

Legal Definition of Tax Havens in Brazil is Changed

Law 11.727/08 enacted on June 24, 2008 created a new concept of tax haven to the Brazilian legislation.

The definition of "tax favorable jurisdiction" was first introduced in the Brazilian legislation by Law nr. 9.430/96 as part of the then recently conceived transfer pricing regulations. The definition was based on two criteria: countries or entities in countries that:

- (i) do not tax income or when doing so at a rate of 20% or lower; or
- (ii) whose national legislation allows confidentiality as to ownership of shares or the corporate organization of legal entities.

Later in 1999, Law 9.779/99 (article 8) also dictated that remittances or payments of interest, royalties or service fees to tax havens became subject to 25% withholding tax instead of the general 15% tax rate.

Given the broadness of that concept, the Revenue Service created a list of tax havens containing 53 jurisdictions (Normative Instruction 188/02) determining which countries and respective transactions could be the target of the transfer pricing audits and the qualified withholding rate.

Under the new legislation, a privileged tax regime is defined as a regime:

- (i) that does not impose tax on income or when doing so at a rate of 20% or lower;

- (ii) that grants a tax benefit to a non-resident individual or entity;
 - (a) without substance requirements;
 - (b) dependent upon the carrying out of non-substantial economic activities;
- (iii) that does not impose tax on foreign income or when doing so at a rate of 20% or lower;
- (iv) that does not allow access to information regarding the corporate organization or structure of the resident entity or the ownership of its shares or stocks or to their economic activities.

Based on the new legislation, effective January 01, 2009 a new and enlarged definition of tax haven might be adopted by the Revenue Service. Such new definition could also lead to a review of the existing list of tax havens.

On the other hand, there is still doubt as to whether the new concept of privileged tax regime will apply only for purposes of the transfer pricing legislation; or whether it will also be applicable to the qualified transactions under article 8 or Law nr. 9.779/99 that are currently subject to the 25% withholding tax to the extent of the concept of favorable tax jurisdiction. At a minimum, the new legislation could be viewed as a trend to influence the interpretation that tax authorities will use when analyzing the aforementioned transactions.



For more information, contact an international corporate tax professional:

São Paulo

Marienne S. Munhoz
+55 11 2183-3182
mmunhoz@kpmg.com.br

Ericson Amaral,
+55 11 2183-3375
eamaral@kpmg.com.br

Luiz Dardes,
+55 11 2183-3188
ldardes@kpmg.com.br

Murilo Mello,
+55 11 2183-3261
murilomello@kpmg.com.br

Rio de Janeiro

Roberto Haddad
+55 21 3515-9469
robertohaddad@kpmg.com.br

Julio Chamarelli de Cepeda
+55 21 3515-9133
jcepeda@kpmg.com.br

If you have any questions or comments or wish to update your data, include other professionals or remove your name from the distribution list, please send an e-mail to kpmgbraziltax@kpmg.com.br.

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