

BRAZIL CHAPTER

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HIGHLIGHTS

National Level Tax Rates

Corporate Income Tax (IRPJ)	25% ¹
Capital Gains Tax	25% ¹
Branch Profits Tax	25% ¹
Dividends Tax	0%
Withholding Taxes on	
- Interest	15%
- Royalties	15%
- Technical Assistance	15%
- Technical Services	15%
- Administrative Assistance Services	15%
- Other Services	25%
- Remittances to “tax havens”	25% ²
Social Contribution on Net Profit (CSLL)	9% ³
Tax losses carry-forward term	unlimited years ⁴
Tax losses carry-back term	not applicable
Transfer Pricing Rules	Yes
Custom Duties (II)	from 0% to 35% ⁵
Excise Tax (IPI)	from 0% to 330% ⁵
Contribution for the Social Integration Program (PIS) ⁶	
- Non-cumulative system	1.65%
- Cumulative system	0.65%

Contribution for Social Security Funding (COFINS) ⁶	
- Non-cumulative system	7.6%
- Cumulative system	3% ⁷
Tax on Financial Transactions (IOF)	from 0% to 25% ⁸
Tax on Rural Property (ITR)	from 0.03% to 20%

Local Level Tax Rates

VAT on Sales and Services (ICMS)	from 7% to 38% ⁹
Tax on Services (ISS)	from 2% to 5% ¹⁰
Tax on Urban Property (IPTU)	from 1% to 1.5% ¹¹
Tax on Vehicles' Ownership (IPVA)	from 1.5% to 4% ¹²
Tax on Real Estate Transfer (ITBI)	2% ¹¹
Tax on Donation and Inheritance (ITCMD)	from 4% to 8% ¹³

Import Taxes

Imports of services

- Withholding Income Tax (WHT)	15% or 25% ¹⁴
- ISS	from 2% to 5%
- PIS-Import	1.65%
- COFINS-Import	7.6 %
- Economic Intervention Contribution (CIDE)	10% ¹⁴
- IOF	0.38% ¹⁴

Imports of goods

- II	from 0% to 35%
- IPI	from 0% to 330%
- ICMS	from 17% to 38% ¹⁵
- PIS-Import	1.65 %
- COFINS-Import	7.6 %

1 The regular rate is 15% but a 10% surcharge is applicable to taxable profits exceeding BRL 240,000 per year (approximately USD 130,000 - estimated exchange rate: BRL 1.80 for each USD 1.00). The 9% (or 15%) Social Contribution on Net Profit (CSLL) is also levied on corporate profits.

2 See Section 1.1.2.3.

3 The applicable rate to financial institutions and insurance companies is 15%.

4 Tax losses offsetting shall not reduce taxable profits in more than 30% in any given period.

5 The tax rate varies according to the tax classification number and, in general, the bottom rate is applicable to food and medicine meanwhile the top rate is applicable to superfluous products, such as cigarettes.

6 Pharmaceutical, automotive, beverage, tobacco and fuel industries, among others, are subject to specific taxation regimes.

7 Financial institutions and insurance companies are subject to a 4% rate of COFINS.

8 Provisory Contribution on Financial Transactions (CPMF) – a contribution that was levied (0.38%) on actual or virtual withdrawals from Brazilian bank accounts - was eliminated on December 31, 2007. To ensure the tax collection after the CPMF elimination, IOF rates were increased by 0.38% in several cases.

9 The tax rates vary according to the State and the type of good or service. We informed the lowest and the highest ICMS rates considering all Brazilian States.

10 The tax rate varies according to the Municipality and the type of service rendered.

11 The tax rate varies according to the Municipality. The tax rates mentioned apply to the city of São Paulo.

12 The tax rate varies according to the State. The tax rates mentioned apply to the State of São Paulo.

13 The tax rate varies according to the State, subject to a maximum rate of 8%. In the State of São Paulo, a 4% rate applies.

14 WHT rate is 15% if the service is technical or 25% if not. CIDE is only charged in case of technical service. IOF is levied on the amount of the foreign currency exchange agreement.

15 The ICMS rates generally applicable on imports vary according to the State where the importer is established and the goods imported.

TREATY TAXATION

Items of Income¹

Countries	Interest	Dividends	Royalties	Technical Services	Technical Assistance
Argentina ¹⁵	15% ^{2,3}	0%	15% ³	15% ^{3,4}	15% ^{3,4}
Austria ¹⁵	15% ²	0%	10/15% ⁵	15% ⁶	15% ⁶
Belgium ^{7,10}	10/15% ^{2,8}	0%	10/15% ⁹	10% ⁴	10% ⁴
Canada ^{10,15}	10/15% ^{2,8}	0%	15%	15% ⁴	15% ⁴
Chile ^{10,11}	15% ^{12,13}	0%	15% ¹²	15% ^{4,12}	15% ^{4,12}
China ^{10,11}	15% ²	0%	15%	15% ⁴	15% ⁴
Czech Rep. ^{10,15}	10/15% ^{2,8}	0%	15%	15% ⁴	15% ⁴
Denmark ¹⁵	15% ²	0%	15%	15% ⁴	15% ⁴
Ecuador ^{10,15}	15% ²	0%	15%	15% ⁴	15% ⁴
Finland ^{10,11}	15% ^{2,3}	0%	15% ⁹	15%	15%
France ¹⁵	10/15% ^{2,8}	0%	10/15% ⁹	15% ⁶	15% ⁶
Hungary ^{10,15}	10/15% ^{2,8}	0%	15%	15% ⁴	15% ⁴
India ^{10,15}	15% ²	0%	15%	15% ⁴	15% ⁴
Israel ^{10,11,14}	15% ^{2,13}	0%	10/15% ¹⁶	10% ⁴	10% ⁴
Italy ^{10,15}	15% ²	0%	15%	15% ⁴	15% ⁴
Japan ¹⁵	12.5% ²	0%	12.5/15% ¹⁷	12.5%	12.5% ⁶
South Korea ^{10,11}	10/15% ^{2,8}	0%	10/15% ¹⁶	10% ⁴	10% ⁴
Luxembourg ¹⁵	10/15% ^{2,8}	0%	15%	15% ⁴	15% ⁴
Mexico ^{10,11}	15% ^{2,12,13}	0%	10/15% ^{12,16}	10% ^{4,12}	10% ^{4,12}
Netherlands ^{10,11}	10/15% ^{2,8}	0%	15%	15% ⁴	15% ⁴
Norway ^{10,15}	15% ³	0%	15% ³	15% ^{3,4}	15% ^{3,4}
Peru ^{10,11,14}	15% ^{12,13}	0%	15% ¹²	15% ^{4,12}	15% ^{4,12}
Philippines ^{10,15}	15% ²	0%	15%	15% ⁴	15% ⁴
Portugal ^{7,10}	15% ^{2,13}	0%	15%	15% ⁴	15% ⁴
Slovak Rep. ^{10,15}	10/15% ^{2,8}	0%	15%	15% ⁴	15% ⁴
South Africa ^{10,11,14}	15% ^{2,12,13}	0%	10/15% ^{12,16}	10% ^{4,12}	10% ^{4,12}
Spain ¹⁵	10/15% ^{2,8}	0%	10/15% ¹⁶	10% ⁴	10% ⁴
Sweden ¹⁵	15% ^{2,3}	0%	15% ³	15% ^{3,6}	15% ^{3,6}
Ukraine ^{10,11}	15% ^{2,12,13}	0%	15% ¹²	15% ^{4,12}	15% ^{4,12}

Additional Remarks

Brazil has signed tax treaties with the following countries which have not been ratified yet and, therefore, are not currently in force: Paraguay, Russia, Trinidad and Tobago and Venezuela.

In some specific cases, the tax treaties may not impose an actual reduction of the taxation nor provide for a more beneficial treatment in Brazil. By way of example, since payment of dividends by a Brazilian company is taxed at a zero rate according to Brazilian rules currently in force, the treaty provisions that limit the rate applicable to such payments in the source State do not produce any practical effect.

1 This table provides information about the applicable taxation on remittances of funds overseas from Brazil. When the domestic rate is lower than the rate applicable based on the relevant treaty, we informed only the local rate.

2 Exemption is granted if the beneficiary is the government of the other State, its political subdivisions or government owned entities.

3 There is no specific limitation in the treaty, thus the domestic tax rate applies.

4 Deemed as royalties according to the corresponding royalties article of the treaty or the treaty protocol.

5 The 10% rate applies to royalties arising from the use of, or the right to use, any copyright of literary, artistic or scientific work, but not including cinematographic films, films or tapes for television or radio broadcasting and the 15% rate applies to all other cases.

6 Deemed as royalties according to a local ordinance.

7 The treaty does not apply to the CSLL.

8 The 10% rate applies to loans that meet some conditions (e.g., minimum repayment terms).

9 The 10% rate applies to royalties arising from the use of, or the right to use, any copyright of literary, artistic or scientific work, including cinematographic films, films or tapes for television or radio broadcasting and the 15% rate applies to all other cases.

10 Such reductions are only applicable to the beneficial owner of the income.

11 The treaty applies to the CSLL.

12 Such reduction is not applicable if the main purpose or one of the main purposes of any party involved in the transaction from which the income arises is taking advantage of the treaty provisions.

13 Applies to interest on net equity.

14 A legal entity that is a resident of a Contracting State and derives income from sources within the other Contracting State will not be entitled in that other Contracting State to the benefits of the treaty if more than 50% of interest in such legal entity is held by persons who are not resident of the first-mentioned State or of any of the Contracting States. However, such limitation of benefits does not apply if that legal entity carries on a substantial business activity in the Contracting State of which it is resident.

15 It is possible to argue that the treaty applies to the CSLL. However, Brazilian tax authorities may not have the same understanding.

16 The 15% rate applies to royalties arising from the use, or right to use, trademarks and 10% for other cases.

17 The 15% rate applies to royalties arising from the use of, or right to use, trademarks and any copyright on cinematographic films, films or tapes for television or radio broadcasting. The 12.5% rate applies to all other cases.

Overview

1. INCOME TAX

1.1 General Aspects

1.1.1. IRPJ and CSLL Rates

The general statutory IRPJ rate for Brazilian entities (including Brazilian branches of foreign companies) is 15%. A surcharge of 10% is applicable for taxable income exceeding BRL 240,000 per year (approximately USD 130,000¹) or BRL 20,000 per month (approximately USD 11,000) in case of base periods shorter than one year. CSLL is due at a 9% rate (except for financial institutions and insurance companies which are subject to a 15% rate).

1.1.2. Taxable Base

Brazilian legal entities may use one of the three following systems to calculate their taxable income: (a) the Actual Profit; (b) the Deemed Profit² or (c) the Arbitrated Profit³. Since the most usual is the Actual Profit, the considerations below relate to this system. Generally speaking, the taxable income is based on the net profit reported in the company's financial statements (according to the Brazilian Generally Accepted Accounting Principles – "BR GAAP"), adjusted in accordance with the additions and exclusions set forth by the tax legislation.

Laws 11638/07 and 11941/09 introduced relevant changes in the BR GAAP, seeking the convergence of the Brazilian rules with international standards. Such rules have already been:

- (i) considered in the latest instructions and opinions of the Brazilian Securities Exchange Commission ("CVM") and the National Accounting Committee ("Comitê de Pronunciamentos Contábeis" or "CPC"); and
- (ii) regularly approved by the Brazilian Federal Accounting Council ("Conselho Federal de Contabilidade" or "CFC"), being, thus, applicable to all Brazilian companies.

As from 2010, all companies, regardless of the taxation regime adopted (Actual, Deemed or Arbitrated Profit system) must use the Transitory Tax Regime ("RTT"), established by Law 11941/09. Under this regime, the calculation of the IRPJ, CSLL, PIS and COFINS is made using the net profits ascertained according to the accounting rules in force on December 31, 2007 (i.e., prior to the changes mentioned above).

A summary of the calculation of the IRPJ and the CSLL taxable basis could be illustrated as follows:

Net profit before IRPJ and CSLL

[+] Additions

[-] Exclusions

[=] Taxable income before tax losses offsetting

[-] Tax losses offsetting (up to 30% of the taxable income)

[=] Taxable income

[x] 15% IRPJ rate

[x] 10% IRPJ surcharge (on taxable income exceeding BRL 240,000 per year)

[x] 9% or 15% CSLL rate

1.1.2.1. Deductions

As a general rule all costs and expenses paid (or accrued) for the performance of the company's activities/undertakings (necessary, normal or usual expenses) are tax deductible, even if related to excluded and/or exempted income. Some expenses, however, are subject to some deductibility requirements or limitations among which we highlight the following.

(A) Provisions: even if necessary for accounting purposes, they are not regarded as deductible expenses for IRPJ and CSLL purposes, except for those expressly authorized by law (e.g., vacations, 13th month salary and certain technical provisions).

(B) Fringe Benefits: fringe benefits paid to the companies' administrators, officers, managers and/or their assistants can be considered tax deductible expenses provided that the values are included in the taxable income of the corresponding beneficiaries, which shall be individually identified.

(C) Taxes: these expenses are deductible on accrual basis, except for: (i) taxes that are being discussed in Courts and (ii) the IRPJ and CSLL.

(D) Royalties: for deductibility purposes, payments must be done under agreements registered with the Central Bank of Brazil ("BACEN") and the Brazilian Patent and Trademark Office ("INPI"). Moreover, the sum of all royalties, technical assistance and other technology transfer payments due cannot exceed percentages varying from 1% to 5% of the net revenues derived from the sale of products manufactured or sold with the use of the relevant industrial property rights or technological knowledge. Technical assistance payments shall only be tax deductible for the first five years of operation of the relevant company or in the case of introduction of a special production process. Limits are not applicable to the CSLL.

(E) Bonus or Profit Sharing: if paid to officers is not tax deductible for IRPJ purposes; whereas, if paid to employees are fully tax deductible⁴.

(F) Depreciation: straight-line method must be used. The main rates acceptable by tax authorities are⁵:

(rates may vary depending on tax classification)

Asset	% per year	No. of years
Buildings	4%	25
Vehicles (depending on type/use)	10 to 25%	4 to 10
Hardware and software	20%	5
Furniture and fixtures	10%	10
Machine and equipment	10%	10

Depreciation may be accelerated: (i) by use (16 hours of use: additional of 50% on the depreciation rate; 24 hours of use: additional of 100%); or (ii) by incentive (sometimes also applicable to the CSLL).

(G) Losses Resulting from the Equity Pick-up Method of Accounting: such expenses are non-deductible.

(H) Amortization of Premium ("ágio") paid for the acquisition of equity stakes in Brazilian companies (investments subject to the equity pick-up method of accounting): with the changes introduced in the BR GAAP, the amount of premium will probably be different from the one that should be registered in accordance with the accounting rules in force on December 31, 2007. Therefore, the rules that allow the earlier deduction of the premium (e.g., in case of merger of the invested company into the investor or vice-versa) must be carefully analyzed in order to determine its tax treatment. If the earlier deduction is not enjoyed, the premium paid (defined as the difference between the price paid and the equity value of the investment) will only be deductible at the time the investment is sold, disposed or written-off.

(I) Payments (of any kind) to beneficiaries domiciled in tax havens or under privileged tax regimes⁶: only deductible if the following cumulative requirements are complied with: (a) the beneficial owner of the foreign entity, who is entitled to the relevant payment, is identified (the beneficial owner is defined as the individual or

legal entity that is not incorporated with the main or sole purpose of achieving a tax saving and that earns income in their own account, rather than as an agent, fiduciary manager or attorney-in-fact acting on behalf of a third party); (b) the operative ability of the non-resident to carry out the transaction is proved; and (c) any documental evidence of the payment of the price and the receipt of the goods, assets, rights or the use of the services is presented.

1.1.2.2. Exclusions (non-taxable income or income with deferred taxation)

(A) Profits arising from the sale of fixed assets: IRPJ and CSLL may be ascertained and paid on a cash basis in case the price is agreed to be paid, partially or entirely, after the termination of the tax base period following the one in which the sale was performed.

(B) Premium received in the issuance of shares or other kind of securities: exempt from taxation provided that the issuer is a corporation (“Sociedade Anônima”) and that the amount received is registered in a special or capital reserve.

1.1.2.3. Tax Havens and Privileged Tax Regimes

Before 2009, the concept of “tax haven” only encompassed (i) a country or location that does not tax income or that taxes it at rates lower than 20%, and (ii) a country or location which ensures the secrecy regarding the shareholding structure or ownership of legal entities. Law 11727/08 broadened the concept of “tax haven” to reach, as from 2009, not only the countries and locations described above, but also any country or location whose legislation does not allow the identification of the actual beneficiary of the income paid or credited to a nonresident.

Normative Instruction 188 of the Federal Revenue Service, dated August 6, 2002, still in force, lists the countries or locations that must be considered tax havens, as follows: American Samoa, Andorra, Anguilla, Antigua and Barbuda, Aruba, Bahamas, Bahrain, Barbados, Belize, Bermuda, British Virgin Islands, Campione D'Italia, Cayman Islands, Channel Islands (Alderney, Jersey, Guernsey and Sark), Cook Islands, Costa Rica, Cyprus, Djibouti, Dominica, Gibraltar, Grenada, Hong Kong, Isle of Man, Lebanon, Lebuán, Liberia, Liechtenstein, Luxembourg (applicable only to holding companies governed by law dated 7/31/1929), Macau, Madeira Island, Maldives, Malta, Marshall Islands, Mauritius, Monaco, Montserrat, Nauru, Netherlands Antilles, Niue, Oman, Panama, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, San Marino, Seychelles, Singapore, Tonga, Turks and Caicos Islands, United Arab Emirates, US Virgin Islands, Vanuatu, Western Samoa.

Most Brazilian scholars consider it as an all inclusive list, i.e. only the countries or locations expressly mentioned therein should be considered “tax havens”.

Law 11727/08 also introduced the concept of “privileged tax regimes”, which are those that meet one or more of the following requirements: (a) do not tax income or taxes it at rates lower than 20%; (b) grant tax advantages to non-residents without requiring the performance of substantial economic activities in the relevant jurisdiction or conditioned to the non-performance of substantial economic activities in the relevant jurisdiction; (c) do not tax the income earned outside the relevant territory, or tax it at rates lower than 20%; and/or (d) do not allow access to information about the shareholding structure of legal entities, ownership of assets and rights or economic transactions performed.

The concept of privileged tax regime is broad and gives room to a certain level of subjectivity in its analysis. The Federal Revenue Service is expected to issue a new black list describing the cases that fall under the new concept of tax havens and privileged tax regimes. Meanwhile, doubts may arise regarding the scope of such concepts.

1.1.2.4. Transfer Pricing Rules

Such rules apply to the following transactions, if carried out with related parties, parties domiciled in tax havens⁶ or under a privileged tax regime⁶:

- import or export of assets, goods, services and rights; and

- interest revenues or expenses arising from transactions not registered with the Central Bank of Brazil.

Transfer pricing rules do not apply to acquisitions or import transactions involving royalties and the remuneration for the transfer of technological know-how (the Federal Revenue Service has extended such exemption to their exports).

Brazilian tax law adopts a mathematical approach when describing the methods to calculate the transfer pricing benchmarks and, although the domestic transfer pricing rules are inspired by the OECD guidelines, there are relevant differences which must be considered.

The most relevant relates to the concept of related parties, which is broader than the concept of associated enterprises used by the OECD and includes not only the transactions between the legal entity and its branches; headquarters; controlled companies; controlling shareholders; managers and their relatives, but also the transactions with (among others):

- affiliated companies, as defined by Law 6404/76 (Corporation Law);
- companies that participate with the legal entity in a joint enterprise, under a “consortium” or “condominium”;
- foreign legal entities that grant to the Brazilian legal entity (as their agent, distributor or dealer), exclusive rights to buy or sell assets/goods/services/rights; and
- foreign agents, distributors or dealers of the Brazilian legal entity, to whom the latter has granted exclusive rights to buy or sell assets/goods/services/rights.

1.1.2.5. Thin Capitalization Rules

Such rules apply to: (i) interest paid to related parties (as defined by transfer pricing rules) or beneficiaries domiciled in tax havens ⁶, (ii) transactions under privileged tax regimes ⁶, (iii) transactions whose guarantor, trustee, attorney-in-fact or any other intervening party is a related party, a resident in a tax haven or a party subject to a privileged tax regime.

The interest paid or credited to foreign related parties shall only be tax deductible (IRPJ and CSLL) if, concurrently:

- the relevant debt of the Brazilian legal entity, on the interest accrual date, does not exceed twice the net worth value of the related party’s investment in the Brazilian legal entity (individual limit); and
- the total debt of the Brazilian legal entity, on the interest accrual date, does not exceed twice the total net worth value of all investments of related parties in the Brazilian legal entity (collective limit).

The interest paid or credited to residents in tax havens or arising from transactions carried out under a privileged tax regime shall only be tax deductible if, concurrently:

- the relevant debt of the Brazilian legal entity does not exceed 30% of its net worth (individual limit); and
- the total debt of the Brazilian legal entity with residents in tax havens or arising from transactions carried out under privileged tax regimes, does not exceed 30% of the Brazilian legal entity’s net worth (collective limit).

Thin cap rules is to be further regulated by the Federal Revenue Service and have already raised several doubts about its scope.

1.1.2.6. Profits and Other Revenues Earned Abroad

The IRPJ and the CSLL are levied on the worldwide income, which means that Brazilian companies must also consider, when calculating such taxes, the capital gains and profits arising from Brazilian investments abroad,

including profits of branches, affiliate or controlled companies abroad. Such income must be taxed on December 31 of the year when they are accrued and, in the case of profits from the investment in foreign branches, controlled or affiliate companies, according to the balance sheet of the invested legal entity. Exchange variations must be studied on a case-by-case basis.

Losses from Brazilian investments abroad cannot be offset against local profits, but they can be offset against foreign profits derived from the same investment.

The legality of the taxation of profits of foreign legal entities is being discussed before the Brazilian Supreme Court, based on some articles of the Federal Constitution and the Brazilian Tax Code. However, a final decision on this matter has not been granted yet. It is important to note that if the investment is made in a country with which Brazil has signed a treaty to avoid double taxation, its provisions must be analyzed to determine the tax treatment of such income in Brazil.

1.1.2.7. Foreign Tax Relief

Taxes paid abroad on profits of foreign subsidiaries or branches, which are included in the taxable basis of IRPJ and CSLL, can be offset against IRPJ and CSLL due (limits must be observed).

1.1.2.8. Tax Losses Carry-forward / Carry-back

Tax losses can be carried forward without any statute of limitations, provided that the offsetting does not exceed 30% of the taxable basis (“actual profit”) of any given period. No carry-back is allowed.

Non-operating tax losses (i.e., negative results from the disposition of permanent assets) may be offset only against non-operating profits, except in the tax base period when the non-operating tax losses accrue (such losses are subject to the 30% limit mentioned above).

A restriction to the tax losses offsetting is imposed in case of change of control and business activities. Accordingly, a company cannot offset its tax losses if from the date of the accrual of such losses to the date of their offsetting, a change in the control of the company and in the company’s business activities occur concurrently.

In case of a spin-off, the company’s tax losses forfeit proportionally to the spun-off part of its net worth. In the case of merger, the merged company’s tax losses cannot be offset against the profits of the company in which was merged.

1.1.2.9. Dividends and Capital Reductions

Distribution of profits/dividends arising as of January 1, 1996 is exempt from income tax, regardless of the beneficiary of the income (individual or legal entity, resident or non-resident). The capital increase with profits arising prior to that date is exempt but subsequent capital reductions can be taxable according to specific provisions. Capital refunds in assets are allowed either at book or market values. In the latter case, the difference between the market value and the book value shall be considered as a taxable capital gain for the invested company, rather than for the recipient shareholder (individual or legal entity).

1.2. Payment and Filing

Under the “Actual Profit”, the IRPJ and the CSLL may be quarterly or annually calculated (according to the taxpayer’s option)⁷.

Taxpayers that calculate their corporate taxes quarterly must pay such taxes up to the last business day of the month following the end of each quarter.

Taxpayers that calculate their corporate taxes annually must make advance monthly payments until the last business day of the month following that on which the taxable event occurs. Such advance payments are calculated on either the actual or estimated income⁸, whichever is lower (at the option of the taxpayer). The difference between the IRPJ and the CSLL calculated on the annual tax return and the advance payments must

be paid up to the last day working day of January or March following the end of the fiscal year, increased, in the last case, by legal interest as from February 1 or, if negative, can be offset against taxes due by the taxpayer as from January 1.

In general, the Corporate Income Tax Return must be filed up to the last business day of June following the end of the fiscal year (Brazilian fiscal year coincides with the calendar year).

1.3. Penalties for Unpaid Tax or Tax Paid Belatedly

Unpaid taxes or taxes paid belatedly are charged with interest calculated by an index, known as SELIC (“*Sistema Especial de Liquidação e Custódia*” – Special System for the Settlement and Custody). For 2009, the SELIC corresponded to 9.5%.

Fines are also imposed on the principal. At the federal level, the following fines apply: (a) delayed payments: daily 0.33% up to a maximum of 20%; (b) tax assessments: 75% (general rule), 112.50% (cases in which the taxpayer does not present documentation if requested by the tax authorities), 150% (clear evidences of fraud) and 225% (fraud and refusal by the taxpayer to collaborate with the tax authorities). Discounts can be granted if the payment is made within certain deadlines.

1.4. Cross-border Payments

1.4.1. Withholding Tax (WHT)

The WHT is levied on the income earned by non-residents from a Brazilian source (income paid, transferred, credited, delivered or otherwise made available to a non-resident).

1.4.1.1. Dividends

Remittances of dividends arising from profits generated as of January 1, 1996 are not subject to WHT, regardless if the beneficiary is an individual or legal entity, resident or non-resident.

1.4.1.2. Royalties, Technical Assistance and Technical / Administrative Services

Such remittances are subject to a general 15% WHT (other taxes are levied on such remittances as shown in the Highlights above – Imports of Services). Such 15% rate may be reduced by applicable provisions of Double Taxation Treaties. A higher 25% rate is applicable to remittances made to tax havens. According to local legislation, technical service is any work which execution depends on specialized professional knowledge, regardless any technology transfer.

1.4.1.3. Other Services

Remittances for services not qualified as technical services or not included in the previous item are subject to a 25% WHT (other taxes are levied on such remittances as shown in the Highlights above – Imports of Services).

1.4.1.4. Interest

Payments of interest on foreign loans are generally subject to a 15% WHT (such rate may be reduced by applicable provisions of Double Taxation Treaties). A higher 25% rate is applicable to remittances made to tax havens.

1.4.1.5. Capital Gains

Capital gains are subject to a 15% WHT (rate is increased to 25% if the seller is domiciled in a “tax haven”).

Until Law 10833/03 was passed, capital gains deriving from the sale of a Brazilian asset closed between two non-residents were not subject to taxation. However, article 26 of this law provides that the attorney-in-fact of the non-resident buyer is responsible for the payment of the income tax on the capital gains earned by the non-resident seller, thus raising controversies regarding this matter.

1.4.1.6. Tax Treaties

Treaties to avoid double taxation generally limit the WHT on certain remittances to 15%.

2. OTHER TAXES

2.1. Excise Tax (IPI)

IPI is a federal tax charged on the import or shipment of goods imported or manufactured. The law defines that, for IPI purposes, manufacturing is the process which modifies the nature, functioning, finishing, presentation or purpose of a product or that improves a product for consumption, such as its conversion, improvement, assembly, packaging, repackaging or restoration.

The taxable basis on imports is the cost, insurance and freight (CIF) price (in compliance with customs valuation rules), plus custom duties. The taxable basis on the shipment of goods in the domestic market is the value of the relevant transaction, as provided by the law. The transactions between related parties are subject to a minimum taxable basis defined by law.

IPI rates vary according to the essentiality of the good (pharmaceutical products, for instance, are subject to zero rates, whereas sumptuous or superfluous articles can be taxed by rates of up to 330%) and its classification under the IPI Table of Rates (“TIPI”), which adopts the same nomenclature used in the Mercosur Common Nomenclature / Harmonized System (“NCM/SH”). IPI rates generally range from 5% to 30%.

IPI is a value added tax, calculated by netting of credits for imports and domestic purchases, and debits from taxable transactions. Exports are not taxed by IPI, but the exporters have the right to keep the related tax credit. The purchase of fixed assets does not imply the appropriation of IPI credit.

2.2. VAT on Sales and Services (ICMS)

ICMS is a state tax levied on:

- (a) imports of goods;
- (b) domestic circulation of goods (note that the tax triggering event is the shipment of the goods instead of the closing of sales or other taxable transactions);
- (c) inter-municipal or interstate transport services (including services originating from abroad); and
- (d) communication services (including services originating from abroad).

Exports of goods and services and financial transactions with gold (financial asset) are not subject to ICMS. Export exemptions shall not impair the taxpayers’ ICMS credit rights, as provided by the Constitution.

Transportation services rendered within the territory of the same municipality are not subject to ICMS, but rather to the ISS. ICMS can be levied on services rendered with the sale of goods, if such services are not reached by the competence of the municipalities to charge the ISS.

Generally, ICMS taxable basis are:

- (a) for imports of goods: the CIF price, plus II, IPI, PIS/COFINS and ICMS (which must be included in its own taxable basis);
- (b) for the circulation of goods: the sales price or value of other taxable transactions, as provided by the law, including PIS and COFINS (IPI shall not be included in the ICMS taxable basis in case of goods for resale or manufacturing inputs; IPI must be included in ICMS taxable basis on transactions with end customers);
- (c) for transportation and communication services: the remuneration charged by the service

provider, plus ICMS, PIS and COFINS (which must be included in its own taxable basis).

Applicable rates on imports, circulation of goods within the territory of the same State and interstate transactions whenever the recipient is not an ICMS taxpayer vary from state to state. Generally ICMS rates are:

- (a) 17% (North, Northeast and Middle West states), 18% (South and Southeast states) on imports and circulation of goods within the territory of the same State and interstate transactions whenever the recipient is not an ICMS taxpayer;
- (b) 25% on communication services; and
- (c) 12% on transportation services.

According to the Brazilian Constitution, a Senate resolution shall provide for interstate rates on transactions executed between ICMS taxpayers. Currently, such rates are:

- (a) 7% on shipments from taxpayers based on the South/Southeast to taxpayers based in the North/Northeast/Middle West and state of Esp rito Santo; and
- (b) 12% on other interstate transactions.

In case of imports of goods, ICMS shall be paid to the state where the importer is based. Disputes among States arise when the recipient is not the ultimate importer.

Regarding the circulation of goods, the tax shall be paid to the state of origin of the goods, as a general rule, except for interstate transactions with petroleum, liquid gas and energy.

In case of transportation services, ICMS shall be paid to the state where the service starts, irrespective of the place where contractors and service providers are based.

In case of communication services, ICMS shall be paid to the state: (i) where the user is domiciled, when the service is rendered through satellite; (ii) where the service is charged; or (iii) where the service provider is based, in case the service is pre-paid by card or similar.

ICMS has also been designed based on the principle that the overall tax burden shall be the same, irrespective of where the goods are produced or the services are performed. For this reason, in case of interstate transactions with fixed assets and goods for own consumption between ICMS taxpayers, the recipient of the goods must pay the ICMS for the state of destination on the value of the transaction at a rate corresponding to the difference between the internal rate and the interstate rate.

ICMS is a value added tax. Hence, taxpayers shall book (i) credits for the ICMS paid on imports or passed on to the price of goods and services and (ii) debts for sales or other taxable transactions. Generally, the tax related to the domestic circulation of goods and services to be periodically collected shall be calculated by netting credits and debts.

Generally, taxpayers cannot book ICMS credits for exempt or non-taxable operations and services and will cancel ICMS tax credits in the case of subsequent exempt or non-taxable operations.

Currently, several transactions are subject to ICMS tax substitution rules. This system consists in the collection of the ICMS by certain participants in the supply chain, determined by law, that shall calculate and pay the tax due in former or subsequent transactions with the goods.

In general, the manufacturers and importers are subject to the tax substitution system. They shall pay the ICMS levied on their own operations, as well as the tax levied on subsequent taxable operations within the State until the product is delivered to the end consumer (ICMS due by tax substitution).

In case of interstate sales, if the state where the supplier/taxpayer is based does not impose the tax substitution system, the company's establishments based in said State only shall pay the tax levied on their own operations (interstate circulation of products).

As determined by Supplementary Law 87/96, in general, the State of destination, where this system is applicable, charges the ICMS-ST (for subsequent taxable transactions carried out within the State until the product is delivered to end consumers) from the purchaser upon the arrival of the goods in its territory.

ICMS incentives and benefits can only be granted by Conventions signed by all federal states to avoid a tax war between different states. Several Brazilian states, aiming at attracting new investments, grant ICMS incentives, such as ICMS refunds, deemed credits, tax exemptions, without such approval.

Parties interested in such incentives shall consider related risks, as the states that receive services or goods from the states that granted the incentives irregularly may challenge the benefit, by means of, for instance, refusing to grant tax credits for the relevant transaction. Because this subject is a source of several disputes, it is being discussed in the proposals under analysis for the Brazilian tax reform.

2.3. Tax on Services (ISS)

ISS is the municipal tax on services levied on the import and the rendering of services listed in Federal Supplementary Law 116/03.

Said law has fixed the ISS maximum rate at 5% and the minimum rate at 2% (some municipalities adopts lower rates, against the law) and ruled the ISS exemption on exports, defining exports as the rendering of services to non-residents as long as the results of such services are not produced in Brazil. Such definition has raised serious concerns, as there is no clear criteria to identify what should be understood by "results produced in Brazil".

Taxpayers are the service providers. However, in the case of imports of services, the importer is responsible for the calculation and collection of the tax due by the foreign party. The ISS taxable basis is the service price and tax rates vary from municipality to municipality by type of service.

As a general rule, the tax must be paid to the municipality where the establishment performing the service is located. However, there are some exceptions to this rule depending on the type of service. For instance, in case of performance of civil construction, hydraulics or electrical engineering services, the ISS is due to the municipality where the service is provided.

Supplementary Law 116/03 allows the municipalities to determine that the engaging party is liable for the withholding and payment of the ISS in certain cases.

2.4. Contribution for the Social Integration Program (PIS) and Contribution for Social Security Funding (COFINS)

PIS and COFINS are federal social security contributions levied on:

- (a) revenues earned by legal entities, with few exceptions (e.g. dividends and revenues derived from exports of goods or services are not taxed, in the last case as long as the export revenues are cashed in Brazil) and
- (b) imports of goods and services. In such cases, taxable basis are, respectively: (i) customs value of the goods plus ICMS and the same contributions (PIS and COFINS must be included in their own taxable basis) and (ii) amounts paid or credited for imports of services, plus WHT, ISS and the same contributions (PIS and COFINS included in their own taxable basis). The Federal Revenue Service has described how PIS and COFINS shall be calculated in this case.

PIS and COFINS are mainly calculated according to the non-cumulative or cumulative systems, which may coexist on a case by case basis. Exemptions and specific rules apply to certain businesses and certain income on

a case-by-case basis.

PIS and COFINS are highly regulated taxes and represent a significant share of the overall Brazilian tax collection. Disputes and controversies are frequent in this field, especially regarding the right to tax credits.

2.4.1. Non-cumulative System

PIS and COFINS are levied on gross revenues of legal entities at rates of 1.65% and 7.6% respectively. Nowadays, financial revenues are subject to a zero percent rate, except for a few cases.

The taxpayer is entitled to tax credits provided by law to offset PIS and COFINS debts, generally corresponding to the rate of each contribution (1.65% and 7.6%), among which we highlight the following:

- (a) contribution paid on (i) domestic purchases or imports of goods for resale or manufacturing inputs and (ii) services hired by the taxpayer to provide services to its customers and/or for producing goods for sale or renting;
- (b) expenses with electric energy, rent of buildings, rent or lease of machines and equipments used for the activities of the taxpayer and transportation costs relating to sales; and
- (c) depreciation expenses relating to fixed assets imported or purchased in the domestic market and used in the manufacturing process, for renting or for the rendering of services (alternatively, such credit can be calculated at 1/48 per month of the cost of acquisition of the relevant fixed asset – general rule – or at 1/24 per month of the same cost in certain cases).

As the law restricts tax credits, the PIS and COFINS tax burden is significant.

Generally, legal entities that calculate their corporate taxes (IRPJ and CSLL) based on the actual profit system are subject to PIS and COFINS based on the non-cumulative system. However, the cumulative system is mandatory in some cases, irrespectively of the method chosen for the calculation of the IRPJ and CSLL.

If a company has activities/revenues subject to the cumulative and non-cumulative systems, PIS and COFINS tax credits must be proportioned to the revenues subject to the non-cumulative system.

2.4.2. Cumulative System

In the cumulative system, operational revenues earned by legal entities are taxed at the rates of 0.65% (PIS) and 3% (COFINS). The taxpayer has no tax credits for the contributions paid on imports or relating to domestic purchases and expenses incurred.

Based on paragraph 1 of article 3 of Law 9718/98, non-operational revenues, including financial revenues, should be included on PIS and Cofins taxable basis in the cumulative system. Such provision was revoked by Law 11941, issued on May, 2009. This happened in line with decisions rendered by the Federal Supreme Court, which determined that the referred provision was unconstitutional. However, for the period before May, 2009, the right to exclude non-operational revenues from PIS and Cofins taxable basis depends on a judicial decision on the matter for each legal entity.

Generally, legal entities that calculate their corporate taxes (IRPJ and CSLL) based on the deemed profit system are subject to PIS and COFINS according to the cumulative system (in some cases, the cumulative system is mandatory, irrespectively of the method chosen for the calculation of the IRPJ and CSLL – e.g. civil construction until the end of 2010).

2.4.3. Specific PIS and COFINS Rules

Specific rules apply per type of revenue or activity, such as:

- (a) financial institutions;
- (b) pharmaceutical, automotive, beverage, and tobacco industries;
- (c) fuel industry; and
- (d) hygiene and cosmetics products.

Among such specific rules, we highlight:

- (a) tax centralization rules, by means of which PIS/COFINS are charged only once, from a chosen person of the relevant market chain; and
- (b) tax substitution rules, by means of which a person appointed by the law must be liable to calculate and collect PIS/COFINS due by other persons, on past or future transactions (in the latter case based on estimate prices).

Such tax centralization and tax substitution rules are frequent in sectors with high informality levels. A tax substitution system applies, for instance, to tobacco industries, in which case importers and manufacturers will be liable for the taxes due at the retail level.

2.4.4. PIS-Import and COFINS-Import

According to Law 10865, since 2004 PIS and Cofins are due on imports of goods and services generally at the rates of 1.65% and 7.6%, respectively.

Regarding these transactions, the taxpayer subject to the non-cumulative system is usually entitled to tax credits.

2.4.5. PIS and COFINS Withholdings

Among other cases, PIS and COFINS withholdings are required:

- (a) on payments for certain professional services rendered by legal entities to other legal entities, at rates of 0.65% and 3% respectively, as prepayments of the beneficiary's contributions, regardless of whether such beneficiary is taxed based on the cumulative or non-cumulative system; and
- (b) on payments made by the federal administration to Brazilian legal entities for goods supplied or services rendered, at rates of 0.65% and 3% respectively, regardless of whether such beneficiary is taxed based on the cumulative or non-cumulative system (state and municipal administration may comply with this withholding obligation as agreed with the federal administration).

2.5. Economic Intervention Contribution (CIDE) on Payments of Royalties, Technical Services and Administrative Assistance

CIDE is a Federal contribution levied at a 10% rate on the amounts paid, credited, transferred, delivered or otherwise made available to non-residents for technology transfer or technology license agreements, patents and trademarks licenses, technical assistance, technical and administrative services⁹ and any agreement involving royalty payments.

In case of service fees, WHT and ISS shall be included in the CIDE taxable basis. A CIDE tax credit is granted for payments of royalties for patents and trademark licenses¹⁰ which may be offset against the amounts to be paid as CIDE in subsequent remittances of the same nature.

2.6. Tax on Financial Transactions (IOF)

IOF is levied on credit, exchange and insurance transactions, as well as on securities at variable rates.

Credit transactions are subject to the IOF at a 0.0041% daily rate and to a 0.38% surcharge. Foreign currency exchange transactions are subject to a general 0.38% rate. Insurance transactions are generally subject to the IOF at rates varying from 0% to 7.38%. Securities transactions are subject to the IOF at rates that vary according to the type of investment and investment period. Generally, floating income investments and fixed income investments for 30 days or more are subject to a zero percent rate.

2.7. Property Taxes

2.7.1. Urban Property Tax (IPTU)

IPTU is a municipal tax levied annually on the ownership or possession of any real estate located in urban areas. The taxable basis corresponds to the fair market value of the property at a rate that may vary according to the Municipality and the use and price of the real estate.

In the city of São Paulo, IPTU rates range from 1% to 1.5% with discounts or additions granted based on the market value (calculated as provided by the Municipal law) and use of the relevant property.

2.7.2. Tax on Vehicles’ Ownership (IPVA)

IPVA is a state tax levied annually on the ownership of vehicles (car, trucks, buses, tractors, boats, yachts and aircraft ¹¹). The taxable basis corresponds to the fair market value, determined every year by the State Treasury Secretariat, that takes into consideration the brand, model and age of the vehicle. The applicable rate may vary according to each State. In São Paulo, for instance, the tax rate varies from 1.5% to 4%.

2.7.3. Tax on Rural Properties (ITR)

ITR is a federal tax levied annually on the ownership or possession of rural property (real estate located outside the urban zones of the cities). The Federal Union may enter into conventions with Municipalities to delegate to such Municipalities the duty to inspect and collect the ITR.

The taxable basis is the value of the taxable area, which shall be calculated in accordance to specific rules. Tax rates vary depending on the total area of the property and level of use of the areas that can be exploited for agricultural purposes, according to the table of rates below.

Total Area of the Property (per hectares)	Utilization Rate - GU (%)				
	Above 80	Above 65 up to 80	Above 50 up to 65	Above 30 up to 50	Up to 30
Up to 50	0.03	0.20	0.40	0.70	1.00
Above 50 up to 200	0.07	0.40	0.80	1.40	2.00
Above 200 up to 500	0.10	0.60	1.30	2.30	3.30
Above 500 up to 1,000	0.15	0.85	1.90	3.30	4.70
Above 1,000 up to 5,000	0.30	1.60	3.40	6.00	8.60
Above 5,000	0.45	3.00	6.40	12.00	20.00

Constitutional Amendment 42/03 has confirmed ITR progressive rates and granted an ITR tax exemption to small sized rural property exploited by its owner, who does not have any other real estate. Note that ITR has been an important tool to discourage unproductive rural properties.

2.8. Tax on Real Estate and Related Rights Transfer (ITBI)

ITBI is a municipal tax levied on *inter vivos* and remunerated transfers of ownership or *in rem* rights over a real estate. The taxable basis corresponds to the fair market value of the property at a rate that may vary according to the Municipality. In the city of São Paulo, the general rate is 2%.

This tax is not levied on the contribution of a real estate and/or *in rem* rights in exchange for capital of a legal

entity or on ownership transfers resulting from corporate reorganizations, such as mergers, spin-off or liquidation, except if, in any such cases, the acquirer's core activity is trading or leasing real estate as provided by the law.

2.9. Donation and Inheritance Tax (ITCMD)

ITCMD is a state tax levied on donations or inheritances. The taxable basis corresponds to the fair market value or value of the relevant donation or inheritance. Applicable rates vary from State to State, subject to a maximum 8% rate. In São Paulo, ITCMD is charged at 4%.

3. CUSTOMS DUTIES AND EXPORT TAXES

3.1. Customs Duty (II)

II is a federal tax levied on imports of goods and charged for the clearance of such goods from customs.

Generally, II taxable basis is the CIF value, with due regard to the 1994 General Agreement on Trade and Tariffs (GATT) customs valuation rules. The Agreement describes six methods, which may be successively applied in order to ensure that II is paid on market prices.

Applicable rates vary per imported item - according to the relevant tax classification under the Mercosur Common External Tariffs Table ("TEC-SH"), organized based on the Mercosur Nomenclature (which is based, in turn, on the Brussels Nomenclature) - and may range from 0% to 35%. II is not a VAT.

Please note that IPI, PIS/COFINS and ICMS are also levied on imports of goods, as described above.

3.1.1. Special Customs Regimes Available

Brazilian law allows the admission of imported goods into the Brazilian territory without the immediate payment of taxes, under special import regimes, as long as certain requirements are met. The most common regimes are as follows.

(A) Temporary Admittance of Foreign Goods

Under this regime, some goods are admitted into Brazil for specific purposes and for a certain term, with total or partial suspension of the relevant federal taxes levied on imports.

The total tax suspension is usually applicable in the case of goods imported for sport competitions, artistic and cultural exhibitions, scientific and trade fairs. If the imported goods are nationalized, the corresponding taxes will be levied as if the tax suspension had never taken place.

The partial tax suspension applies to goods imported for economic purposes, such as the rendering of services or the manufacturing of other goods (e.g., import of equipment and machines under operational lease agreements). When such goods are admitted into the national territory, relevant taxes are charged proportionally to their respective useful life and term of stay in the country.

If such imported goods are nationalized, relevant taxes are due according to the remaining time of their useful life. Among other requirements, for the partial tax suspension, a guarantee must be provided.

The total/partial tax suspension applies to Custom Duties, IPI and PIS/COFINS on imports, and an ICMS exemption or a taxable basis reduction may apply, as provided by the law of each state, as authorized by the Agreement no 58/99.

(B) Drawback

It is applicable to the import of goods used for manufacturing products to be exported or that had already been

exported. The regime allows (i) the suspension of taxes due on imports provided that the taxpayer uses the imported products to manufacture products to be exported within a specified term (generally one year, but it may be extended for the same term); or (ii) the exemption of the federal taxes due on imports for replacement of stocks of imported goods subject to taxes and used in the manufacturing of products that had already been exported.

If such exports are not carried out (or if exported amounts are lower than the amounts that should be exported) the taxes suspended must be paid with penalties and interest.

In case of suspension of federal taxes (Custom Duties, IPI and PIS/COFINS on imports), an ICMS exemption may be granted, as provided by the law. In case of exemption of federal taxes, the drawback will not be applicable to the ICMS.

This special regime (drawback suspension) can be combined with drawback “green – yellow” (drawback “verde – amarelo”), in which the taxpayer can buy inputs in the domestic market to manufacture products to be exported. This tax benefit does not apply to ICMS.

(C) Bonded Warehouse

Under this regime the goods are admitted into consignment in Brazil for a period of one year (which may be extended for two more years from the time custom clearance) and the payment of import taxes is suspended as long as the goods are stored at certain customs areas.

The beneficiary of the regime shall be liable for the stored goods and for all measures required for the nationalization of such goods, as the case may be (the goods belong to the consignor as long as stored at the bonded warehouse).

This regime applies to Custom Duties, IPI, ICMS and PIS/ COFINS on imports.

(D) Industrial Warehouse (RECOF)

According to this regime the industrial establishment remains under customs control and the taxes are suspended provided that the beneficiary exports a minimum amount of goods manufactured with imported raw-materials. This regime applies only to manufacturing of products related to aviation, vehicle, telecommunication, information and high technology electronics fields.

If the minimum amount is not exported after a certain period of time, taxes will be charged as in an ordinary import, increased by penalty and interest and the beneficiary’s right to the RECOF benefits may be cancelled.

To be entitled to this regime the company must, among others: (i) have a net worth equal or greater than BRL 25 million (approximately USD 14 million); (ii) undertake to export goods manufactured with imported inputs equivalent to 50% of the total imported goods and not less than USD 10 or 20 million per year, depending of the manufacturer’s activity; (iii) use, in one year, at least 80% of the imported inputs on the manufacturing process; and (iv) have a computerized stock control system accessible by Federal Revenue Service Agents. This regime is applicable to Custom Duties, IPI and PIS/ COFINS on imports.

3.2. Export Tax (IE)

Export tax is a federal tax levied on exports of national or nationalized products, imposed when the products leave the Brazilian territory. Generally speaking, the taxable basis is the export price of the product. The rate may vary according to the tax classification number of the product, but, currently, the rate is zero for virtually all products, except for (i) leather, fur and dead animal skin, which are subject to the tax rate of 9%; and (ii) cigarettes and guns destined to Latin America, subject to tax rate of 150%.

4. PAYROLL TAXES / WELFARE CONTRIBUTIONS

4.1. Social Security Contributions

The Brazilian Social Security System is basically funded by contributions of both companies and employees. These contributions are levied on the employee's overall salary. The companies' contributions vary from 26.3% to 31.8% (aggregate rates), according to the company's activities, the company's Accident Prevention Factor (FAP) which is calculated, among other factors, based on the company's accident occurrence index, and include, among other contributions, the contribution to fund Social Service and Training Programs (such as SESI, SENAI, SESC and SENAC).

The employees' contribution must be withheld by the employer at rates varying from 8% to 11%, as provided by law, limited to a maximum monthly contribution of BRL 375.82 (approximately USD 209). As for third service providers (individuals), the companies must: (a) contribute with 20% of their overall compensation and (b) withhold 11% of said compensation, on behalf of such professionals (in this latter case the limit of BRL 375.82 also applies).

4.2. Severance Indemnity Fund (FGTS)

The employer must make monthly deposits in accounts opened for each employee with a governmental financial institution. Such funds can only be withdrawn by the employee in certain circumstances. Currently, the total FGTS cost corresponds to 8% of the employee's overall compensation.

In case of dismissal without cause, the employer is also subject to pay a penalty corresponding to 50% of the total FGTS deposits it has made in the employee's account (40% deposited in said bank account and 10% paid to the Federal Government).

5. TAX INCENTIVES

5.1. Free Trade Zones

5.1.1. Manaus Free Trade Zone ("ZFM")

ZFM incentives are granted by the Brazilian Constitution until 2023 and comprise federal, state and municipal tax benefits, such as:

Federal taxes incentives:

- II: up to 88% tax reduction on several inputs used in the manufacturing process at ZFM according to a Basic Producing Process defined by law;
- IPI: exemption on imports of certain inputs to be manufactured or consumed at the ZFM, on shipment of products made in Brazil to ZFM for consumption in the region and on shipment of products manufactured in ZFM to other regions within the national territory, including ZFM;
- IRPJ: tax reduction for applications filed with the ZFM until December 31, 2013;
- PIS and COFINS: 0% on imports from ZFM of (i) inputs to be manufactured at the ZFM and (ii) fixed assets listed in Decree;
- PIS and COFINS: 0% on revenues arising from sales by legal entities based outside ZFM of goods to be consumed or manufactured inside ZFM and on revenues arising from sales of raw-materials, intermediate products and packaging materials by legal entities based inside ZFM to ZFM companies;
- PIS and COFINS: reduced rates on sales of products manufactured by ZFM (provided that certain characteristics of the purchaser are met).

State taxes incentives:

- ICMS: exemption on the shipment of national products from other Brazilian States to ZFM companies;

- ICMS: tax refund for companies established in ZFM on the shipment of goods to other States, varying from 55% to 100% of the tax accrued.

5.1.2. Other Free Trade Zones

There are other free trade zones in Brazil, to which similar benefits apply. Similar IPI benefits are also granted to taxpayers based in the West Amazon region (States of Acre, Rondônia, Roraima and Amazonas).

5.2. Regional Development Incentives

Companies in the North, Northeast and in certain States in the Middle West (Mato Grosso) and Southeast (certain areas of Espírito Santo and Minas Gerais) can benefit from federal, state and municipal incentives.

The most important one relates to the IRPJ, which is expected to expire in 2013. In general terms, a 75% IRPJ reduction can be granted for a period of up to 10 years to activities considered of priority (as defined by Presidential Decrees) for the development of those regions. The benefit shall be approved by the Federal Revenue Service based on a prior technical analysis of the Amazon and Northeast Development Superintendence (SUDAM/SUDENE).

Special rules (“lucro da exploração”) apply for the calculation of the incentive. The tax waiver must be registered as a profit reserve and can only be used to offset losses or increase the company's capital (cannot be distributed to its partners).

5.3. Technological Innovation Incentives

Applicable to legal entities that carry out researches of new products, new manufacturing processes and improvements in quality, productivity and competitiveness of existing products and manufacturing processes.

IRPJ and CSLL benefits:

- Deduction of expenses with technological innovation R&D and payments of certain royalties;
- Exclusion of certain percentages of amounts paid as technological R&D, patented technological development or registered cultivars;
- Full depreciation in the year of acquisition of new assets used in the technological R&D;
- Accelerated amortization of amounts paid to purchase intangibles linked to the technology innovations R&D;

Other benefits:

- 10% credit of the tax withheld on payments or credits to non-residents of royalties, scientific or technical assistance and technical service fees. Valid until December 31, 2013 upon compliance of certain requirements;
- 0% rate for payments or credits to non-residents for the registration and maintenance of trademarks, patents, and cultivars abroad;
- 50% reduction of the IPI levied on the purchase of assets destined for technological R&D;
- Government subvention of up to 60% of the value of the remuneration of researchers holding masters or PHD degrees.

5.4. Other Incentives

Culture, Sports	Reduction of the IRPJ due of percentages of the amounts
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and Audiovisual Activities	invested in approved cultural or sports projects or approved Brazilian independent films. Conditions must be met.
Informatics and Automated Products Incentives	<p>IPI reduction of:</p> <ul style="list-style-type: none"> - 13% (until 2014), 18% (2015) and 23% (until 2019), if established in the regions under the jurisdiction of the Amazon and Northeast Development Superintendence (SUDAM/SUDENE) - 80% to 95% (until 2014), 75% to 90% (2015), 70% (until 2019), if established in other Brazilian regions <p>Reductions are granted regardless the maintenance and use of credits derived from the purchase of raw-material, packaging and intermediate products. Requirements must be met.</p> <p>IRPJ and CSLL deduction of up to 160% of the expenses with technological R&D. Further rules can provide for a deduction of 180%, depending on the number of employees and researchers hired by the taxpayer.</p>
PADIS (Technological Development of Semiconductors) and PATVD (Technological Development of Equipment for Digital TVs)	100% income tax reduction on profits arising from technological development of semiconductors and equipment for digital TVs; 0% CIDE on remittances related to such activities; 0% PIS, COFINS, IPI and II on transactions involving certain goods and assets and beneficiaries of the regime. Requirements must be met.
PROUNI (Educational Activities Incentives)	IRPJ, CSLL, PIS and COFINS exemption on income/revenues arising from educational courses. Requirements must be met.
RECAP (Special Regime for the Purchase of Capital Goods by Exporters)	<p>PIS and COFINS suspension on transactions involving certain fixed assets and legal entities entitled to the regime. 0% rate applies if requirements are met.</p> <p>Regime applicable to Brazilian exporters (whose exports represent 70% or more of their annual sales) and Brazilian shipyards with imports and purchases in the domestic market of new capital goods listed by decree.</p>
REIDI (Infrastructure Development Incentives)	<p>PIS and COFINS suspension on transactions involving goods, new fixed assets or services to be used in infrastructure projects. 0% rates apply if certain requirements are met.</p> <p>Regime applicable to legal entities engaged in infrastructure projects in the transportation, ports, energy, sanitation and irrigation areas.</p>
REPES (Special Regime for Information Technology Export Platform)	<p>IPI, PIS and COFINS suspension on transactions involving new fixed assets and services and entities entitled to the regime. IPI exemption and 0% PIS and COFINS apply if certain requirements are met.</p> <p>Regime applicable to legal entities whose, at least, 60% of their annual gross revenues refer to exports of software and</p>

	information technology services.
REPORTO (Modernization of Brazilian Ports)	II, IPI and PIS and COFINS suspension on imports and domestic purchases of certain assets used in the provision of port services and in the training of port employees. II and IPI exemption and 0% PIS and COFINS apply upon compliance with certain requirements.
SIMPLES (Special Tax Regime for Small Businesses)	<p>Payment of federal, state and municipal taxes under a simplified regime (in one single collection document). Taxes are calculated based on progressive rates (varying per type of company, activity, tax and gross revenue ceiling) on the gross revenues of the taxpayer.</p> <p>Regime applicable to small companies with annual gross revenues in the preceding year not exceeding to R\$ 240,000 (USD 130,000) – “Microempresas” – or R\$ 2,400,000 (USD 1,300,000) – “Empresas de Pequeno Porte”. Not applicable to certain companies or activities (e.g. corporations, companies with foreign shareholders and companies engaged in consulting services).</p>

6. PUBLIC DIGITAL BOOKKEEPING SYSTEM (SPED)

Since 2000, the Federal Union, States and Municipalities have worked to link their electronic systems and to share a common electronic platform, where information related to books and documents that comprise the commercial and tax bookkeeping of legal entities shall be received, validated and stored. This common data base must be available for consultation by the Federal, State and Municipal tax administrations and other governmental agencies.

The SPED was officially launched by Decree 6022/07, later supplemented by the Normative Instruction of the Federal Revenue Service 787/07 and its amendments.

The SPED should simplify the paper work and tax returns, as some of the most important information about taxpayers shall be available on-line. Once SPED is fully implemented, Brazilian tax authorities will have access to detailed information about the taxpayers' economic activities. The Federal Revenue Service – which manages, governs and supervises the SPED – is frequently working on the improvement of the digital system and issuing new rules for its regulation.

As part of the SPED, all legal entities that pay corporate taxes based on the actual profit system must keep their accounting records in digital format and submit such files to the Federal Revenue Service since 2009.

The implementation of e-tax books also started in 2009, for the legal entities expressly listed by State law. Moreover, commercial invoices started to be issued electronically, per economic activity, gradually.

It is worth mentioning that, at present, some of the most important tax returns, such as the legal entities' income tax return, are already filed electronically. In some cities, such as São Paulo, service invoices are also issued electronically.

We point out that taxpayers cannot oppose their commercial secrecy against Brazilian tax authorities, as a general rule. The banking secrecy has also been relaxed by Supplementary Law 105/01. In light of such framework, taxpayers must be alert to the need of receiving adequate protection as regards their secrecy rights.

¹ Estimated exchange rate: BRL 1.80 per each USD 1.00.

² Usually applicable to small-size companies with total revenues of less than BRL 48 million (approximately USD 26.7 million) in the previous year, that are not subject to restrictions otherwise imposed by law (e.g., financial institutions, companies earning profits/income from abroad etc.). The taxable basis (deemed profit) is calculated on a quarterly basis upon the applicability of certain percentages on the company's gross sales revenue which may vary per activity

performed by the company. The general percentages are 8% (for IRPJ) and 12% (for CSLL). In case of services the percentage is 32% for both taxes. Other revenues may be subject to other specific percentages or may be fully added to the taxable basis.

3 For a long time used at the sole discretion of the tax authorities. Recently the companies have been authorized to use this income tax system in some specific cases, such as when their accounting records are not reliable for the calculation of the taxes due. It is similar to the "Deemed Profit System" (also calculated on a quarterly basis), but the percentages applicable on the companies' revenues are 20% higher for IRPJ purposes.

4 The profit sharing or bonus paid to employees is taxable for the respective beneficiaries.

5 An experts' report can be used to support different rates.

6 See definitions on Section 1.1.2.3.

7 Under the "Deemed Profit" and the "Arbitrated Profit" such taxes must be calculated on a quarterly basis.

8 The taxable basis is calculated by applying certain percentages on the gross sales revenues (similar to the Deemed Profit System – see footnote 2 above). The general percentages are 8% (for IRPJ) and 12% (for CSLL). In case of services the percentage is 32% for both taxes. Other revenues shall be fully added to the taxable basis.

9 Even if they do not involve technology transfer (as of January 1, 2002). In the case of computer programs, the tax shall only be levied in case of transfer of technology (as of January 1, 2006).

10 For taxable events as of January 1, 2009 up to December 31, 2013 the tax credit is of 30%.

11 Although Brazilian Superior Court has decided that IPVA is not due on the ownership of aircraft and boats, but only on land vehicles ownership, some States are still charging this tax on these vehicles and the taxpayers should discuss the matter in Courts.