



**LEVY OF ICMS ON TRANSACTIONS WITH DIGITAL GOODS AND
MERCHANDISE NEW REGULATION BY THE STATE OF SÃO PAULO^[1]**

Technology evolves at an impressive speed, a fact that is generating a certain mismatch between the rules governing the sector and reality. In this situation, the taxation applying to transactions with digital goods and merchandise in Brazil is a challenge.

Article 37 of the Transitional Provisions of the Value-Added Tax (ICMS) Regulation of the state of São Paulo (RICMS/SP), introduced by Decree 61791/16, establishes that – until it is defined where the ICMS triggering event occurs (for definition of the establishment responsible for paying the tax) – the ICMS levied on transactions with off-the-shelf software, programs, applications, digital files, and electronic games, provided by means of digital data transfer (download or streaming) will not be due.

With the enactment of ICMS Agreement 106/17 (Agreement), concluded by the National Council of Financial Policy (CONFAZ), published on October 5, 2017, it was defined that, in domestic shipments and imports of digital goods and merchandise, such as software, programs, electronic games, applications, digital files and the like, off the shelf (even if they have been or can be adapted) and sold by means of electronic data transfer, the ICMS: (a) will be due to the state where the acquirer is domiciled or established; and (b) must be paid by the legal entity that owns the website or digital platform that sells or provides the digital goods and merchandise. The Agreement also defined the events in which the liability for paying the ICMS can be ascribed.

It has been established that legal entities holding websites or electronic platforms that sell or provide digital goods and merchandise by electronic data transfer must be registered as ICMS taxpayers in all states in which they have transactions with end-consumers.

Based on this Agreement, the state of São Paulo enacted Decree 63099, published on December 23, 2017, which changes the RICMS/SP to enable the levy of ICMS on transactions with digital goods and merchandise by means of electronic data transfer, and revokes article 37 of the transitional provisions of the RICMS/SP. With this, the ICMS will be effectively chargeable by the state of São Paulo in the transactions being analysed.

In addition to the provisions above, Decree 63099/17:

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- (a) defines that the website or electronic platform that sells or provides digital goods and merchandise by electronic data transfer, even in the case of periodic payments, is an autonomous establishment;
- (b) authorises the Finance Secretariat of São Paulo to establish a simplified procedure for registration of establishments that sell exclusively digital goods and merchandise, and to grant special regimes for compliance with ancillary obligations;
- (c) releases the holder of the website or platform that performs transactions with digital goods exempt from or not taxed by the ICMS from the obligation to enrol in the state of São Paulo taxpayers' register; and
- (d) provides that transactions with digital goods and merchandise sold by electronic data transfer that happen before the exit for the end-consumer will be exempt from the ICMS in the state of São Paulo while ICMS Agreement 106/17 remains in force.

The fact is that, as of April 1, 2018 – the date on which ICMS Agreement 106/17 and Decree 63099/2017 will start to produce their effects – the new provisions will bring more difficulties and legal uncertainty to taxpayers due to formal and material defects existing in them.

ICMS Agreement 106/17 – on which Decree 63099/2017 was based – violated article 146 of the Federal Constitution (when it defined the taxpayer and the state to which the tax should be paid), which grants to the supplementary law – rather than to an agreement or decree – jurisdiction to define triggering events, taxable bases and taxpayers.

In addition, the new rules generate a clear conflict of jurisdiction between states and municipalities, to the extent that, as per article 156 of the Federal Constitution, municipalities have the jurisdiction to charge the tax on services (ISS), including in relation to services in the area of technology (as defined by Supplementary Law 116/03, with the wording given by Law 157/2016).

In particular, the wording of Decree 63099/2017 is curiously inaccurate and allows the interpretation that the ICMS will be levied on any activity with digital goods and merchandise occurring by electronic data transfer, including, for example, on the download of applications and news and the streaming of music and movies.

Furthermore, unlike the provisions of ICMS Agreement 106/17, Decree 63099 does not limit the levy of ICMS to off-the-shelf digital goods and merchandise. To this extent, the state of São Paulo may require the ICMS on transactions with software developed on a made-to-order basis, which is a service provision and should be subject to the ISS.

In other words, with the new rules the same events would, it appears, be taxed by the states (ICMS) and municipalities (ISS). For the taxpayers, an important question, among others, remains: what is the tax owed and who is the legitimate creditor?

Further, although ICMS Agreement 106/17 also provides for the levy of the tax on imports of digital goods and merchandise carried out by electronic transfer, Decree 63099/2017 did not address the levy of the ICMS on imports.

In this complex situation, a favourable point is that the reduction of the ICMS taxable basis was maintained in transactions with software, programs, applications and digital files, off the shelf (even if they have been or can be adapted), provided by any means, so that the tax burden results in 5% of the value of the transaction, according to ICMS Agreement 181/2015, Decree 61791/2016, and article 73 of Annex II to the RICMS.

As it can be seen, these new rules of the state of São Paulo increase the ancillary obligations (which will become even more complex and costly), the tax burden (in transactions that were not previously taxed with the ICMS), and the taxpayers' legal uncertainty, which could become even worse when the other states adapt their rules to ICMS Agreement 106/17.

This situation may generate, soon, a large increase in discussions and tax proceedings in the technology sector, since the new rules will come into force on April 1, 2018, in the state of São Paulo.

This newsletter contains information and general comments on legal matters that may interest our clients and friends. It does not represent the legal opinion of our firm on the subjects addressed herein. In specific cases, readers should rely on proper legal assistance before adopting any concrete action relating to the matters addressed herein.

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