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Corporate Tax

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CONTENTS

Brazil

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Overview of corporate tax work

Overview: For tax purposes, a company is deemed to be resident in Brazil if incorporated under Brazilian law. Resident companies are subject to Brazilian Corporate Income Tax ("*Imposto sobre a Renda de Pessoas Jurídicas*" – "IRPJ") and Social Contribution Tax on Profits ("*Contribuição Social sobre o Lucro*" – "CSL"), jointly referred to as Brazilian Corporate Taxes, which are levied based on an assessment of their income generated in operational and non-operational (active and passive) activities performed either in Brazil or abroad (worldwide income).

The amount of foreign income tax paid can be used to offset Brazilian Corporate Taxes through a tax credit imputation system, which is limited to the joint IRPJ/CSL rate levied on foreign profits recognised in Brazil.

The Brazilian subsidiary of a foreign company pays Brazilian Corporate Taxes based on its actual profit method (*"lucro real"*). However, a company may opt for a presumed profit method (*"lucro presumido"*) if its total gross revenue was equal to or below BRL 48m in the preceding calendar year, among other requirements. This option is generally determined by how profitable a company is and its plans for future investments, among other factors.

The following entities are mandatorily subject to the actual profit method: (i) financial institutions such as banks, leasing companies and insurance companies; (ii) factoring; (iii) Brazilian entities having subsidiaries or branches abroad; and (iv) entities enjoying IRPJ exemptions or benefits.

The standard IRPJ tax rate is 15% plus an additional surtax of 10% on taxable profits exceeding BRL 240,000 annually, while CSL is generally levied at 9%, resulting in a combined Brazilian Corporate Taxes general rate of 34%.

For companies involved in financial activities, CSL is levied at a higher rate of 15%. The Brazilian Corporate Taxes rate for these entities reaches 40%.

Actual profit method (*"lucro real"*): under this method, the tax for Brazilian Corporate Taxes corresponds to the accounting profit ("*lucro contábil*"), adjusted by inclusions and exclusions determined by law. The company can choose for taxation based on quarterly or annual balance sheets.

In general, operating expenses are deductible for corporate tax purposes, provided that the company demonstrates that these transactions are necessary, normal and usual for its activities. Tax losses may be carried forward indefinitely, but not carried back or adjusted for inflation. Tax losses carried forward may be used to offset up to 30% of a company's taxable income in a given tax period (which means that no less than 70% of the income tax basis must be taxable in the relevant period).

Presumed profit method (*"lucro presumido"*): a company opting for the presumed profit method calculates Brazilian Corporate Taxes based on a tax basis made up of a set percentage of gross sales and service receipts. Such percentage varies depending on the type of business the company is engaged in. Non-operational revenues – such as capital gains or other financial revenues – are not included in the presumed taxable income and consequently are fully taxed according to criteria set out in the actual profit system. The presumed profit is calculated quarterly, on March 31st, June 30th, September 30th and December 31st of each taxable year. If various activities are carried out (services and goods), the presumed profit percentages should be split: (i) 32% would be the presumed profit margin applicable to gross revenues deriving from services; and (ii) 8% for IRPJ and 12% for CSL applicable to gross revenues derived from sale of goods. The result would then be subject to a maximum 34% Brazilian Corporate Taxes rate. Once the maximum 34% rate is applied, the total tax burden on gross revenue is 3.08% for goods and 10.88% for services. The presumed profit tax method does not permit tax losses to be carried forward in order to be offset by a company's taxable income, neither the offset of foreign tax credits against Brazilian Corporate Taxes.

Double taxation treaties ("DTT") network: although Brazil is not an OECD member, its DTTs follow the OECD model. However, Brazil has not adopted the interpretation commonly applied under OECD guidelines for some articles of the OECD model DTT. The Brazilian DTT network currently comprises Argentina, Austria, Canada, Chile, China, the Czech Republic, Belgium, Denmark, Ecuador, Finland, France, the Netherlands, Hungary, India, Italy, Israel, Japan, Korea, Luxembourg, Mexico, Norway, Peru, the Philippines, Portugal, Slovakia, South Africa, Spain, Sweden and Ukraine.

Tax-favourable jurisdictions and privileged tax regimes: under Brazilian law, tax-favourable jurisdictions (tax havens) are those countries or jurisdictions that do not impose taxes on income, or that set income tax at a rate inferior to 20%. Tax havens have been recognised and registered in a "black list" by the Brazilian tax authorities (exhaustive list). "Privileged tax regimes" are special treatment tax regimes in some countries (not tax haven jurisdictions) that apply a low rate of taxation and/or do not tax foreign income or foreign residents. Privileged tax regimes have also been recognised and registered in a "grey list" by Brazilian tax authorities (exemplary list). Although transactions conducted between residents in Brazil and residents either in black- or grey-listed countries are subject to Brazilian transfer pricing controls, only transactions with blacklisted countries are subject to a higher withholding income tax ("WHT") rate (25%) in comparison to the general 15% rate.

Thin capitalisation: Brazilian thin capitalisation rules apply in case of interests involving: (i) financing granted by foreign persons in the same group; (ii) residents in tax havens; and (iii) entities benefiting from tax privileged regimes. Interest paid in connection with such financing is not deductible when it relates to a principal amount that exceeds the following percentages:

Loan from a	Limit	Calculation basis
directly related non-resident person	200%	of the non-resident's stake in the net equity of the Brazilian company
indirectly related non-resident person	200%	of the total net equity of the Brazilian company
non-resident person based in a tax haven, or a beneficiary of a tax-privileged regime	30%	of the total net equity of the Brazilian company

Transfer pricing: Brazil has unique transfer pricing rules for both export and import transactions carried out with related parties or with legal or natural persons domiciled in tax havens. These rules do not follow the OECD standards and are based on alternative comparison methods, as defined by Brazilian law. These methods have been recently changed by new legislation passed in 2012 and will mandatorily impact the calculation of Brazilian Corporate Taxes as of 2013 (for 2012 there is just an option to adhere to the new rules).

Brazilian taxation on remittance of funds overseas: (i) dividends or profits payable by a Brazilian subsidiary to any foreign investor are always tax-exempt; (ii) interest on net equity (*"Juros sobre capital próprio"* – "JsCP") is a unique income type created by Brazilian legislation, which is calculated as the interest gained on the net equity of a company, limited to the Long-Term Interest Rate (*"Taxa de Juros de Longo Prazo"* – "TJLP", fixed quarterly by Brazilian Government at around 6% in the last few years), and is subject to a general 15% WHT rate (25% in case of tax havens); (iii) interests deriving from inter-company loans paid to non-residents are subject to general 15% WHT rate (25% in case of tax havens); (iv) fees, commissions and any other income payable by a Brazilian obligor to an individual, company, entity, trust or organisation domiciled outside Brazil, in connection with any royalties or technical assistance agreements involving the transfers of technology or know-how, are subject to a 15% WHT rate or any other lower rate previously established by DTT (but which never falls under 10%); (v) payments referring to royalties and technical assistance are also subject to an economic intervention contribution (*"Contribuição de Intervenção no Domínio Econômico"* – "CIDE") of 10%, which should be collected directly from the Brazilian subsidiary making the payment.[1]

Capital gains of non residents: since 2003, Brazilian domestic legislation provides for a specific WHT obligation on capital gains generated by non-residents alienating Brazilian assets. The applicable rate corresponds to 15% (raised to 25% in case of tax havens) and reaches even transactions executed outside Brazil among non-residents (i.e., even if there is no financial flow through Brazilian territory). The effectiveness of such tax provision is achieved by Brazilian authorities imposing a tax liability on the Brazilian purchaser of the assets or its Brazilian attorney in law, in case of a non-resident purchaser. None of the Brazilian DTTs, except the one executed with Japan, impose any limitation of such Brazilian tax competence to tax as source state, differing from the standards of the OECD model.

PIS/COFINS: corporations in Brazil must also pay Social Integration Program Contribution Tax ("*Contribuição ao Programa de Integração Social*" – "PIS") and Social Security Financing Contribution Tax ("*Contribuição para o Financiamento da Seguridade Social*" – "COFINS"), which are levied over the monthly gross revenue arising from the sale of goods or provision of services.

As a general rule, companies opting for the actual profit method would pay PIS/COFINS under a non-cumulative regime representing a total rate of 9.25% on monthly gross revenue. Under that regime, a manufacturing company is entitled to get PIS/COFINS tax credits arising from the purchase of raw materials and services used in its production activities, while a company solely engaged in sales may use PIS/COFINS tax credits from the acquisition of goods for resale. The extension of the non-cumulative system is very controversial: while the tax authorities have a very strict understanding about the transactions generating tax credits, taxpayers in Brazil have been struggling before the administrative and judicial tax courts in order to defend a more flexible application of the non-cumulative regime (see *The year ahead,* below).

Companies opting for the presumed profit method are, in general, subject to cumulative taxation for PIS/COFINS purposes, representing a total rate of 3.65% over their gross revenues from the sale of goods or provision of services.

Insurance, capitalisation and financial companies or institutions, as well as companies from telecom, energy, newspaper and broadcasting, transportation, health care, education, IT, call centre and telemarketing, highways, hotel, fairs and events' companies, among others, are mandatorily subject to the PIS/COFINS cumulative regime, even when opting for the actual profit method.

Capital gains are not subject to PIS/COFINS; financial revenues are currently subject to a 0% rate; and exports are PIS/COFINS tax-free.

Significant deals and highlights illustrating aspects of corporate tax

Premium amortisation: in 2012, the Brazilian Administrative Tax Court (*"Conselho Administrativo de Recursos Fiscais"* – "CARF"), all of whose members are considered to be tax experts, issued an important decision (the "Gerdau case"), ruling in favour of a taxpayer that amortised a share price premium for Brazilian Corporate Taxes purposes that had been generated in a reorganisation carried out between companies belonging to the same economic group ("internal premium"). Besides the discussion regarding the requirements for enjoying the tax amortisation of the premium, the decision also encompasses some relevant aspects related to the limits of tax planning in Brazil.

In order to understand the extent of this decision, a brief explanation about the deductibility mechanism of share price premiums for corporate tax purposes is necessary.

Under certain circumstances, the acquisition of Brazilian company shares – through any kind of transaction, such as purchase and sale, swap or subscription for capital stock – can generate tax benefits to the purchaser, which, as a rule, would not occur if the assets had been acquired directly (e.g. real property, trademarks). Thus, from a tax optimisation standpoint, in principle the acquisition of a Brazilian company's shares is better than the acquisition of its assets.

According to tax legislation in force since 1998, when a Brazilian company acquires shares of another and registers this investment through the equity accounting method, the acquisition cost of the investment must be divided into: (i) the value of the participation of the investor in the net equity of the invested company; and (ii) the premium (or discount) corresponding to the positive (or negative) difference between the investment's acquisition cost and its net equity value.

For tax purposes, the premium must be based on one of the following economic reasons: (a) the fair value of assets of the invested company is higher than the accounting cost (book value); (b) expected future earnings of the invested company; or (c) goodwill, intangibles or other economic reasons. The premium related to reason (a) can be deducted accordingly but only if the underlying assets are susceptible to depreciation or amortisation. The premium related to reason (b) can be deducted if it is supported by an appraisal report, and only if it extends over a minimum period of five years. Finally, the premium related to item (c) is not deductible.

Additionally, the premium paid and registered by the Brazilian investor company and the economic grounds for the same, found in the invested company, must be "united" through a merger, amalgamation or spin-off of the two companies. This is the moment when the amortisation of the premium is triggered for tax purposes. In this case, the surviving entity will book the original expense from the premium as an asset, subject to amortisation, that will generate deductible expenses for tax purposes.

Though premium amortisation structures are very common in Brazil, they are not completely free of risk. The tax authorities scrutinise such structures for an effective business purpose in this kind of tax planning, and disregard some of them after a case-by-case analysis of the respective economic substance. The controversy is based on the requirements imposed by the tax authorities for validating taxpayers' structures, many of them with no legal grounds.

In the Gerdau case, the premium was generated by transactions that occurred within the Gerdau Group, i.e., performed by related parties with a common ultimate shareholder. Summarising the facts, the Gerdau Group holding company had two controlled companies and decided to subscribe for new shares in one of them, with shares of the other. As the transaction was conducted at fair value, the holding company booked the shares it subscribed for at an amount higher than their equity value, based on expected future earnings and backed up by an appraisal report. At the same time, it accrued (i) a capital gain from the disposal of the shares as payment for the subscription, and (ii) a premium by the amount exceeding the shares' equity value. Later, one controlled company merged with the other, triggering the premium amortisation for tax purposes.

The tax authorities considered the corporate reorganisation an artificial scheme for tax evasion, carried out through deceptive accounting, which improperly generated a deductible premium within the same economic group, without any actual cash disbursement.

However, the CARF ruled in favour of the taxpayer and decided that the tax authorities had committed several mistakes in the notice of deficiency. First, they had unduly reduced the concept of acquisition to the idea of purchase, ignoring the possibility of acquisition through the subscription for new shares. Second, they had confused the concept of economic justification for premium with that of purchase payment or dropdown. Third, although internally generated, the premium arose from a legitimate appreciation, accrued in accordance with applicable legislation and supported by proper documentation. Fourth, the distinction between the internal goodwill and the one generated in transactions performed by independent parties is only relevant for accounting purposes, but not for tax purposes.

The decision also addressed the concepts of tax avoidance and tax evasion, by stating that planning to intentionally mitigate the tax burden is not illegal (*"it would be odd to assume that taxpayers are only allowed to seek tax avoidance casually or accidentally"*, stated the decision), revealing a strong opposition by the CARF against any requirements imposed by the tax authorities not found in law.

<u>Treaty overrule on article 7</u>: also in 2012, the Brazilian Superior Court of Justice issued its first precedent (the "Copesul case") on the application of article 7 of a DTT entered into by Brazil, which is traditionally overruled by the tax authorities under a distorted interpretation and application of article 21 to technical, scientific, administrative or similar assistance fees. The case is relevant because, although the Superior Court of Justice did not recognise the hierarchical prevalence of DTTs over internal tax legislation, it did rule in favour of special status of international tax law, preventing the Brazilian tax authorities from taxing at source the remittance of fees for services provided by foreign residents of other jurisdictions which do not have permanent establishment in Brazil.

Key developments affecting tax law and practice

Tax on financial operations (*"Imposto sobre operações financeiras"* – "IOF") on international loans: the Brazilian government has constantly employed this tax as an intervention mechanism to fight interest rate arbitrage on short term contracts for international loans. At the same time, it has been concerned that this tax burden might intimidate foreign investors and create an uncertain investment environment. The search for this delicate balance resulted in the following four changes to IOF in 2012: (i) in February 2012, a 6% IOF rate was applied to contracts for less than 720 days, whereas there was a 0% rate for international loans for longer periods; (ii) in March 2012, the minimum loan period for the 0% rate was extended to 1,800 days; (iii) three months later, in June 2012, the 720 days limit was again imposed; and (iv) finally, in December 2012, the Brazilian government reduced the period to the current 360 days.

Such changes significantly affected company plans for Brazil in 2012, since each modification to the IOF rate is immediately applicable, without any "grandfathering" protection (see *Attraction for holding companies* below).

Reduction of social security taxes: in late 2011, the Brazilian government initiated a significant change to the 20% Social Security Contribution on Payroll (*"Contribuição Previdenciária sobre Folha de Salários"* – "INSS contribution"), allegedly aiming to reduce the corresponding tax burden of some specific, strategic sectors. Under this initiative, those sectors migrated from a payroll-basis contribution – which has always been a serious obstacle to job creation and economic growth – to a gross revenue basis contribution, which was later named the new Social Security Contribution on Gross Revenue (*"Contribuição Previdenciária sobre Receita Bruta"* – "CPRB").

However, at the same time that the CPRB was applied to some sectors in clear economic difficulty – the textile industry, for example – it was also applied to some specific industries where the level of informal employment (and consequently INSS contribution tax evasion) was historically high – such as IT services, the hotel industry, and the transportation sector, among others.

During the whole of 2012, many other economic activities were included in the CPRB regime, with rates currently varying from 1% to 3.5%. There is a clear tendency of the Brazilian government to gradually replace the old INSS contribution tax with the CPRB for all economic activities.

SISCOSERV and intangible transactions: in May 2011, the Brazilian government created the Integrated System of Foreign Trade in Services (*"Sistema Integrado de Comércio Exterior de Serviços"* – "SISCOSERV"), obliging Brazilian individuals and corporations to provide information regarding any kind of transactions with foreign-resident or domiciled persons, involving services, intangibles or other transactions generating variations in the assets of individuals, legal entities or depersonalised entities. SISCOSERV was originally created to work as a statistics database system for the international trade in services, intangibles and other transactions. However, by the end of 2011, it was officially transformed into a tax control instrument, which will provide information for the Brazilian tax authorities to track and control transactions performed by informal/non-registered economic entities in Brazil. Non-compliance with the mandatory SISCOSERV information requirements may result in a BRL 5,000 fine for companies or individuals for each month of delay in providing the information, and a 5% fine over the transaction value in the case of concealed, incomplete or inaccurate information. The underlying concern surrounding SISCOSERV resides in the database which tax authorities will start to create in order to monitor and audit more closely the Brazilian outbound remittance of funds with the correct segregation of intangibles and different types of services (which, in some cases, are subject to specific tax rates).

Attractions for holding companies

The Brazilian tax environment is definitely not one of the most receptive in terms of the incorporation of holding companies as platforms/hubs for international investments.

Since January 2002, the Brazilian Controlled Foreign Company rules ("CFC rules") have implemented a "presumed dividends" regime on any accrued profits existing every December 31st on a foreign subsidiary's balance sheet, including all types of foreign income (active and passive), regardless of the tax domicile of the foreign subsidiary (in a tax haven or not). A single 10% participation in the capital of a foreign subsidiary, or a minimum level of management influence, is enough to trigger the application of the aforementioned CFC rules.

From a comparative law perspective, the Brazilian CFC rules definitely sound quite bizarre and unreasonable, exactly because they do not encourage the expansion of Brazilian multinationals into the global market. If, on the one hand, the Brazilian government allows for foreign tax credits (but with some restrictions for tax credits generated by indirectly controlled companies), on the other hand the 34%/40% Brazilian Corporate Taxes are levied on Brazilian companies' worldwide income, thus restricting their competitiveness against other players operating offshore with reduced tax rates.

On top of the CFC rules, the Brazilian foreign currency exchange controls are some of the most bureaucratic in the world, in addition to an IOF rate of 0.38% on the total amount of foreign currency converted into BRL.

The main concern with regard to IOF is that the rules may be amended without a change in statute: IOF rules may be changed with a simple decree or federal administrative measure, which makes it a very "efficient" economic policy instrument for the Brazilian government to interfere in the value of the Brazilian currency. Only the maximum IOF rate for exchange transactions if provided for by statute, is not to exceed 25%.

There is very little to do when a given modality undergoes IOF changes, and dealing in a previously "IOF-free" environment does nothing to prevent future changes either: there are no "grandfathered" assets/contexts as far as IOF goes. That is, if the rules do change down the road, investors might suddenly find themselves in a new IOF context (being obliged to pay IOF when previously it was unnecessary).

Brazilian companies aiming to expand their horizons to foreign lands usually utilise the Brazilian DTT network to obtain a minimum level of protection against their awkward national CFC rules. Spain and Austria are the preferred jurisdictions, due to the participation exemption regime on dividends provided for by both treaties. Nevertheless, relevant litigation is taking place in Brazilian courts without a clear tendency emerging. The tax authorities accuse taxpayers of engaging in fraudulent "treaty shopping" and ignore the existence of holdings companies in order to tax the undistributed dividends of indirectly controlled companies. In their defence, taxpayers allege the hierarchical prevalence of the treaties over domestic legislation; supplemented, in some cases, by evidence of economic substance present in the foreign holdings.

In the past, Denmark was another jurisdiction preferred by Brazilian multinationals due to a specific treaty clause prohibiting Brazilian taxation of the undistributed dividends of Danish companies (which, in practice, annulled the effects of the Brazilian CFC rules in force since January 2002). The Brazilian tax authorities moved fast and a protocol to the treaty with Denmark was executed in Copenhagen on March 23, 2011, to exclude that provision. The protocol has not yet taken effect, given that legislative ratification procedures are still pending.

Finally, it is worth mentioning that instead of incorporating a Brazilian holding company in such an unfriendly environment, one may consider utilising an already existing operational and profitable Brazilian company to simultaneously serve as a platform to hold stakes in other foreign operational subsidiaries, in order to optimise the tax deduction of the Brazilian "exotic" JsCP. In the event that the corporate tax burden of the foreign jurisdiction equals or exceeds 34%/40%, there is no additional tax burden in Brazil under such a holding structure.

On top of Spain and Austria, Brazil has also participation exemption regimes on dividends in the treaties executed with Argentina, Ecuador and India. This means that those jurisdictions would also fit well below a Brazilian operational company from a tax structuring perspective.

The accrued profits existing on every December 31st in the corresponding balance sheet of the foreign entities would increase the Brazilian taxable profits and thus allow a higher payment of JsCP to the foreign shareholders, with a net 19% corporate tax savings in Brazil. One disadvantage, though, if and when the foreign dividends actually flow into Brazil, is an IOF of 0.38% on the currency exchange transaction.

Industry sector focus

Transfer Pricing ("TP"): Brazil's already peculiar transfer pricing methods were changed last year, and applied optionally in 2012 for Brazilian Corporate Taxes calculations, but mandatorily for 2013. Some of those modifications aimed to reduce the great amount of litigation between taxpayers and the tax authorities, caused by the two sides' different interpretations of the TP provisions. Some other changes, however, were imposed in order to tie up some loose ends in the TP provisions concerning international transactions with commodities and international loans.

In relation to the first kind of modifications, Brazilian legislation created a new resale price method (*"Preço de Revenda menos Lucro"* – "PRL") on imports, replacing the presumed profit mark-ups previously imposed on imports destined for resale (PRL-20%) or local production (PRL-60%) with new mark-ups per economic sector, namely: (i) PRL-40% for pharm-chemical and pharmaceutical goods, tobacco, optical equipment/instruments, photo/cinematographic equipment, machinery/devices/equipment for dental/medical/hospital use, and oil extraction/natural gas/oil-derivative products; (ii) PRL-30% for chemicals, glass/glass products, pulp/paper/paper products, metallurgy; and (iii) PRL-20% for other economic sectors.

In terms of tying up loose ends, the Brazilian Congress eliminated the best method approach for international transactions with commodities, which allowed some companies to transfer profits overseas whenever their profit mark-ups were higher than 15% by using the cost-plus taxes and profit method (*"Custo de Aquisição ou de Produção mais Tributos e Lucro"* – "CAP-15%"). In place of any other methods, international transactions with commodities were then subjected to: (i) in the case of exports, the Export Commodities Quotation Price Method (*"Preço sob Cotação na Exportação"* – "PECEX"), with the average daily price found in international commodities exchange or research institutes as the parameter price; and (ii) in the case of imports, to the Import Commodities Quotation Price Method (*"Preço sob Cotação na Importação"* – "PCI"), with the average daily price found in international commodities exchange or research institutes or the price determined by Brazilian Public Regulatory Agencies as the parameter price.

Finally, in relation to international loans with related parties, recent legislative changes: (i) have eliminated the BACEN interest rate register safe harbour[2]; (ii) have imposed TP controls on inbound and outbound loans[3]; (iii) have created four different parameter interest rate determination methods[4]; and (iv) have allowed the Ministry of Finance to determine by administrative fiat what the maximum interest rate market spread should be.

The year ahead

Brazilian CFC rules: Brazilian legislation on taxation of foreign controlled companies has evolved from the absolute absence of taxation until 1995 (when Brazil still used to tax income on a territorial basis) to the current taxation of foreign companies' profits under a legal fiction, and without exclusively aiming at structures created for tax avoidance purposes. From a taxpayer's point of view, this distorted CFC legislation is unlawful because: (i) it results in extraterritorial taxation of income; (ii) it creates taxation by a legal fiction; (iii) it allows the taxation of income in disregard of a corporate entity's domicile; (iv) it does not comply with the proportionality principle; (v) it is incompatible with article 7 of DTT; and (vi) it damages the outbound investments in jurisdictions with income taxation less burdensome than Brazil's internal taxation.

Notwithstanding those arguments, in 2011, the Brazilian Supreme Court considered the CFC rules to be in accordance with the Brazilian Constitution, namely in the case of directly controlled foreign companies. There was still not unanimity among the Supreme Court justices in relation to the taxation of profits arising from indirectly controlled foreign companies. During 2013, the Supreme Court should decide a new case on the issue, forcing a final position on the matter.

PIS/COFINS reform: due to the uncertainty of the PIS/COFINS non-cumulative system, the Brazilian government has been considering promoting a deep reform on the social contribution legislation, probably eliminating the dual cumulative/non-cumulative regimes and unifying the tax rates. If implemented in 2013, this modification may affect on-going investments in Brazil, which have been made taking into consideration the possibility of recovering PIS/COFINS from the purchase of assets, or the acquisition of goods for resale or as inputs for production.

Increase on the presumed profit method limit: there is already under discussion a bill before Congress proposing an increase in the limit on revenue entitling a company to the presumed profit method, from BRL 48m to BRL 72m per year. If this bill is passed, its application could include fiscal year 2013 and benefit many companies that are currently mandatorily subject to the actual profit method.

Premium amortisation on the acquisition of negative equity situation: another relevant question that may arise in the next few years, especially in the CARF's jurisprudence, is the formula that should be used to calculate and amortise the premium on the acquisition of shares in the case of an invested company with negative equity. The possibilities under speculation vary from the absolute impossibility of amortisation, to the amortisation of the positive premium plus the negative equity amount registered in the invested company, including a middle position only authorising the amortisation of the positive amount of the premium.

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Endnotes

1. Such transactions would also be taxed by: (i) municipal tax on services (*"Imposto sobre serviços"* – "ISS"), which rate varies between 2% and 5%, depending on the municipal legislation and the service involved; (ii) PIS/COFINS on the importation of services (at the total consolidated rate of 9.25%); and (iii) Tax on Financial Operations (*"Imposto sobre operações financeiras"* – "IOF") at 0.38%.
2. Whenever the loan contract was registered with the BACEN, the corresponding rate was considered to be in compliance with Brazilian TP rules if it was BACEN-approved.
3. Previously, the TP controls only applied to inbound international loans into Brazil.
4. Interests will be limited to a market spread percentage to be set annually by an act of the Minister of Finance, in addition to the following rates: (a) for loans denominated in USD with fixed rates – the market rate of the sovereign bonds issued by the Brazilian Government on the external market and indexed in USD; (b) for loans denominated in BRL with fixed rates – the market rate of the sovereign bonds issued by the Brazilian Government on the external market and indexed in BRL; and (c) for loans denominated in all other foreign currencies or with floating rates – the 6-month London Interbank Offered Rate – LIBOR.

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