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Federal Courts Hold for and Against Government in Recent Tax Cases

In Brazil, two separate courts recently handed a victory and a defeat to the Federal government in two tax disputes. In one case, the Federal Superior Court of Justice (STJ) held, five to three, for the government concerning the phase out and repeal of a tax credit that applies to exports of manufactured goods. In the other case, the Federal Supreme Court (STF), by a vote of six to four, held for the taxpayer in finding Law nr. 9.718 (1998)—which expanded the tax base for application of certain social taxes on gross receipts—was unconstitutional.

IPI: Notional Credit on Exports

In Brazil, a federal excise tax (*Imposto sobre Produtos Industrializados—IPI*) applies for manufactured goods. The IPI credit on exports (also known as “IPI premium credit”) was added by Decree-law nr. 491 (1969) as an incentive to boost exports by allowing taxpayers a tax credit equal to the amount of IPI tax levied throughout the production chain of manufactured products intended for export.

Subsequently—due to concerns expressed in the context of certain trade negotiations—Decree-law nr. 1.658 (1979) provided for a phase out of the IPI tax benefit, with final repeal in 1983. Also, in 1979, Decree-law nr. 1.724 was issued which granted extraordinary powers to the Ministry of Finance to increase, decrease, or extinguish the IPI premium credit. After the constitutionality of Decree-law nr. 1.724 (1979) was challenged by numerous taxpayers, the Federal Superior Court of Justice found that this 1979 decree was unconstitutional. That decision opened the way for taxpayers to dispute Decree-law nr. 1.658 (1979) that phased out the IPI tax benefit.

After a series of defeats concerning this issue in the lower courts, the Federal Superior Court of Justice recently held for the government concerning the IPI phase out and repeal.

This recent decision of Federal Superior Court of Justice unifies and rectifies the court’s previous interpretation concerning the IPI tax credit. Note that the taxpayer/plaintiff in this case could exercise its right to

appeal the decision to the Federal Supreme Court, whose ruling would be the ultimate holding in the dispute.

PIS and COFINS Taxes

PIS (Programa de Integração Social) and *COFINS (Contribuição para o Financiamento da Seguridade Social)* are federal taxes imposed on gross receipts.

The first paragraph in article 3 of Law nr. 9.718 (1998) expanded the tax base of receipts subject to *PIS* and *COFINS* taxes, by adding a new definition of gross revenues that was not dependent on the taxpayer’s type of business or accounting classification. Until enactment of this law in 1998, *PIS* and *COFINS* were levied on gross sales receipts of products and services, by simply referring to the taxpayer’s invoices under the rules of Complementary Law nr. 70/91.

Taxpayers disputed the constitutionality of Law nr. 9.718 (1998) in light of the fact that Constitutional Amendment nr. 20 (1998)—the legal foundation for the law—was enacted only 18 days after



Brazilian Federal constitution bars certain types of new taxes from taking effect within less than 90 days after enactment). The Federal Supreme Court agreed and found the 1998 law was unconstitutional.

While these decisions are enforceable only between the respective taxpayers and the government, these court cases set the tone for future decisions concerning the litigated issues. Therefore, similarly situated taxpayers may rely on the Federal Supreme Court's decision as precedent to dispute the issue in their cases. Some observers note that the amount of losses which the government could face with respect to this issue could reach R\$ 30 billion (approximately US\$ 14 billion). Taxpayers who are successful in their disputes or litigation concerning the *PIS* and *COFINS* issue may be able to claim a tax credit that can be used to offset other Federal taxes and contributions.

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