



THE BRAZILIAN TAX SYSTEM

A Guide for New Zealand Businesses



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Notice

This report was prepared by Carvalho, Machado, Timm and Deffenti Advogados for the New Zealand Ministry of Foreign Affairs, which funded the study under its Investment Promotion Fund. The purpose of the report is didactic and informative. The information contained in this report is provided as general guidance for New Zealanders interested in Brazil and does not constitute, under any circumstances whatsoever, a legal opinion issued by this firm. Carvalho, Machado, Timm and Deffenti Advogados strongly recommends that any individual who needs specific in-depth information about intellectual property in Brazil consult a specialized law firm. Cover photos supplied by the New Zealand Ministry of Foreign Affairs and the Tourism Secretariat of the São Paulo State Government.

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THE BRAZILIAN TAX SYSTEM A Guide for New Zealand Businesses

1. INTRODUCTION

Brazilian tax laws and regulations are some of the most confusing and difficult to comply with in the world. The myriad of rules, which are set out at the Municipal, State and Federal levels, is daunting for Brazilians and is often perplexing to foreign investors. This is especially the case for those used to the New Zealand tax system, which is substantially simpler, better structured and more flexible in its application.

There are three separate entities that may levy taxes in Brazil: Municipalities, States and the Federal Union. Municipalities have the power to impose services taxes and levies on the maintenance and transfer of real estate. States are empowered to impose taxes on certain services, on the sale of goods, over assets transferred in succession and on gifts. Finally, the Union is responsible for the tax collection on income, capital gains, the sale of industrialised goods, currency transactions, the importing of goods and various other areas.

The complicated tax framework is exacerbated by the numerous different rates that apply to the goods and services being supplied. The classification of a particular type of good, service or intellectual property right under a specific heading, and the Municipality (there are over 5,000 of them in Brazil) and State (there are 26 States, plus the Federal District) where the good or service is being manufactured, delivered or rendered, can turn a great business opportunity into a loss-making enterprise, and vice-versa.

Before any deals are concluded it is essential for those looking to enter the Brazilian market (whether by supplying services or goods to Brazilian companies or by setting up or acquiring a local company) to become well versed on Brazil's tax system.

Under Brazilian law, obligations can be divided into two: obligations to *give* something and obligations to *do* something. The former are generally taxed as a good and the latter are generally taxed as a service. This difference becomes blurred in a variety of scenarios, especially in relation to intellectual property rights. Keep these distinctions in mind when considering the taxes that may apply to the goods, services or intellectual property rights that you intend to supply to Brazilian customers.

This guide was prepared in order to provide New Zealand businesspeople with little or no knowledge of the Brazilian tax system to engage in preliminary negotiations with their Brazilian counterparts. It should not be relied upon for final

decisions, as exceptions of all types will apply to specific situations. Also, while this report is accurate as at the time of writing, rules can change at any moment. Therefore, suitable professional advice should be sought as soon as negotiations begin.

The guide is structured in three parts as follows:

Part 1 defines the most important taxes and highlights particular tax issues. First, we address the Federal taxes, duties and levies. These apply throughout Brazil. Second, we consider the State taxes which generally apply to services provided and sales made within States, between States and to the State of destination of imported goods. Thirdly, we consider Municipal taxes. These generally apply to services provided within a Municipality or where the Municipality is the destination of certain services.

Next we consider tax incentives. As there are many incentives available – at Federal, State and Municipal levels – we have only addressed some of the main ones. A summary of the rules applicable to transfer pricing rules follows. Brazil's provision generally follows World Trade Organisation's rules.

The all-important sanctions applicable to non-compliance with tax rules are considered next. Brazil's tax rules can be unforgiving on those that do not comply with them. Tax penalties are often the cause for the demise of many Brazilian businesses. Unusual Brazilian tax rules are considered in the next section. The comments are based on what we considered as the most at odds with New Zealand's tax system. Those already familiar with foreign tax systems may find some features that are similar.

Once the reader has become familiarised with the key Brazilian taxes and rules, Part 2 outlines applicable taxes for certain business situations. We address the specific rules most relevant to those looking to export goods, those looking to provide services and those looking to licence intellectual property rights to Brazilians. Although we understand that rarely a deal will involve only one of these (quite the opposite – they generally involve all three), understanding how the rules apply to each will assist with the learning process.

For those who may be considering setting up a company in Brazil, next we provide a summary of the most commonly applied taxes. Note that Brazil is not a shelf/shell company-friendly jurisdiction.

Finally, we provide specific examples and how the taxes applicable to them are calculated.

Part 3 provides comments on other sources of potentially useful information and contains a glossary of key terms.

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We hope you find this guide useful and wish you good luck doing business in Brazil.

PART 1: FEDERAL, STATE, AND MUNICIPAL TAXES, DUTIES AND LEVIES

2. FEDERAL TAXES, DUTIES AND LEVIES

2.1. Import Duty

Import duty (*Imposto de Importação*) is levied on imported goods, depending on the type of product and/or number of items being imported. Import duty varies dramatically among the products being imported. Rates generally range from 2% to 35% on the value of the goods, in the case of *ad valorem* duty.

On arrival in Brazil, import duty as well as all other taxes levied on sales will need to be paid up front or else the goods will not clear customs.

Most goods imported from other Mercosul countries (Argentina, Uruguay and Paraguay), as well as Chile and Bolivia may be imported free of import duty. There are many exceptions to these, so care should be taken before finalising pricing decisions.

2.2. Income Tax

(a) Company Income Tax and Additional Income Tax

Company Income Tax (*Imposto de Renda de Pessoas Jurídicas*, “**IRPJ**”) is a federal tax levied on income received by companies registered in Brazil. It is assessed at 15%.

Brazilian companies will also be subject to Additional Tax on Income (*Adicional do Imposto de Renda*, “**AIR**”). AIR applies over those profits (actual or deemed) that exceed R\$60,000 in a given quarter.

In general terms, IRPJ and AIR operate like New Zealand income tax. Yet, most companies opt for the deemed profit taxation regime, which is substantially different to New Zealand taxation. Another marked difference is that there are much stricter limitations on the availability of deductions. The deemed profit and actual profit methods are described in section 13.3.

(b) Withholding Income Tax

Withholding Income Tax (*Imposto de Renda Retido na Fonte*, “**IRRF**”) is a federal tax imposed on income paid, credited, remitted or delivered to non-residents, at the rates of 15% or 25% according to the nature of the income and the country of destination.

IRRF withheld in Brazil is likely to be allowed to be applied as a tax credit in New Zealand. As Brazil does not have a double taxation agreement with New Zealand, New Zealand tax residents have no advantage over those from other jurisdictions. Note, however, that New Zealand is also not regarded as a tax haven – thus New Zealand tax residents are also in no disadvantage over competitors from other jurisdictions.

2.3. Social Contribution over Net Profits

Social Contribution over Net Profits (*Contribuição Social Sobre o Lucro Líquido*, “**CSLL**”) is a federal tax imposed over the company’s net profits (calculated in accordance with the deemed profit regime or the actual profit regime). While it is called a “contribution”, in essence CSLL operates much in the same way as income tax.

It is assessed at 9%. A 1% reduction will apply where the company pays all of its taxes on time and in strict adherence to the laws and regulations for a period of 5 years. Due to the bureaucratic difficulties involved, this 1% reduction is seldom obtained by taxpayers.

2.4. Program for Social Integration and Contribution for the Financing of Social Security

Program for Social Integration (*Programa de Integração Social*, “**PIS**”) and Contribution for the Financing of Social Security (*Contribuição para o Financiamento da Seguridade Social*, “**COFINS**”) are federal levies imposed over a company’s gross revenues, whether or not the company has made a profit. PIS-Import and COFINS-Import are also federal levies imposed at a rate of 1.65% and 7.6%, respectively, and are assessed over the total value of imported merchandise or services, following a complex formula.

In transactions between Brazilian companies, PIS and COFINS are generally levied at the rates of 0.65% and 3%, respectively, over gross amounts – for those companies that adapt the deemed profit regime. For companies which use the actual profit regime, rates are 1.65% and 7.6%, respectively. Companies are generally allowed to offset their PIS and COFINS obligations with credits obtained from inputs.

For PIS-Import and COFINS-Import, the calculation takes into account the customs value of the goods as well as the ICMS, IPI, import duty, insurance, freight and other related costs. Where services are being imported, the following formula applies:

$$\begin{aligned} \text{COFINS-Import} &= d \times V \times Z; \\ \text{PIS-Import} &= c \times V \times Z, \text{ where:} \end{aligned}$$

$$Z = [(1 + f) / (1 - c - d)]$$

V = amount paid, credited, delivered, placed towards or sent abroad, before withholding income tax;

c = PIS-Import rate;

d = COFINS-Import rate;

f = applicable ISS rate.

For the importing of goods, the following formula applies:

$$\text{COFINS-Import} = d \times (VA \times X)$$

$$\text{PIS-Import} = c \times (VA \times X), \text{ where:}$$

$$X = \{1 + e \times [a + b \times (1 + a)]\} \div [(1 - c - d) \times (1 - e)]$$

VA = customs value;

a = import duty rate;

b = IPI rate;

c = PIS-Import rate;

d = COFINS-Import rate;

e = ICMS rate; and

D = any other taxes, fees, contributions and customs-related expenses.

Where the goods have a specific IPI rate (i.e. a rate which is imported per item), an even more complex formula applies.

Various exemptions and tax credits apply and the application of these exemptions needs to be looked at on a case by case basis.

It is difficult to draw an analogy of PIS/COFINS to any New Zealand taxes. PIS/COFINS-Import is loosely similar to New Zealand's import duty, while PIS/COFINS have peculiar characteristics that have no equivalent in New Zealand.

2.5. Tax over Industrialised Products

Tax over Industrialised Products (*Imposto sobre Produtos Industrializados*, “**IPI**”) is a federal tax imposed on the production or importation of “industrialised goods”.

Rates are assessed on the value of the industrialised goods, and vary in accordance with the nature of the merchandise. On average, IPI is levied at rates between 5% to 18%.

As for imported goods, IPI will be levied on the customs value of the manufactured goods plus the amount of import duty payable. Therefore, the IPI formula is as follows:

$IPI = IPI\ rate \times (VA + II)$, where:

VA = customs value of the goods;

II = import duty; and

$IPI\ rate$ = the applicable IPI rate.

IPI operates similarly to the GST in New Zealand and input tax credits may be claimed by the taxpayer.

2.6. Contribution on the Intervention over the Economic Domain

Contribution on the Intervention over the Economic Domain (*Contribuição de Intervenção no Domínio Econômico*, “**CIDE**”) is a federal levy charged on money transferred abroad for the payment of royalties (other than for the licensing of software, unless there is a technology transfer) or technical assistance. The rate is currently 10% and is payable by the licensee.

CIDE applies to:

- the supply of technology;
- the provision of technical assistance, namely:
 - technical support;
 - specialised technical services;
- technical services, administrative and similar assistance;
- the transfer and licensing of trademarks;
- the transfer and licensing of patent explorations.

In certain circumstances, imputation credits may be allowed as deductions of CIDE payable.

Although called a “contribution”, CIDE operates much the same way as IRRF. An argument may be made that the CIDE withheld by the Brazilian payor may be credited against New Zealand’s income tax under reciprocity principles. It is advisable to consult with IRD in relation to this.

2.7. Tax on Credit and Exchange Transactions, Insurance or Securities

Tax on Credit and Exchange Transactions, Insurance or Securities (*Imposto sobre Operações de Crédito, Câmbio e Seguro ou relativas a Títulos e Valores Mobiliários*, “**IOF**”) is a tax on credit and exchange transactions, insurance and securities and is assessed:

- on the amount of Brazilian currency purchased or sold (currently set at 0.38% for sending funds abroad for the payments of services retained and at 5.38% for the payment of loans whose term is less than 90 days);
- on the amount of bank loans and similar transactions (currently set at 0.0041% of the loan amount); and
- on insurance premiums (varying from zero up to 25%).

IOF is a *sui generis* tax. No analogy can be made to any New Zealand tax.

2.8. Rural Land Tax

Rural Land Tax (*Imposto Territorial Rural*, “**ITR**”) is a federal tax applied to properties located outside the urban areas. The taxpayer is the owner of the real estate, the holder of its useful ownership or the person in possession of the land.

The formula used to determine the ITR payable is complex and takes into account the value of the rural property, the taxable area, the value of the taxable empty land, the serviceable area, effectively used areas and the degree of use.

3. STATE TAXES

3.1. Tax over the Movement of Goods and Services

The Tax over the Movement of Goods and Services (*Imposto Sobre a Circulação de Mercadorias e Serviços*, “**ICMS**”) is a State tax levied on products and the provision of certain services, including where these are imported from abroad.

ICMS is a value added tax and, to some extent, it works like the GST in New Zealand. ICMS is limited to the commercialisation of certain merchandise, communication services, electricity and transportation of goods. Imported merchandise is also subject to ICMS.

Rates generally vary between 18% to 25%, but there are major reductions or increases depending on the type of good or service involved. Interstate rates vary from 7% to 12% (depending on the state and where the goods will be sold).

Where ICMS is payable on the importing of goods, the following formula applies (the ICMS itself is considered as part of the formula):

$ICMS = (T \div 0.82) \times 0.18$, where:

$T = (VA + II + IPI + PIS-Import + COFINS-Import + IOF + CIDE + \text{customs expenses})$

VA = customs value;
II = amount of import duty payable;
IPI = amount of IPI payable;
PIS-Import = amount of PIS-Import payable;
COFINS-Import = amount of COFINS-Import payable;
IOF = amount of IOF payable (if any);
CIDE = amount of CIDE payable (if any); and
customs expenses = customs expenses paid or payable in Brazil.

No ICMS is payable where goods are being exported from Brazil and any taxes paid on inputs will be credited to the exporting company.

3.2. Tax on the Transfer Due to Death and Gifts

The Tax on the Transfer Due to Death and Gifts (*Imposto de Transmissão Causa Mortis e Doação*, “**ITCMD**”) is an estate and gift tax. They generally vary between 1% and 4% over the value of the good or right being transferred or gifted over.

4. MUNICIPAL TAXES

4.1. Municipal Services Tax

Municipal Services Tax (*Imposto Sobre Serviços*, “**ISS**”) is a municipal tax over revenues received from the provision of services, and applies to almost all services provided within Brazil. The ISS rate varies between 2% to 5%. As ISS is levied over gross revenues, the company will be liable for it even where it makes a loss.

A company which acquires services from providers who are based abroad are likely to be liable for the tax. Also, unlike New Zealand’s GST, no tax credits or deductions are available.

4.2. Intervivos Real Estate Transfer Tax

Intervivos Real Estate Transfer Tax (*Imposto de Transferência de Bens Intervivos*, “**ITBI**”) is a municipal tax levied on property transfers for in exchange for something of value, granting of security rights over real estate, as well as assignment of rights over real estate.

The market value of the real estate as assessed by the Municipal tax authorities is used for the purposes of calculating ITBI. The applicable rate is usually 3%, depending on the Municipality. Transfers of properties or rights incorporated to a legal entity, assets transferred to pay up capital, or the transfer of goods and rights originating from mergers, incorporations, spin offs or extinguishment of legal entities are exempt from ITBI.

4.3. Tax over Buildings and Land

The Tax over Buildings and Land (*Imposto Predial e Territorial Urbano*, “**IPTU**”) is levied on any real estate (land or buildings) located in urban areas. The taxpayer is the owner of the real estate, the holder of its useful ownership or possessor of any type. The formula for calculating IPTU considers the market value of the property. The rate charged on the value of the property is, on average, 1%, depending on the Municipality where the building or land is located.

5. TAX INCENTIVES

There are a number of tax incentives available at Federal, State and Municipal levels. We will address the ones most likely to apply to a New Zealand company looking to do business in or with Brazil, yet the list below should not be seen as exhaustive as many other incentives may be available.

5.1. Federal Tax Incentives and Reductions

(a) *Ex-tarifário* regime

The *ex-tarifário* regime allows for certain imported capital goods, and telecommunication and information technology products (as well as their respective parts and components) to enter Brazil paying substantially less tax where no similar items are manufactured in the country at the time of the application. The goods which successfully obtain certification are called *ex-tarifários*.

Specific procedures for obtaining the tax reductions apply – an application must be made to the Federal Chamber of International Trade (“**CAMEX**”) and to the relevant State Chambers of Commerce where the goods are to be used.

The key advantages of an item obtaining *ex-tarifário* certification relate to tax reduction, yet there are other advantages. These advantages include:

- Reduction of import duty rates from 14% to between 0% and 4%;
- Reduction of ICMS rates to 0% (this exemption will depend on the type of good being imported and the rules of the State of final destination of the good);
- Reduction in the IPI payable, as the formula used for calculating it takes into account import duty and ICMS;

- Market-entry edge over competitors, where the certification is granted for a specific classification which meets only a specific foreign manufacturer's product.

Reductions will remain in place for up to two years from the time certification is granted.

It is advisable that the application be filed some months prior to the first product being shipped to Brazil. This maximises the possibility of the *ex-tarifário* certification being granted and minimises the tax burden right from the beginning. On average the *ex-tarifário* application will be assessed within three to four months.

As *ex-tarifário* certification is not guaranteed, it is recommended that the parties consider negotiating how the gains/losses are to be shared if certification is or is not obtained. Contracts should clearly provide for both outcomes.

(b) Manaus' Free Trade Zone

The Manaus' Free Trade Zone (*Zona Franca de Manaus*, “**ZFM**”) was established in 1957 with the aim of improving the economic conditions of the Amazon region. Companies established in the ZFM are given import duty, IPI and ICMS exemptions. These are generally available for high tech industries and require the employment of local staff and minimum levels of investment.

The tax advantages for the companies established in the area have been extended from time to time. In 2003 the time for expiration of the benefits was extended for a further 10 years (from 2013 to 2023).

(c) Basic Production Process

The Basic Production Process (*Processo Produtivo Básico*, “**PPB**”) is a program that grants tax reductions or exemptions for a particular product to companies which set up (or delegate to third parties in certain circumstances) manufacturing processes in Brazil for that product.

The PPB may also allow the manufacturer to benefit from advantages in tenders published by the Federal government. These may include tenders specifically set up for those who have obtained PPB approval.

The products covered by the PPB program generally require sophisticated manufacturing or high levels of technology.

A PPB grant is issued through a ruling for a particular product. Any companies that manufacture (or delegate to third parties to manufacture) the relevant product, seek approval and comply with the terms of the PPB (as well as the research and development spending requirements), will be granted PPB status.

The key advantages of the PPB involve the reduction of import duty (if the goods are manufactured in the Manaus Free Trade Zone) and IPI. The full gamut of benefits will depend on the State and region where the product will be manufactured.

(d) REPES and RECAP

The Special Tax Regime for the Export Platform of Information Technology Services (*Regime Especial de Tributação para a Plataforma de Exportação de Serviços de Tecnologia da Informação*, “**REPES**”) and the Special Regime for the Acquisition of Capital Goods for Export Companies (*Regime Especial de Aquisição de Bens de Capital para Empresas Exportadoras*, “**RECAP**”) are also specific programs available for companies registered in Brazil.

REPES is available for software developers or providers of information technology services which agree to export at least 60% of their production. RECAP is available for those companies that in the year prior to filing obtained 70% of their gross revenues from the sale of goods and services exported and that undertake to continue having these levels of exports for the following two years. Businesses that qualify for REPES or RECAP can acquire certain goods for the purposes of developing software and providing services free of import duty, PIS/COFINS and IPI.

(e) SUDENE Incentives

The Superintendence for the Development of the Northeast (*Superintendência do Desenvolvimento do Nordeste*, “**SUDENE**”) is the body responsible for the development of the North and North-eastern regions of Brazil. More specifically, investments in the States of Acre, Alagoas, Amapá, Amazonas, Bahia, Ceará, Mato Grosso, Maranhão, Pará, Paraíba, Pernambuco, Rio Grande do Norte, Rondônia, Roraima, Sergipe and Tocantins, as well as parts of the states of Minas Gerais and Espírito Santo.

SUDENE oversees a variety of programs which provide for tax incentives. These include reduction of income tax, grants for reinvestments, accelerated depreciation, PIS and COFINS, IOF and Levy for the Renovation of the Merchant Ships.

5.2. State and Municipal Tax Incentives

There are a number of State and Municipal tax incentives available to companies. These include deferments and reductions of ICMS, ISS, IPTU and ITBI exemptions. Often incentives also include land concessions.

Each State and Municipality will have its own conditions for granting incentives. The most common areas incentivised include technology-intensive industries (especially investments in research and development), investments aiming to improve environmental conditions, mining exploration and generally where local jobs will be made available. The incentives can be very substantial – for instance, the Rio de Janeiro Fund for Social and Economic Improvement provides loans at 6% per annum to grantees (as opposed to the market rate which currently stands at over 20%).

It is recommended that these be looked into before choosing the location where the company is to be established.

6. TRANSFER PRICING RULES

Transfer pricing rules apply to related entities and transactions with entities in tax havens, and aim to ensure that these companies relate to each other on an arm's length basis.

Transfer pricing rules apply both to export as well as import transactions. For import transactions (i.e. goods being imported into Brazil), the price for the good, service or right being imported will be assessed in accordance with the following methods:

- Compared Independent Prices (*Preços Independentes Comparados*, “**PIC**”) method;
- Resale Price Less Profit (*Preço de Revenda Menos Lucro*, “**PRL**”) method; and
- Production Cost Plus Profit (*Custo de Produção Mais Lucros*, “**CPL**”) method.

Under the PIC method, the prices of goods, services or rights purchased abroad are compared with similar or identical goods, services or rights that are bought or sold by the company selling the goods to unrelated entities and those bought and sold among other unrelated companies. The calculations take into account the payment terms, quantities, warranties, packaging, freight and insurance, among other things. The weighted average of these prices will be used for the purposes of deductions of income tax and CSLL.

Under the PRL method, the weighted average of the resale prices applied by the importer less the unconditional discounts offered, taxes and levies paid on the sale is calculated and added to one of the following profit margins:

- (a) 20% on the resale of goods, services and rights;
- (b) 60% on the resale of goods, services and rights applied in the production process.

In relation to (b), where Brazilian goods are also used in the production process, the costs relating to these will be taken into account.

Finally, under the CPL method, the average costs in the country where the good is manufactured, the service is provided or the right is created, will be calculated. The cost-base will take into account taxes and fees charged by the country of origin, as well as the cost of raw materials, personnel, lease, maintenance, depreciation, amortisation and reasonable damages and losses in the manufacturing process. The average cost will be added by 20%, which is the deemed profit.

The importer can choose any of the three methods set out above for the purposes of assessing whether the transaction complies with transfer pricing rules.

7. SANCTIONS FOR NON-COMPLIANCE

Brazilian law provides for a number of sanctions in the case of non-compliance. Sanctions vary from the imposition of hefty fines and seizure of imported goods to imprisonment terms, depending on the gravity of the offence.

Often, the first practical consequence of any non-compliance with deadlines and tax payments is that the company's tax number (*Cadastro das Pessoas Jurídicas*, "CNPJ") appears as non-compliant on the Municipal, State, and/or Federal database. This prevents companies from applying for seeking credit, setting up bank accounts and entering into contracts with a number of companies (it is common that more sophisticated businesses request evidence that the company has no outstanding tax debts).

Penalties include a 75% fine over the amount of taxes owed for simple non-payment (increased to 112.5% if the company does not provide information to the tax authorities when requested to do so) and 150% where fraud is proved (increased to 250% if the company does not provide information to the tax authorities when requested to do so), as well interest at 12% per annum (in addition to having the debt adjusted to inflation) and up to 20% for simple lateness in payment – among other sanctions.

Therefore, retaining a careful and skilled accountant is especially important in Brazil. However, note that mistakes are to be expected as even the best

professionals find it difficult to keep up with the constantly changing rules and the interpretation given to them by the tax authorities.

8. UNUSUAL BRAZILIAN TAX ISSUES

8.1. Legal Uncertainties: Court and Administrative Challenges

As a civil law country (as opposed to the common law system which applies in New Zealand) the doctrine of precedent does not apply. This means that lower courts and the various tax departments are not bound by court decisions that address a particular point of law. Municipalities, States or the Federal Union will only be bound by decisions to which they are a party until, many decisions from the courts reach the same conclusion. It is not unusual for thousands of legal actions to be brought addressing the same legal issue.

Also common are *mandado de segurança* actions. These are *writs of mandamus* issued by the courts that aim to mandate a particular government employee to do (such as clear goods at customs) or not to do (such as not to impose a tax) something. *Mandados de segurança* are available whenever a certain right which is protected by law is being violated or is threatened to be violated by a government employee. Therefore, taxpayers will often file *mandados de segurança* proceedings where a particular right has been found to exist but is not being followed by the tax department. *Mandados de segurança* are often issued on an interim basis until a final decision is obtained.

8.2. Immunities, Non-Levying, Exemptions and Zero-Rating

Brazilian taxation law differentiates between immunities (*imunidades*), exemptions (*isenções*), non-levying (*não-incidência*) and zero-rated (*alíquota zero*) classifications.

Immunities relate to taxes that cannot apply due to provisions set out in the Federal Constitution. These apply to the taxation of religious temples, assets, income or services of political parties, trade unions, educational and non-profit organisations and on the sale or importing of books and paper to be used for the printing of books.

Importantly, it also applies to the taxing of different entities which make up the Brazilian Union: the Federal Union, States and Municipalities cannot impose taxes on one another, insofar as these taxes relate to *assets, income or services*. Government entities are likely to be able to avoid payment of the other Federal entities' taxes (for instance, when supplying goods to a Municipality, for as long as the goods are to be incorporated as part of that Municipality's assets, then no Federal taxes are likely to be payable – although some of the contributions may be). This can be of benefit to New Zealand companies looking to supply goods and services in international tenders put out by Municipalities, States and the Union.

Non-levying relates to those transactions where the elements required to trigger a tax event do not in fact occur. Taxes can only be imposed when all elements which make up a taxable event are met. When they do not, the tax cannot be imposed.

Exemptions assume that a tax exists and that it would be levied in a particular set of circumstances. But for the exemption being set out in the law, the tax would have been levied in those circumstances. The taxpayer has the burden to show that the conditions set out in the law for the exemption to apply are met.

Finally, zero rating relates to imposing a rate of *nil* where the company would otherwise meet the requirements to be taxed. A taxable event occurs but no tax is imposed as the rate is set at zero.

8.3. Tax Invoices

There are specific rules applicable to tax invoices. Tax invoices may not be issued by companies in the company's chosen format and numbering. Tax booklets (*talonários fiscais*) must be specifically requested by the taxpayer and must follow certain formatting requirements. These booklets are printed at printers certified by tax authorities. The carbon copies of the issued tax invoices must at the end of the year be printed and bound. Losses of booklets can create major difficulties with tax compliance.

This old-fashioned way of ensuring tax booklets contrasts with the electronic invoice (*nota fiscal eletrônica*, “**NF-e**”) system. NF-es have been gradually introduced since 2006, and are likely to become mandatory within the next several years for all companies in all sectors. Under the NF-e system, a tax invoice is issued electronically. The data is sent to a Federal government database and a number is issued for that transaction. The validity of an NF-e can be checked on a Federal government website.

8.4. Joint and Several Liability

Under Brazilian law, it is not uncommon that both parties to a transaction be jointly and severally liable for tax obligations arising from that transaction. For instance, banks may be held liable if the proper taxes are not paid on certain international remittances.

Directors of companies as well as shareholders are also often found personally liable for tax debts incurred by the company itself. There is no sure way of avoiding this liability, however, risks can be minimised by undertaking audits and seeking evidence that other parties to transactions are compliant with their tax obligations.

8.5. “IOUs” by Governments (*Precatórios*)

Under Brazilian law, and the Union, States and Municipalities are allowed to pay debts over 60 minimum wages (approximately R\$30,000 or NZ\$18,000) in 10 annual instalments, rather than as a lump sum, as a consequence of a judgment. These “IOUs” are called *precatórios*.

While the Federal *precatórios* have generally been paid on time or with a one to two year delay, States have been notoriously slow in complying with their obligations – there are states where some judgment debts have not been paid in over a decade. Therefore, it is recommended that utmost care be taken when effecting tax payments, as overpayments may take many years to be recovered.

There is even a secondary market for *precatórios*, as these may be used for setting off tax debts of other parties in specific circumstances.

PART 2: APPLICABLE TAXES FOR CERTAIN BUSINESS ACTIVITIES

9. ARE YOU LOOKING TO EXPORT GOODS TO BRAZIL?

9.1. Customs Valuation

Brazilian customs valuation rules are similar to New Zealand's.

For the purposes of calculating *ad valorem* taxes, the customs value of the goods will be calculated in accordance with the general principles set out in article VII of the General Agreement on Tariffs and Trade (“**GATT**”). Where a specific rate applies per unit, then the number of units will be used for the purposes of calculating the payable duties and taxes.

The valuation principles set out under article VII of the GATT require that customs use the actual value of the merchandise. The “actual value” must be assessed based on the “merchandise sold or offered for sale in the ordinary course of trade under fully competitive conditions”. The assessment also considers the quantity of the goods involved in the transaction. The authorities will take into account either: (a) comparable quantities; or (b) “quantities not less favourable to importers than those in which the greater volume of the merchandise is sold in the trade between the countries of exportation and importation”.

The Brazilian Customs Regulations contain further details for assessing customs value. It provides that when assessing the customs value the following will be added to the value of the merchandise:

- (a) the costs of transporting the merchandise to the port or airport where the merchandise will be cleared;
- (b) the expenses relating to the stevedoring/handling of the merchandise for transporting them to the customs office where the goods will be cleared from there they were disembarked;
- (c) insurance costs relating to (a) and (b) immediately above.

Further, Customs Regulations provide that the following will be disregarded for the purposes of custom valuation:

- (a) fees relating to “construction, installation, assembly, maintenance or technical assistance relating to the imported merchandise, carried out after the importation”; and
- (b) transportation and insurance costs after the goods are cleared in Brazil.

Any interest charged by the exporter where the purchase is financed will also not be considered for the purposes of customs valuation, for as long as:

- (a) the interest is set out separately on the invoice;
- (b) there is a written agreement providing for the financing of the purchase;
- (c) the importer can prove that:
 - (i) the goods would be sold for the price declared as effectively paid or to be paid;
 - (ii) the interest rate charged does not exceed that which is generally charged for the type of transaction and in the country which provided the financing.

Where information is stored in a storage device (i.e. a CD or pen drive), only the value of the storage device will be considered for the purposes of customs valuation. This rule does not apply for devices that contain integrated circuits, semiconductors “and similar devices”, and goods that contain these. Also excluded from these are storage devices that contain “music, cinema or video” – in these cases valuation will consider the value of the information stored (i.e. the CD and the songs stored in it).

9.2. Applicable Taxes

Brazil’s Common External Tariff (*Tarifa Externa Comum*, “**TEC**”)¹ is the list that contains the rates applicable to goods imported from abroad. The rules of classification, with their respective numbers, are found in the Common Nomenclature of the Common Market of the South (“**Mercosul**”), known as the “**NCM**”.²

These documents are the equivalent of New Zealand’s *The Tariff and Working Tariff Document*. Their Brazilian counterparts generally follow the same numbering system yet, there are differences on various products. Note that the rates set out in the TEC are supposed to apply equally to Mercosul members, there are differences among the members and associate members. Rates are used by the Brazilian Federal government to protect particular industries, sometimes without any perceptible (or actual) logic as to how this is done.

It is essential that the correct classification be found for the good being imported. Any mistake on the classification is likely to result in long delays, fees and hefty

¹ The TEC may be found here:
<http://www2.desenvolvimento.gov.br/sitio/secex/negInternacionais/tec/apresentacao.php>.

² The NCM may be found here:
<http://www.braziltradenet.gov.br/ClassificacaoNCM/Pesquisa/frmPesqNCM.aspx>.

finer – unlike the New Zealand system, Brazilian customs rules are very strict, with great adherence to formalities and very little flexibility on the part of customs officers. Where there is doubt as to the proper classification, to avoid fines the importer may apply for a ruling from the Federal Tax Department. The ruling may take some time to be issued, yet the very application for a ruling allows the importer to avoid the payment of any fines arising from a wrong classification.

Once the good is classified under the NCM, the importer will need to look into the classification under the Tax on Industrialised Products (*Imposto sobre Produtos Industrializados*, “**IPI**”). The IPI Table (*Tabela do IPI*, “**TIPI**”) contains the IPI rates applicable to the goods.

PIS/COFINS-Import (see further below) will also apply on the importing of the goods at a rate of 9.25%.

Finally, the importer needs to classify the goods under the Tax on the Movement of Goods and Services (*Imposto sobre a Circulação de Mercadorias e Serviços*, “**ICMS**”). The applicable ICMS rate is set out in the ICMS Regulations (*Regulamento do ICMS*, “**RICMS**”), which will vary from State to State. The applicable rate will be that of the State where the goods will reach their final destination.

There are specific immunities, exemptions, non-levying and zero-rated goods for each of the taxes set out above. These are varied and numerous, depending on the State and type of goods and services involved. Agricultural products tend to receive the greatest benefits from States.

The taxes likely to apply to the importing of foreign goods and their respective rate ranges (*ad valorem*) are as follows:

Import duty	Between 0% and 35%, calculated over the customs value
IPI	Between 0% and 30%, calculated over the customs value added by the import duty paid
PIS/COFINS Import	9.25%, calculated in accordance with a complex formula (see further above)
ICMS	12% to 18%, calculated in accordance with a complex formula (see further above)

Importers may be able to obtain import duty exemption where they obtain *ex-tarifário* approval. See further under ***Ex-tarifário regime*** (paragraph 5.1(a), further above).

Furthermore, the following levies and fees are *generally* payable:³

- commercial ship fleet tax (25% over the insurance premium paid for the transport of the good being imported);
- international trade computer system (SISCOMEX) usage fee (US\$30);
- customs broker trade union levy (between US\$71 and US\$160);
- import licence fee (if applicable, US\$150);
- port storage fee (0.65% of the CIF value for each 15 day period); and
- terminal handling fee (US\$100 per container).

10. ARE YOU LOOKING TO EXPORT SERVICES TO BRAZIL?

A radically different system applies to the taxation of services provided by foreign companies as compared to Brazilian companies providing services domestically. The applicable taxes will vary in accordance with the type of service provided as well as the location where the service will be provided.

At the Federal level, taxes will be levied when the services are paid for. IRRF will be paid when the party which obtained the benefit from the services transfers the funds abroad (or otherwise compensates the credits through other means). IRRF will apply to most services provided by foreign personnel at the rate of 25%, while those services provided from abroad are likely to be taxed at 15%. Also payable at the time of the transfer will be the Contribution on the Economic Domain (*Contribuição no Domínio Econômico*, “**CIDE**”), at the rate of 10%.

While at the Federal level classification for the services is fairly easy to ascertain, at the Municipal level a separate type of classification applies. Most services are likely to be taxed at 5%, however each Municipality has its own rules and rates. The rates will vary between 2% and 5% depending on the Municipality where the services will be provided or where the benefit of the services will be felt, in the case of services provided from abroad.

There are no State taxes relating to the importing of services.

The taxes likely to apply to the provision of services and their respective rate ranges are as follows:

³ There will be different fees and taxes depending on whether the import transaction is effected by air or by ship.

IRRF	15% to 25% (if New Zealand is the destination of the funds)
PIS/COFINS Import	9.25%
CIDE	10%
ISS	2% to 5% (5% more likely)

11. WHAT ABOUT LEASING GOODS TO BRAZILIAN COMPANIES?

If goods are to be leased, the applicable taxes will depend on the type of leasing involved. The Federal Supreme Court has decided that there are three types of leasing contractual structures: *operational* leasing, *financial* leasing and *sale and lease-back*.

Operational leasing is similar to a standard New Zealand lease with an option to purchase. Here the good is provided in exchange for a periodic (generally monthly) payment and a final (“balloon”) payment is made at the end of the lease period to acquire the good. The total periodic payments must not be greater than 75% of the total price for the good. *Financial* leasing transactions must involve a Brazilian registered financial institution (i.e. the financial institution is the lessor). Finally, a *sale and lease-back* transaction is one where the good is sold to a company who then leases the good back to its original owner.

Financial leasing and *sale and lease back* transactions are deemed to be obligations to do something, therefore are treated as services for tax purposes – and will be taxed as explained under **Are you looking to export services to Brazil?**, item 10, further above. On the other hand, *operational* leasing is deemed to be an obligation to give something, therefore it is considered as a good for tax purposes and will be taxed as explained under **Are you looking to export goods to Brazil?**, item 9, further above.

12. ARE YOU LOOKING TO LICENSE INTELLECTUAL PROPERTY RIGHTS TO BRAZILIAN BUSINESSES?

The taxes to be levied on intellectual property rights will depend on the type of right being licenced or transferred. Different rights are taxed differently, depending on how the right is classified.

Taxation over intellectual property rights in Brazil is complex, especially at the international level. Given the different possible outcomes depending on the type of right involved, often parties chose to structure their deals primarily considering their tax burden (for instance, it is not uncommon for companies to set up wholly owned Brazilian subsidiaries merely to hold intellectual property rights which are to be licensed to Brazilian clients).

12.1. Software

The taxation of software will depend on whether the programme is sold as a ready-to-use application (for instance, those sold in a package) or whether the software is customisable.

Where the software is **ready-to-use**, then it will be deemed to be a **good**. Taxes will be levied as set out further below under **ARE YOU LOOKING TO EXPORT GOODS TO BRAZIL?**

However, where the software is **customisable**, then it will be taxed as a **service** (please refer to **ARE YOU LOOKING TO EXPORT SERVICES TO BRAZIL?** below). There are two further important issues relating to software: CIDE does not apply to any payments made in relation to customisable software licences and ISS is generally set at a lower rate at the Municipal level. Some Municipalities set the ISS rate at 2% where the software is customised in the Municipality itself, while keeping the 5% rate for imported software.

The taxes likely to apply to customisable software and their respective rate ranges are as follows:

IRRF	15% (if New Zealand is the destination of the payment)
PIS/COFINS Import	9.25% (yet note that there are divergent interpretations as to whether PIS/COFINS-Import should apply)
ISS	2% to 5%

12.2. Copyright (other than Software)

The taxation of licensing of copyright over works other than software is murky. There is little doubt that IRRF is payable and that ISS is not. However, there is great uncertainty as to whether PIS/COFINS-Import and CIDE are payable.

Taxes likely to apply and their respective rate ranges:

IRRF	15% (if New Zealand is the destination of the payment)
PIS/COFINS Import	9.25% (yet note that there are divergent interpretations as to whether PIS/COFINS-Import should apply)
CIDE	10% (the better view is that it does not apply)

In relation to foreign films and similar audio-visual works an additional contribution of 11% is payable. This tax is called the Contribution for the Development of the National Cinematographic Industry (*Contribuição para o Desenvolvimento da Indústria Cinematográfica Nacional*, “**CODECINE**”). Note also that substantive fees are payable for the broadcast and commercial presentations of foreign movies and related audio-visual works.

12.3. Patents

While the taxation over patents is also not clear. There is some doubt as to whether PIS/COFINS-Import should also apply.

Taxes likely to apply and their respective rate ranges:

IRRF	15% (if New Zealand is the destination of the payment)
PIS/COFINS Import	9.25% (yet note that there are divergent interpretations as to whether PIS/COFINS-Import should apply)
CIDE	10%

12.4. Trademarks

Our comments in the sections immediately above relating to the application of PIS/COFINS-Import also apply in relation to the licensing of trademarks and franchising rights.

The taxes likely to apply to trademark licences and their respective rate ranges are as follows:

IRRF	15% (if New Zealand is the destination of the funds)
CIDE	10%
PIS/COFINS Import	9.25% (there are divergent interpretations as to whether PIS/COFINS-Import should apply)
ISS	2% to 5% (5% more likely)

In relation to franchising rights, the above taxes are likely to apply, except for CIDE.

12.5. Know-How/Technology Transfers

General concepts such as “know how” and “technology transfers” are regarded as separate sets of intellectual property rights under Brazilian law and taxed accordingly.

The taxes likely to apply to the licensing or transfer of know how/technology transfers and their respective rate ranges are as follows:

IRRF	15% (if New Zealand is the destination of the funds)
CIDE	10%
PIS/COFINS Import	9.25% (yet note that there are divergent interpretations as to whether PIS/COFINS-Import should apply – the better view is that it does not)

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12.6. Cultivars

As the licensing of cultivars is not common, there is some uncertainty as to how they are to be taxed.

The likely applicable taxes and ranges for the licensing of cultivars are as follows:

IRRF	15% (if New Zealand is the destination of the funds)
PIS/COFINS Import	9.25% (there are divergent interpretations as to whether PIS/COFINS-Import should apply)

13. ARE YOU LOOKING TO SET UP A COMPANY IN BRAZIL?**13.1. Generally**

Brazilian taxation law is generally not welcoming of “shelf”/“shell” companies. Unless the company is to be used merely to hold certain assets (including intellectual property rights), Brazilian law does not easily accommodate for companies without actual operations within the country.

Tax compliance is also extremely bureaucratic. In accordance with the World Bank’s Doing Business publication, tax compliance in Brazil requires 2,600 hours per year. Brazil ranks amongst the worst countries in the world in regards to the time required for complying with tax obligations. All companies must have an accountant to deal with their tax issues. Choosing a suitably qualified accountant is an essential step for those who wish to succeed in doing business in Brazil.

13.2. Key taxes

The following are the key taxes that Brazilian companies are likely to be subject to:

IRPJ	15% over profits
AIR	10% over the amount of profits above R\$60,000 in a given quarter
CSLL	9% over profits
PIS/COFINS	3.65% over gross revenues without tax credits (if the company is taxed under the deemed profits regime – see below) 9.25% over gross revenues with tax credits (if the company is taxed under the actual profits regime – see below)
ICMS	7% to 18% (depending on the State of destination)
ISS	2% to 5% over gross revenues (depending on the Municipality where the service is provided and the type of service provided or right licensed)

13.3. Taxation Regimes: the Deemed Profit Method and the Actual Profit Method

Companies registered in Brazil generally have the choice of one of the following tax calculation regimes:

- the *deemed profit* regime; and
- the *actual profit* regime.

The *actual profit* regime uses the actual profits made by the company considering its gross revenues and allowable deductions, while the *deemed profit* regime deems a certain percentage of a company's gross revenue as its profits. From a compliance standpoint, the actual profit regime is substantially more bureaucratic than the deemed profit regime. Companies with a turnover of more than R\$48 million in a given year must adopt the actual profit regime in the following year.

The most tax effective method will generally depend on the level of gross revenues and costs expected and the type of services or goods the company will be manufacturing and supplying.

Under the deemed profit regime, where a company supplies goods, 8% of its gross revenues will be deemed as profit. Where a company provides services, 32% of its gross revenues will be deemed as profits.

14. PRACTICAL EXAMPLES

14.1. Selling Merchandise to a Brazilian Private Company

A New Zealand company makes an agreement to sell certain merchandise to a Brazilian company. The product is being sold whole and is ready to be used. The contract provides for the purchase of 100 of the products, for NZ\$650 each on a CIF basis. We assume that the exchange rate will make each product to be valued at R\$1,000 (the value of the import transaction totalling R\$100,000 for customs valuation purposes). The goods are not unique, so *ex-tarifário* exemption is not available and customs expenses are assumed to be R\$5,000.

Taxes levied:

- (a) *Federal taxes:* The importer will be liable for import duty, IPI and PIS/COFINS-Import over the merchandise.
- (b) *State taxes:* The importer will be liable for ICMS.
- (c) *Municipal taxes:* As no services are provided, no ISS will be levied.

Therefore:

Federal Taxes	Application	Rate and Calculation Method
Import Duty	Levied over the customs value of the products	Rates will generally vary between 2% to 35%, depending on the TEC classification. We will assume here that the rate would be 12%, thus the importer would pay R\$12,000 as import duty.
IPI	Levied over the customs value of the products, plus the import duty payable	Rates will vary between 5% to 18%, depending on the TIPI classification. We will assume here that the rate would be 10%. As the IPI formula takes into account the import duty payable, for the purposes of IPI calculation we would multiply R\$12,000 by 0.1, making R\$11,200 the total IPI payable
PIS/COFINS-Import	Levied over the customs value of the goods in accordance with a complex formula	<p>PIS/COFINS-Import would be calculated as follows:</p> $COFINS-Import = d \times (VA \times X)$ $PIS-Import = c \times (VA \times X), \text{ where:}$ $X = \{1 + e \times [a + b \times (1 + a)]\} \div [(1 - c - d) \times (1 - e)]$ <p>VA = customs value = 100,000; a = import duty rate = 10% = 0.1; b = IPI rate = 10% = 0.1; c = PIS-Import rate = 1.65% = 0.0165; d = COFINS-Import rate = 7.6% = 0.076; and e = ICMS rate = 18% = 0.18 (see further below).</p> <p>Therefore:</p> $X = \{[1 + 0.18 \times [0.1 + 0.1 \times (1 + 0.1)]] \div [(1 - 0.0165 - 0.076) \times (1 - 0.18)] = 1.3682456$ $PIS-Import = 0.0165 \times (100,000 \times 1.3682456) = R\$2,258$ $COFINS-Import = 0.076 \times (100,000 \times 1.3682456) = R\$10,399$

		Total PIS/COFINS-Import payable: R\$12,657
State Taxes		
ICMS	Levied over the customs value of the storage device, plus all taxes and contributions levied	<p>ICMS would be calculated as follows:</p> $ICMS = (T \div 0.82) \times 0.18$, where: $T = (VA + II + IPI + PIS-Import + COFINS-Import + IOF + CIDE + customs\ expenses)$ $VA = \text{customs value} = 100,000$ $II = \text{amount of import duty payable} = 12,000;$ $PIS-Import = \text{amount of PIS-Import payable} = 2,258;$ $COFINS-Import = \text{amount of COFINS-Import payable} = 10,399;$ $IOF = \text{amount of IOF payable} = 380;$ $CIDE = \text{amount of CIDE payable} = 0;$ and $customs\ expenses = \text{customs expenses paid or payable in Brazil} = 5,000.$ Therefore: $T = (100,000 + 12,000 + 2,258 + 10,399 + 380 + 0 + 5,000) = 130,037$ $ICMS = [130,037 \div 0.82] \times 0.18 = 28,545$ Total ICMS payable: R\$28,545

In sum:

Taxes:

Import duty: R\$12,000

IPI: R\$11,200

PIS/COFINS-Import: R\$12,657

ICMS: R\$28,545

Total taxes payable by importer: R\$64,402

14.2. Licensing Software to a Brazilian Company

A New Zealand company exports software to Brazil. The software needs to be customised to the particular customer. The customer is a local private company.

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The object-code is stored on a CD (the CD's value is NZ\$1). The software licence is R\$100,000 per year and is payable by the Brazilian importer/licensee.

Taxes levied:

- (a) *Federal taxes:* The importer will be liable for import duty, IPI and PIS/COFINS-Import over the *storage device* which is being imported (i.e. the CD, DVD, etc), as it is a good. For the *software*, which is deemed to be a service, only PIS/COFINS-Import will arguably apply. For the services component, the New Zealand company will be liable for IRRF, which will be withheld by the Brazilian payor (i.e. the importer/licensee).
- (b) *State taxes:* Given that the software is customisable, it is deemed to be a service rather than a good. Therefore, ICMS will only apply over the storage device being imported.
- (c) *Municipal taxes:* As the software is deemed to be a service, ISS will be payable. The rates for the software and the services will vary depending on the final destination of the software and for the services where the services are provided.

Therefore:

Federal Taxes	Application	Rate and Calculation Method
Import Duty	Levied over the customs value of the storage device	As import duty will only be levied over the NZ\$1 CD, import duty will be nil (amounts less than R\$10 are not charged by the tax authorities).
IPI	Levied over the customs value of the storage device plus the import duty payable	As above.
PIS/COFINS-Import	Levied over the customs value of the storage device and probably levied over the software (the complex formulas explained above apply here)	Over the CD, the comments in the box above apply here. Over the software, it would probably be levied at 9.25% over the licence value for the software (in addition to other taxes). Note that there are arguments which may avoid the payment of these – see discussion further above.
IRRF	Levied over amounts being	IRRF will be levied at 15% over the software licence. May be offset against New

	remitted or credited to the licensor (NZ company)	Zealand income tax.
State Taxes		
ICMS	Levied over the storage device (the formula set out further above applies here)	As import duty will only be levied over the NZ\$1 CD, import duty will be nil (amounts less than R\$10 are not charged by the tax authorities).
Municipal Taxes		
ISS	Levied over the value of the software licence	Rates will vary between 2% and 5% (more likely to be the latter, so here we will assume that a 5% rate would apply), depending on the Municipality where the licensee is located. ISS is calculated over the value of the software licence

In sum:

Taxes:⁴

Import duty: Nil

IPI: Nil

PIS/COFINS-Import: Nil (over the CD) and R\$9,250 (over the licence)

IRRF: R\$15,000

ICMS: Nil

ISS: R\$5,000

Total taxes: R\$29,250, of which R\$15,000 may be able to be set off against the licensor's New Zealand income tax

14.3. Selling Telecommunications Equipment to Brazilian State and Municipal Governments

A New Zealand company exports radio equipment which is used by police and security forces in Brazil. The police force of a Brazilian State publishes a tender. Brazilian tenders require that all Brazilian taxes be paid by the bidders. To minimise tax exposure, the New Zealand company makes a consortium with a Brazilian service provider (under Brazil's Procurement Law a Brazilian company must be a member of the consortium in international tenders). What taxes would apply and how are they calculated?

⁴ Note that we are not including in the calculations the taxes payable on the importing of goods or any intellectual property rights.

Taxes levied:

- (a) *Federal taxes:* As the Union cannot tax the States, and the State as the importer of record is the taxpayer, Federal *taxes* cannot be imposed on the transaction under immunity principles. Federal *contributions*, however, are prima facie payable and their payment will depend on whether any exemption applies.
- (b) *State taxes:* The sole potentially applicable State tax is ICMS. States can tax their own bodies (including its own police department), so whether ICMS would be payable would depend on the relevant State's ICMS.
- (c) *Municipal taxes:* As no services are provided, no Municipal taxes are payable.

14.4. Taxes on a Brazilian Subsidiary of a New Zealand Company

Here the New Zealand company, together with one of the New Zealand's company's wholly-owned subsidiary⁵ (as Brazilian companies require at least two shareholders) becomes a shareholder of a Brazilian entity and chooses to apply the *deemed profit regime*. The company sells in a given trimester R\$500,000 in goods and R\$500,000 in services (say, engineering services). We assume that the company's purchased inventory would be R\$200,000 (and that it obtained R\$20,000 in IPI credits and R\$30,000 of ICMS credits – for purchasing the goods within Brazil or from abroad, including from the parent company) and operating expenses in a given year would be R\$50,000 and that it chose to be taxed under the *deemed profits regime*.

Taxes levied over the goods:

- (a) *Federal taxes:* For manufactured goods (i.e. not raw materials) IPI will apply.
- (b) *State taxes:* ICMS will apply on the sales of goods.
- (c) *Municipal taxes:* No ISS will apply.

Taxes levied over the services:

- (a) *Federal taxes:* No Federal taxes will apply.
- (b) *State taxes:* No State taxes will apply, as ICMS does not apply over engineering services.
- (c) *Municipal taxes:* ISS will apply over the services revenues and levied by the municipality where the services are provided.

⁵ Or having an individual as a shareholder – Brazilian or otherwise.

Taxes levied over revenues:

- (a) *Federal taxes:* IRRF, AIR and CSLL will be levied.
- (b) *Municipal taxes:* Municipal taxes will be levied over the revenues obtained from the provision of services.

Here is how the taxes will be calculated:

Federal Taxes	Application	Rate and Calculation Method
IRPJ	Levied over deemed income in a given trimester	As the Brazilian entity has chosen the <i>deemed profit regime</i> , 8% of its gross revenues obtained from sale of goods and 32% of its gross revenues will be deemed to be the company's profits. IRRF will be levied at 15% over the deemed profits. Therefore: Revenues from goods: R\$500,000 Deemed profit: R\$40,000 Revenues from services: R\$500,000 Deemed profit: R\$160,000 Total deemed profit: R\$200,000 Total IRPJ payable: R\$30,000 (15% of R\$200,000)
AIR	Levied over deemed profits above R\$60,000 in a given trimester	AIR will be levied at 10% over the deemed profits of the company. As the deemed profits total R\$200,000 in the given trimester, the AIR payable will be R\$14,000 (10% over R\$200,000 minus R\$60,000).
CSLL	Levied over deemed profit	CSLL will be levied at 9% over the deemed profit of the company. As the deemed profit total R\$200,000 in the given trimester, the CSLL payable will be R\$18,000 (9% over R\$200,000).
PIS/COFINS	Levied over gross revenues	PIS/COFINS will be levied at 3.65% over the company's gross revenues. As the gross revenues were R\$1 million, the PIS/COFINS component will be R\$36,500 (3.65% over R\$1 million).
IPI	Levied over the	As the goods are not being imported, the

	sales of manufactured goods	calculation is likely to be the IPI rate multiplied by the amount of the goods sold. For present purposes, we will assume that the IPI applicable is 10%. Considering also our assumption that the IPI credits would be R\$20,000, the IPI component would be \$30,000 (10% over R\$500,000 - R\$30,000 of imputation credits).
State Taxes		
ICMS	Levied over sales of goods	ICMS will generally be levied at the rate of 7% for interstate sales and 18% for intrastate sales. Assuming that the company will be sharing 50/50 between its interstate and intrastate sales, and that it is based in the State of São Paulo, the ICMS payable would be as follows: ICMS payable on interstate sales: R\$17,500 ICMS payable on intrastate sales: R\$45,000 On our assumption that the company had R\$30,000 of ICMS credits, the total ICMS payable would be R\$32,500 .
Municipal Taxes		
ISS	Levied over revenues obtained from services	ISS will be levied at between 2% and 5% over the company's revenues derived from services provided. As in our example the company provided engineering services, it is likely that the municipality will impose a 5% rate on the revenues derived from them, resulting in the ISS payable being R\$25,000.

In sum:

Revenues:

R\$500,000 from the sale of goods
Plus R\$500,000 from the provision of services
Total revenues: **R\$1,000,000**

Less taxes:⁶

IRPJ: R\$30,000

⁶ Note that we are not including in the calculations the taxes payable on the importing of goods or any intellectual property rights.

AIR: R\$14,000
CSLL: R\$18,000
PIS/COFINS: R\$36,500
IPI: R\$30,000
ICMS: R\$32,500 (assuming the company already paid R\$30,000 on importing inputs or the final product for resale)
ISS: R\$25,000
Total taxes: **R\$186,000**

Less inventory and operating expenses:
Assumed for the purposes of the example: R\$250,000

Profits available for repatriation: **R\$564,000.**

As there are **no taxes on repatriation of funds** (other than the 0.38% of IOF payable on the conversion of reals into foreign currency), the New Zealand holding companies would receive the full New Zealand dollars equivalent of R\$564,000.

PART 3: ANNOTATED BIBLIOGRAPHY OF OTHER SOURCES OF INFORMATION ON DOING BUSINESS IN BRAZIL

15. REVIEW OF AVAILABLE SOURCES OF SUMMARISING BRAZIL'S TAX SYSTEM RELATING TO FOREIGN INVESTMENTS

Below we analyse some of the key sources in English that provide useful further information in relation to the Brazilian tax system, including one on doing business generally. There are other guides, such as the *Legal Guide for Foreign Investors in Brazil*, which may be useful in parts but not as useful as the ones below.

15.1. Brazil Business Guide – UK Trade & Investment (UKTI)

Available at:

<http://www.ukti.gov.uk/export/countries/americas/southamerica/brazil/doingbusiness.html>

UKTI's guide does not aim to address taxation issues. However, it is the best guide we found for those with little or no experience in doing business in Brazil. It covers a variety of topics and is directed towards British investors. Given New Zealand's legal and tax system resembling Britain's, New Zealand readers are likely to find UKTI's guide both practical and interesting.

The guide contains a quick summary of the taxes and customs issues relating to exports to Brazil (including relevant documentation, yet from a United Kingdom standpoint).

15.2. Doing Business and Investing in Brazil – PricewaterhouseCoopers

Available at:

http://www.pwc.com/pt_BR/br/publicacoes/assets/doing-business-brazil05.pdf

This guide provides more than just taxation information. It is divided into four parts: Investment Climate, Doing Business, Audit and Accounting and Taxation.

Amongst other matters, the guide covers incentives available to foreign investors, details about the auditing processes and applicable rules, the Brazilian system as a whole, issues relating to the day-to-day tax administration, taxation of Brazilian and foreign companies, taxation of shareholders. Further, the guide covers foreign operations of Brazilian companies and joint ventures.

While the guide covers a number of issues, the information provided is fairly brief. Readers are likely to find useful the points at the outset of each chapter, where you find the key issues relating to each different matter addressed in the guide. The document is well written and easy to understand.

15.3. Investment in Brazil – KPMG

Available at:

http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Documents/inv_brazil_O_0809.pdf

KPMG's guide is very comprehensive. It covers 198 pages in total. The guide is very well structured – the best of the guides available – making it easy for the reader to find the most relevant parts and find the information being sought.

At the outset the guide provides general information about Brazil, including its history and relevant matters relating to Brazil's government and legislative structure. It follows with details about the benefits of setting up a business in Brazil, including an optimistic analysis of the Brazilian macroeconomic potential.

The KPMG guide is more detailed than PricewaterhouseCoopers', providing more in-depth information to readers. On the negative side, was prepared in July 2008 (and, thus, it is not fully up to date in certain parts) and it requires greater attention by the reader to read each of its sections.

15.4. Doing Business in Brazil – Ernst & Young

Available at:

[http://www.ey.com/Publication/vwLUAssets/Doing_Business_in_Brazil_2007/\\$FILE/Doing_Business_in_Brazil_2007.pdf](http://www.ey.com/Publication/vwLUAssets/Doing_Business_in_Brazil_2007/$FILE/Doing_Business_in_Brazil_2007.pdf)

Ernst & Young's guide is also very comprehensive. It covers a wide range of topics that may be relevant to foreign investors, in a variety of different sectors. It spans over 81 pages.

Parts that may be useful to New Zealand businesspeople include chapter C.4, which covers incentives available to foreign investors and chapter C.5, which provides details about funding sources. Chapter C.6 also contains relevant information about the importing and exporting process – which is a major source of headaches to most foreign companies exporting to Brazil. The section on transfer pricing (F.3) is also detailed.

The negative points include the section on joint ventures, which lacks sufficient detail, and the heading under trusts, which oversimplifies how trusts are considered under Brazilian law. The section on corporate taxation is also quite convoluted and difficult to follow and the section on indirect taxes covers less than what is provided elsewhere.

15.5. International Tax and Business Guide – Deloitte

Available at:

http://www.deloitte.com/assets/Dcom-Global/Local%20Assets/Documents/Tax/Intl%20Tax%20and%20Business%20Guides/2010/dtt_tax_guide_2010_Brazil.pdf

Deloitte's guide provides very general information for those with little or no knowledge about the Brazilian tax system. The document is not well structured, with the information being gathered under broad headings.

The two positives in relation to this guide are that it is up to date and that it is only 19 pages long, making it useful for those readers with little time on their hands.

15.6. Company Formation in Brazil – Pinheiro Neto

Available at:

http://www.pinheironeto.com.br/upload/tb_pinheironeto_livreto/pdf/071108092707CompanyFormation_ing.pdf

Although this guide focuses on company formation, it contains sections addressing corporate taxation and a useful table summarising the main Brazilian taxes (paragraph 10.12). It also contains brief explanations on customs procedures (paragraph 10.10.2) and transfer pricing rules.

15.7. Foreign Investment in Brazil – Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados

Available at:

http://www.mattosfilho.com.br/en/FIB_new/index.html (html version)
http://www.mattosfilho.com.br/en/FIB_new/FIB_english.pdf (pdf version)

Unlike the other guides, Mattos Filho's document is also available in an easy-to-read format and clearly defined headings.

Chapter 6 deals with taxation, but goes no further than being a guide. It also translates certain terms in a way that may confuse the reader (such as "real profit system", rather than "actual profit method"). For those with more sophisticated tax structures, the guide contains comments on tax havens that may be useful.

16. GLOSSARY

“**AIR**” means the Additional Tax on Income (*Adicional do Imposto de Renda*);

“**CIDE**” means the Contribution on the Economic Domain (*Contribuição no Domínio Econômico*);

“**COFINS**” means the Contribution for the Financing of Social Security (*Contribuição para o Financiamento da Seguridade Social*);

“**CODECINE**” means the Contribution for the Development of the National Cinematographic Industry (*Contribuição para o Desenvolvimento da Indústria Cinematográfica Nacional*);

“**CNPJ**” means the company’s tax number (*Cadastro das Pessoas Jurídicas*);

“**CPL**” means the Production Cost Plus Profit (*Custo de Produção Mais Lucros*) method used for transfer pricing purposes;

“**CSLL**” means Social Contribution over Net Profits (*Contribuição Social Sobre o Lucro Líquido*);

“**GATT**” means the General Agreement on Tariffs and Trade;

“**Mercosul**” means the Common Market of the South;

“**ISS**” means the Municipal Services Tax (*Imposto Sobre Serviços*);

“**NCM**” means the Common Nomenclature of the Mercosul;

“**ICMS**” means the Tax on the Movement of Goods and Services (*Imposto sobre a Circulação de Mercadorias e Serviços*);

“**IOF**” means the Tax on Credit and Exchange Transactions, Insurance or Securities (*Imposto sobre Operações de Crédito, Câmbio e Seguro ou relativas a Títulos e Valores Mobiliários*);

“**IPI**” means the Tax on Industrialised Products (*Imposto sobre Produtos Industrializados*);

“**IPTU**” means the Tax over Buildings and Land (*Imposto Predial e Territorial Urbano*);

“**IRD**” means New Zealand’s Inland Revenue Service;

“**IRPJ**” means Company Income Tax (*Imposto de Renda de Pessoas Jurídicas*);

“**IRRF**” means Withholding Income Tax (*Imposto de Renda Retido na Fonte*);

“**ITBI**” means the *Intervivos* Real Estate Transfer Tax (*Imposto de Transferência de Bens Intervivos*);

“**ITCMD**” means the Tax on the Transfer Due to Death and Gifts (*Imposto de Transmissão Causa Mortis e Doação*);

“**ITR**” means the Rural Land Tax (*Imposto Territorial Rural*);

“**PIC**” means the Compared Independent Prices (*Preços Independentes Comparados*) method used for transfer pricing purposes;

“**PIS**” means the Program for Social Integration (*Programa de Integração Social*);

“**PRL**” means the Resale Price Less Profit (*Preço de Revenda Menos Lucro*) method used for transfer pricing purposes;

“**RICMS**” means the ICMS Regulations (*Regulamento do ICMS*);

“**TEC**” means the Common External Tariff (*Tarifa Externa Comum*) which applies to Mercosul members; and

“**TIPI**” means the IPI Table (*Tabela do IPI*).