

# Overview of the Brazilian tax system for corporate entities

The Brazilian tax system is regulated by the 1988 Federal Constitution as well as special sets of sub law and their revisions. Taxation can be levied at the federal, state and local (municipality) levels. Individuals and corporate bodies are subject to different taxes and are identified separately below.

The Brazilian tax year runs on a calendar year basis. Every business in Brazil needs to complete an annual tax return for the previous calendar year. The deadline for submission of this return is the last working day of June each year. Payment of the main corporate income tax and social security contributions is on a quarterly basis (much like our own quarterly corporation tax instalments, though in Brazil it applies to all companies, and the four quarters of the year are considered independent tax periods). Theoretically it is possible to get a refund if the quarterly instalments are overpaid, though this can be a long process.

## Corporate tax

There are multiple layers of taxation in Brazil. The main corporate direct taxes are, corporate income tax (IRPJ) and social security contributions (CSLL), though there are others. A corporate is

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considered resident in Brazil if it is incorporated in Brazil, and a non-resident company is subject to tax in Brazil if it has a branch or tied agent (legally able to bind the corporate) in Brazil.

IRPJ is currently 15%, with a 10% surcharge on taxable income above R\$240,000 (£86,000).

The main rate of CSLL is currently 9% (Financial Institutions pay 15%) and is based on taxable income of the corporate entity.

## Calculating taxable income

Both of IRPJ and CSLL are a percentage of the taxable income which is calculated on the basis of gross income less allowable deductions (generally, expenses necessary for the commercial

operation of the business). Depreciation is allowed on a straight line basis at various rates depending on the asset class, and there are special provisions for production companies that operate extended hours or around the clock. These companies can be entitled to a rate of up to 150% or 200% of the standard depreciation deduction. Special rules cover exchange gains and losses, royalty payments abroad and certain benefits to directors. There are also enhanced reliefs for research and development activities.

There is an option to tax on a presumed income basis. This involves calculating gross income (turnover) and then applying a presumed profit margin. Tax under this system is still payable quarterly.

Relief is given for losses brought forward (they can be carried forward indefinitely), but the extent to which they can be used is restricted by type and by percentage of taxable profit.

Capital gains of resident corporate bodies are added to the taxable income figure.

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## Withholding taxes

A non-resident corporate is subject to a withholding tax of 15%. A non-resident corporate located in a 'tax haven' is charged a 25% withholding tax. Royalties paid overseas are subject to a 15% withholding tax, subject to treaty relief. This increases to 25% for royalties paid to corporate bodies located in 'low tax' countries. (Note: there is also a special tax on certain transfer of technology or technical assistance payments).

Interest payments are subject to a 15% withholding tax, again with an increase to 25% if the recipient is resident in a 'low tax' jurisdiction.

Dividends are not subject to withholding taxes.

## Transfer pricing

As with most developed tax systems, there are provisions under Brazilian law to prevent multinationals from 'moving' profits. Unusually there is no arm's length principle, instead there is a fixed margin principle using transactional pricing methods (i.e. cost plus or comparable uncontrolled price). Interest rates allowed as deductions are specified, however there are no thin capitalisation rules and, provided loans are registered, the interest expense can be deducted in full.

## Double tax treaties

Brazil has a reasonable number of double tax treaties (28), though there is not one with the UK. The treaty benefits are primarily a reduction in the withholding taxes on interest payments and dividends.

## Indirect taxes

There are three main types of VAT, federal, state and local. Federal VAT covers the manufacture of goods in Brazil and import of goods (exports are exempt). The rate depends on the type of goods being manufactured or imported. State VAT applies to goods and certain services at a rate of between 7% and 18% depending on the

location of the recipient. Local VAT applies to services which are not subject to state VAT, with the rate depends on the type of service.

In addition to VAT there are also indirect social taxes that operate along similar lines to VAT; these contribute to state pension provisions and to a savings initiative.

## Employment taxes

Personal income taxes are withheld monthly from salary payments at rates up to 27.5%.

Social insurance contributions are payable for various different benefits (8% to a length of service guarantee fund, 20% to the public pension system and up to 8.8% for various other social taxes).

## Other taxes

Property transfers are taxed at a rate of between 2% and 6% and there are annual taxes based on the value of the property. Special taxes are currently in place to try to prevent the appreciation of Brazilian currency and the effect it has had on exports.

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## Summary

Brazil is by far the largest of the South American economies, and has a complex tax system. Brazilian assets have been in high demand since the start of the financial crisis as it remained relatively unaffected (having had a fairly closed economy, with exports accounting for only 15% and little reliance on foreign credit).

An investment in Brazil can be very worthwhile, however when putting together the financial model it is important to consider all of the local tax issues. Kingston Smith's Latin American Desk contacts can help you with that process.



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