

# BRAZIL

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Currency: Reals (R\$)

Dial Code To: 55

Dial Code Out: 00

## CITY

## NAME

## CONTACT INFORMATION

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## A. TAXES PAYABLE

### FEDERAL TAXES AND LEVIES

**COMPANY TAX:** In general, income is aggregated and subject to a single tax. Corporate taxable income is taxed under a unitary system whereby a single tax rate is applied. This rate is 15%, plus 10% over US\$ 86.000. Corporate income tax generally is computed on an annual basis on 31 December. However, payments are made monthly on estimated advance taxes.

The Social Contribution is another federal tax calculated on net income. This rate is 9% computed on an annual or quarterly basis. Payments are made monthly as estimated advance taxes.

Income tax can also be paid in a percentage of a quarterly sales basis.

Sales up to US\$ 17,000,000 p.a. can make a tax option for Income Tax and Tax Contribution quarterly on a sales basis.

**FRINGE BENEFITS TAX:** Companies participate mandatorily in different forms of social security obligations to federal agencies. These benefit, either directly or indirectly, pension programs, working time compensation, social work assistance, and health programs, among others. All contributions are deductible for corporate income tax purposes.

**COFINS:** Social Security Contribution monthly payment, to meet health, social work assistance and social security program of the Federal Government.

In general all Companies pay 7.6% from total sales monthly on a non-cumulative basis and can be deducted 7.6% of the total materials and services operational costs.

Same as income tax, this tax contribution can be paid on a 3% monthly based on sales but without deductions.

Importation of goods and services pays Cofins of 7.6% but it can be deducted from monthly Cofins payable. Export is exempt of Cofins.

**PIS -** Social Integration Program Contribution monthly, destined chiefly to unemployment insurance funds, professional skill training and yearly bonus to low income workers.

This tax, Companies pays 0.65% of total sales on a monthly non-cumulative basis and can be deducted 1.65% of the operational costs of goods and services.

**Payroll Tax:** Monthly obligation for social security and others levied on payroll.

TAX	RATE (%)
Social Security (INSS)	20
Accident Insurance (SAT)	1,0 to 3,0
Employee Indemnity Guarantee Fund (FGTS)	8,5
Education Fund (SE)	2,5
Other	3,3

Employees contribute monthly to the social security system at the rate of 7.65% to 11% of a progressive-scale base salary with a maximum contribution, of US\$ 895.

Federal law obliges companies to distribute part of their annual net income to employees. Participation is negotiated by each company, and disputes are settled by arbitration. Amounts distributed are deductible for corporate income tax purposes and not subject to social security.

#### LOCAL TAXES:

**Value-Added Sales and Services Tax (ICMS):** This state tax is levied on sales or physical movement of goods, freight, transportation, communications services, and on electric energy. Intrastate transactions are taxed at 18%, interstate transactions 7% to 12%, and most imports 18% to 25%. The lower rates normally are charged on transfers to less-developed states. Some states offer rate reductions or more time for payment as a fiscal incentive for installation of factories. Communication services are taxed at 13% to 35%.

**Real Estate Tax (ITBI):** A property transfer tax is normally payable at a rate of up to 4% on inheritances and donations of properties and rights.

**City Tax:** A services tax is imposed by many cities. Rates vary substantially between municipalities. Higher rates are more common in larger cities. Hospitals, schools, colleges, construction, leasing, tourist and other services pay between 2% and 5%. Entertainment activities are taxed at 10%. Additionally, a real estate tax is also assessed. The annual tax amounts to between 2% and 5% of assessed fair market value of the real property.

Exportation of service is exempt of ISS if the service benefit is overseas.

#### OTHER TAXES:

**Excise Tax (IPI):** This federal value-added is levied on nearly all sales and transfers of products manufactured in or imported into Brazil, depending on the degree of necessity. Examples of rates for various products and groups of products are as follows:

Product	%.
Food in general	0
Soft drinks	44
Alcoholic drinks	11 to 143
Plastic and rubber	0 to 20
Textile materials	0 to 15
Machinery and equipment	0 to 20
Precision instruments	0 to 15
Transport	13 to 35
Other	0 to 60

Most exports are exempt from IPI. Imports are normally taxed at the same rate as Brazilian-made products. Rates change frequently. For all manufactured products, the tax is paid monthly. For imported products, the tax is paid when the goods are released from customs.

**Financial Operations Tax (IOF):** This tax is levied at various rates on financial transactions such as loans and credit operations, insurance policies and foreign exchange operations for certain services rendered. Rates change frequently.

**Rural Real Estate Tax (ITR):** The basic rate is 0.2% per annum on assessed property values but can be increased up to 3.5%, depending on the stage of utilization and exploration of the property.

**Tax on Financial Operations (CPMF):** This tax is calculated on each financial transaction in checking accounts at the rate of 0.38%. The tax is paid weekly and designated to support official health programs.

## **B. DETERMINATION OF TAXABLE INCOME**

To determine the income tax payable, items deductible from gross income include the expenses needed to obtain, maintain and preserve such income. The income tax law contains specific regulations for determining the cost of products, fixed assets, real estate or securities being disposed of, as well as for deducting uncollectible debts and calculating depreciation/amortization. Business income is determined on the accrual basis. Brazil established a transfer pricing system on the importation of goods, services and rights acquired abroad. These prices are based on three methods: Comparative Independent Price (PIC), Resale Price Less Profit (PRL), or Production Cost Plus Profit (CPL). The same system applies for export.

**DEPRECIATION:** Fixed assets may be depreciated over an estimated useful life on a straight-line basis. For real estate the depreciation rate is 4% annually on the portion attributable to the building. For other fixed assets, the depreciation rate varies from 5% to 25% annually. Assets subject to depletion (mines, quarries, etc.), may be depreciated proportionately to the units extracted in each period. In some cases, for new assets used for industrial production, the taxpayer may opt for accelerated depreciation.

**LEASING:** In Brazil there are two types of leasing: financial leasing and operational leasing. In financial leasing, the installments are identified as operational expenditures for tax purposes, provided that leased goods are related to the operational activity of the lessee. Duration of contracts may be from 2 to 3 years, depending upon the useful life of the asset. Residual value is around 1% of the total. Under the operational leasing system, the financed amount may not be higher than 75% of the goods value and the preemption buying value is the market value of the goods.

**STOCK/INVENTORY:** The cost of goods sold for production materials and supplies consumed is on the "average price" method, although the FIFO (first in, first out) basis may be elected. The method adopted determines the basis for the valuation of the closing inventory.

**DIVIDENDS:** Brazil follows a system in which corporate income is taxed to the company. Amounts distributed to shareholders resident in Brazil or abroad are not subject to withholding tax.

**INTEREST DEDUCTIONS:** For companies, there is no limit to interest expense. However, interest has to be related to activities subject to tax. The calculation of interest on a partner's or shareholder's capital is permitted. The interest is deductible for income tax and social contribution, up to the limit of the official long-term interest rate (TJLP). The distribution assumes the existence of profits for the period or for previous periods at a sum equal to or higher than double the value of interest to be distributed. This interest is subject to a 15% withholding tax at source. Interest may be deducted or capitalized.

**LOSSES:** Fiscal losses are offset by up to 30% of fiscal profits. Losses that are offset may be carried over indefinitely. A company, who is a successor by means of incorporation, merging or separation, may not offset fiscal losses of the previous company. Non-compensated losses must be fully absorbed by later profits before by-laws of a corporation can require distribution.

**INCENTIVES:** Brazil offers incentives through the reduction of domestic taxes or non-withholding of tax in the forwarding of royalties or commissions on international financing. In addition to incentives for export, there are incentives for the installation of industrial units in specific regional areas. There are also some programs linked to research activities or technological and cultural activities, in which investments enjoy tax incentives.

### **ROYALTIES AND TECHNICAL ASSISTANCE EXPENDITURES:**

Royalties are deductible expenses when they contribute to the maintenance of the producing source. Deductible expenditures are restricted to a percentage between 1% and 5% of the corresponding sales revenues. Monies paid for the acquisition of invention patents or for manufacturing formulas and processes are considered capital investments and are entered as intangible assets and are amortized over time of utilization of the privilege. The same holds true for the acquisition of the registration of industrial or commercial brands. Outlays with copyright, software and franchising, in a general way, are deductible from operational results if they are related to the activities of the company.

Expenditures for technical, scientific, and administrative expenditures and royalties paid to foreign companies who have direct or indirect control of the Brazilian company are deductible if the contracts are duly registered with the Brazilian Institute of Industrial Property (INPI) and with the Brazilian Central Bank (BCB). There are no restrictions for the remittance of these monies abroad.

### **C. FOREIGN TAX RELIEF**

Profits and gains from foreign sources were taxable. In Brazil, income taxes paid abroad can offset proportionally the profits and Gains that were computed in the result of the company. The losses with foreign investments are not compensated with Brazilian achieved profits.

The profit to be considered for taxation in Brazil is the accounting profit; in case of losses being verified abroad, these will not be compensated by the profits achieved in Brazil.

Beginning 2005, exchange rate variation, on overseas investments is considered financing income/expenses for Social Contribution tax. For Income Tax purpose this will start on 2006.

### **D. REMITTANCES TO ABROAD**

Almost all remittances to companies or persons domiciled abroad are subject to Income tax at the source. The remittance of capital gains or returns of capital is not subject to tax withholding, solely when the exemption has been expressly indicated. The overall withholding tax rate is 15% (25% in special situations), and it may be lesser in the case of remittances of installments of leasing or agreements to avoid double tax.

### **E. CIDE - ECONOMIC TECHNOLOGY CONTROL CONTRIBUTION**

This Tax contribution has the objective to develop the Brazilian technology program.

Overseas services payments will be taxes on 15% for income tax and 10% for CIDE.

### **F. CIDE ON FUELS**

Importation of oil, gas and alcohol, is taxed for Cide based on cubic meters or tons of the import monthly.

### **G. CORPORATE GROUPS**

For tax purposes, consolidation of affiliated companies is not allowed. Losses can only be offset against profits of the same company.

### **H. RELATED PARTY TRANSACTIONS**

Charges from foreign affiliates or head offices are only allowable for specific items related to the local company or branch. A pro-rata allocation of the foreign entity's expenses is generally not acceptable for tax purposes.

### **I. WITHHOLDING TAX**

**Personal Withholding Tax:** All personal income in general is subject to withholding tax at rates of 15% to 27.5%. Payments are monthly and personal income tax is filed annually. Capital gains, not arising out of financial investments, are subject to income tax at 15% to 20%. Stock exchange transactions are taxed at 10% and 20% until 2002.

**Legal entitles:** Basically services rendered by professional companies, financial investments, and remittances abroad are subject to withholding tax at the source, which in some cases may be offset. Rates vary between 1.5% and 15%. Some operations and transactions that generate yield or returns and capital gain are leveled to fixed income investments with the charging of withholding tax at 20%. For foreign investors, the same taxing rules are applicable for transactions of residents in Brazil.

### **J. EXCHANGE CONTROL**

The Central Bank allows the official exchange rate to float freely within periodically established bands, but participation is restricted to authorized dealers. The bank intervenes when there are signs of speculative operations. There is an active parallel exchange market that, although illegal, is quoted in the daily newspapers, as well as an official tourist rate that normally approximates the parallel rate.

## **K. TREATY AND NON-TREATY WITHHOLDING**

Brazil has signed treaties to avoid double taxation with several countries, such as: Argentina, Austria, Belgium, Canada, Chile, People's Republic of China, Czech Republic, Denmark, Ecuador, Finland, France, Germany, Hungary, India, Italy, Japan, Korea, Luxembourg, Netherlands, Norway, Philippines, Portugal, Slovakia, Spain and Sweden.

The overall rate of income tax at the source used in the remittance of interest and royalties is 15%. Currently, there is no tax on the remittance of dividends.

Brazil is a member of a Latin American Integration Association (LAIA) and a signatory to the World Trade Organization (WTO), formerly the General Agreement on Tariffs and Trade (GATT). Until now, membership in LAIA has not affected the size of the market available to local industry and the foreign investor.

Brazil, Argentina, Paraguay and Uruguay are the signatory members of Mercosul (Mercado Comum do Cone Sul), which was officially ratified on 1 January 1995 after a phasing-in period. Under the treaty agreement, most tariffs have been reduced to zero. Movement of labor, goods and services is unrestricted, capital investment encouraged, macroeconomic policies coordinated and foreign trade policies and tariffs for non-member countries harmonized.