

# International Tax Brazil

TAX

July 2005

## Tax law changes introduced through Provisional Measure

In order to mitigate the “side effects” produced by the attempt of implementing some tax law changes during 2005 the government issued a new Provisional Measure introducing tax benefits, mainly, for the export sector, software developers and technological innovation activities. The implementation of such changes still rely on the final Congress approval.

### Tax relief for export companies, software developers, and technology innovators

The Brazilian government recently approved regulations that, by affording certain tax relief measures, are intended to provide support for the country’s import–export industry, boost the software industry, and encourage technology innovation (*Medida Provisória 252 of June 15, 2005* and *Decreto 5467 of June 15, 2005*).

### Export companies

Under a special tax regime that applies to imports of capital goods (*Regime Especial de Aquisição de Bens de Capital para Empresas Exportadoras - RECAP*), companies with export revenues greater than 80 percent of their annual sales for the last calendar year would no longer be required to pay *PIS*, *PASEP*, and *COFINS* with respect to their imported capital goods for a three–year period that begins after the regime’s approval.

Note that qualifying companies must commit to maintaining their export

revenue percentage for a period of two years, and to be eligible for this special tax regime, companies must be current in their compliance with respect to their tax positions and under the *PIS* and *COFINS* non–cumulative regime (*Medida Provisória 252/05, articles 13 to 16*).

### Software developers

Under the rules that apply for exports of information technology services (*Regime Especial de Tributação para a Plataforma de Exportação de Serviços de Tecnologia da Informação - REPES*), companies that are involved exclusively in the development of software applications and other technology services and that have export revenues that are greater than 80 percent of their annual sales would no longer be required to pay *PIS* and *COFINS* with respect to imported goods and services, if certain conditions (for example, concerning direct import transactions or with respect to compliance with mandatory *PIS* and *COFINS* non–cumulative regime and current taxes) are met (*Medida Provisória 252/05, articles 1 to 12*).

Moreover, the new rules establish a five–year period for the grant of the tax exemption with respect to the amount of *PIS* and *COFINS* levied on imported goods and services under this regime. A zero tax rate of *PIS* and *COFINS* (*Programa de Inclusão Digital*) is also available with respect to revenues derived from the selling of related

hardware equipment (*Decreto 5467/05*).

### **Technology innovation**

Under a new incentive (*Incentivos à Inovação Tecnológica*), certain entities may benefit from the following tax incentives:

For income tax purposes, companies can claim as a deduction from their net income the amount of expenditures dedicated to technology research and innovation.

Qualifying companies can reduce up to 50 percent the amount of the *Imposto sobre Produtos Industrializados* (a tax on industrialized products) with respect to equipment and tools that are dedicated to technology research and innovation.

For income tax purposes, accelerated depreciation (generally, at a double rate of depreciation) is provided for goods dedicated to technology research and innovation, and accelerated amortization is provided for intangibles involved in technology research and innovation in an amount that would be equal to expensing the full cost in the year of acquisition.

A tax credit equal to 20 percent of the withholding tax on royalties and a fee for technical services paid abroad under technology transfer agreements approved by the Federal Intellectual Property Agency (*INPI*) will be granted for years 2006 through 2008. For years 2009 through 2013, the tax credit will be equal to 10 percent of the amount of the royalty paid abroad. To benefit from this special regime, companies need to commit to invest in research and development in Brazil in an amount that is double the amount of the tax benefit received. A zero withholding tax rate is available for amounts paid to foreign companies concerning the registration and maintenance of patents and copyrights.

Under these rules, companies that benefit from the research and

development tax incentives must be prepared to provide related information to the tax authorities under a special tax audit program that has not been finalized (*Medida Provisória 252/05, article 17*).

### **Regional tax incentives (ADA and ADENE)**

Corporations that acquire assets for projects approved under special regional tax incentives – *ADA and ADENE* – would be allowed: (1) accelerated depreciation for Income tax purposes and (2) recognition of *PIS and COFINS* tax credits for a period of twelve months. These tax benefits are still pending until regulations are issued. The new rules are planned to apply from January, 2006 through December, 2013 (*Medida Provisória 252/05, article 31*).

### **Construction industry taxation**

Construction companies' financial income, for presumed profit system calculation, should be added to the regular tax base for the purpose of calculating income taxes. Under this system the tax authority will presume a net income between 1.6 percent and 32 percent of revenues, depending on the entity's type of activity. These tax changes will be effective from October, 2005 (*Medida Provisória 252/05, articles 33 and 73*).

*Medida Provisória* introduces a modification to the special tax regime that applies to companies engaged in the construction sector (*Regime Especial de Tributação – Patrimônio de afetação*). Construction companies may elect a flat tax rate of 7 percent for the payment of federal taxes (corporate taxes and gross revenues taxes). They must separate revenues from other activities from revenues attributable to specific construction projects which are subject to the special tax regime. This federal tax

payment would be *considered as definitive not as a prepayment*. *Revenues, costs and expenses in connection with a specific construction project would be kept apart from the construction company's other activities*.

### **Offsetting of tax credits social security debts**

Tax authorities may offset federal tax credits against social security liabilities for a particular taxpayer. The taxpayer would be provided the opportunity to endorse or refuse this option. The taxpayer must present written acceptance or refusal within 15 days after receiving a formal letter issued by the tax authorities (*Medida Provisória 252/05, article 69*).

### **Individual capital gains taxation**

Income tax exemptions for individuals are granted for certain capital gains arising from the sale of residential real estate. To receive the exemption, an individual must use the amount received in the transaction to acquire additional residential real estate. The new real estate property would be required to be bought within a six-month period after the first real estate property was sold. The benefit could only be granted once during a five year period.

For individuals, the nontaxable limits are increased on capital gains resulting from sales of capital assets of minor value. The new limit is R\$ 20,000 (US\$ 8,356) for the sale of securities and R\$ 35,000 (US\$ 14,623) for the sale of other assets (*Medida Provisória, articles 35 and 36*).

For more information, contact a tax professional in São Paulo:

Marienne Shiota Munhoz,  
+55 (11) 3067 3182, [mmunhoz@kpmg.com.br](mailto:mmunhoz@kpmg.com.br)  
Murilo Mello,  
+55 (11) 3067 3261, [murilomello@kpmg.com.br](mailto:murilomello@kpmg.com.br)

© 2005 KPMG Tax Advisors – Assesores Tributários Ltda., the Brazilian member firm of KPMG International, a Swiss cooperative. All rights reserved.

The information contained in International Tax Brazil is general in nature and based on authorities that are subject to change. Applicability to specific situations is to be determined through consultation with our tax advisors.

The KPMG logo and name are trademarks of KPMG International, a Swiss cooperative.