

Chile

International Estate Planning Guide

IBA Private Client Tax Committee

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I. Introduction: restrictions on the freedom to dispose assets in Chile for estate planning purposes

Chilean inheritance law is governed by a civil law framework that imposes significant limitations on testamentary freedom to dispose of assets by individuals upon death and to carry out the giving of gifts during lifetime. Unlike common law jurisdictions, where testators enjoy broad discretion to carry out such activities, Chilean law reserves substantial portions of the deceased's estate for so-called 'forced heirs' (*legitimarios*). Forced heirs are those heirs whose hereditary rights must be legally respected by the testator and, typically, consist of the descendants, the surviving spouse (or civil partner) and the ascendants of the deceased.

The Chilean Civil Code establishes express forced heirship laws, with freedom given to the testator to assign only 25 per cent of their estate. Under the forced heirship order, the descendant's estate shall be distributed as follows:

- 50 per cent is attributed to forced heirs (as determined by the rules below);
- 25 per cent may be assigned by the deceased to privilege some of their forced heirs and other familiars; and
- only 25 per cent of the estate may be freely assigned.

In such a context, forced heirship is determined according to the relevant succession order as follows:

- First order: descendants and the surviving spouse (or civil partner). If the deceased person has descendants and a surviving spouse, the distribution must be as follows:
 - one descendant and a spouse by halves; and
 - where there are two or more descendants and a spouse, the spouse receives double that of each descendant and never less than 25 per cent of half of the estate.
- Second order: if the deceased has no descendants, the surviving spouse will receive two-thirds of the estate, while the surviving ascendants receive the remaining third.
- Third order: siblings. In cases where the siblings are deceased, the rightful heirs are the siblings' children (ie, the nieces and nephews of the deceased).
- Fourth order: collaterals, up to the sixth grade (ie, uncles and aunts, and if they are deceased, then the cousins).
- Fifth order: the Chilean state.

The law seeks to enforce this order during the life of the person: for instance, judicial authorisation is required in order for the person to give a gift in order to control their compliance with the forced heirship regime. Since the forced heirship regime is a public order regime, any provisions or structures used by the parties that conflict with the portions established by law will be null and void.

In addition, the Chilean Civil Code provides a mechanism for reconstituting the estate of the deceased in cases where, during their lifetime, the decedent made gifts to relatives or third parties that exceed the forced heirship rules. This is designed to prevent any violations of the forced heirship rules and to ensure equitable treatment among the heirs.

II. Succession and asset transfer upon death

Upon the death of an individual, the deceased's estate passes automatically and by operation of the law to the heirs, who acquire ownership of the assets and assume the obligations of the decedent. For such purposes, certain legal procedures must be followed to distribute the assets, which are analysed further below.

In accordance with Chilean law, upon the death of an individual, the law of the decedent's domicile will apply and will control the dispositions of their personal property, real estate property, the formalities of their will and the inheritance rules in general.

A. Importance of wills for estate planning purposes

In such a context, one of the most well-known and common instruments for a person to dispose of their assets upon their death is by the granting of a will. Under Chilean civil law, a will is a unilateral, solemn and revocable act, according to which a person (the 'testator') disposes of all or part of their assets upon their death.

A will allows the testator to establish the distribution of their estate (they may freely dispose of 25 per cent of their estate, as explained above), appoint heirs or legatees, recognise children or include personal declarations, provided such dispositions do not infringe on forced heirship rules established by law and referred to above. Such forced heirship rules apply to half of the testator's estate.

1. FORMALITIES AND TYPES OF WILLS

A will must comply with a series of formalities to produce legal effects in Chile. In fact, Chilean law establishes two types of wills: solemn wills and less solemn wills (or privileged wills). Additionally, the legislation also regulates the legal effects of foreign wills.

Solemn wills

In general, solemn wills must meet three requirements: (1) they must be in writing; (2) they must be executed in the presence of the required number of witnesses established by law; and (3) they must comply with all other legal formalities, which will depend on the type of will to be granted. Solemn wills are the most common type of wills granted in Chile.

There are two types of solemn wills, as follows:

- **Open will:** In regard to this type of will, the testator openly communicates the content of their will to the witnesses. This type of will may be executed either before a public notary and three witnesses or, alternatively, before five witnesses without a notary. The notary may be substituted in certain exceptional cases by a civil court judge or by a civil registry officer.
- **Closed will:** In regard to this type of will, the testator does not communicate nor reveal the content of their will to anyone; it is kept secret. This type of will must be executed before a public notary and three witnesses, and the notary may only be substituted by a judge. For such purposes, the testator provides the public notary with a sealed envelope and declares that such documents correspond to their will, with such a process being carried out before the three witnesses and the public notary.

Less solemn wills or privileged wills

Under Chilean law, privileged wills (less solemn wills) are exceptional forms of wills that may be executed pursuant to more relaxed formalities due to extraordinary circumstances. They are recognised in the Chilean Civil Code as valid alternatives to solemn wills when the testator is unable to comply with the usual formal requirements, particularly during emergencies or in regard to specific professional or geographical situations. There are three types of privileged wills, as follows:

- Verbal will: this form of will is only permitted in cases of imminent danger to the life of the testator, where it appears that there is no means or sufficient time to execute a solemn will.
- Military will and maritime will: granted during periods of war.

2. WILLS GRANTED IN A FOREIGN JURISDICTION

Under Chilean law, a Chilean citizen or a foreigner domiciled in Chile may grant a will in a foreign country with valid effects in Chile if they comply with certain formalities. The law distinguishes between two different scenarios regarding foreign wills, as outlined below.

Wills granted in a foreign jurisdiction in compliance with foreign law

Chilean law admits foreign wills to the extent they are in writing and comply with the formalities of foreign law. For such purposes, to execute a foreign will in Chile, it must be proven that the will fulfils the formalities required in the foreign country. Additionally, the authenticity of the will must also be accredited.

Wills granted in a foreign jurisdiction in conformity with Chilean law

This type of will benefits Chileans and foreigners residing in Chile and corresponds to solemn wills granted before Chilean diplomatic authorities. These types of wills must be granted before certain specific authorities, such as ambassadors, legation secretaries (of the embassy) who hold an official title granted by the Chilean president and consuls who have been assigned as part of the consular commission. These wills may be open or closed, as detailed above, and must fulfil certain specific rules before the said authorities.

B. Intestate successions (successions without a will)

In the absence of a valid will, the succession of a deceased person in Chile is governed by the rules of intestate succession. In such cases, the estate is distributed among the legal heirs according to a strict order of priority, as described above for the forced heirship rules. Therefore, depending on the presence of the heirs in accordance with the forced heirship order, descendants and surviving spouses (and civil partners) inherit over ascendants. Within each succession order, close relatives exclude remote ones.

In this regard, Chilean law regulates a compulsory form of distribution of assets in the absence of testamentary instructions, which evidences the lack of flexibility in the country in regard to estate planning purposes.

C. Procedures to assume ownership of assets by heirs under Chilean law

Upon the death of an individual, the heirs must undertake a formal legal process known as '*posesión efectiva*', through which they are officially recognised and authorised to assume the ownership of the deceased's estate. The applicable procedure varies depending on whether the succession is intestate (without a will) or testate (with a valid will), as follows:

- Intestate succession: where no valid will exists, the heirs must initiate an administrative process before the Civil Registry Office (Servicio de Registro Civil e Identificación). This involves submitting a formal request for recognition as legal heirs, supported by documents that fully identify the heirs and detail the assets of the estate. Once the Civil Registry verifies the information and confirms the legal entitlement of the heirs, it issues a Certificate of *Posesión Efectiva* (*Certificado de Posesión Efectiva*), which serves as legal proof of heirship. Before the heirs can dispose of or transfer inherited assets, applicable inheritance taxes must be paid, as detailed in subsequent sections.
- Testate succession: in cases where the deceased left a valid will, the heirs must initiate a judicial process before the civil court, corresponding to the last domicile of the testator. The court petition must include the original will, the death certificate and documents identifying the heirs and listing the estate's assets. The court will review the will's validity and confirm whether it is in compliance with Chilean legal formalities and forced heirship rules. Upon the granting of its approval, the court issues a judgment of *posesión efectiva*, which authorises the registration and transfer of inherited assets, such as real estate, vehicles and financial instruments, to the named heirs. As with intestate successions, inheritance taxes must be paid prior to the disposal of any inherited property.

D. Inheritance tax applicable to successions

1. CHARACTERISTICS OF INHERITANCE TAX

Chile imposes an inheritance, legacy and gift tax (CIT) under Law No. 16,271 (the 'CIT Law'), which is applicable to the transfer of assets upon death, as well as *inter vivos* gifts. It is levied on the beneficiary, not the estate. The tax is levied on the net value of the assets received, after deducting debts, funeral expenses and other expenses and concepts. It is a progressive tax, with rates ranging from one per cent to 25 per cent, depending on both the value of the inheritance and the degree of kinship between the deceased and the heir. Closer relatives, such as spouses, children and parents, benefit from lower tax rates and a higher amount of exemptions, while more distant relatives or unrelated beneficiaries face higher rates and fewer deductions.

Surcharges and deductions are applicable depending on the degree of familiar relatedness between the decedent and the heir. According to CIT Law, if the beneficiary is the husband/wife, parent or adoptive parent, child, adoptee or grandchild of the deceased, there is no applicable surcharge. Where the beneficiary is the brother/sister, half-brother or sister, nephew, uncle/aunt, grandnephew/niece, cousin or grand uncle/aunt (second-, third- and fourth-degree relatives), the surcharge is 20 per cent. If the beneficiary has a more distant or no familiar relatedness to the deceased, there is a 40 per cent surcharge.

The CIT shall be declared and paid simultaneously by the heirs within two years from the date of the death of the deceased. Payment of the tax is a prerequisite for the registration and legal disposal of inherited assets, such as real estate or shares. Such taxation must be calculated based on the individual portion (*asignación*) of the inheritance corresponding to

each heir. Additionally, the CIT Law provides certain rules in order to value the assets subject to the CIT depending on the type of asset (real estate property, stocks and rights, among others). Moreover, if the CIT Law does not provide a specific rule to value a certain asset, then it shall be valued at its fair market value. Additionally, the CIT Law provides for certain deductions where the respective portion of the inheritance is subject to encumbrances/liens.

Taxes paid abroad in connection with the assets to be taken into consideration for inheritance tax purposes are creditable against the CIT payable in Chile. Nevertheless, a credit for tax paid abroad is limited by the CIT Law, given that the CIT paid in Chile cannot be lower than the tax that would correspond if assets only located in Chile were included on the inventory.

2. SPECIAL ANTI-AVOIDANCE RULES REGARDING CIT

The CIT Law grants the Chilean Internal Revenue Service (SII) with the authority to scrutinise certain legal transactions or contracts and recharacterise them for tax purposes. Specifically, the SII may challenge agreements or transactions that, in substance, constitute a gratuitous transfer of wealth, even if formally structured otherwise.

Where such arrangements are found to lack a legitimate commercial rationale or are deemed to be primarily aimed at circumventing inheritance or donations tax, the SII may treat them as deemed donations. This recharacterisation results in the application of the corresponding tax obligations under the CIT Law, including potential penalties and interest.

3. DISCUSSION REGARDING CIT CONNECTING FACTORS

The CIT Law states that, for the purposes of applying the CIT, as a general rule, assets located abroad must be included in the inventory for determining the corresponding CIT. In the case of successions of foreigners, the assets located abroad must be considered only to the extent that they were acquired with Chilean source funds.

However, the applicable connecting factors under the CIT Law has been a matter of discussion. On the one hand, it is clear that for a Chilean decedent residing in Chile and having their last domicile in the country, with Chilean *situs* assets and foreign properties, the said succession would be subject to CIT in Chile. However, the SII has not held a consistent position in terms of the applicable connecting factors in order to levy CIT on an individual's estate.

In fact, the SII, in certain case law, has interpreted and applied much broader connecting factors, for example, taking into account the taxpayer's nationality. In the next section, we will describe certain recent interpretations by the SII in relation to the said connecting factors.

III. Asset transfers by means of gifts

Chilean civil law regulates asset transfers through gifts (donations) by establishing a formal process for such purposes. A gift is executed by a contract in which the donor voluntarily transfers the ownership of an asset to the donee without receiving consideration in return.

Gifts (donations) must comply with a well-regulated process that requires compliance with formal legal requirements. The granting of gifts must also respect forced heirship rights. In fact, as a general rule, donations must obtain judicial authorisation known as *insinuación*.

This involves the donor submitting a request to the civil court, which reviews the donation to ensure it does not infringe on the rights of forced heirs, and that the donor is legally and financially capable of making the donation. If the court approves the donation, it issues a resolution authorising the gift, after which the donation contract can be legally perfected. Without this authorisation, the donation is null and void.

Additionally, gifts and donations are subject to CIT. The donee is responsible for paying the tax. The tax rates and other characteristics of the applicable tax on donations and gifts are equivalent to the CIT described above, since gift tax is governed by the same provisions in the CIT Law. In such a context, in regard to the judicial process for obtaining the authorisation of a gift, the said process requires filing a tax return for the gift tax before the SII.

The connecting factors for determining the applicability of Chile's gift tax have been subject to debate. According to the SII's interpretation, the tax applies when either (1) the donor resides or is domiciled in Chile, or (2) the donated assets are located in Chile. On the other hand, gift tax is not applicable, in accordance with recent SII interpretations, when:

- the donation is executed abroad;
- the donor resides and is domiciled in a foreign jurisdiction;
- the donee resides and is domiciled in Chile; and
- the donated assets are located abroad and were not acquired with Chilean source income, to the extent that the foreign gift may qualify as a donation for Chilean purposes.

IV. Transfers of assets involving trusts and private foundations

A. Trusts

Trusts are not regulated under Chilean law. The most similar structure is the *fideicomiso* recognised under the Civil Code, which is considered a property limitation (property is left to a person subject to a particular condition in order to transfer the assets to a third person when certain conditions are met).

Despite the non-existence of special rules for trusts, offshore trust arrangements governed by foreign laws should be recognised in Chile to the extent that they are valid under such laws. For example, some tax regulations have recognised that foreign trusts can be deemed as controlled entities for the purpose of controlled foreign corporation (CFC) rules. Chilean tax law also includes a definition on trusts.

Given the lack of regulation, the tax effects that should derive from foreign trusts is unclear. The tax effects derived from these entities have not been clarified by domestic law or the Chilean tax authority. In fact, there are many topics on this matter that are subject to debate, including:

- the tax treatment applicable in Chile in regard to the contribution of assets to trusts;
- the effects of distributions made by a trust to beneficiaries in Chile; and
- the tax treatment in Chile applicable to the income derived from assets held by a trust.

According to Chilean tax law and the instructions set forth by the SII, trusts must subject annual reports to the tax authorities by means of a special affidavit. Additionally, due to CFC rules, trusts may be seen as separate entities and, thus, qualify as controlled foreign entities, which must be reported to the SII. Passive income perceived or accrued by those entities should also be reported and taxed in Chile by Chilean-domiciled controllers.

If a Chilean resident serves as a settlor, beneficiary or trustee of a foreign trust, Chilean law places an obligation on them to annually submit information regarding the trust, its settlor, trustees and beneficiaries.

With regards to succession and forced heirship rules in Chile, it is not clear if the assets of a trust should be included in the inventory of a deceased settlor. In most cases, if the trust is irrevocable, the assets held in a trust are not considered part of the deceased's estate. Eventually, it could be argued that in regard to the establishment of a trust, the settlor is giving a gift in favour of the beneficiaries. If that is the case, the settlor should have obtained judicial authorisation to transfer the assets, and gift tax would apply.

B. Private foundations

Private foundations that are incorporated in foreign jurisdictions are not regulated under Chilean law. However, Chilean legislation regulates certain special non-profit foundations, which must comply with a series of strict requirements, and which are subject to certain tax benefits (only applicable to this type of entity). Particularly, Chilean non-profit foundations correspond to entities with legal personality that may own assets; additionally, said foundations must be strictly non-profit and cannot pursue profit-making purposes. Moreover, such non-profit foundations may not benefit nor allow profit distributions to its founders.

Under Chilean law, private foundations incorporated under foreign law are recognised as valid entities in Chile. However, there are no rules governing these types of vehicles, except for some administrative interpretations that apply with similar effects to the ones discussed in regard to trusts.