

JOSÉ MAURÍCIO MACHADO
CARLOS AUGUSTO DA CRUZ
MAURI BÓRNA
RENATA ALMEIDA PISANESCHI
ROBERTO FLEURY A. CAMARGO
RENATO SILVEIRA
JULIANA MARI TANAKA
EDUARDO AMIRABILE DE MELO
FERNANDO FARINELLI
STEPHANIE JANE MAKIN
DANIELA CATTUCCI CARONE
NATHÁLIA DE A. MARQUES FRAGA
LÚCIO BRENO PRAVATTA ARGENTINO
LEONARDO URQUIZA F. PORTELADA
RENATA ÁBBUD DE OLIVEIRA
IVA MARIA SOUZA BUENO
MATEUS BATISTA ARAÚJO
MANUELA CURTO DUARTE SILVA
RENATO CARVALHO DE CASTRO
INGRID CRISTINA SILVA DE SOUZA
VICTOR ANTONIO BRUNO MOREIRA
JOSÉ MARIA QUEIROZ JUNIOR
ISADORA PRADO MAIA E SILVA
GABRIELE M. HOLLAND RONDON

ISABEL A. BERTOLETTI
EDMILSO GOMES DA SILVA
LISIANE B. H. MENOSKI PACE
FABIO MEDEIROS
LUCIANA FELISBINO
ROCHELLE RICCI
LANA PATRÍCIA PEREIRA BAPTISTA
GABRIEL CALDIRON REZENDE
ELAINE ALVES FERREIRA
ANDRÉ BLOTTA LAZA
FERNANDO V. A. TELES DA SILVA
RAFAELA SCORZA DE A. CASTRO
NATÁLIA MAZIERO DE OLIVEIRA
AMANDA DE OLIVEIRA GOMIDE
MABEL DE ÁVILA SANTOS
MARILIA LUIZA DA COSTA RAMOS
DANIELLA CAMARGO DE BARROS
BEATRIZ DE CARVALHO EDINALDO
CASSIO M. GUALBERTO NEVES
EMANOIL CONSTANTINO SAMIOTIS
GIOVANNA HOFF DOMINGUES
MARIA ALMEIDA SANCHES
DEBORA FREIRE GONÇALVES
GABRIEL BARONI DE ANDRADE

LUÍS ROGÉRIO G. FARINELLI
CRISTIANE M. S. MAGALHÃES
RICARDO M. DEBATIN DA SILVA
ERIKA YUMI TUKIAMA
GUSTAVO DE FREITAS LEITE
SORAIA MONTEIRO DA MATTA
MARCEL AUGUSTO SATOMI
MIRELLA ANDREOLA DE ALMEIDA
PEDRO CAVALCANTI BOTELHO
AMANDA ALVES BRANDÃO
MILTON DOTTI NETO
GUILHERME LANZELLOTTI MEDEIROS
ROGÉRIO GASPARI COELHO
RENATA DALLA TORRE AMATUCCI
ROBERTO MAGNO RIBEIRO NETO
AMANDA REGIANI ZELI
RAFAEL ANGELO DE SALES SILVA
ANNA RIZZO MICELI
KAROLINA DE MELLO PEREIRA
GABRIELLA OLINTO DOS ANGELOS
PATRIK MATOS GONÇALVES
IGOR MUNIZ BENITE
RAFAELLA TCHAKERIAN HAKIM

JÚLIO M. DE OLIVEIRA
ROSIENE SOARES NUNES
DANIEL LACASA MAYA
PAULO ROGÉRIO GARCIA RIBEIRO
MAURO TAKAHASHI MORI
CAROLINA ROMANINI MIGUEL
SUZANA CAMARÃO CENCIN
LORENA MORAIS XIMENES CAMPOS
ANDRÉ T. JUNQUEIRA AMARANTE
RAPHAEL OKANO P. DE OLIVEIRA
PALOMA YUMI DE OLIVEIRA
RAPHAEL GOUVEIA BELLO
CAIO FINK FERNANDES
DANIELLE RAMOS DA SILVA
MARTHINA GASQUES TEIXEIRA
FELIPE AFFONSO BEHNING MANZI
VICTOR BULÇÃO MARTINELLI PINTO
RODRIGO GONZAGA DE OLIVEIRA

CONSULTOR
NELIO B. WEISS



SÃO PAULO
AV. BRIGADEIRO FARIA LIMA, 1656
11º ANDAR (01451-918)
SÃO PAULO - SP - BRASIL
T. + 55 11 3819 4855

BRASÍLIA
COMPLEXO BRASIL XXI - BLOCO A
SHS QUADRA 06 CONJ.6 - SALA 808
ASA SUL (70316-100)
BRASÍLIA - DF - BRASIL
T. + 55 61 3039 8081

RIO DE JANEIRO
PRAÇA FLORIANO, 19 - 4º ANDAR
CENTRO (20031-050)
RIO DE JANEIRO - RJ - BRASIL
T. +55 21 3550-3000

www.machadoassociados.com.br

LEGAL LETTER / MARCH 2017

BRAZIL: NEW TAXABLE SERVICES AND TACKLING HARMFUL TAX COMPETITION¹

Carolina Romanini Miguel and Gabriel Caldiron Rezende²

Supplementary Law 157/16 regarding the municipal service tax (ISS) was brought in to allow the taxation of new services and to reduce the harmful tax competition between municipalities.

1. The ISS is levied on the provision of services listed in the supplementary law.
2. On December 29 2016, the Brazilian federal government published Supplementary Law 157/16, which altered the general guidelines of the tax that were established by Supplementary Law 116/03. The amendments made some new services subject to ISS and introduced unprecedented measures to limit the granting of tax benefits by municipalities.

New taxable services

3. Supplementary Law 157/16 introduced some activities in the list attached to Supplementary Law 116/03 that will now be subject to the ISS, which includes:
 - 1.03 – Processing, storage or hosting of data, texts, images, videos, electronic pages, applications, and information systems, among other formats, contrary to the previous wording that stated only data processing;
 - 1.09 – Provision, without permanent transfer, of audio, video, image, and text content through the internet, respecting the immunity of books, newspapers and periodicals (except for content distribution by providers of conditional access services, as per Law 12485/11, subject to the state value-added tax – ICMS); and

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

² Carolina Romanini Miguel and Gabriel Caldiron Rezende are members of the Indirect Tax and Customs area of **Machado Associados**

- 17.25 – Insertion of texts, drawings and other advertising materials in any media (except in books, newspapers, periodicals and in radio broadcasting and broadcasting of sounds and images with free reception).
4. As per the Federal Supreme Court’s case law and Articles 155, II, and 156, III, of Federal Constitution, activities that do not characterise an effective “obligation to do”, or which typify a service subject to the ICMS (communication and interstate and inter-municipal transports), cannot be subject to the ISS.
5. Therefore, to verify the constitutionality of the inclusion of these activities in the list of services subject to the ISS, it is necessary to assess if the activity does typify a service provision not subject to the state’s jurisdiction.
6. As an example, items 1.03 and 17.25 mentioned above allow the levy of the ISS on streaming services and exhibition of third party advertising material. We believe that the inclusion of such activities in the ISS taxable services list might not solve the previous controversies, as the states may still sustain their understanding that they are communication services. This matter will probably be taken to court to find a resolution.
7. To charge the ISS on such activities, each municipality must change its legislation in relation to the new services that are now taxable. Furthermore, the levy of the ISS cannot be carried out in the same year of the publication of the new municipal legislation, and only after 90 days of such publication. In practical terms, we believe that the levy of the ISS on such new taxable services will only occur from 2018.

Measures to avoid harmful tax competition

8. Pursuant to the Brazilian Federal Constitution, supplementary law should determine the minimum and maximum ISS rates and, while it was not enacted, the minimum rate was 2% and the granting of benefits that resulted in a lower tax burden was prohibited. Upon the issue of Supplementary Law 116, only the maximum rate was defined, corresponding to 5%.
9. As the ISS is usually paid to the municipality where the service provider is located, to attract new companies and investments to their territories, several municipalities grant ISS benefits such as the reduction of the ISS taxable basis of establishments located there, thus reducing the ISS payable to under 2%.
10. On the one hand, the granting of ISS benefits managed to draw companies away from capitals to smaller municipalities in the search for a tax reduction. On the other hand, this measure led to harmful tax competition between municipalities, most notably because of:
- Companies that simulated their existence in a favoured ISS municipality only to enjoy tax benefits;



- Municipalities where the service receiver is located that charged ISS from service providers located in other municipalities, even though the ISS was paid to the service provider's municipality;
 - Several court disputes between municipalities that try to nullify the tax benefits granted by other municipalities; and
 - Municipalities that grant new benefits when their benefits are nullified by courts, perpetuating the discussions.
11. In an attempt to reduce such tax competition, Supplementary Law 157/16 brought in the minimum ISS rate of 2% and stated that any law or act that grants ISS benefits that reduce its burden to under 2% of the service price is deemed null.
12. To ensure compliance with this rule, Supplementary Law 157/16 also changed Law 8429/92, which established the sanctions applicable in case of administrative improbity. Accordingly, any act or omission to grant, apply or maintain a financial or tax benefit that reduces the ISS burden to under 2% of the service price is now considered as administrative improbity.
13. Irrespective of any criminal, civil or administrative penalties provided for in specific legislation, the penalty for the agent responsible for such administrative improbity might be the loss of his/her public office, suspension of his/her political rights for five to eight years, and a civil fine of up to three times the amount of the financial or tax benefit granted.
14. This is an unprecedented measure in Brazil to avoid harmful tax competition. In practical terms, mayors or other public authorities that grant or maintain ISS tax benefits may be personally liable for the tax collection reduction that the municipalities might suffer.

São Paulo, March 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.