to several Bilateral Investment Treaties and the Washington Convention of 1965 that set up the International Center for Settlement of Investment Disputes (ICSID).

Taxation. Business income tax rates are set to be comparable with rates prevailing in countries likely to promote foreign investment. The effective rate payable on foreign investment profits remitted abroad is normally 35%, a 16% corporate tax being payable at the time profits are realized with the balance due at the time of payment overseas. An 18% value added tax contributes about 60% of fiscal revenue. Foreign investors may be able to fix certain tax rates applicable to their investment for 10 to 20 years.

POLITICAL, SOCIAL AND ECONOMIC BACKGROUND

- Stable democratic government. High level of integrity in public institutions.
- Market-oriented economic policies.
- Significant natural resources, including copper, nitrate, timber and fish.
- Scarcity of capital and technology relative to abundance of human and natural resources.

- Stable currency, independent Central Bank. The Central Bank may not issue new money or make loans for public spending. Foreign exchange controls exist (see *Exchange Controls-Formal and Informal currency markets*) but there is a realistic exchange rate.

- A Record of Robust Growth. The Chilean economy is one of the most stable and solid in Latin America. Between 1990 and 2001, annual growth averaged 5.9%, ahead of the rest of the region and among the top rates in the world. High growth was interrupted only in 1999, when the economy contracted by 1.0%, following the Asian financial crisis and a sharp drop in the price of copper, Chile's main export. However, the contraction was short-lived and in 2000, GDP expanded by 4.4%. Similarly in 2001, despite a global economic downturn, Chile achieved 2.8% growth, performing better than most other emerging markets. By 2001, Chile's GDP had reached US$ 66.5 billion, up by 86.5% on 1990. Over the same period, per capita income increased by 65.2% to US$ 4,314 (and around twice that amount in PPP terms). Inflation dropped from 27.3% in 1990 to 2.6% in 2001.

- Foreign investment represents approximately 24% of GNP (investment generally represents 30%).

- Chile has an open economy with an 8% duty on imports (see *Importing and Exporting*).

- Chile's open economy, combined with an active policy of bilateral, regional and multilateral trade agreements, has meant a steady increase in foreign trade and in the country's international competitiveness. Between 1975 and 1979, foreign trade represented just 38.6% of GDP but, by 1991-2001, this had risen to 42.9%. In the decade to 2001, exports expanded at an annual average rate of 6.9%, while imports rose at an average of 7.6%.

- Chile has ratified GATT, has entered into free trade agreements with United States, the European Union, Mexico, Venezuela, Colombia, and Canada, and participates as an associate member in Mercosur.

- Chilean culture is characterized by respect for the law.

- Chile has a long history of governmental efficiency, which has prompted various international studies regarding its low level of corruption.

EXCHANGE CONTROLS - FORMAL AND INFORMAL CURRENCY MARKETS

Restrictions on Outflow of Foreign Currency

While Chilean law establishes the right of Chileans and foreigners alike to freely buy and sell foreign currency, some exchange controls restrict the outflow of convertible currencies by requiring certain sales and purchases of foreign currency to be effected in a formal currency market (Chapter 11 of the Foreign Exchange Regulations of the Central Bank). The Central Bank must also be notified of certain transactions. To make avoidance of the controls more difficult, transactions normally carried out in foreign currency and required to be transacted in the formal market cannot be effected in local currency.

Formal & Informal Currency Markets

There are two legal currency markets - the formal and the informal market. Currency transactions take place in the formal currency market when entered into with authorized banks and financial institutions and informal market when entered into with any other parties. Rates in the formal market are not fixed but are kept within certain bands by the Central Bank, which sells U.S. dollars to authorized banks and financial institutions and limits the foreign exchange transactions that the banks and other financial institutions may enter into.

The value of the Chilean peso (denominated by the $ symbol) in the formal market is usually slightly higher than in the informal market. The Central Bank may buy or sell local currency if it considers the gap between the rates in the two markets to be too large.

The following Chilean Peso / US$ rates appear daily in the local press (rates quoted for March 17, 2003):

US *Dóllar acuerdo* ($551,22) - The rate at which the Central Bank effects certain foreign currency transactions which it enters into in accordance with the law.

US *Dóllar observado* ($740,3) - The formal market rate, as observed and published by the Central Bank.

US *Dóllar libre/ informal* ($750) - The informal market rate.

Foreign Investment Transactions and Offshore Accounts to Hold Export and Loan Proceeds

Most transactions relating to foreign investments must be performed in the formal market, including credit transactions, deposits, investments and capital contributions. Appropriate Foreign Investment Committee approval (discussed in *Foreign Investment Legislation and Regulations*) must be obtained upon the commencement of a foreign investment when it is executed under the Foreign Investment Statute. In such case, the Central Bank must also receive prior notification of investments.

In the case of investments exceeding US$50 million in industrial or extractive (including mining) projects, the Foreign Investment Committee, in conjunction with the Central Bank, may allow foreign investors to maintain offshore foreign currency accounts permitting the use of export proceeds to make certain foreign currency payments directly, including payments of foreign financing costs, import costs, foreign tax deductible expenses and remittances of capital and profits. The payments from these offshore accounts must be approved by the Central Bank. Such accounts may only be operated after more than US$50 million has been invested in Chile.

With Central Bank approval, a trustee may be appointed to operate the offshore account to protect the interests of financiers of the foreign investment (see *Financing Chilean Investments-Foreign Loans*)

The operation of an offshore account of this type may raise the following issues for iinvestors:

(1) the Foreign Investment Committee is authorized to limit local borrowing to a certain percentage of the amount of the investment if the investor is permitted to maintain an offshore account. At present, foreign investment contracts which allow the maintenance of an off-shore account normally do not limit local financing; and

(2) funds in the account representing profits will remain subject to First Category/ corporate tax (see *Tax Regime and Income Taxes*).

Foreign investors may also be able to maintain an offshore account to hold all or part of foreign loan proceeds abroad (see *Financing Chilean Investments-Foreign Loans*).

Other Foreign Currency Accounts

There are no restrictions on keeping foreign currency accounts in or outside of Chile.

FOREIGN INVESTMENT LEGISLATION AND REGULATIONS

Foreign Investment Statute & Foreign Exchange Regulations

Foreign investment is regulated principally by the Foreign Investment Statute (Decree Law N° 600) (the "Statute") and Chapter XIV of the Foreign Exchange Regulations of the Chilean Central Bank (the "Regulations"). The Foreign Investment Statute is administered by the Foreign Investment Committee which is comprised of five government ministers and is directly responsible to the President of the Republic of Chile. The Central Bank administers the Foreign Exchange Regulations.

Neither the Statute nor Regulations impose any domestic ownership requirements (i.e. 100% foreign ownership is possible). In addition, there is no limit on the amount of time that foreign investments may remain in Chile.

Investment Approval under the Foreign Investment Statute

Normally, the approval for foreign investments is obtained under the Foreign Investment Statute, which is administered by a Committee chaired by the Minister of the Economy. Approval is granted by the vice-president of the Foreign Investment Committee with the consent of the Minister of Economy (or by the Committee itself in the case of investments over US$5 million, in the case of foreign public entities or in the case of investments related to mass media, public services or other activities normally carried out by the State). Approval is usually granted within 25 days. However, authorization for the immediate liquidation of capital may be granted at the moment of filing a foreign investment application. The minimum investment which may be approved under this statute is US$1 million. This minimum does not apply to investments made in physical assets and technology which have a minimum of US$25,000.

On approval, the Chilean government and the investor execute a simple contract setting out their rights and obligations. Among other items, the contract states the time within which capital must be brought into the country, specifies the form of the capital contribution, guarantees that the foreign investor will not be subject to discriminatory conduct and contains provisions regarding the repatriation of capital and profits. The contract may also fix the rate of certain direct and indirect taxes applicable to the investment (see *Foreign Investor Tax Invariability Options*).

Foreign investment contracts authorize investment up to a specified amount but there is no penalty if the full amount is not invested. Applications to modify foreign investment contracts (for example to increase the investment or change the investment structure) are dealt with promptly.

The government cannot unilaterally suspend a foreign investment contract, as private property rights (including contractual rights) are protected by the Constitution. For example, during the 1983 Latin American debt crisis, capital loans approved under the Foreign Investment Statute were exempt from the general suspension of the repayment of foreign loans (although it is worth noting that the level of such loans is significantly greater today than it was in 1983).

Entry and Type of Capital Contributions

Upon specific authorization by the Foreign Investment Committee, a foreign investor may exchange investment capital in the form of cash in the local formal currency market immediately after filing an application for approval of the investment with the Committee. Approved investment capital must be brought into Chile within three years of foreign investment approval for non-mining projects (which may be extended to up to eight years for projects over US$50 million) and within eight years for mining projects (which may be extended to up to 12 years if exploration is required).

In addition to foreign currency equity and debt capital, capital contributions may consist of tangible assets (such as goods or equipment), intangible assets (such as technology) and capitalized profits (although it is worth noting that authorization for capital contributions other than foreign currency or tangible assets is not as easily obtained as authorization for immediate capitalization until the Foreign Investment Committee has examined the issue).

Investment under the Foreign Exchange Regulations

If an investment application under the Foreign Investment Statute is not approved (which is unusual), or in other cases, such as the unavailability of information required for the approval of a foreign investment, the investment can nevertheless be effected under Chapter XIV of the Foreign Exchange Regulations of the Chilean Central Bank. However, no foreign investment contract may be executed and the other guarantees and investor protection measures contained in the Foreign Investment Statute will not be available to investors who do not obtain approval under that Statute. In addition, investment under the Foreign Exchange Regulations may only consist of cash, whereas the Statute allows the contribution of assets. The minimum investment which may be effected under the Regulations is US$10,000.

Even when approval is granted under the Foreign Investment Statute, investors must also inform the Central Bank of foreign investment transactions in accordance with the Foreign Exchange Regulations.

Repatriation of Capital and Profits Under the Foreign Investment Statute

Foreign investment equity capital may be remitted overseas one year after entering Chile but only from the proceeds from the sale or liquidation of all or part of the assets, business, shares or rights representing the investment. Capital comprising reinvested profits are not subject to the one-year restriction.

Annual profits may be remitted overseas at any time. Interim profits and dividends may be remitted quarterly if supported by audited financial statements and permitted by the foreign investment contract with the government.

In general, foreign currency required to repatriate capital and profits must be obtained in the local formal currency market. The Foreign Investment Committee issues certificates authorizing the purchase of the foreign currency, normally within two business days in the case of profits. Investors may be able to operate offshore foreign currency accounts which may be used to repatriate capital profits directly (see *Exchange Controls-Formal and Informal Currency Markets*).

The Foreign Investment Statute guarantees that restrictions applicable to the remittance of capital and profits will not be less favorable than those applying to the acquisition of foreign currency to pay for imports.

Non-discrimination

The Foreign Investment Statute prohibits the discriminatory treatment of foreign investments, which are subject to the laws generally applicable to domestic investments. Laws are deemed discriminatory if the foreign investor is excluded from the whole or major part of a specific productive activity or if he or she is refused access to a free trade zone or special regime despite complying with the conditions imposed on local investors. However, the Statute provides that the restriction of foreign investors' access to local credit will not be considered discriminatory. No general legislative restriction of this type currently exists, and foreign investment contracts which allow maintenance of off-shore accounts normally do not limit local financing (see *Exchange Controls-Formal and Informal Currency Markets*).

The Foreign Investment Statute sets out a procedure for challenging discriminatory conduct through the Foreign Investment Committee and the courts.

Dispute Resolution and Governing Law of Contracts

Foreign investment contracts under the Foreign Investment Statute normally require disputes arising under the contract to be resolved by the courts of Chile rather than the courts or forum of an independent country or body. However, the courts of Chile have recognized dispute resolution by means of foreign arbitration and in 1990 Chile ratified the International Center for the Settlement of Investment Disputes (ICSID) accord which establishes an arbitration and litigation mechanism for resolving differences in the area of foreign investment.

Chilean law governs foreign investment contracts, which normally also apply to some or all of the other contracts relating to a foreign investment. Changes to Chilean law may therefore directly or indirectly modify these contracts.

However, investors under the Foreign Investment Statute do have the protection of the guarantee of non-discriminatory treatment and of the Constitutional guarantees discussed in *Legal System*.

In addition, Chile has approved several Bilateral Agreements regarding the protection of foreign investment that contemplate mechanisms for the settlement of disputes.

Representative Offices

Foreign investment approval is normally not required to merely export products to or maintain a representative office in Chile. The obligation only arises when capital is to be brought into Chile under the Foreign Investment Statute. For example, an exporter to Chile may appoint representatives in the country to market its products without obtaining foreign investment approval (or deriving income in Chile for Chilean income tax purposes) provided sales are concluded abroad between the exporter and local buyer. However, the carrying on of certain activities (such as banking or finance activities) will require regulatory licenses or in some cases the establishment of a Chilean operating entity, which will in turn require foreign investment approval.

Constitutional Background

The Constitution defends the rights of private property (including contractual rights and intellectual property). The expropriation of properties (or of their inherent attributes or essential rights), can only be done in conformity with a law that authorises such expropriation for the public benefit in the national interest. The owner has the right to challenge the legitimacy of the expropriation action and to be indemnified for any physical damages that he or she suffers. The indemnification must be paid, in cash, before the expropriation and, unless there is an agreement between the government and the owner, be sanctioned by the Court of Justice.

The Constitution also guarantees to Chilean and foreigners equality before law and the right to develop any economical activity not contrary to ethics, public order or national security, subject to the legal regulations that govern these activities.

The Constitution also establishes the various powers of the State (legislative, judicial and executive), providing, specifically, for the independence of the judiciary.

Legal System

Chile has a civil law system similar to that one used in continental European countries, particularly France, Germany and Spain. In civil law systems traditionally statutory language is authoritative and judicial decisions do not create compulsory precedents for similar disputes or actions in the future. As a practical matter, however, decisions of the Court of justice have a large influence on future decisions with respect to similar issues. The Chilean Courts of justice also can base their decisions upon statutory history and on the documents which are relevant to a particular case.

The Chilean judicial system is comprised of the ordinary justice courts, whose decisions can be reviewed by the Court of Appeals and, under exceptional circumstances, by the Supreme Court. Depending on the issues, trials can last up to five years. However, if a person alleges a violation of a constitutional guarantee, a cause of action may be expeditiously presented directly to the Court of Appeals, in accordance with Article 20 of the Constitution.

FINANCING OF CHILEAN INVESTMENTS

Thin Capitalization Restrictions

The current policy of the Foreign Investment Committee is to impose a 75% borrowing limit on investments approved by it, measured at the commencement of the investment at December 31 of each year (requiring the maintenance of a debt to equity ratio of 3 to 1). Although this 75% level may change in the future, it will not affect existing investments because

the current requirement is included in the foreign investment contracts which investors have already entered into with the government.

Local Credit

In the past locally available credit has generally been short term and rolled over on a monthly or quarterly basis. However, the local capital market is developing due to the tremendous amount of savings being invested by private pension funds (These funds were formed as a result of the introduction of a private social security system in 1981 and are now the biggest institutional investors in the financial markets after banks).

Syndicated loans from local banks for the terms agreed by the parties are possible and projects may also be financed by bonds issued to local institutional investors. Pension funds also offer appropriate businesses access to long term funding utilizing pension fund savings.

Registration of Foreign Loans

Foreign currency borrowings financing Chilean investments must be registered with the Central Bank. The parties must also notify the Central Bank of any modifications of either the general terms (such the name of the creditor or debtor and the payment schedule) or financial terms (such as whether or not prepayments are allowed and the applicable interest rate) of the loan. The registration requirement also applies to capital raised through leasing-based financial arrangements and the issuance of bonds, notes and other financial instruments.

The information requirement for foreign currency borrowings and their subsequent registration are met by the filing of a form setting forth the details of specified financial terms of the loan. In fact, the Central Bank registers these details rather than the loan documents themselves.

Normally, disbursements of loans are obtained when filing the relevant information with the lending commercial bank. However, when the loans relate to investments under the Foreign Investment Statute, the application may be filed within 30 days after the loan is granted. In these circumstances the Central Bank is obliged to approve and register the loan if its terms are consistent with terms available in the international financial markets. However, to avoid potential disputes with the Central Bank it is preferable to obtain prior registration of at least the initial loan.

Interest and Principal Payments

Foreign currency to be paid or remitted overseas through the formal currency market may be obtained in the formal or informal currency market.

The approval of a foreign loan under the Foreign Investment Statute gives the investor the right to acquire foreign currency in the local formal currency market to pay interest, principal loan fees and expenses with respect to the loan (see *Exchange Controls-Formal and Informal Currency Markets* regarding currency restrictions). Prior to acquiring foreign currency for these purposes the Foreign Investment Committee must issue a certificate authorizing the specific amount of foreign currency to be acquired in the local currency market.

There are two ways in which financing (and certain other) costs can be paid directly rather than through the formal currency market. First, when the loan will be used to finance imports or payments for services contracted abroad, following notification to the Central Bank all or part of loan proceeds may be maintained in an offshore account. Payments, which can be made from the account, include payments for principal, interest payments, fees and expenses with respect to the loan and importing costs (including importing related costs such as transportation and insurance). The Central Bank must be notified when these payments are made.

Second, in the circumstances discussed in *Exchange Controls-Formal and Informal Currency Markets*, foreign investors may maintain offshore foreign currency accounts permitting the use of offshore income, such as export proceeds, to directly

make payments (including prepayments) of interest, principal, etc. provided that the Central Bank is informed of such payments.

Offshore Lender Security

There are no special restrictions on foreign investors' rights to grant security to lenders with respect to their Chilean and offshore assets.

By requiring borrowers to establish offshore accounts as described in *Interest and Capital Payment*, lenders are able to reduce the risk of the inconvertibility of borrowers' overseas income. This risk arises, for example, where loan and export proceeds are converted into Chilean pesos and need to be reconverted to pay overseas loan and other costs. With Central Bank approval, a trustee may be appointed to control the offshore account to protect lenders' interests.

When a foreign investment exceeds US $50 million, the investor may also be given the right to transfer its interest in the applicable foreign investment contract to the financiers of the investment represented by a trustee or agent approved by the Central Bank. The assignment only requires prior written notice to the Foreign Investment Committee.

To give lenders comfort that loan and related agreements will not be rendered void by Chilean laws, Decree Law 2349 provides that agreements of this type with non-Chilean entities may be governed by foreign laws and related disputes may be resolved by foreign courts. The law also states that any Chilean laws restricting amounts recoverable by lenders will not apply to loans granted by foreigners.

Loan Stamp Duty

Stamp tax is applicable to financing documentation (including foreign loans) assessed on the principal at a rate of 0.134% on the amount of the loan for each month, or fraction thereof, from the date of authorization until termination, up to a maximum of 1.608%. Negotiable instruments payable on demand are subject to a unique rate of 0.67%. The tax is payable when the documents are brought into the country or when the capital raised is recorded in the borrower's books. Foreign loans from multilateral lending institutions (such as the World Bank or the International Finance Corporation) are exempt from this tax. To avoid triggering a new stamp duty liability, changes to borrowing terms should be structured as an amendment to the existing loan and use the same loan documents with any necessary attachments. Loans entered into with foreign or international banking institutions are also subject to the regulations of the Chilean and external banking market, whether or not such practices are applicable in Chile.

LABOR AND PENSION LAWS

Labor Contracts

Every employee has the right to enter into a written contract with his or her employer. In general, the employer should prepare the contract and deliver a copy to the employee within 15 days of the commencement of the date of employment. Failure to comply with this requirement can result in a fine for the employer.

Every labor contract must provide at least the following:

(i) the date and place of the contract;

(ii) details regarding each party, including name, nationality, date of birth of the employee and the date on which work will commence;

(iii) a general description of the services which the employee will provide and the place such services will be provided;

(iv) salary, form and frequency of payment;

(v) days and hours of service;

(vi) the term of the contract. Contracts which do not specify a term are deemed to be indefinite, as are contracts which are renewed for a second time after the first renewal termination date;

(vii) all other terms agreed by the parties, including any additional benefit to which the employee has a right (such as use of a company car).

Nationality of Employee

The personnel of companies with more than 25 employees must be comprised of at least 85% 85% Chilean nationals or foreign nationals who meet at least one of the following criteria:

(i) they have been Chilean residents for five years or more;

(ii) they are married to or widows of Chilean nationals; or

(iii) they have children who are Chilean nationals.

Foreign experts or persons for whom a Chilean equivalent is not available are not subject to the restrictions set forth above.

Hours per Week

The normal maximum work week is 48 hours (starting from January 1, 2005, the normal maximum work week will be 45 hours), which may be divided into five or six days of 10 hours or less each. These restrictions do not apply to managers, directors, or executives or to certain employees who work independently from their employers, among others. In addition, the 48-hour week may be extended under certain limited circumstances contemplated by law, and additional shifts may be permitted for certain activities which because of their nature must function continuously.

Persons who work overtime must be paid 50% more than their regular hourly wage, and each employer is required to maintain a system to record the hours worked by each employee (such as a punch clock or official book). Overtime may be used by employers to provide for the temporary needs of a company and overtime arrangements must be agreed to in writing for a maximum of 3 months which can be renewed. Employees have the right to at least one half hour break during each work day.

Vacations

Employees who have worked for an employer for at least one year have the right to 15 working days of paid vacation per year, preferably in the spring or summer. An employee who has worked for an employer or a series of employers (whether or not continuously) for a period of ten years or more has the right to one extra vacation day for each three years worked in excess of ten years. The employer is required to authorize the vacation time set forth above and is not permitted to simply pay extra salary in compensation for unused vacation time.

Finally, it should be noted that weekends cannot be included as vacation days, even if the employer usually works weekends.

Bonuses

Each company must distribute a portion of its annual taxable profits to its employees. Companies have two alternatives in order to comply with this obligation which are described below. Companies are permitted to freely change from one system to another.

Under the first system, the company must distribute 30% of its annual taxable income at year end to all of its employees in an amount proportional to such employee's salary. The taxable income of the company is established by the tax authorities in order to assess such company's income tax and may be adjusted to take into account various discounts and increases. This system is usually used by companies with low profits.

In the second system, the employer must pay each employee 25% of such employee's annual salary, adjusted for inflation, up to a maximum of one month's current salary at minimum wage multiplied by 4.75% (approximately US$700). In general, the system is simpler to apply than the first system described, and is often used by companies earning higher profits.

Internal Guidelines

Companies employing 10 or more people are required to have internal guidelines establishing:

(i) shift hours, if any;

(ii) break times for employees;

(iii) the time, date and place where employees should pick up their paychecks;

(iv) any special standards regarding conduct;

(v) any risks or dangers associated with the employment;

(vi) standards regarding health, security and hygiene of the employees;

(vii) sanctions for violation of company guidelines; and

(viii) the names and titles of those people to whom employees should lodge complaints

The employer may only amend the internal guidelines upon 30 days prior written notice to the employees. In any event, the employer should provide a copy of the internal guidelines in at least two visible places in the workplace and deliver copies, free of charge, to:

(i) each employee;

(ii) the union or employee representative; and

(iii) the Health and Hygiene Committee described below.

In addition, the employer should provide copies of the internal guidelines to the Ministry of Health and to the Work Inspectors, entities which are empowered to comment on and require modifications to the internal guidelines.

Maternity

Women employees have the right to six weeks paid maternity leave prior to the birth of a child, and 12 weeks paid maternity leave after the birth. These periods can be extended based on a medical certificate. In the event that the mother dies during childbirth or during the 12 weeks following the birth, the father of the child has the right to use the remaining maternity leave as paid paternity leave.

In addition, a woman who has pregnancy-related health problems has the right to medical leave for as long as necessary pursuant to a medical certificate. Finally, when a child of less than one year old is seriously ill, the mother or father, at the election of the mother, has the right to paid leave to care for the child.

None of the rights described above can be waived, and the employer must guaranty the mother's or father's position during any leave for a period of one year after such leave. In addition, while an employee is pregnant, she cannot be required to participate in activities which are considered dangerous to the health (such as lifting heavy items, remaining standing for long periods of time and working overtime). In the event that such activities form a part of such employee's job, the employer is required to assign her to another position during her pregnancy without any reduction in salary.

Companies with 20 or more women employees must provide a place for such employees, separate from the work area, where mothers can feed and leave their children under two years old. Employers located in the same geographical area may request authorization for the establishment of a common center.

If the mother prefers to leave her child in a day care center, the employer may elect to pay the cost of sending the child to the day care center, rather than establishing a child care area. In such cases the employer must pay directly to the day care center. In any manner such child care is provided, working mothers have the right to two breaks per day, of one hour in total, not including travel time which may be significant, to feed their children. This time is considered working time for all legal effects and the right to such time may not be waived.

Benefits and Pensions

Employees are required to contribute a portion of their earnings to a pension fund, health insurance plan, life insurance plan and unemployment insurance plan. Employers must withhold such amounts from the salaries of each of their employees, but are not required to contribute to such funds or plans, other than certain contributions related to work-related accidents and illnesses as well as to the unemployment insurance plan, as described below.

(i) Employee Contributions

Chilean employees must contribute 10% of their monthly earnings, up to a maximum of 60 "Unidades de Fomento".[1] (approximately US$1,350), to a personal retirement account maintained with a Pension Administration Fund ("AFP"). Foreign employees working in Chile may continue contributing to the social security systems in lieu of contributing to the AFP provided that certain requirements are met.

As a general rule, male employees are entitled to retire at the age of 65 and female employees at the age of 60. At such age, employees may receive a pension from an AFP or may obtain a special form of insurance which provides a cash benefit for life.

In addition, employees must contribute 7% of their salary to healthcare institutions and between 2.84% and 3.4% to life and disability insurance.

Finally, employees must also contribute a 0.6% of their salary (with a maximum limit for the equivalent of 90 UF, approximately US$2,000) to the Unemployment Insurance Fund.

(ii) Employer Contributions

Employers are obligated to pay as a contribution to employee labor benefits a sum which ranges from 0.9% to 4.4% of the total aggregate payroll. This percentage varies based upon the risk factor for the type of activity undertaken by the company and is intended to finance: (i) accidents involving its employees during the course of their employment or during their commute to and from work; and (ii) work-related illnesses set forth in specific regulations.

In addition, employers must contribute a 2.4% of the taxable salaries to the Unemployment Insurance Fund, with a maximum limit of 90 UF.

[1] Chilean Indexed Currency (herein after "UF")

Termination of Employment Relationship

In general, the Labor Code permits the employer to terminate employment (i) for cause; (ii) for business reasons; and (iii) without cause (in the case of executives with the power to represent the company).

(i) Termination for cause. The Labor Code permits an employer to fire an employee for cause. Generally, events which justify firing for cause are serious and must truly compromise the employer's operations. For example, an employee can be fired for acts or omissions which affect the security or functioning of the business or the health or safety of the other employees. An employer who validly and legally fires an employee for cause is not obligated to give the employee notice or pay any indemnification.

(ii) Termination for business reasons. The Labor Code also permits an employer to lay off an employee if the "corporate requirements" of the company so dictate. Reasons for such a lay off include: (a) the need to modernize or reduce operations; (b) a reduction in productivity; (c) changes in market conditions or economic conditions. The employer who lays off an employee for business reasons must give notice and pay severance to the employee based on the years of his or her service.

(iii) Termination without cause. Finally, the Labor Code permits an employer to fire without cause executives and other employees who have administrative duties, such as managers, assistant managers, agents or other representatives. The employer who takes advantage of this option must give notice and pay severance pay to the employee based on their years of service.

Termination Notice or Substitute Indemnification

An employer who wishes to terminate the work contract of an employee must send a "termination notice" to the employee. The employer must deliver the termination notice to the employee personally or by certified mail and must send a copy of such notice to the appropriate labor inspector. In the case of termination for cause, the employer must provide the termination notice to the employee within three working days from the date of his or her termination. In all other cases, the employer must provide such notice 30 days in advance. Instead of delivering such prior notice, the employer may elect to pay the employee one month's salary.

The termination notice must specify: (i) the reasons for the termination of employment and the substantiation of those reasons and (ii) the status of the employee's benefits.

In the majority of cases, the employer is bound by the statements made in the termination notice and cannot later justify the termination based on other acts or circumstances. Any error or omission in the termination notice may result in fines against the employer.

Severance Payment Based on Years of Service

When an employer terminates the employment relationship with an employee, either for business reasons or without cause when so permitted, the employer must pay the employee severance pay based on the employee's years of service in accordance with the Labor Law Code. Pursuant to this requirement, the employee is entitled to receive an amount equivalent to one month's salary for each year (or 6-month or more period thereof) the employee worked for the employer, up to a maximum of 330 days of salary. In each case, the employee also has the right to receive the equivalent of his salary, in cash, for vacation time accrued during the last year of service.

The calculation of both the severance pay in lieu of notice and the severance pay for years of service are based on the salary of the employee during the last month worked. This is equal to the total amount the employee earned during his last 30 days of employment, in cash or in kind, including amounts retained for his pension, but excluding overtime and annual bonuses. In the case of an employee whose monthly salary varies (such as because of commissions), the monthly salary is calculated by averaging the employee's salary during the last three months worked.

Notwithstanding the foregoing, in calculating the indemnification for years served the Labor Law Code establishes a maximum monthly salary of 90 UF.

Any employee who believes that the termination of his contract was unjust, unnecessary or did not comply with the relevant procedure can lodge a complaint before a labor law judge within 60 business days of the date of such termination.

If the judge accepts the employee's complaint, he can order the employer to pay a severance amount in lieu of notice and a severance amount based on years served if such amounts have not already been paid. In addition, the judge can order a 30% increase in the severance pay for years served and in some cases of unjust termination of employment for cause up to a 100% increase.

In spite of the above and from a tax perspective, legal and voluntary severance for years served is deemed non-taxable income for employees employed in the private sector up to an amount equal to one month of remuneration for the years effectively served. To this effect, the monthly remuneration to be considered is the average of the remuneration paid over the last 24 months received by the employee, duly restated by the domestic CPI, excluding bonuses and other extraordinary remuneration.

Accidents and Work-Related Illnesses

The Labor Code Law requires employers to provide a safe, clean work environment for all workers. In addition, the National Health Service (SNS) is empowered to inspect workplaces and can require employers to comply with all measures which it deems necessary to bring the workplace into compliance with applicable regulations.

The failure to comply with orders by the SNS can result in a fine.

Safety and Hygiene Committee

Any business which employs 25 or more persons must create one or more safety and hygiene committees (the "Committee") to:

(i) train and instruct employees in the correct use of safety equipment;

(ii) recommend and institute safety, hygiene and protection measures and supervise the completion thereof; and

(ii) investigate the causes of accidents and work-related illnesses. The employer must implement the Committee's recommendations, or be subject to fines.

Notwithstanding the foregoing, the employer may appeal such recommendations to the relevant health authorities within 30 days from the date of the recommendation, if it believes that they are incorrect, excessive or impractical to the smooth functioning of the business.

IMPORTING AND EXPORTING

Imports

(i) Customs Service Approval

All types of goods and services may be imported by any individual or entity except a limited number of specifically prohibited items (for example, used cars).

Imports must be registered with the Customs Service prior to shipment and comply with all applicable laws and regulations. Import licenses are generally provided if import prices are consistent with market levels (to combat transfer pricing the Customs Service may not approve imports at inflated prices).

Normally imports must be shipped within 120 days of grant of the license.

(ii) Customs Duty

Customs duty is normally payable on imports at a rate of 7% of the CIF value of the imported goods, although this rate may be increased to counter-balance the effect of proven foreign subsidies. The target is to reach a 6% rate in the year 2003.

A number of treaties and trade associations have had the effect of reducing (or eliminating) the normal customs duty rate for certain products traded with other Latin American countries and Canada. Further treaties are continually being negotiated, including the entry by Chile into a TLC with the United States of America.

Customs duties may be deferred for up to seven years on certain equipment, tools and machinery imported for productive purposes and having a CIF value of greater than approximately US $3,600 approx. (or approximately US $4,550 in the case of vehicles for highway transportation (both figures are annually readjusted in relation to the Wholesale Price Index of the United States of America). If such equipment is used to produce or manufacture goods for exports, customs duties may be deducted as a credit.

(iii) Value Added Tax

Subject to a number of exceptions, such as if the goods to be imported are included in the list contained in a Supreme Decree of capital assets, a value added tax of 18% also applies to imports (see Value Added and Other Indirect Taxes).

(iv) Free Trade Zones

Customs duties (and VAT) may not apply in free trade zones in the north and south of Chile.

Exports

All types of goods and services may be exported by any individual or entity (provided the exports comply with applicable laws and regulations), except a limited number of specifically prohibited items. For example, some agricultural products may be subject to seasonal restrictions. The Customs Service must be notified in advance of exports with the exception, among others, of transactions of up to US $3,000 FOB (or authorized by certain government bodies, when particularly sensitive products are at issue, such as copper, which requires authorization by the Copper Commission).

As with imports, the Central Bank is entitled (under Article 45 of the Central Bank Organic Law) to object to export prices it considers to be inconsistent with prevailing market levels. In the case of long term export contracts, each export shipment will require Central Bank approval, and approval will not be granted if the export price is not inconsistent with market levels prevailing at the time of the shipment (irrespective of the pricing terms of the long term contract). The purpose of the Central Bank approval process is to combat transfer pricing.

Foreign currency proceeds of export sales (net of related overseas expenses) do not have to be returned to Chile, and if returned such proceeds do not need to be converted into local currency. If not returned to Chile, the exporter is obliged to inform the Central Bank accordingly.

Export incentives are available for "non-traditional" exports, an amount of up to 7% of the value of such products to be exported, provided that less than US$15 million of such kind of merchandise, as classified by Customs, was exported in the previous year.

TAX REGIME

General

(i) Income Taxes

The Chilean Income Tax Law combines two principles. Individuals and juridical entities resident or domiciled in Chile, are subject to taxation on their worldwide income regardless of whether the income comes from a Chilean or foreign source. On the other hand, individuals and juridical entities, neither resident nor domiciled in Chile, are subject to taxation in Chile only on Chilean source income. To this end, income arising from assets located or activities conducted in Chile are deemed to comprise Chilean source income. Shares issued by Chilean corporations and rights representing interest in Chilean juridical entities other than corporations are deemed to be located in Chile. Royalties are deemed Chilean source income provided the intangible is used or exploited in Chile. Interest accrued or paid regarding loans is deemed to be Chilean source income provided that the debtor is domiciled in Chile.

Chilean Income Tax Law is structured to encourage investment. To promote savings and investment, business income taxation is divided into two stages:

First, at the business entity or corporate level a 16%[2] yearly tax rate is assessed on the entity's net taxable income determined in accordance with the Income Tax Law and full accounting records (except for to limited cases in which taxation is based on presumed income and accordingly no accounting records are needed to evidence the taxable base). The 16% corporate tax is credited against the amount due based on second level taxation.

Second, taxation at the second level takes place only when business profits are distributed to the ultimate business owners (resident individuals who are partners or shareholders of the business entity, subject to Surtax or *Impuesto Global Complementario*, whereas non-resident individuals or foreign juridical entities which are partners or shareholders are subject to the Withholding Tax or *Impuesto Adicional*). The effective rate payable on profits remitted abroad to a nonresident partner or shareholder, as the case may be, is normally 35% (16% being payable at the time profits were accrued at the corporate level with the balance (35%, less 16% credit) due on payment or remittance or profits overseas).

According to this structure, in addtion to the 16% corporate tax, there are no other taxes applicable to undistributed business profits or affect business profit distributions made by a business entity to another business entity which does not qualify as the ultimate business owner, thus avoiding an internal double taxation. Further, under some circumstances, the ultimate business owner may be entitled to a tax deferral on profit remittances which are reinvested in another business entity within twenty days. Consistent with this structure, non-deductible expenses and amounts which are deemed to be a covert profit distribution to the ultimate business owners are penalized with second level taxation or subject to a special 35% tax in the case of Chilean corporations.

Business profits are subject to the 16% corporate tax, called First Category Income Tax. Salaries and work-related compensation are subject to Second Category Income Tax[3]. The difference is that First Category Income Tax affects business income arising mainly from capital, whereas Second Category Income Tax affects income arising mainly from personal services rendered by a resident or domiciled individual as employee, technician, independent worker, Board Director or advisor.

Withholding taxes are important when dealing with offshore payments of Chilean source income made to a foreign individual or juridical entity neither resident nor domiciled in Chile. These withholding taxes (*Impuesto Adicional*) are

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[2] Please note that Law N° 19,753 published in the Official Gazette on September 27 of 2001, will increase progressively by the Corporate Tax rate up to 17% by year 2004. The rate for 2002 is 16% and 16.5% for year 2003.

[3] Law 19,753 also reduced the Second Category Tax and Surtax, increased the amount of salaries which are exempt of such taxes and reduced the maximum rate from 45 to 40%.

assessed on profit remittances and dividends (35%), royalties (30%), film distribution fees (20%), interest on foreign loans (35% or 4%, as the case may be), remuneration for services rendered abroad (35%, except for engineering work or technical assistance, in which case a 20% rate applies), premiums for foreign insurance policies (22%) and reinsurance policies (2%), leasing of movable assets (1.75%) and compensation to foreign individuals nor domiciled in Chile but are render technical, sport, scientific or cultural services in Chile (20%).

The Surtax[4] (*Impuesto Global Complementario*) is a personal yearly tax calculated on a progressive scale ranging from 0 to 45% affecting individuals who are resident or domiciled in Chile on their worldwide income.

(ii) Indirect Taxes

Considerable emphasis is placed on indirect taxation through an 18% VAT which contributes about 60% of fiscal revenue (see *Value Added and Other Indirect Taxes*). Due to recent amendments, the Municipal Tax has added a significant tax burden and should also be considered by persons considering investing in Chile.

Chilean Income Taxes Affecting Foreign Investment

The main taxes applicable to income are described in more detail below. Foreign investments are affected primarily by First Category Tax (corporate tax at the first level), Additional Tax (withholding tax at the second level) and the tax imposed on non-deductible expenses. As previously explained, VAT and Municipal Tax should be also considered.

(a) First Category Tax (Corporate Tax)

General. First Category Tax, often referred to as the Corporate Tax, is paid by all business entities based on their accrued income from operations at a rate of 16%. Chile has a fully integrated tax system allowing this corporate tax to be credited against the Surtax (*Impuesto Global Complementario*), a personal income tax payable by resident investors when business profits are withdrawn, or to be credited against the Withholding Tax (*Impuesto Adicional*), in the case of foreign investors when profits are remitted overseas.

First Category Taxpayers need to be enrolled before the Chilean Internal Revenue Service (*Servicio de Impuestos Internos*, or IRS), keep full accounting records, substantiate the operations with duly stamped invoices and comply with their tax obligations.

Net Taxable Income or Computing Net Business Income. According to the Income Tax Law, net taxable income is reached by deducting from gross revenues accrued during the year the direct cost of inventories sold and qualifying deductible expenses. Some final adjustments are then to be made and monetary correction provisions are to be applied. The result is the net taxable income or the taxable base for the First Category Income Tax

a) Gross revenues comprise all revenues from business operations with the sole exclusion or deduction of certain non-taxable events (such as capital contributions, monetary corrections made to initial net tax equity, capital reimbursement distributed upon formally documented capital reductions or upon the liquidation of the business entity, and certain capital gains if realized by a Foreign Institutional Investor which are not dividends).

b) less: direct cost of the acquisition of inventories sold during the year. Direct cost is equivalent to the amounts disbursed in the acquisition as set forth in the domestic invoices or import documents plus customs duties, customs expenses, as the case may be. Domestic freight and insurance for stored inventories may be credited or treated as an expense. If VAT is not recovered as a fiscal credit it should also be subtracted. Direct cost of inventories manufactured is equivalent to the direct cost of raw material and parts following the same rules plus the direct labor cost attributable to production. Unsold inventories are determined by years end subject to a monetary correction adjustment to reflect replacement cost.

[4] Idem.

c) less: deduction of necessary expenses. Business expenses are deductible if necessary to produce income. To satisfy this requirement the expense must be related directly to the business activity, be obligatory or unavoidable (in nature and amount), be appropriately registered in the accounting records and substantiated with sufficient information and documentation. Foreign expenses must be backed up by documentation issued by the foreign supplier and translated into Spanish

Only certain inter-company charges will satisfy this criteria.

c1) In addition, there are special rules regarding some specific expenses, including:

(i) Interest paid or due by the taxpayer regarding loans applied for working capital are deductible without limitation (see Capitalization Rules below).
(ii) Salaries. Employee remuneration, compensation and workrelated benefits are generally deductible, provided such benefits are agreed to in an employment or collective bargaining contract or instrument. Voluntary payments will only be deductible if provided on some objective basis or general standard. Voluntary payments will not be deductible if prove selective or discriminatory.
(iii) Losses. Losses incurred in a given year must be absorbed with undistributed tax earnings (carry back) and if a remnant exists, losses are to be carried forward, without any time limitations. Please note that the losses of a company may not be deductible if certain changes in the control of the company occur, encompassing changes in the corporate line of business of the company or its extension.
(iv) Chilean taxes are deductible, except for the income taxes and VAT if the latter constitute a fiscal credit.
(v) Depreciation on fixed assets is deductible. Depreciation is calculated using the straight line method based on useful life of the relevant asset set by the IRS. Accelerated depreciation (one-third of normal useful life) is available for new and used imported fixed assets and new domestic assets with a useful life of more than five years. However, only the straight line method will be considered when assessing second level taxation. Taxpayers may switch from normal to accelerated depreciation provided the requirements are met. Conversely, taxpayers may switch from accelerated depreciation into normal depreciation, waiving this tax benefit.
(vi) Amortization of start up expenses and expenses incurred in the introduction of new products to the market. Taxpayers are allowed to choose whether to deduct such expenses in the year in which they were incurred (this might generate a tax loss which may be carried forward, without limitations in time) or deduct them for a period of up to six years in the case of start up expenses or up to three years in the case of start-up expenses incurred by a manufacturer. Expenses or investment in intangible assets may not be amortized.

c2) Non-deductible expenses.

Expenses relating to the acquisition and maintenance of automobiles (including cars and vans, but excluding trucks) are not deductible unless they pertain to the line of business of the taxpayer. Some examples of non-deductible items are expenses incurred in the acquisition of non-business related assets, disbursements which are not necessary for the business, expenses incurred by the business entity which benefit the owners or are deemed a covert profit distribution, amounts charged to tax results in excess of those accepted by law and expenses which are not duly evidenced by back up information.

c3) Thin capitalization rules.

Currently three thin capitalization rules exist. One deals with royalty payments made by a Chilean licensee who is allowed to deduct royalty payments as a necessary expense in an amount up to 4% of annual gross revenues. This rule does not apply if a foreign licensor and the Chilean licensee are totally unrelated entities in terms of control, management or otherwise (as must be evidenced in a sworn statement to be filed yearly before the IRS) or if in the jurisdiction of the foreign licensor income is subject to a tax rate equal or exceeding 30% (as provided in a Supreme Decree, which is still not in force). The second rule derives from a Resolution adopted by the Foreign Investment Committee and affects only those foreign

investors that have entered into a foreign investment contract with the Republic of Chile under Decree Law 600. Although the tax regime does not formally impose restrictions on debt/equity ratios, there is in reality an indirect limit on indebtedness because the Foreign Investment Committee currently limits borrowing levels when approving investments (25:75). The third rule enforceable since January 1 of 2003 restricts the applicability of the special 4% withholding tax rate, regarding interest payments, made by a Chilean business entity insofar an "excess of related indebtedness" occurs (i.e., if there is a , 3 to 1 debt/equity ratio) and provided that the withholding tax applicable to such interest is the reduced 4% rate. The interest paid on the excess of indebtedness will be subject to the general 35% rate to be borne by debtor.

d) final additions and deductions. To reach the net taxable income some further additions must be made corresponding to the non-deductible items referred in c2 above. Far more important are deductions. They correspond to income which is exempt from corporate tax, including profits received as a shareholder or partner from another business entity. These amounts are exempt provided that profit distributions were subject to corporate tax at source. The exemption is designed to avoid internal double taxation.

e) monetary correction. Net equity existing at January 1 of each calendar year is to be restated by the domestic CPI. Capital increases and decreases occurred during the year are also restated by CPI. Non-monetary assets and nonmonetary liabilities existing at year end (December 31) are also restated to reflect the impact of the variation of Chilean or foreign currency, as the case may be. Restatement of the initial net equity, capital increases and non-monetary liabilities are charged to net taxable income, thus constituting a loss in the tax statement. Restatement of capital decreases and of non- monetary assets are to be credited to tax results as a profit. According to the Chilean Income Tax Law, the net restatement amount corresponding to monetary correction of initial tax equity and its variations are to be registered as an equity reserve and considered a non-taxable event.

f) Tax Deferral on Profit Remittance. According to the Chilean Income Tax Law, the ultimate business owner may be entitled to a tax deferral from Withholding Tax assessed on profit remittances, provided that they are reinvested within twenty days in another business entity obliged to determine its gross revenues with full accounting records. The reinvestment is subject to several other requirements in order to be entitled for the deferral.

Presumed Income.

Some businesses must pay income tax calculated on a presumed basis, including small to medium-sized mining, transportation and agricultural operations[5]. In these cases, no net taxable income is to be computed nor accounting are required to determine the tax base subject to 16% corporate tax

(b) Capital Gains Tax

A Capital Gains Tax as such does not exist in Chile. Depending on the circumstances, capital gains are taxed either as a normal business income, deemed a non- taxable event or finally subject to a sole 15% tax.

(i) gains arising from the sale of rights in partnerships, gains arising from the sale of shares by a recurring seller of shares if held for less than a year and recurring sales of real estate are deemed ordinary business income and subject to the 35% burden divided at two taxation levels.

(ii) gains arising from the sale of real estate and movable property done on a non-customary basis are deemed a non-taxable event.

(iii) gains arising from the sale of shares held for more than one year by a non-customary seller, gains from bonds, debentures and mining rights, provided those rights do not form part of the taxpayer's fixed assets, are subject to the sole 15% First Category Tax and no further taxation applies at the second level.

[5] Law 19,749 created a new type of taxpayer, the " Microfamily Enterprise", which is also subject to corporate tax on a presumed income basis

(iv) Notwithstanding the above, gains arising from the sale of shares of a publicly traded corporation, or from the sale of bonds issued by the Republic of Chile, the Central Bank or entities authorized to issue bonds obtained by a foreign institutional investor and provided certain requirements are met, is exempt from taxes, according to new Article 18bis of the Chilean Income Tax Law.

(c) Sole Second Category Tax and Surtax (or Global Complementary Tax)

Residents pay these progressive personal income taxes (0% - 40%[6]) on salaries and wages, income earned overseas and withdrawn business income.

Business profits withdrawn from certain business entities and invested in another entity in Chile within twenty days are not subject to tax until finally withdrawn or remitted overseas. Simple procedural requirements must be followed strictly to achieve this deferral of tax liability.

(d) Additional Tax (Withholding Tax)

Additional Tax of 35% is payable by non-resident individuals and entities, on Chilean-source business income withdrawn from Chile, paid from Chile, made available for or remitted abroad. This tax is withheld by the payer entity.

As in the case of progressive personal income taxes, the 16% corporate tax effectively paid is credited against Additional Tax due. As a result, the effective rate payable on foreign investment profits remitted abroad is normally 35%, 16% being payable at the time profits are earned (at the corporate level) and the balance is due upon payment overseas.

Withholding tax (normally at the rate of 35%) is also assessed on most other payments made abroad. For example:

(1) 30% on royalty payments and patent, license and similar fees;

(2) 4% on interest payments made to a foreign or international bank or to a foreign international financial institution registered as such with the Central Bank. To be registered, a financial institution must have corporate purposes which include financing and paid-in capital of at least US$2.2 million. An investor may be able to arrange financing through a wholly-owned registered financial institution. A 35% rate applies to interest payments to all other entities and if excess of related indebtedness exists;

(3) 1.75% of lease payments made by lessees regarding leases of imported capital assets;

(4) 20% on technical assistance or engineering work rendered in Chile or abroad; and also on remuneration of a technical or scientific nature of a non-resident foreign individual. Other source payments remitted abroad are subject to the 35% withholding tax rate.

A foreign recipient of payments subject to withholding tax who is unable to obtain or use a tax credit for deduction will normally prefer to establish a Chilean entity to receive the payments. The local entity will be able to claim the deduction of expenses incurred; applying a 35% withholding tax to profits remitted abroad.

(e) Non-Deductible Expenses Tax

A sole tax of 35% is paid by stock corporations on non-deductible expenses. While other entities are not subject to this tax, the "rejected expense" is added to net taxable income for the purpose of applying corporate tax and is deemed withdrawn from the partners or shareholders for the application of the personal taxes.

Income Tax Payment

Chile has a calendar tax year Jan 1 - Dec. 31) and tax returns must be filed by April 30 of the following year. Business entities are required to make monthly provisional payments (PPMs) of First Category corporate tax equal to a percentage of the

[6] See footnote number 2.

previous month's gross revenue. The percentage is determined by the ratio of gross revenue to First Category Tax for the business entity for the preceding year. Any further tax due must be paid on filing of the relevant tax return. Excess tax paid is recoverable after filing. PPMs are suspended if the taxpayer has registered a loss in the preceding quarter and must be resumed the quarter subsequent to that during which profits were registered.

Employers must withhold, file and pay to the Treasury Service the personal income tax (Second Category) assessed on its employees' total gross remuneration or salaries, which includes non-monetary labor benefits and excludes social security and health insurance contributions. However, with regard to calculating the latter contributions, the maximum remuneration to be considered is up to 60 UF (currently approximately US$ 1,330). Notwithstanding the above, foreign employees may continue under certain circumstances participating in the social security system of their home countries.

Intercompany Transactions/Transfer Pricing

Chilean Transfer Pricing regulations are generally patterned on the Organization for Economic Cooperation and Development (OECD) guidelines. Article 38 of the Chilean Income Tax Law (ITL) regarding prices or values charged by the branch or subsidiary to its Parent Company or vice versa refers to prices or values that are inconsistent (higher or lower) with prices that would be charged in an arm's length terms. Further, for services rendered by a branch or subsidiary to a parent company, fees should evidence a reasonable profit considering the circumstances of the transaction, for which a "cost plus" method is typically employed. However, no specific guidelines regarding the costs plus percentage are provided by the Chilean rules and further no safe harbors exist. As a result, the criteria for determining whether a fee would or would not be acceptable under such Transfer Pricing rules is problematic. It must be also be noted that the Income Tax Law affords the Chilean Internal Revenue Service considerable leeway in determining whether the price or value is acceptable.

In addition, imports and exports of goods and services must be approved by the Customs authorities and the Central Bank and if inconsistent with prevailing market prices will not be approved or the Chilean Customs may assess tax differences arising thereof.

Resident Foreigners

Until residence for tax purposes is acquired, foreigners working in Chile are subject to a single tax of 20% on fees or salaries for scientific, technical, cultural or sporting activities. The rate is 35% for other activities. Once residence has been acquired for tax purposes, foreign individuals are subject to the same tax treatment as Chilean citizens; namely, to the Second Category Tax, which is a progressive tax ranging up to 40%. Foreigners are subject to tax exclusively on Chilean source income for the first three years (with a possible extension) and thereafter are taxed on their worldwide income.

Tax residence is acquired when the individual remains in the country for more than six months in two consecutive calendar years. It should be noted that certain Double Taxation Treaties set forth different rules for determining the individual residence.

Accounting Records

Normally accounting records must be kept in Chilean currency (pesos). However, the IRS can allow records to be kept in a foreign currency if the relevant capital has been contributed in such currency or the substantial part of the taxpayer's operations are expressed in that currency.

Double Taxation Treaties (DTT)

Chile has a DTT with Canada and Mexico based on the OECD Model (though in some matters patterned after the United Nations Model). DTT's entered into with Norway, Brazil, Peru, Poland and Ecuador are pending Congressional approval. Chile has a DDT with Argentina based on the principle of the income source patterned after Decision 40 of the Andean Pact. Chile also has several limited treaties with other countries related to air, land, sea and river transportation. Negotiations with Spain and the United States of America are currently being conducted.

VALUE ADDED AND OTHER INDIRECT TAXES

Value added tax (V.A.T.) at a 18% rate applies on the sale of movable goods made on a customary basis, certain real estate (i.e., new buildings owned by construction companies) and some services, regardless if performed on a customary basis or not, including industrial, commercial and construction services and most local leasing and licensing arrangements.

The tax extends to the import of goods. The IRS may exempt the importing of raw materials used in the production, processing or manufacture of goods for export. Importing of capital goods forming part of an investment under the Foreign Investment Statute are also exempt if included in a list contained in a Supreme Decree of the Ministry of Economy. Exports (of goods but also of some services) are entitled to the zero mechanism in terms exports are exempt but remain entitled to recover amounts paid with respect to acquisitions and services deemed as exports.

V.A.T. paid on the purchase of goods and services used to produce goods and services which are subject to V.A.T. may be credited against V.A.T. due on subsequent sales, provided that a percentage equal to the V.A.T levied with respect to the purchase is paid to the seller or the person who renders the service.[7] The V.A.T. credit can be carried forward indefinitely until completely absorbed by future tax debits. Excess V.A.T. credit accumulated over a period of six consecutive months or more may be reimbursed by the Treasury, provided such excess pertains to the acquisition of fixed assets used to produce V.A.T.-related activity.

Customs Duty

A customs duty is normally payable on imports at a rate of 6% (as of 2003) assessed on customs value, which is normally equivalent to OF values. Certain imports are exempt from customs duties, such as hardware computing equipment.

Property Tax

Property Tax, normally 2% per annum, is payable on properties whose value exceeds certain threshold values which vary according to type of property (such as residential, agricultural and commercial). Commercial and industrial properties are subject to a 30% surcharge and some other types of properties are entitled to reductions or temporary exemptions. Vacant urban lots are subject to a 40% surcharge. For the purpose of calculating the tax, property values are updated at the beginning of each year and adjusted for cost of living increase mid-year.

Municipal Taxes

Most commercial activities (including mining activities) are subject to a municipal tax. This tax ranges from 0.25% to 0.5% of the net tax equity of the taxpayer per year (the rate depends on the municipality), subject to a maximum of 8,000 Monthly Tax Units (approximately US$ 310,292 per year).

FOREIGN INVESTOR TAX INVARIABILITY OPTIONS

The Foreign Investment Statute allows foreign investors to choose to be subject to an overall income tax rate of 42%, fixed for ten years (rather than the normal 35% rate which may change). As in the case of 35% rate, a credit is allowed for the 16% First Category Tax (corporate tax) paid. This effectively allows investors to pay a 7% tax rate premium as security against a future adverse tax rate change. This rate has been fixed taking into account taxes applicable in countries likely to invest in Chile, particularly the U.S. corporate tax of 34%. Unless the U.S. Government decides to raise its rate, Chile may be reluctant to increase its 35% rate.

In the case of investments exceeding US$ 50 million in industrial or extractive (such as mining) projects, investors may also be entitled to:

[7] Please note that this requirement was recently introduced by Law N°19,738 and, as mentioned, will become enforceable by December 31 of 2002.

(1) the fixed income tax rate of 42% for up to twenty years (rather than ten years);

(2) rely (for a period of up to 20 years) on laws and rulings in force when the investment is approved relating to depreciation, carrying forward of losses, organizational and start-up expenses and the right to maintain accounts in U.S. dollars; and

(3) rely on laws and regulations in force when the investment is approved relating to the right to export freely for a period of up to 20 years.

Foreign investors choosing to take advantage of any of these "invariability" options may waive any or all of them once only during the life of their investment. After the waiver they will be subject to the normal tax regime, effective from the tax year in which the waiver is made.

Foreign investors may also choose to fix rates of import duties and value added tax current when the investment is approved for the period of implementation of their investment.

STRUCTURE OF INVESTMENTS/INVESTMENT VEHICLES

Making Foreign Investments

A foreigner may make an investment in Chile by:

(1) the commencement of a new business through a Chilean entity formed by the investor;

(2) the purchase of the assets of an existing Chilean business through a Chilean entity formed by the investor;

(3) the purchase of shares or other rights in an existing Chilean corporation or partnership/ company, either directly or through a Chilean entity formed by the investor;

(4) the direct purchase of shares or other rights in a non-Chilean entity which owns (by any of methods (1), (2) or (3) an investment in Chile; or

(5) direct investment in Chilean securities in accordance with Law 18,657 (see *Chilean Regulation of Foreign Investment-Foreign Investment Funds*).

In alternative (3), the purchaser effectively assumes the existing liabilities of the acquired entity. This is avoided when only business assets are acquired (alternative (2)) although even in this case, if the seller ceases to carry on business after the sale, the purchaser normally becomes liable for any outstanding tax liabilities affecting the assets sold. The purchaser may also be liable for certain pre-acquisition obligations to employees of the acquired business.

Alternative (3) does not require formation of a Chilean entity by the investor to acquire the Chilean shares/or other ownership rights. Such rights can be purchased by the foreign investors directly. However, a Chilean holding company might be necessary if the acquisition is to be financed by Chilean borrowings and may be desirable for tax and liability reasons.

Alternative (4) does not require Chilean foreign investment approval because the identity of the foreign investor has not changed. However, the Foreign Investment Committee or the Central Bank will need to be notified of the acquisition, depending on whether the offshore parent's original Chilean investment was approved under the Foreign Investment Statute or the Foreign Exchange Regulations. There is no set time period for notification. In addition, Chilean securities legislation (see *Mergers and Acquisitions*) and trade practices and anti-trust legislation (see *Trade Practices and Anti-Competitive Conduct)* may be relevant to the acquisition. Chilean tax law should not apply to the acquisition.

Types of Investment Vehicles

The establishment of an investment vehicle in Chile is straightforward and relatively inexpensive. The tax treatment afforded to the various types of corporate entities is very similar and home country considerations will often be decisive in determining the appropriate entity. The principal types of business entity are limited liability companies /partnerships, stock corporations and branches.

Limited Liability Partnership or Company *(Sociedad de Responsabilidad Limitada)*

(1) Nature of Entity. This is the most commonly used business entity in Chile. Like corporations, the liability of members is limited and, unlike many foreign partnerships, the entity is legally distinct from the partners. Accordingly, partnership losses may not be set off against partners' other income.

(2) Partners. A minimum of two partners is required and a maximum 50 partners is permitted. A partnership is automatically dissolved if there is only one partner or one partner is deemed to have total control through ownership of related entities or control of a nominee partner. Foreign legal entities may be partners.

(3) Regulation. Limited partnerships are not subject to the control of a regulatory authority or similar body and have no obligation to publish or file accounts. The name of one of the partners or the type of business activity must be incorporated into the partnership name and the name must also end with the word "Limitada".

(4) Formation, Modification and Dissolution. Limited partnerships are constituted by a public partnership deed, an extract of which must be published in the Official Gazette and registered in the Commerce Registry. Any amendment or modification to the partnership deed, including change of partners, modification of the corporate purpose, or to the powers of management, needs to be agreed to by unanimous consent of all the partners. Chilean law sets forth the circumstances in which a partnership will be dissolved, which circumstances include when agreed to by all of the partners or after the expiration of an agreed term (which is not renewed). The partners may enter into a separate agreement (similar to a shareholders agreement) binding them to consent to deed amendments, sales of partnership interests or dissolution in the circumstances set out in the agreement.

Once a person in Chile has been authorized by a power of attorney to undertake the procedural steps to form the partnership, it normally takes three to four weeks to establish the partnership.

(5) Management. The partnership deed will set out how the partnership is to be managed. Management powers may be exercised by one or more of the partners, a board of directors or by a third party.

(6) Capital. A partnership's capital is set out in the partnership deed. Capital contributions may consist of cash, property (including technology) or services provided to the partnership. Capital may be increased or reduced by agreement of all partners and amendment of the partnership deed. Approval of the Internal Revenue Service is also required in the case of a decrease of capital.

(7) Limitation of Liability. The liability of partners is limited to the amount of their capital contributions to the partnership or such greater amount set out in the partnership deed.

(8) Distribution of Profits and Loans to Partners. In contrast to Chilean corporations, annual profits may be distributed without recouping previous years' losses and loans to partners are treated as distributions of profits.

(9) General and Silent Partnerships. General partnerships are the same as limited partnerships except that the liability of partners is unlimited. Silent partnerships consist of management partners whose liability is unlimited and silent partners whose liability is limited to their capital contributions to the partnership. The identity of the silent partner need only be revealed to the tax authorities.

Corporation or Stock Company *(Sociedad Anonirna)*

(1) Public/Private. A corporation may be either public/open or private/closed. A corporation is public if it is registered with the Superintendency of Securities and Insurance or has at least 500 shareholders or greater than 10% of its issued capital is held by more than 100 shareholders. Shareholders who hold more than 10% of the share capital are excluded for the purpose of this final calculation. All other corporations are private.

(2) Public Corporation Regulation. Public corporations are subject to the control of the Superintendency of Securities and Insurance and must list their shares on the Stock Exchange, publish (and send to all shareholders) an annual report and audited annual financial statements and distribute at least 30% of net profits (unless all shareholders agree otherwise). These requirements do not apply to private corporations.

(3) Shareholders. A minimum of two shareholders is required. A corporation is automatically dissolved if all its shares are held by one entity. As with partnerships, total control is deemed to occur when ownership is held through related or nominee entities.

(4) Directors and Managers. Management is in the hands of a board of directors, formed by a minimum of three directors in the case of private corporations and by a minimum of five for public corporations. Directors may be of any nationality and are appointed at an ordinary general meeting of the shareholders. Elections for the entire board must be held once every three years (or more frequently as set forth in the company's bylaws pursuant to a shareholders vote) and directors may be reelected indefinitely.

The board of directors may exercise all powers of the corporation not reserved to the shareholders by the law of corporation's by-laws. The power of the board to delegate its powers is subject to a number of limitations. The board may not delegate all its powers and can only delegate to managers, assistant managers, lawyers or members of the board (although delegation to other persons is possible for specifically determined purposes).

(5) Formation. Corporations are incorporated by public deed, which contains the corporation's by-laws. An extract of the by-laws must also be published in the Official Gazette and Registered in the Commerce Registry. Corporation names must include the words "Sociedad Anonima" or the initials "S.A.".

(6) Capital. A corporation's capital is set out in its by-laws and may consist of contributions of cash or property. Shares may not be issued as payment for personal services or for formation of the corporation. Capital must be subscribed and paid within three years. Capital may be increased or reduced by agreement of an extraordinary shareholders' meeting and requires the approval of the Internal Revenue Service in the case of a decrease. Existing shareholders have a "right of first refusal" to acquire new shares and that right is transferable to third parties. Preferential shares may be issued.

(7) Dividends. Corporations may not pay dividends (i.e., distribute profits) out of annual profits until the previous years' losses have been "recouped". Interim or provisional dividends may be declared by the directors from profits realized during the distribution period, but the directors are personally liable if such dividends exceed annual profits available for distribution.

(8) Share Transfers. The board of directors cannot restrict share transfers and the by-laws of public corporations cannot limit the free transfer of shares. However, shareholder agreements restricting transfer (and other) rights are permitted and must be registered with the corporation and made available to other shareholders and interested third parties.

(9) Shareholder Loans. Loans to shareholders are not treated as distributions of profits for tax purposes.

(10) Merger or Division. Mergers and splitting up of a corporation is permitted by a resolution of at least two-thirds of the shareholders having the right to vote passed at an extraordinary general meeting.

(11) Minority Rights. In the case of a merger, liquidation of a corporation's assets, the issuance of preferred shares and certain other circumstances, dissenting shareholders have the right to require the corporation to buy their shares, at book value in the case of private corporations and market value in the case of public corporations.

(12) Dissolution. A corporation may be dissolved by a resolution of at least twothirds of shareholders having the right to vote, passed at an extraordinary general meeting. Dissolution may also be required in other circumstances by the law or the corporation's by-laws.

Branch of a Foreign Entity (*Agencia*)

Foreign corporations may establish a branch by appointing by public deed a person present in Chile with broad powers to represent the corporation. The foreign corporation must also register and publish certain information about itself, including the amount and form of its capital in Chile. The obligations of the branch must be supported by liquid assets retained in Chile although no minimum capital is required.

Foreign corporations are fully liable for the activities of their Chilean branch and the financial statements of the branch must be published. Branches are taxed on locally derived income only.

Joint Venture

Joint ventures are not separate legal entities and are regulated by the applicable joint venture agreement. Joint venture partners often operate in Chile through a jointly formed Chilean corporation, partnership or branch office.

Association (*Asociacion o Cuentas en Participacion*)

An "Asociacion o Cuentas en Participacion" is basically a contractual relationship pursuant to which two or more parties participate in one or more business ventures which are carried out in the name and under the responsibility of one party only. This party, known as the manager or administrator, is responsible for rendering accounts to the other participants and distributing profits and losses between them in agreed proportions. The manager is responsible for all dealings with third parties in relation to the association and relevant business ventures.

An agreement between the parties sets out the purpose, form and terms of the association and the parties' respective interests. The arrangement is essentially private and does not create a separate legal entity.

INVESTMENT INCENTIVES

Introduction

Generally it is not government policy to provide specific incentives; investment is encouraged by offering foreign investors stability, certainty and a guarantee of non-discrimination. However, some industry incentives are available for forestry, petroleum, nuclear, irrigation, transport and small mining enterprises and regional incentives (including free trade zones) exist in the north and south of the country. Foreign investors may also be assisted by the activities of ProChile and Fundacion Chile. Incentives for "non-traditional" exports are discussed in *Importing and Exporting*.

Regional Incentives

Free trade zones exist in Iquique in the far north and Punta Arenas in the far south of Chile, and mining free trade zone in Tocopilla also in the north, with the following features:

(1) Entrance of goods into the zones does not require a permit and is only subject to a 3% tax; however, the application of this tax has been suspended for several years and thus is not currently applicable;

(2) Goods imported from the free trade zones into the rest of Chile are subject to customs duty on foreign components only;

(3) Value added tax does not apply to sales within the free trade zones by enterprises located in the zones; and

(4) Enterprises located in the free trade zones are not liable to First Category/ Corporate tax.

A limited free trade zone also exists in Arica near the Peruvian border. Regional incentives also apply to the First Region in the north, the Eleventh and Twelfth Regions and Chiloe in the south and the Chilean Antarctic Territory. Incentives include the exemption of a percentage of workers' income for tax purposes. Special incentives exist with respect to Easter Island. Another investment program known as the Southern Plan attempts to encourage investments in the Eleventh and Twelfth Regions by granting investors, among other benefits, a tax credit of up to 40% of the amount invested until the year 2008.

ProChile

ProChile is a semi-official agency encouraging Chilean exports. It provides information to prospective exporters and may assist in negotiations to remove or minimize restrictions imposed by foreign countries affecting Chilean exports. ProChile's services are available to both locally and foreign owned export businesses operating (or proposing to operate) in Chile.

REGULATION OF SPECIFIC INDUSTRIES

Mining

Under Chilean mining law the State has exclusive ownership and control of all mineral deposits. However, the law separately recognizes the right to own land in which mineral deposits are located and allows private investors to carry out mining activities under licenses (a "concesion") or through a joint venture with the government-owned copper company Codelco (which controls the copper industry and holds large areas of prospective mining territory). Specific restrictions exist in relation to oil, natural gas, lithium, uranium and thorium (see *Oil, Gas, Lithium, Uranium and Thorium,* below).

Some extractable substances are not considered minerals and are excluded from the mining regime, including sand, gravel, rock and other materials used in the construction industry, surface clay and artificial salt deposits on the shores of lakes and the ocean. These substances belong to the respective owners of the land or salt deposits.

Private investors may acquire mining concessions which grant the right to exploit and/or explore particular areas. In addition, legislation enacted in 1992 permits Codelco to enter into joint ventures with private investors for the purpose of exploration and exploitation. Private sector involvement in the copper industry by way of sub-contracting as well as joint venture has been encouraged by falling Codelco revenue caused by low copper prices and the limited amount of government funds available for further exploration and exploitation of Codelco held sites. Unions and the ruling political coalition continue to resist any suggestion of privatization of Codelco and the copper industry but such a step will continue to be a possibility over the next few years.

The key features of the mining regime governing the grant of exploration and exploitation concessions are:

(1) Concessions may be granted in relation to exploration or exploitation rights. They may not be granted for mineral deposits within Chilean territorial waters unless accessible by tunnel from land. Some other zones are also excluded. For example, for national security considerations, mining rights in relation to land on and near the borders of Chile will not be granted.

(2) Once granted, the concession confers the exclusive right on the holder to carry out the designated exploration or exploitation (subject to obtaining appropriate prior foreign investment approval in the case of foreign holders). The concession extends to all types of minerals within the relevant area, excluding oil, gas, lithium, uranium and thorium (see *Oil, Gas, Lithium, Uranium and Thorium*, below).

(3) Mining titles are granted by way of a judicial process which takes six months to a year for exploration rights and approximately one and a half years for exploitation rights (assuming no major objections from landholders or third parties are received).

(4) The grant of a concession may be subject to certain conditions, including payment of compensation to landholders affected, a right of expropriation by the government in certain circumstances and payment of an annual license fee.

(5) Exploration rights are granted for a two-year period with a two-year extension available. 50% of the territory must be surrendered after the first two years. The license fee is approximately US$0.85 per hectare per year.

(6) Exploitation rights may be held indefinitely subject to payment of the annual fee which is approximately US$4.00 per hectare.

(7) Holders of concessions must indemnify the owner(s) of the land against damage arising from the exercise of their rights.

(8) Mining rights are freely transferable subject to appropriate notification being given to the Mining Registry.

Oil, Gas, Lithium, Uranium & Thorium

Exploration for and exploitation of lithium and, with some limited exceptions, gaseous and liquid hydrocarbons is reserved to the State of Chile. However, private investors may enter into "risk contracts" with the government for the exploration or exploitation of specific areas giving the investor a right to participate in exploration and exploitation income.

The Government of Chile also has a first option to purchase minerals containing uranium or thorium.

Banks and Financial Institutions

Traditionally, national legislation has permitted banking institutions to supply directly only those banking services which are considered traditional.

The new Banking Law (whose revised text was published in the *Diario Oficial* on December 19, 1997) broadened the business activities which such banking institutions may undertake (nationally and internationally), allowing them to participate in affiliated "factoring" institutions, custody and transfer of stock, collection agencies, stock brokerages (except for stock related to social security) and title securitization companies. In addition, according to the new law, banks may act as placement agents for initial public offerings by open stock companies and offer to individuals who are not clients services supporting such lines of business.

Financial institutions (as distinguished from commercial banks) are not permitted to operate commercial accounts or carry out foreign trade operations.

Chilean law does not distinguish between banks established in Chile (Chilean institutions) and branches of foreign banks authorized to do business in Chile, so that both are subject to the same regulation regarding requirements, operations and supervision.

(i) Superintendency of Banks and Financial Institutions (SBIF)

The SBIF is an autonomous institution with legal capacity, which is related to the government through the Ministry of Finance.

It supervises the State commercial bank, banking institutions and financial entities whose supervision is not by law granted to any other institution.

The SBIF has the following powers with respect to financial institutions:

- To apply or interpret the laws, regulations and other rules which apply to financial institutions, and to promulgate rules for their implementation.
- To grant authorization for the operation of banks, financial institutions, affiliates thereof in Chile and abroad, and institutions which support banking activities.
- To revoke operating authorization.
- To authorize the opening and closing of branches or offices in Chile and abroad.
- To authorize modifications to the bylaws and operating rules of the supervised entities, including increases and decreases in capital.
- To enforce the completion of all legal obligations and restrictions.
- To review the operation of banks through inspections and the review of financial statements and any other information.
- To review the records regarding offerings and investments, other balance sheet items and internal procedures and controls.
- To determine penalties and other corrective measures.

In the case of a violation of rules or laws, absent a specific sanction provided by law, the SBIF may impose the following sanctions: warning, censure, fines, restrictions of operation, appointment of an inspector, assumption of the administration of the institution and declaration of the institution in involuntary liquidation.

(ii) Authorization of Banking Licenses

In order to be established in Chile, a banking institution must have SBIF authorization, for which it must present a report setting forth the fundamental characteristics of the proposed business. The authorization is subject to applicable law and criteria established by SBIF. In this regard, the new Banking Law establishes as a prerequisite for approval of a license the verification of the solvency and the integrity of the shareholders. The same conditions apply when a person acquires a percentage of 10% or more of the capital of a bank, or when its total holdings exceed 10%.

In order to prove solvency, the law requires that the founding shareholders of a bank have net consolidated assets equivalent to the proposed investment, with a minimum of 800,000 UF (approximately US$18 million as of November 2002) and 400,000 UF in the case of a financial institution. With respect to meeting the requirement regarding the integrity of the shareholders, in addition to their commercial history they must be able to show an absence of fraudulent or serious or repeated criminal activity which could put at risk the stability of the institution which they propose to create, or the security of the deposits made therein. The conduct referred to in the law relates to commercial activities and financial administration, especially banking activities.

SBIF will verify the completion of the conditions set forth above, and analyze requests on a case by case basis, permitting the Central Bank to opine on the effect such authorization of a new bank could have on the stability of the banking system or the adherence to the Rules of the Central Bank.

(iii) International Activities

A fundamental aspect of the most recent revision to the Banking Law is the ability to carry out international transactions by national banks. Such transactions can be carried out in three ways:

(a) by establishing branches or offices outside of Chile;

(b) by making crossborder investment and placements; and

(c) by directly investing in the shares of banking institutions or entities supporting banking services established outside of Chile.

Crossborder placements are loans which are authorized to be made by banks from Chile to offshore locations where such banks do not have a direct commercial presence. Such loans may be authorized by a local bank in favor of its clients in order to finance offshore operations or to new clients domiciled outside of Chile. Banking regulations require that a favorable report from the Central Bank must be obtained in order to carry out such activities. Such regulations mainly relate to the amount and type of operation permitted, as well as an evaluation of the country risk involved.

Regarding foreign branches or affiliates, the law establishes a procedure to be followed for a Chilean bank to establish itself outside of Chile and permits the creation of entities supporting banking services equivalent to those services which are permitted to be carried out in Chile. With respect to such services, the most important requirements relate to the macroeconomic stability of the country where the branch will be operating and the existence of a regulatory system which insures the proper functioning of the branch and permits SBIF to supervise the relevant entity to the extent it considers necessary.

(iv) Main Regulatory Issues

Net Worth Requirement. Prior to the promulgation of the revisions to the Banking Law, the law established a limit for banking operations based on the level of the institution's debt. Under the prior law, liabilities of banks could not exceed twenty times their capital and liabilities of other financial institutions could not exceed fifteen times their capital.

The new law eliminated this form of regulating levels of assets and liabilities and replaced it with capital requirements based on minimum requirements for capital established by the Basel Convention, which are calculated based on the assumed risk of various assets held by the bank. Such capital requirements have been adopted universally and have been incorporated in the Banking Law by means of a requirement of valuing total assets which may not be less than 8% of the assumed debts. The adoption of this system, among other advantages, permits increased transparency and a uniformity of indexing the net worth of Chilean banks.

Lending Limits. Individual lending limits are 5% of the total assets of a bank for unsecured debts.

However, the bank may grant loans of up to 25% of its total assets if the amount that exceeds the 5% limit for such loans is secured with physical assets or real estate with a value equal to or greater than such excess or by other guarantees authorized by law.

The individual lending limit is increased to 10% if the excess corresponds to export credits payable in foreign currency. For such credits, the limit with a guarantee is up to 30% of the total assets of the bank.

In addition, the lending limit is increased to 15% if total net worth of the excess corresponds to credits, in any currency, to be used to finance public works to be completed pursuant to concessions system contemplated in the Ministry of Public Works decree No. 164 of 1991.

Finally, bank loans made to other financial institutions subject to the Banking Law may not exceed 30% of the total assets of the lending bank.

Related Party Transactions. In the case of natural persons or entities related to the property or business of the bank, the aggregate amount of loans made to a related person or group must be within individual lending limits. In any event, the total amount of loans to related persons or entities must not exceed the net total assets of the bank.

Loans to related persons must be made on an arm's-length basis, without more favorable rates, terms or guarantee requirements than those granted to third parties for similar transactions.

Solvency and Administration. The new Banking Law establishes a system of periodic qualification of banks based on solvency and administration, which promotes a process of self-regulation among institutions.

Moreover, those entities which are well evaluated will be able to take advantage of increased business opportunities and can develop more fully in the capital markets, particularly with regard to the incorporation of subsidiaries in Chile or abroad and making investments in banks which are established abroad.

Government Guarantee. Finally, it should be noted that the Republic of Chile guarantees the obligations arising in connection with deposits and certificates of deposit, savings accounts and certain other instruments. This guarantee only protects natural persons and covers 90% of the total amount of the obligation which the financial system owes to such person, up to 120 U.F. (approximately US$2,700). In addition, the Central Bank provides a guarantee of demand deposits with terms of ten days or less. These guarantees cover all banks authorized to operate in the national market.

Insurance

(i) Legal Framework

Insurance regulations in Chilean law have their origin in the Commercial Code of 1865. As the concept of insurance has evolved, both nationally and internationally, the insurance laws as originally conceived have been repeatedly modified and amended.

The provision of insurance is actually regulated by a broad set of rules in addition to those established in the Commercial Code, which are divided mainly between land and maritime insurance.

Moreover, many laws have been passed which were intended to regulate insurance authorities, the contents of insurance policies, and the limitations of insurance contracts, among others.

Finally, it should be noted that notwithstanding the rules referred to above, insurance policies, due to their character as a contract, are also subject to the general rules for contracts set forth in the Civil Code.

(ii) Regulatory Authorities

The authority charged with regulating the operations of insurance companies is the Securities and Exchange Commission (Superintendency of Stocks and Insurance, "SVS"), which is an autonomous institution with legal capacity and independent funds and which relates to the Chilean government through the Ministry of Finance.

In the insurance area, the SVS supervises entities which participate in the business of insurance and reinsurance in any manner. In practice, the SVS ensures that the persons and institutions supervised act in accordance with the laws, regulations, statutes and other rules applicable to the insurance industry.

(iii) Principal Powers of the Superintendency

- Administrative interpretation of the laws, regulations and other rules applicable to supervised persons and entities and the establishment of rules, giving of instructions and application of orders for the application of and adherence to law.
- Hear consultations and petitions and investigate accusations and complaints.
- Provide reports required by courts.
- Review operations, assets, books, accounts, files and documentation of members of the insurance industry, supervise the activities thereof and request such information as it deems necessary.
- Establish rules for the creation and presentation of annual financial statements, balance sheets and other financial information of insurance companies.
- Inspect supervised entities.

(iv) Regulatory Framework

The Chilean system contemplates a set of requirements for insurance and reinsurance companies, which are designed to maintain greater stability and solvency.

Article 8 of DFL No. 251 distinguishes between two types of insurance companies. The first group includes companies which insure against risk of loss or damage to property or assets and the second group includes companies which cover risks to persons, for a specific term, amount, settlement policy, or income for the insured or his beneficiaries.

Article 4 establishes that insurance companies must be stock companies established in Chile, and can only be involved in the business of insuring risks and those activities which support or complement such line of business, previously authorized by the Superintendency.

In addition, insurance companies must only be involved in either general insurance or life insurance (corresponding to groups one and two described above) and are prohibited from offering both types of insurance. In addition, credit risks, which are risks of loss or damage to assets caused by the failure to pay a financial obligation, can only be covered by insurance companies corresponding to group one.

The reinsurance of contracts executed in Chile must be made by companies authorized to provide insurance or reinsurance in Chile. Insurance companies may only reinsure risks within the group in which they are authorized to operate. Foreign reinsurance companies are also authorized to reinsure in Chile if they are registered with the SVS and meet the other requirements established by law.

Insurance and reinsurance companies in Chile are formed as and must meet all requirements applicable to open stock companies and must also conform to the requirements described below.

Insurance and reinsurance companies must have secured a charter issued by the Superintendency of Securities and Insurance authorizing their existence in order to be incorporated.

Upon incorporation of an insurance company, its capital may not be less than 90,000 UF (approximately US$2,0 million), and in order for the Superintendency to charter its existence, capital must be fully subscribed for and paid in. If the company decreases its capital to less than this figure during its term, the company is required to make up the deficiency or its charter will be terminated.

Local reinsurance companies must have a minimum owner's equity of 120,000 UF (approximately US$2,7 million) for each group worked by them.

Foreign reinsurers must, in order to reinsure local risks, be classified in a BBB risk category or its equivalent, by an international prestigious risk rating company.

Indebtedness at companies in the first group cannot exceed five times its owner's equity. For companies in the second group, the debt-equity ratio cannot exceed 15 to 1.

The companies must set up technical reserves for outstanding risks as regards short-term insurance premiums; mathematical reserves for long-term insurance premiums; loss reserves for obligations arising from actual unpaid and/or unreported losses; additional reserves for risks with an unknown, fluctuating or major loss ratio which are deemed necessary by the Superintendency; difference reserves for the risks caused by term, interest rate, currency and investment instruments differences, between the assets and liabilities of the company; and fund value reserves.

Insurance companies must retain at least two different and independent risk rating companies.

(v) Superintendency Charter

Article 126 of Stock Companies Law 18,046 provides that insurance and reinsurance companies are established, exist and evidence their existence by means of a public instrument, by securing a charter from the Superintendency and by recording and publishing the special certificate issued by the Superintendency.

On reviewing these data, the Superintendency must be afforded sufficient assurance that the company meets the legal and financial requirements for charter issuance and maintenance.

Once the company's existence is chartered, the Superintendency will issue a certificate evidencing this circumstance and including an excerpt of the clauses from the company's bylaws. The excerpt must be recorded in the local Commerce Registry and published in the Official Gazette within 60 days from the charter date.

Entities failing to meet the above requirements are absolutely forbidden to engage in the insurance business.

(vi) Enforcement, Sanctions and Remedies

The Superintendency of Securities and Insurance is amply authorized to sanction the insurance companies that breach the laws, regulations, bylaws and other rules that govern them or which do not comply with the instructions and orders issued by the Superintendency.

The sanctions which may be imposed by the Superintendency upon insurers include censure, fines which are paid to the Government of Chile, suspensions and charter termination.

The Superintendency is also authorized to sanction individuals subject to its oversight (directors, adjusters, etc.) who may likewise be censured and subject to fines to the benefit of the Government of Chile as well as being suspended from their jobs or having their appointments terminated.

It must be noted that, as regards any fine levied on a company or its directors or adjusters, the directors or adjusters who voted affirmatively on action that gave rise to the sanction are held joint and severally liable for the action.

Finally, the law contemplates the power to file a Remedy of Complaint with the Superintendent whenever it is believed that the administrative acts of the Superintendency, or its failure to act, are contrary to applicable regulations. Also, if a person believes that any instruction, notice, resolution or omission of the Superintendency is illegal and that they have been harmed, he or she may file a complaint with the Appellate Court of Santiago, Chile.

(vii) Investments

The investment of capital and technical reserves is regulated in order to assure investment reliability, liquidity and diversification and to safeguard the insurer's credit worthiness.

In this sense, Articles 21 et seq. of Statutory Decree 251 provide that the technical reserves and venture capital of the insurance companies -notwithstanding any deposits held in checking accounts -must be backed by investments in several instruments and assets detailed in legislation, such as Government-issued or - backed certificates, or Central Bank notes, term deposits, endorsable mortgage securities, bonds, notes, debentures, investment fund and mutual fund shares and listed corporate stock.

Regulations also govern investment caps in the various different types of instruments or assets representing the technical reserves and venture capital.

(viii) Ownership and restrictions to the free transfer of corporate stocks and rights

Chilean law presently allows for the unrestricted investment of foreign capital in local insurance companies. Also along these lines, taxes on insurance policies taken out abroad have been substantially reduced as regards local assets.

(ix) Unregulated premium rates and fees

The Chilean insurance market is totally deregulated as regards premium rates and insurers therefore have complete discretion to set their premiums.

Pension Funds

The main purpose of the Chilean Pension System is to ensure a stable income to the workers who have concluded their working life and secure that such income has some kind of relation to the income received during his/her active life.

The Pension System is based on individual capitalization. Each contributor has an individual account where his/her social security contribution is deposited, which are capitalized and earn profits based on the investments made by the Administrator with the resources of the Funds. At the end of their active life, this capital is returned to the retiree, or his/her surviving beneficiaries as a pension or distributed as required according to law.

The Pension System is managed by private entities, denominated Pension Fund Administrators (PFA). These institutions are special stock corporations which have the exclusive purpose of managing a pension fund and the performing of other activities strictly related to social security and to grant and administer the benefits established by law.

The worker chooses the entity he or she wishes to contribute to and may designate a different entity at any time in accordance with procedures that are established by law.

On February 28th, 2002 Law 19,795 was published in the Official Gazette, amending the Chilean pension system, which created "multi-funds" and liberalized the limits for the investments of such funds.

The new system allows the AFP affiliates to define, according to their particular needs and preferences, the way in which their pension savings will be invested, so that they may choose between 5 different types of funds representing alternatives of investment portfolios.

(i) Guaranteed Benefits

With the purpose of keeping proportionality in the benefits granted by the System, all the contributors who comply with certain basic requirements have the right to receive a minimum pension, guaranteed by the Government of Chile, even the balance in their individual account is not great enough to pay such benefits.

If an Administrator does not reach a minimum level of profitability in a 12 month period as compared to the average profitability of all the Pension Funds in the same period when all the instances established by law have been exhausted, the Government of Chile supplies the lacking compensation and then liquidates the Administrator.

(ii) The Authority

The PFA are controlled by a technical authority called the Superintendency of Pension Fund Administrators (SPFA), which is an autonomous institution with juridical capacity and patrimony of its own and with indefinite duration.

(iii) The Regulatory Framework

The PFA have to be constituted as stock corporations, with a minimum capital of approximately US$ 120,000, which should be subscribed for and paid in at the moment of incorporation. The law also mentions that these administrators should permanently maintain a patrimony at least equal to the minimum required capital, which will increase in relation with the number of contributors kept by the PFA. The law also establishes that no one, neither natural nor juridical persons, which have not been incorporated in accordance with the PFA law can act as an administrator.

(iv) Legal Coverage

The Pension System of Individual Capitalization is mandatory for all employees and optional for those workers who were subject to the prior system at the time when the reform was implemented, as well as for the independent contractors.

(v) Affiliates and Contributors

All workers who opt into the system of individual capitalization acquire the status of "affiliate" and will only lose such status if a worker, upon complying with all applicable legal requirements, elects to withdraw from the individual capitalization system and return to the prior system.

Furthermore, all persons who are engaged in the capacity of workers, either as employees or as independent contractors, may become affiliates without regard to the activities they perform or which employer they perform them for. At the moment of establishing an affiliation with an administrator, the worker participates in the pension system, even if he/she changes employers, becomes unemployed or retires from the work force.

The category of contributor (*cotizante*) refers to those affiliates who contribute each month in accordance with the salary earned the former month, excluding the pensioners of the new system who continue contributing.

(vi) System Financing

Old age pensions are financed with an individual contributions equal to 10% of the taxable income of a person, with a 60 OF cap (approx. US$ 1,450), plus the profits earned by the investment of these contributions. In the event of the disability or death of the affiliate during his/her active life, the individual saving is complemented with disability and survival insurance, which is contracted by the PFA for their affiliates with life insurance companies. This insurance and the administration expenses of the system are financed with contributions in addition to the 10% contributions mentioned above. This contribution is also expressed as a percentage of the taxable income.

(vii) Division Between PFA and Fund

The Pension Fund is not the property of the Administrator. The accumulated resources by the Pension' Fund are the property of each one of the affiliates in the System based on the percentage of their investments. Also, the Administrator is require to maintain separate accounts for the Pension Fund it administers. The assets and rights of a Pension Fund may not be seized.

The Administrators have the right to be compensated for their administration of the Fund and their compensation is comprised on commission paid by the affiliates, which are deducted from either individual capitalization accounts or from withdrawals, whichever may be the case. These commissions are meant to finance the Administrator and the disability and survival insurance.

Every affiliate has the ability to transfer the value of his/her contributed share to another Pension Fund Administrator by giving at least 30 days' prior notice to his or her employer and to the institution in which he or she contributes.

(viii) Pension Types and Modalities

The main benefits produced by the system are the granting of old age pensions, disability pensions and survival pensions. Likewise, the law establishes the existence of the following modalities of pension, each one with its own way of financing and administration which affiliates can elect: Planned retirement, Life Rent and Temporary Rent with Deferred Life Rent.

(viii) Contributions

The pension fund is constituted by the contributions of workers equalling 10% of his or her taxable income up to a maximum amount of approximately US$ 1,330. A worker is only required to contribute 10% of their income but is free to make additional contributions.

There are also voluntary contributions, agreed deposits and voluntary social security saving deposits. While the law does not establish a limit regarding voluntary contributions, FPA Regulations indicate that such contributions should not be made for amounts greater than a worker's salary. The purpose of these additional contributions is to obtain greater retirement funds and to avail a worker of the benefit that the contributions are not taxable.

Telecommunications

Some of the most important features of the Chilean telecommunications market is its subsidiary control by the State, its provision of unrestricted access to service providers and intense competition.

Competition is largely the outcome of radical legislative changes over the past 20 years. These changes led to the privatization of Government-owned local and long distance telephone companies and to the break up of a Government monopoly.

The General Telecommunications Law was enacted in 1982. It established the principle of unrestricted access for individuals and companies to provide all kinds of services and to develop telecommunications infrastructure without any type of geographical or exclusivity restrictions.

This law was amended in 1994 to allow for the creation of a competitive long distance market, including enhanced interconnectivity standards and safeguards to prevent and correct the distortions caused by the abuse of dominant market positions.

At present, several local phone companies are working together with at least six long distance carriers and five cellular and PCS service providers, including some of the world's largest telecommunications conglomerates.

Market competition is so intense that Chile boasts a multi-carrier system in which telephone subscribers may choose to place their calls with any of the existing carriers without signing a contract by only dialing the carrier's 3-digit prefix.

This is the natural outcome of a telecommunications market based on free-market principles that encourage the introduction of innovative services and technologies, erode artificial barriers to entry, and prevents and simultaneously corrects anti-competitive behavior.

(i) Applicable Legislation

Chilean telecommunications legislation is made up of several legal and administrative regulations, divided into laws, decree-laws, decrees and resolutions promulgated by the Undersecretary of Telecommunications (SUBTEL), the government agency in charge of telecommunications.

Law 18,168, issued in October 1982 (General Telecommunications Law), is the most important piece of legislation governing the installation, operation and use of telecommunications services. This law also regulates telecommunications activities, which may only be exercised under SUBTEL's supervision.

This law was further complemented by the General Telecommunications Statute, which is a more thorough exposition of the issues set forth in the law.

These regulations classify telecommunications services in Chile as follows:

a) Free reception of telecommunications and radio services, defined as transmissions to be received freely and directly by the public at large, including sound, television and other broadcasts.

b) Public telecommunications services, defined in the law as services that meet the telecommunications needs of the community in general and may be contracted by any person who pays for those services.

c) Limited telecommunications services, defined as services that meet the specific telecommunications needs of certain companies, entities or individuals under an existing contract. These services may include the same kind of broadcasts as indicated in i) above, but may not give access to traffic from and to users of public telecommunications networks.

d) Amateur radio telecommunications services, defined as services the purpose of which is radio intercommunication and technical/ scientific experiments carried out on a personal and non-profit basis.

e) Intermediate telecommunications services, defined in the law as services provided by third parties through facilities and networks in order to meet the transmission or connection needs of general telecommunications licensees, or allow carriers to provide long distance telephone services to the community.

The permits or licenses required to deliver the above services, the application procedures and essential requirements to be met, as well as the conditions therefor, are also set forth in the law.

One must generally secure a license to provide public and intermediate telecommunications services.

These licenses may be transferred by the licensee with the prior approval of SUBTEL, which shall verify whether the assignee meets the licensee requirements provided by law.

In this regard, the General Telecommunications Law indicates that only those entities established and residing in Chile may act as telecommunications license operators. No minimum capital or specific corporate organization is required.

Except for the above limitation, the nationality requirement imposed on Chilean telecommunications licensees does not extend to their shareholders or partners.

In turn, the officers, managers and directors (in the case of a corporation) are not subject to any particular nationality requirements.

Infrastructure

Despite the country's spectacular growth over the past few decades that led to the overall modernization of its economic and productive activities, one area has persistently lagged behind in the process - public infrastructure. Slow infrastructure growth could ultimately impair Chile's competitiveness and efficiency, as well as jeopardize its future growth. Aware of this danger, recent administrations have invested great effort in promoting the execution of infrastructure works indispensable for the country's sustainable development.

In the past decade, investments on infrastructure works reached an average of US$570 million annually. For the 2000 - 2009 period, capital expenditure requirements for public infrastructure will average approximately US$1.8 billion each year, of which only US$800 million will be public investment. The balance will have to be funded by the private sector.

Starting in 1993 the government implemented a public works concession policy whereby several infrastructure projects have been granted as concessions to private concerns in order to build and operate them over a given period of time.

Preference has been given to projects that are both socially and economically attractive, helping investors obtain a sound return on their capital.. The Government of Chile will thus focus its efforts on infrastructure projects that, on the one hand, will be highly beneficial from a social standpoint but, on the other hand, will not warrant the involvement of the private sector.

(i) Regulatory Framework

To implement the concession system, the Government enacted the Public Works Concessions Law that regulates the types of works which may granted as concessions, eligibility requirements for the applicants and the procedures to grant these concessions. The regulatory entity in charge of this area is the Ministry of Public Works.

(ii) Procedure to Grant Public Works Concessions

The process begins with an international call for bids, after which the consortia interested in participating are placed on a short list. The consortia and the Government then discuss and exchange relevant technical and financial information. The terms for the bid are then drawn up, including the technical and financial conditions of the project. These terms are the basis on which the consortia file their respective offers, including the concession term, maximum authorized rates, existence or non-existence of minimum guaranteed revenue, payment or non-payment of consideration for the concession, etc.

At this stage, each consortium conducts its own technical and economic research and then files its offer. After all offers have been delivered, they are rated as to their compliance with the bid terms. Then the consortium that delivers the most convenient offer is awarded the concession.

Over 27 projects have been given to the private sector over the past eight years. Several are already operational and others are underway. In the aggregate, these projects account for over US$4.5 billion in capital expenditures.

(iii) Roads

Investment requirements for roads and highways over the next few years by far exceed the Government's financial resources. Chile has 90,000 kilometers of roads of which only 16,500 are paved. Concessions in this area have an immense potential for growth.

Investments for the 2000 - 2009 decade will reach US$4.8 billion, this is a 17% increase over investments in the area during the last decade. This means that Chile will have with a 25,173 kilometers of paved roads within the coming years.

Several concessions exist regarding roads. Noteworthy among these are several sections on Highway 5 between La Serena and Puerto Montt (1,600 km) as well as the Santiago - Valparaiso and Santiago - San Antonio Highways.

A group of concessions is currently being discussed for urban road works in Santiago.

(iv) Airports

Airports -a vital tool for Chile's international growth and the development of overseas trade-are a major infrastructure weakness. National and international air passenger traffic has skyrocketed almost 200% over the past 10 years and air freight has increased sixfold.

New infrastructure is urgently needed to bolster up air terminal capacity and increase throughput in the face of constant growth. Terminals must also be outfitted with the latest technology in air traffic control equipment, weather monitoring, etc. This is yet another area in which the Government has flung the door wide open to private investors. The best proof of this is that the Santiago International Airport - the country's leading air terminal - is currently under the control of private concession holders.

An estimated public investment in airports of approximately US$90 million is expected for the 2000 - 2009 decade.

(v) Ports

In a country with as extensive as coasts as Chile has, port infrastructure plays a very important role in connecting the country with the rest of the world. Ports are the main exit route for Chilean exports and also a weak flank in the infrastructure sector. As of today, Chile counts has 11 publicly-owned ports and 25 private ports. To modernize port activities, the administration is transferring management, operations, profit-making and maintenance activities in Chile's leading maritime terminals to private investors.

Investment goals in the port area for the 2000 - 2009 period are estimated to be US$250 million, which means an increase of 65% compared with the last decade.

(vi) Water Utilities

The country's potable water supply meets the needs of 90% of its population and over 99% of its urban population. Sewer systems also cover 80% of the country's demand. Although by far the best such indicators in Latin America, there is still room for improvement. Water utilities are still largely under Government control.

Over the next ten years, estimated investments in the amount of over US$2 billion will be required to meet 100% and 70% of potable water and wastewater treatment requirements, respectively.

Fishing

Notwithstanding the principle of non-discrimination embodied in the Foreign Investment Statute, foreign investors will only be entitled to invest in Chile's fishing sector to the extent that the foreign investor's country of domicile allows Chilean investors to participate in that country's fishing industry.

The fishing industry is regulated by the Fisheries and Aquaculture Law, N° 18,892 of 1989. For the purpose of preserving marine resources, the law grants to the Ministry of the Economy and Fisheries Sub-secretariate a variety of powers, including power to:

(1) prohibit the capture of certain species;

(2) fix annual quotas for species and fishing areas;

(3) fix maximum and minimum sizes for species which may be caught in determined areas; and

(4) determine the dimensions and characteristics of fishing equipment.

In order to carry on fishing activities a fishing license must be obtained for each boat to be used. The license sets out the species and fishing areas to which it extends and is valid indefinitely. Licenses are transferable with the boat to which they relate.

Aquaculture or fish farming activities also require a license and may only be carried on in areas declared appropriate for Aquaculture by the Ministry of Defense based on studies conducted by the Fisheries Sub-Secretariat. Fundacion Chile (see *Investment Incentives*) established the first fish farming operations in Chile (which have now been sold to Japanese investors) and provides research facilities, quality certification services and other resources to assist the industry.

Shipping

Generally, coastal trade is restricted to Chilean vessels. However, foreign ships may bid for cargoes exceeding 900 tons, their bids being increased by the normal customs rate.

Water Rights

Under the Water Code, national waters are state property held for public benefit and may only be used or exploited by those with rights granted pursuant to the Code or as otherwise contemplated by the Code. The Code applies to all inland water bodies but does not apply to the ocean.

Water rights are generally granted pursuant to an application procedure set out in the Code. Applications must be accompanied by a study of the proposed water use and are publicized to give interested parties the opportunity to object. Water rights granted are recorded in a register maintained by the *Direction General de Aguas*. In some cases the Water Code permits the grant of water rights by simpler means, for example, in the case of well water for drinking and domestic use. The Water Code also confers on owners of mineral and oil bearing land the right to use water sources found during exploration and exploitation for the purpose of exploitation. The Mining Code contains a similar provision allowing the holders of exploration and exploitation concessions (see *Mining*, above) to use discovered waters for the purpose of the exploration or exploitation.

Water rights granted under the Water Code are perpetual and may be transferred independently of the land where the water is located. Water rights may not be exercised in a way which pollutes the water or prejudices the rights of third parties to use the same water (whether the prejudice relates to the quantity or quality of the water available for use, access to the water or any other characteristic relating to use of the water). Water rights may allow consumption of the water in the course of the relevant activity or may require the holder to restore the water used. The latter type is normally granted for mining activities and requires the water to be restored uncontaminated to its source.

FOREIGN INVESTMENT REGULATIONS REGARDING CHILEAN SECURITIES

General

Foreign investors may invest in Chilean securities by:

(1) forming a Chilean investment vehicle for this purpose and obtaining the appropriate Foreign Investment Committee or Central Bank approvals discussed in *Foreign Investment Legislation and Regulations*. Income derived from the investment will be taxed in the manner discussed in *Tax Regime and Income Taxes*; or

(2) Acquiring securities directly as permitted by Public Law 18,657 and discussed in the following Section. This procedure is available to foreign investment funds and attracts a favorable tax regime.

Foreign Investment Funds - Public Law 18,657

Chilean Law 18,657 of 1987 allows certain investment funds organized outside Chile as a foreign fund or as a foreign investment fund hedged to invest directly in Chilean securities, capital markets and over the counter securities with the benefit of a less demanding tax regime. A minimum of US$1million must be invested and the shares or other securities issued by the fund must be nonredeemable.

The investment fund will be exclusively taxed at a rate of 10% on all remitted amounts corresponding neither to the capital originally invested nor to capital gains obtained by the fund under Article 18bis of Chilean Income Tax Law. This exclusive rate will be maintained throughout the period of the fund's investment in Chile.

There are no restrictions on the remittance of profits derived from dividend and interest income or realized capital gains. Capital may be repatriated after five years.

The investment must be made under either the Foreign Investment Statute or Chapter XVIII of the Foreign Exchange Regulations.

The foreign investment fund's Chilean investments must be managed by a special purpose Chilean corporation (which may be wholly foreign owned) unless the fund is a foreign institutional investor. The Chilean Management Company must have a minimum paid-in capital of US$125,000 and be authorized by the Chilean Securities and Insurance Commission. The Management Company and fund will be subject to supervision by the Commission.

Foreign investment funds investing under Law 18,657 are subject to certain investment limitations and diversification requirements. For example, the fund may not hold more than 25% of the shares of a Chilean corporation. Permitted investments include publicly traded shares, securities issued or backed by the government, Central Bank or a bank or financial institution, bonds and negotiable instruments registered in the Securities Register of the Commission and other securities authorized by the Commission.

MERGERS AND ACQUISITIONS

Chilean stock markets and securities regulation is in the process of developing from a family-oriented system of ownership regulation to a more democratic, professional and transparent system.

Mergers and acquisitions involving corporations whose stock is publicly traded must comply with various requirements in the Securities Exchange Law 18,045 designed to protect minority interests and creditors including:

(1) publication, and notification to the Superintendency of Securities and Insurance and to the stock exchange market, of the intention to obtain control of a public corporation. The notice of intention must include the price and other terms of the transaction;

(2) need to make, voluntarily or when ordered by law, a Public Offer to acquire control shares of a corporation whose stock is publicly traded; and

(3) notification to the Securities and Insurance Commission and to the stock exchange market when a share holding (direct or indirect) in a public corporation reaches 10% and notification of subsequent changes within two days of such change.

In the case of non-compliance with these requirements and other circumstances, Law 18,045 permits the Securities and Insurance Commission to suspend the trading of shares in open corporations for up to 120 days and thereafter to revoke the corporation's registration.

Disclosure of dealings in shares or other rights in closed corporations or limited liability companies/partnerships is not required by law, although corporate bylaws and partnership deeds may require that certain procedures be followed. As discussed in *Structure of Investments / Investment Vehicles*, the sale of a partnership interest requires the consent of all partners.

Mergers or consolidations of corporations must be approved by the shareholders of the participating corporations. Dissenting shareholders may require "the corporation in which they hold shares" corporation to buy their shares at market value in the case of open/listed corporations and at book value in the case of private corporations. Mergers proceed by canceling the shares of the "absorbed" corporation, transferring the absorbed company's assets to the "absorbing" corporation and issuing shares in the absorbing corporation to the shareholders in the absorbed corporation. Normally tax benefits such as accrued losses cannot be transferred from the absorbed corporation to the absorbing corporation. In a consolidation, which is less common, a new corporation is formed which issues shares to shareholders in the merged corporations. In both a merger and consolidation the merged or new entity assumes the liabilities of the non-surviving corporation or corporations.

Chilean case law on issues concerning mergers and acquisitions is very limited. Hostile takeovers and leveraged buyouts are infrequent because of low profile Chilean business practices and insufficiently developed legislation.

Chilean trade practices/anti-trust legislation may be relevant to a proposed acquisition or merger (see the following Section).

TRADE PRACTICES AND ANTI-COMPETITIVE CONDUCT

Trade practices and antitrust issues are regulated principally by Decree Law 211 of 1973. The law applies to all categories of people and entities, local or foreign, and although normally applying to acts within Chile, it extends to activities abroad which have anti-competitive effects in Chile.

The law is intended to cover all anti-competitive conduct. Articles 1 and 2 prohibit any act, agreement, decision or arrangement tending or designed to restrict free competition. When applying these provisions, the courts have examined such factors as the tendency and purpose of the acts, independent of the actual intention of the parties involved or the actual effect of the acts.

Cartels, trusts and horizontal or vertical integration arrangements are given as examples of potentially anti-competitive conduct in the law. In relation to distribution arrangements, the courts have distinguished distribution by agents from that by independent traders. Restrictions such as the fixing of terms of sale and limits on the territory in which products may be sold have been considered legal in connection with agency distribution but illegal for distribution arrangements with an independent trader. However, recent rulings of the antitrust authorities have stated that such acts, whether performed by an agent or an independent trader, do not violate antitrust laws and therefore are not deemed contrary to free market practices, provided the relevant market is an open one, and the acts in question do not cause a real restriction on free competition.

Articles 6 and 8 of Decree Law 211 deal with the abuse of market power, prohibiting conduct such as selective discrimination and tied contracts.

Anti-competitive conduct (including monopolies or oligopolies) may be authorized where such arrangements are in the national interest and are necessary for the stability or development of national investment. Investors concerned that certain conduct might be considered anti-competitive may apply for a ruling relieving them of responsibility under Decree Law 211 in relation to the conduct.

Sanctions for anti-competitive conduct include fines, modification or termination of applicable agreements and arrangements and dissolution of relevant corporations and other entities. Criminal penalties may also apply although the above comments relate to civil breaches of the law only. Different considerations and procedures apply to criminal breaches.

ENVIRONMENTAL PROTECTION

The Chilean Political Constitution

Environmental protection became a public priority in Chile in 1980, when the Chilean Political Constitution recognized, for the first time, the importance of protecting the environment and preserving nature. The Constitution guarantees every person "the right to live in an environment free of pollution". It also sets forth that the Government has a duty to protect said right and to seek the preservation of nature.

As may be understood, a constitutionally guaranteed right to live in an environment free of pollution creates potential conflicts with other basic constitutional rights such as "the right to perform any economic activity" or "the property right". The Constitution takes note of this conflict and stipulates that curtailing basic constitutional guarantees for the sake of environmental protection can only be made effective by law, thereby excluding any administrative regulation. Finally, the Constitution provides that environmental protection laws cannot affect the "essence" of other basic constitutional rights.

The Environmental Act

The Environmental Act sets forth the general criteria upon which the coun environmental policy should rest. This law is effective throughout the entire national territory and regulates all activities and projects that may cause a significant environmental impact. The Act recognizes the force and effect of all previous environmental regulations, except those regulations it tacitly amends or abrogates as contrary to the Act.

The Environmental Impact Assessment System

The most meaningful contribution made by this Act is the creation of the "Environmental Impact Assessment System", which establishes the procedure to determine whether the environmental impact of a given activity or project is consistent with legislation effective from time to time. This procedure is implemented by the CONAMA when it involves more than one region of the country, or by the respective COREMAS when it involves a single region.

An "Environmental Impact Assessment" ("EIA") is defined as "the document which conveys an itemized description of the features of a project or activity intended for execution or the modifications to be introduced with respect hereto". Said assessment must provide well-founded background data for predicting, identifying and interpreting the environmental impact and also describe the action(s) which shall be performed to prevent or minimize its materially adverse effects. In turn, an "Environmental Impact Statement" ("EIS") is "the document which describes an activity or project intended for execution or the modifications to be introduced with respect hereto issued under oath by the respective titleholder, and whose contents enable the competent authority to assess whether the environmental impact of such activity is consistent with the environmental legislation effective from time to time".

An EIA is applicable when a project generates some of the effects contemplated by the Act, including health hazards for the population or material adverse effects on the quantity and quality of renewable natural resources, including soil, water and air. Projects which are included in the Environmental Impact Assessment System and do not require preparation of an EIA since they do not generate any effect described in the Act should file an EIS. Unlike the EIA, and EIS is a simple description of the contemplated activity.

Community Participation

The Act clearly intends to encourage citizen's involvement within the environmental decision making process. Lawmakers provide for community involvement in three different instances:

a) in the making of environmental standards, plans and regulations;

b) in the Environmental Impact Assessment System, under which community organizations and directly affected individuals will be able to make comments to the EIA of the EIS, which the authority must evaluate before approving or rejecting such documents; and

c) in the possibility to bring charges based on alleged environmental violations.

Environmental Liability for Violators

Despite the fact that the Environmental Act creates the so-called "Environmental Damage Liability", it introduces no new material innovation with regard to the general rules on tort liability set forth in the Chilean Civil Code, according to which the basic components of said liability are negligence and malice.

Notwithstanding the foregoing, this Act is unique in that it legally presupposes liability of the person who causes the damage in case environmental protection laws are violated. Therefore, the burden of proof as to negligence or malice rests on the violator, who must successfully claim the existence of Acts of God or Force Majeure in order to disprove said negligence or malice.

The Act also provides that if the party who causes the damage can prove full compliance with environmental standards, such party shall not be forced to repair the damaged environment. This is without prejudice to said party's liability to indemnify the affected party.

The Act stipulates that other bodies of law which set forth special rules on liability regarding environmental damage, shall take precedence over it the act itself. This calls for thorough analysis on a case-by-case basis regarding the potential existence of special rules on liability which could exclude those provided under the Act. The Act adds that, in matters not covered by either the Act itself or special laws, the general provisions related to tort liability in the Chilean Civil Code shall apply.

The Act states that both the environmental liability, which forces the violator to repair the damaged environment and the civil liability, which stipulates monetary indemnification for the affected party have a 5-year statute of limitation as from the date when the damage becomes evident. This statute of limitation rule makes it very difficult for the violator to avoid, based on time considerations, its eventual environmental liability.

Finally, criminal liability for environmental damage exists only in very specific cases where the violator's willful misconduct causes a major environmental damage.

INTELLECTUAL PROPERTY

General

Intellectual Property rights are regulated principally by Industrial Property Law 19,039 of 1991, dealing with trademarks, invention patents, utility models and industrial designs; and Intellectual Property Law 17,336, dealing with copyright protection. In addition, there are other laws dealing with the registration of plant varieties and animal breeds.

Chile is also member of the following international conventions concerning Intellectual Property rights:

(1) Paris Convention for the Protection of the Industrial Property.

(2) Interamerican Convention on Copyright of Literary, Scientific and Artistic Works.

(3) Universal Convention on Copyright.

(4) International Convention on the Protection of Interpreter or Performing Artists.

(5) Records Producers and Broadcasting Entities.

(6) Convention on World Intellectual Property Organization.

(7) Convention of Bern for the Protection of Literary and Artistic Works.

(8) Convention for the Protection to Records Producers against Non-Authorized Reproduction of their Records.

Commercial Trademarks

Commercial Trademarks, which can be registered in Chile pursuant Law 19,039, include every visible, novel and distinctive sign which can be used to distinguish products, services or industrial or commercial establishments. Likewise, it is possible to register advertising or publicity text, provided such text is related to a previously registered trademark and includes such trademark.

Article 20 of the Industrial Property Law sets out types of trademarks which are not registrable, including expressions used to indicate the nature, origin, nationality or quality of the applicable products, services or establishments. Trademarks

containing common, generic or descriptive words may be registered, but registration does not confer any rights in respect of such words or terms in isolation.

In 1971 Chile adopted the International Classification of Goods and Services (Nice Classification).

Law 19,039 protects both product and service trademarks. In addition, it contemplates two local special classes: the commercial establishment for the sale of products and the industrial establishment for product manufacturing. Trademark registration confers protection throughout Chile, except for those trademarks distinguishing Commercial Establishments where protection is conferred only in the regions for which the mark is registered. According to Law 19,039, previous use of a trademark is not required in order to obtain its registration. Trademark ownership and the right to use such trademark is only acquired through registration or the mark. Moreover, use of a registered trademark is not required to keep it in force, and it is not possible to cancel a trademark based on non-use. Similarly, it is not necessary to prove use of a trademark in the market in order to renew such trademark.

Registration formalities include an examination prior to the acceptance to publication by the Trademark Registrar, a 30-day waiting period to allow third parties to file an opposition, and a final examination by the Head of the Trademark Department, who finally decides if the trademark can or cannot be registered.

The registration term is ten years from the granting date which can be indefinitely renewed for successive ten-year periods.

Famous and well-known trademarks receive special protection by law, due to the fact that the owner of such trademark is entitled to oppose the registration application filed by someone who is not the real owner. In the case that the trademark has been registered, the owner can, for a five-year period after registration, petition for its cancellation. In both cases, it is necessary to prove the trademark's fame and reputation.

Trademark infringement is penalized with a fine and law 19,039 grants the trial judge the authority to order the seizure of tools and elements used in the falsification or imitation of an item as well as the objects containing the counterfeited trademark.

Registered trademarks are transferable like other industrial property rights by public deed. Transfers must be recorded with the Trademark Register. Trademark applications are also transferable, by a private deed in which the signatures have been authorized by a Notary Public.

Invention Patents

Law 19,039 defines the term "invention" as every solution to a technical problem created by an industrial task. An invention can be a product or a process or can be related thereto. Invention patents are granted for a non-renewable period of 15 years.

Inventions are patentable when they are new, have an inventive level and are susceptible to industrial application. An invention is considered to be new when it does not previously exist in the "state of the art". The state of the art includes everything that has been disclosed or made accessible to the public, anywhere in the world, through a publication or in a tangible manner, the selling or commercialization, the use or any other means, prior to the filing date of the patent application in Chile. The state of the art also includes the contents of a patent application before the Intellectual Property Department whose filing date is prior to that of the application being examined. An invention is considered to have inventive level if, for a person normally knowledgeable in the corresponding technical matter, this is not obvious nor has it been evidently derived from the state of the art. An invention is considered to be susceptible to industrial application when its object can, in principle, be a product of or can be used in any kind of industry. Pharmaceutical products are included.

With respect to a patent that has been previously applied from abroad, the filing party shall have a priority for a one-year term, commencing from the date of filing in the country of origin in order to file the same patent application in Chile.

Patents requested in Chile for inventions already patented or whose applications are being processed abroad, shall only be granted for the period of time resting for the patent application or the granted patent to expire in the country of origin, without exceeding the above-mentioned term. Modifications of existing inventions are patentable if novel and obviously advantageous to the original invention.

The following items cannot be patented:

(1) discoveries, scientific theories and mathematical methods;

(2) plant varieties and animal breeds (there are other protections available for them);

(3) economic, financial or commercial systems, methods, principles and plans which may be verified and understood simply and those which are purely intellectual (i.e. without practical application);

(4) methods of surgical or therapeutic treatment of people or animals and diagnostic methods applicable to people or animals but excluding products required to put such methods into practice; and

(5) new uses or modifications of a known item without changing the essential qualities of the item or resolving a technical difficulty associated with the item.

Under Law 19,039, Industrial Property rights derived from the work of hired persons who are devoted to a creative or inventive task, susceptible to be protected by some of the instruments contemplated by Law, belong to the employer or the person who entrusted the service.

All background information of the pending patent shall be kept in the Industrial Property Department at the disposal of the public, after its publication to allow for opposition by third parties. Patents are not subject to annual fees.

Law 19,039 provides for fines as the penalty for patent infringements. A judge may order the seizure of tools and elements used in the infringement task and also, the objects illegally manufactured shall be confiscated for the benefit of the patent owner.

Utility Models

The law defines utility models as those instruments, appliances, tools, devices and objects or parts thereof in which shape can be claimed, either in its external appearance or in its functioning, and provided that it produces a benefit, advantage or technical effect that formerly it did not have. The same regulations regarding invention patents are applicable, to utility model patents.

Like patents, utility models may be patented when new and susceptible to industrial application, and patents are granted for a non-renewable period of 10 years, from the date of application.

Industrial Designs

Industrial design includes any three-dimensional shape, related or not to colors, and any industrial or handcraft article serving as a pattern for the manufacture of other units thereof, which can be differentiated from those similar to it, in shape, geometric configuration, ornamentation or a combination thereof, provided that those characteristics give it a special appearance perceptible by sight, thus resulting in a new, original and different physiognomy. The privilege of using an industrial design is granted for a non-renewable period of 10 years from the date of application.

Industrial Secrets

Industrial secrets are protected by Article 284 of the Penal Code, which imposes imprisonment or a fine on those fraudulently communicating manufacturing secrets of the company where the person is or was hired.

Copyright

Law 17,336 protects rights acquired by the mere creation of the work of art, by authors of works in the literary, artistic or scientific fields, whatever the form of expression, and also related rights which are specified by it.

As an example, the law mentions art works that are expressly protected, such as: books, articles, encyclopedias, dictionaries, conferences and speeches, dramatic works, musical compositions, television and radio adaptation of literary works, newspapers and magazines, photographs and engravings, cinematographic works, architectural projects, paintings and drawings, sculptures, videos and computer programs or software. Copyright includes patrimony and moral rights, protecting the exploitation, paternity and integrity of the artwork.

The protection granted by law lasts all of the author's life, his/her spouse's and his/her single or widowed daughters' or married daughters' lives if their husbands have definitive work incapability. Such protection extends for 30 years after the author's death with respect to the author's heirs, beneficiaries and assignees and shall last 50 years in case of perpetuation of the memory of a famous author and if so expressed in a presidential decree.

The laws protect the rights of Chileans and foreigners resident in Chile. Copyrights of foreigners not resident in the country shall enjoy the protection granted by international conventions to which Chile is a party. The Chilean Copyright Law states that infringements of it are punishable with fines and imprisonment.

Plant and Animal Variety Rights

Decree Law 1,764 of 1977, which regulates the production of seeds, was created the Registry of Ownership of Plant Varieties to protect the creators of new plant varieties. The period of registration and protection is limited and determined by a technical committee of the Servicio Agricola y Granadero (the Agriculture and Cattle Service).

Other registries exist for the protection of rights associated with certain species and breeds of animals such as thoroughbred horses and beef and dairy cattle.

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