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LEGAL LETTER / APRIL 2017

BRAZIL FEDERAL SUPREME COURT DEEMS INCLUSION OF ICMS IN THE PIS/COFINS TAXABLE BASIS UNCONSTITUTIONAL¹

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The Brazilian Federal Supreme Court ruled in favor of the taxpayers, determining that the state VAT should not be included in the concept of “gross revenues” for the purpose of the PIS/COFINS taxable basis.

1. On March 15, the Full Bench of the Brazilian Federal Supreme Court (STF) ruled that the inclusion of the state VAT (ICMS) on the social contributions on gross revenue (PIS and COFINS) taxable basis is unconstitutional (Extraordinary Appeal No. 574706).
2. The main argument to grant the taxpayer’s appeal to not include the ICMS on the PIS/COFINS taxable basis was that, in summary, even though the ICMS amounts are charged by the seller as part of the product’s price, such amounts will be transferred to the state treasury department. Therefore, they will not be added to the company’s assets and will not fall within the concept of gross-revenue, which is the taxable basis for the PIS/COFINS.
3. Regarding the issue of establishing a date for the STF ruling to take effect, despite the request made by the Attorney of the National Treasury in the oral arguments, STF’s Justice Rapporteur Carmen Lucia found that there was no claim in this regard in the court documents. Therefore, this matter was not subject to trial. However, the Attorney General of the National Treasury might file a Motion to Clarify this issue in court.
4. Given the uncertainty of the effective date of the ruling, it would be best to have a lawsuit filed on the matter. This would allow the taxpayer to reclaim the PIS/COFINS paid in excess (the ICMS amounts included in the sales price) in the five years before the date of the

¹ This article was first published by **International Tax Review** in April 2017 on www.internationaltaxreview.com

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claim. This is because, even if the STF rules in favour of establishing a date for the decision to take effect – which in practical terms generally, prevents the recovery of overpaid taxes –, based on its case law, the STF tends to protect the taxpayers that have already claimed their rights by filing a lawsuit. It should be noted that the five years is the statute of limitation period according to Brazilian tax legislation.

5. Furthermore, taxpayers may henceforth exclude the ICMS from the PIS/COFINS taxable basis. If companies adopt a conservative approach, they should obtain a ruling that allows the suspension of the payments and, thus, inform said suspension in the federal debts and credits accessory obligation form (DCTF). However, companies may decide to suspend payments immediately based only on the STF ruling. In this case, the possibility of the Federal Revenue assessing the companies, based on the legislation that was deemed unconstitutional but is still in force, should not be ruled out.

6. Additionally, the government, to mitigate the decrease in tax collection and absorb the impact arising from the refund regarding the past five years, may increase the PIS/COFINS tax rate. This increase would be aligned with the previous government decision to increase the PIS/COFINS rate levied on the import of good, when the STF (in [Extraordinary Appeal 55937](#)) decided to exclude the ICMS and the PIS/COFINS from the goods' import taxable basis. The increase of the PIS/COFINS may be performed in the same fiscal year. However, a period of 90 days must be respected before it is enforceable.

7. Finally, based on the content of the STF ruling, a case law was established that may increase the taxpayers' chances of favourable outcomes regarding the following pending court discussions:

- The exclusion of the municipal tax service (ISS) from the PIS/COFINS taxable basis; and
- The exclusion of ISS and ICMS from the social security contributions (INSS) calculated on gross-revenues.

8. In such cases, a similar understanding to the ruling on the Extraordinary Appeal 574706 could be reached, as the ISS and ICMS amounts will be transferred to, respectively, the municipal and state treasury departments and would, therefore, not fall within the concept of “gross-revenues”.

9. In summary, although there are several questions about the future impacts and developments of the STF ruling on the Extraordinary Appeal 574706, taxpayers should be alert and adopt the proper measures and counselling to reap benefits from the decision.

São Paulo, April 2017

This legal letter contains information and general comments on the matter. In specific cases, it is advisable to rely on proper legal assistance before adopting any concrete actions relating to the matters dealt with herein.