An insight into doing business in Brazil

GENEVA GROUP INTERNATIONAL

Seres Baum

3.6.2. Employee Contributions

Payroll charges for social security employee contributions are rated at 8% to 11%, limited to a maximum monthly contribution of R$375.82 (effective as at February 2010).

Besides retaining employee contributions, employers are asked to withhold 11% on monthly payments made to self-employed persons and directors up to the same maximum sum of R$ R$375.82.

4 Brazilian Social Security Benefits

Brazil's social security system provides only minimal benefits. To some extent, the state health care system is inadequate and consequently, the majority of employees have access to private health insurance plans provided by corporate employers or trade unions.

4.1. Unemployment Insurance

There is no regular unemployment insurance, other than unemployment pay, which is restricted to a maximum of three minimum wage or salary payments over the first six months of unemployment.

4.2. Health Insurance

Employers are obliged to pay an employee's salary during the first 15 days of sick leave. If the insured is unable to work after a 15 day absence, sickness benefit is paid to the insured by the INSS for the duration of sick leave. This insurance may be converted into a disability pension.

4.3. Retirement Pension

This benefit is paid to men over 65 and women over 60, provided they have made 180 monthly contributions. For farm workers, the qualifying age drops to 60 years for males and 55 years for female workers. An early retirement pension is granted if a male employee has worked for 30 years (25 years for women). The maximum pension is available after 35 years of service for men and 30 years for women.

4.4. Other Benefits

These include, among others, maternity insurance, funeral insurance and disability pensions.

Please see the next chapter on how Brazilian Tax System operates

V – TAXATION

According to World Bank research, Brazil has the most complex tax system in the world. Being a Federative Republic, under federal constitutional structure, Federal, State and Municipal governors are allowed to create and administer their own tax systems. The system comprises different categories of taxes, whose main elements can be classified under TAX, CONTRIBUTION and FEES. Municipalities may charge a series of different fees for services rendered to citizens who requested these and tax is levied on services, onerous real estate transfers and urban real estate ownership. States may raise funds based on fees for services rendered to any individual and tax may also be levied on non-onerous transfer of all types of goods and real estate (inheritance). There is a vehicle ownership tax (cars, motorcycles and aircraft), as well as a non-cumulative tax on the commercialization of any goods (state VAT). In addition to many different fees, the Federal governor or union has the authority to ask for tax to be levied on rural real estate ownership, individual and corporate income tax, import / export tax, production (excise) tax and credit / exchange / insurance tax. The Union may also introduce a series of contributions whose main elements are contributions levied on payroll, revenues (sales of goods and services) and some overseas remittances (royalties, technical and administrative services). Treaties to avoid double taxation have been agreed with many countries.

V - Taxation

Summary

In Brazil, taxation may be established by any of the three levels of Government (Federal Union, the States, and the Municipalities), in accordance with specific powers conferred under the Constitution. These may take the form of taxes, fees, contributions, and compulsory loans.

1 Basic Composition Of Brazilian Taxation

Brazilian tax system comprises different categories of taxes, the main elements of which may be classified under tax, contributions, fees and compulsory loans.

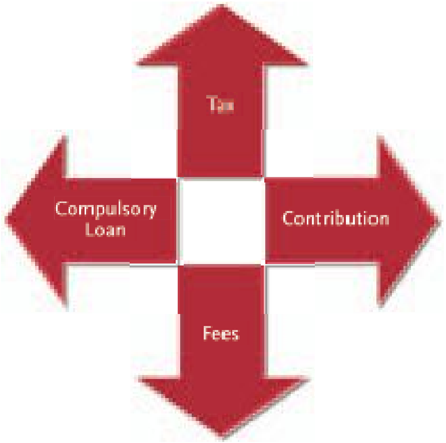

Fig. 18 Qualitative Composition of the Tax System

1.1. Tax

Tax may be cited as a fee charged ("levied") by a government on a product, income, or activity whose application is determined by Government decision. It certainly is "the price of citizenship".

1.2. Contributions

Contributions are collected for a specific purpose or may be applied to a single use. With a few exceptions, general contributions can only be levied by the Federal Government. Contributions to finance social security (INSS) and contributions relating to interventions in the economic domain (CIDE) are examples of contributions.

1.3. Fees

Fees are collected and used to fund services rendered upon request of a taxpayer. The sole beneficiary of such public services rendered is the taxpayer. The price paid for construction licensing is an example of Municipality fees.

1.4. Compulsory Loans

Compulsory loans can be instituted only by the Federal Government for the purposes of essential public investment benefiting the relevant national interest, or for extraordinary expenses resulting from public disasters or foreign wars.

Nationally, there is no compulsory loan being charged at the moment and the last was done by late 1980's.

General Structure Of The Brazilian Tariff System 2

In accordance with specific powers conferred under the constitution, any of the three levels of Government (Federal Union, the States, and the Municipalities) may establish taxes as shown in the chart below.

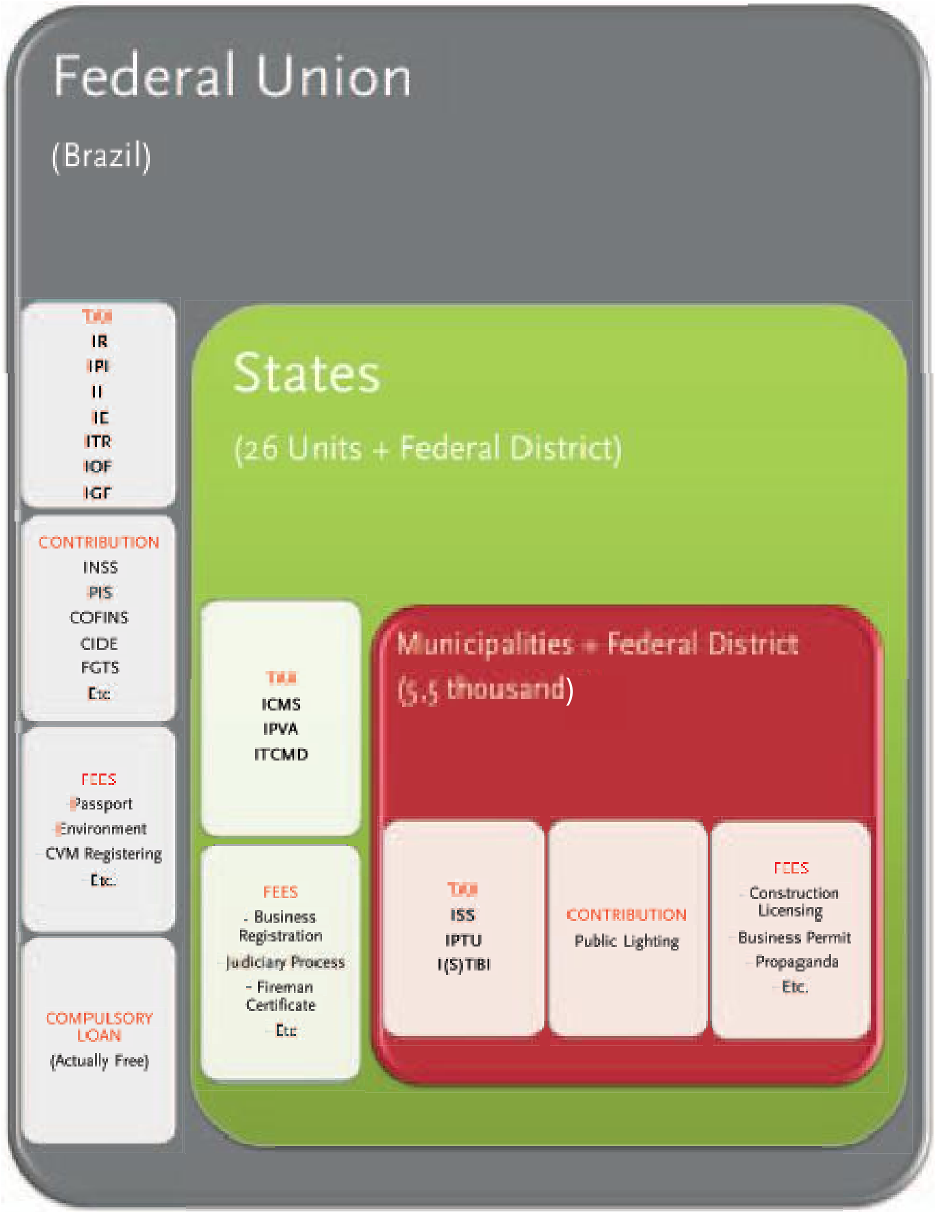

Fig. 19 Brazilian Tax System

Municipal Charges 3

3.1. Taxes

Constitutional powers allow the Municipalities and Federal District to levy the following taxes:

- IPTU - Urban Real Estate Property Tax
- ISTBI - Onerous Real Estate Transfer Tax
- ISS - Services Tax

ISS – Service Tax is a non-cumulative tax imposed on certain services listed in federal law, where rates allowed under the constitution vary from 2% to 5%.

3.2. Contributions

Starting from 2003, a Constitutional Amendment gave power to the municipalities to charge a permanent public light contribution. This contribution is estimated on the basis of public lamps installed within the municipal urban territory and usually comes as an item of the consumer electricity bill.

Municipalities that hire over 1,000 civil servants (employees) may establish their own social security systems and introduce social contributions to keep their financial and actuarial balance. Of course, in this case, the fee is payable solely by public sector employees.

3.3. Fees

Municipal revenue is composed of hundreds of different fees. Business permits and construction licensing are examples of the various types of municipal fee.

State (And Federal District) Taxes 4

4.1. Tax

The States and Federal District are empowered to levy the following taxes:

- ICMS - tax on purchase and sales of goods, interstate and inter-municipal transport, and communications (State VAT);
- ITCMD - Inheritance and Donation Tax ;
- IPVA- tax on ownership of motor vehicles (car / boat / aircraft).

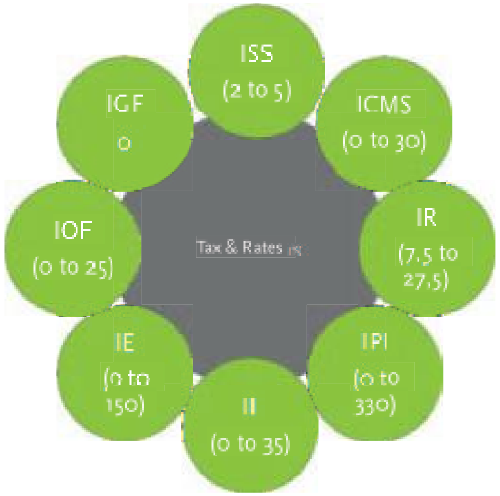

Fig. 20 Main Taxes & Rates

ICMS is the main State tax, and is due on operations involving the circulation of goods (including manufacturing, marketing, and imports) and on interstate and inter-municipal transport and communications services. It is non-cumulative (debit may be offset by credits arising from the purchase of raw materials, intermediary products, and packaging materials), and the rates below apply:

- Tax credits for goods destined to become fixed assets may be accepted, subject to certain restrictions;
- Intrastate transactions rates normally vary from 0 % to 30%;
- Rates applied to interstate commerce are 7% or 12%, depending on the destination of the goods;
- Export goods are exempted from ICMS and the credit may be kept.

4.2. Contributions

The Brazilian federal constitution allows public entities to establish their own social security system and introduce social contributions to keep their financial and actuarial balance. The social contribution is payable by civil servants (public employees only).

4.3. Fees

As well as the municipalities, States may charge for services which are specifically requested. Examples of fees charged by the States and Federal District relate to business registration and also to the initiating proceedings in the state judicial system.

Federal Taxes 5

- IR – Income Tax
- IPI – Tax on Industrialized Goods
- II – Import Tax
- IE – Export Tax
- IOF - Tax on Credit and Exchange Transactions
- ITR – Rural Land Property
- IGF - Tax on Large Fortunes

5.1. IR

IR – Income tax (Imposto de Renda) is levied on the income and increases in the assets of individuals and eligible legal entities.

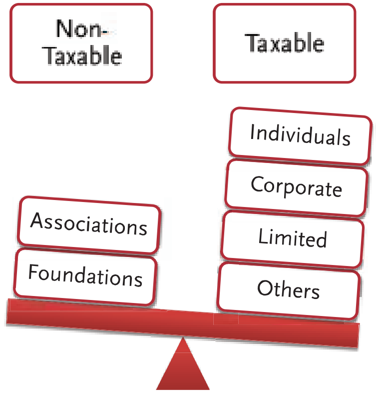

Fig. 21 Main Taxable & Non-Taxable Entities

5.1.1. Individual Income Tax

IRPF - Income tax on individuals is assessed on income and wealth increases of resident individuals from domestic or foreign sources at rates of 15% and 27.5% (depending on the income bracket), and on capital gains the rate of 15%, except for gains originating from investment in the stock exchange and financial funds, for which the rate is 20%.

5.1.2. Corporate Income Tax

IRPJ – Income tax on legal entities (corporation tax) is assessed on profits and capital gains generated by operations in Brazil or abroad. Since the companies comply with the required terms, they may choose the basis on which their profits are liable for tax, which may be their net profits, their presumed profits or their arbitrated profits.

5.1.2.1. Presumed Profits

This system is very common in Brazil and the choice must be elected by April of each tax year.

Under the presumed system, a company's real profit is irrelevant. Taxes are levied on basis of an estimated profit of between 1.6% and 32%. Profits are taxed at normal rates of 15% plus 10% on profits above R$ 240,000.00. The tax basis for the social contribution payable on profits is 12% of gross income or 32% in case of service companies.

Corporate entities MAY NOT choose to pay under the presumed profits system if:

- their annual income was in excess of R$ 48,000,000.00 (past year);
- they are commercial banks, investment banks, development banks, savings and lending organizations, credit, financing and investment organizations, real estate credit entities, securities or currency exchange houses, leasing companies, credit co-operatives, insurance companies and retirement plan bodies open to the public and factoring entities;
- they receive profits, capital gains or income from overseas;
- they wish to benefit from tax incentives;
- they have paid tax under the estimated system during the same tax year.

Alternatively, there is the SUPER-SIMPLES option for those companies whose annual gross revenue is limited to R$2,400,000.00.

In Brazil, fiscal year follows the calendar year, i.e (jan-dec).

5.1.2.2. Net or Real Profit

Taxable net or real income is equal to net profit as determined in the quarterly or annual balance sheets and adjusted for additions and deductions specified by income tax legislation. Corporations taxed on the basis of net profit may choose to pay tax in monthly installments on the basis of estimates, provided they follow certain conditions established under income tax legislation.

The current corporate income tax rate is 15%, whether calculated on net profit, assumed profit, or arbitrated profit, whatever the company's business, but a 10% supplementary tax is applicable to the portion of net profits which exceeds R$ 20.000,00 per month.

5.1.2.3. Profit Taxation

As of January 1, 1996, regardless of whether assessed on the basis of net profit, assumed profit, or arbitrated profit, the profits or dividends assessed, paid out or credited to individuals or corporations domiciled in Brazil or abroad, are no longer subject to income tax (either withheld at source or due on taxpayer's return).

5.1.2.4. Tax Losses

In Brazil, carry-back of losses is not allowed. Although companies may carry forward tax indefinitely against future profits, there is a limitation and companies can only set off 30% of the current year's taxable income.

5.1.3. Non-resident Income Tax

Withheld income tax (Imposto de Renda na Fonte – IRF) is due on income (not profit) paid, credited, remitted, or delivered to non-residents, at the rate of 15% or 25% depending upon the beneficiary's country of residence and the nature of the income.

5.1.3.1. CIDE

As of January 1, 2001, a 'Contribution of Intervention in the Economic Domain - CIDE' is due, at the rate of 10%, on remittances of royalties or compensation deriving from technology transfers in cases where the withheld income tax rate is 15%. This does not apply to profits and dividends, which are exempt from withheld income tax.

For more information about this federal contribution, please see the topic "Union Federal Contribution".

5.1.3.2. Transfer Pricing

As of January 1, 1997, new rules were introduced in income tax law to regulate transfer pricing in business transacted by resident individuals or corporations with non-resident parties for import and export, and interest payments abroad. These rules apply in the following situations:

- When a corporation domiciled in Brazil conducts business with non-domiciled related parties;
- When a domiciled individual or corporation carries out business with a related or unrelated party domiciled in a country where income tax is not charged or is assessed at a rate lower than 20%, or where the domestic legislation maintains secrecy with regard to equity participation or corporate ownership.

For more important information on transfer pricing, please see the relevant section in the chapter on FOREIGN TREATIES & TRADES.

5.2. IPI

IPI - The tax on industrialized goods (Imposto sobre Produtos Industrializados) is liable to tax on output and on the importation of industrialized goods. IPI is non-cumulative and therefore, tax due may be offset by credits arising from the purchase of raw materials, intermediary products, and packaging materials. However, no credits are granted for goods that become fixed assets.

The rates at which IPI is charged on the value of industrialized goods, as they are imported or dispatched from domestic plants, varies in accordance with the nature of the goods.

Export goods are exempted from IPI.

5.3. IOF

IOF (IOC) - Tax on credit and exchange transactions, insurance and securities (Imposto sobre Operações Financeiras) is due on bank loans and similar transactions, foreign currency transactions, insurance premiums, and securities traded. The tax is due on loans made by any legal entity to an individual (stock holder, director, employee, etc.) and the rate varies depending on the type of operation.

5.4. IGF

IGF - The tax on large fortunes (Imposto sobre Grandes Fortunas – IGF) is provided for by the federal constitution, but has not yet been instituted.

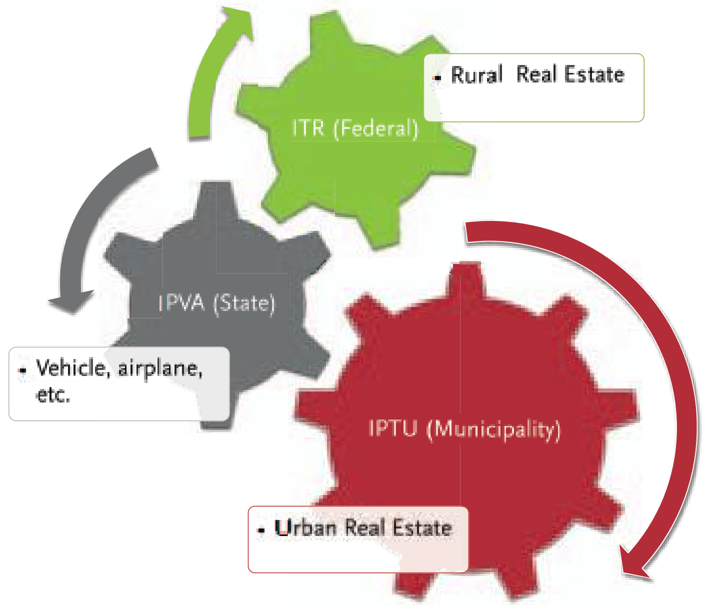

Fig. 22 Property´s Taxes

Federal Contributions 6

The Federal Government has "the key to the door" to open an array of federal contributions. The following charges (or social contributions) to fund social programs are the most commonly levied contributions.

6.1. CSL

CSL- Social contribution on corporate profits levied on pre-tax profits, assessed in accordance with commercial law, with adjustments and exceptions as set forth in law. The general current rate is 9%.

6.2. COFINS

COFINS - Social contribution for funding social security levied monthly on the gross income. Current rates are 3% and 7.6%, the former being cumulative and the latter non-cumulative, in accordance with criteria as set forth in law. Export goods are exempted from COFINS.

6.3. PIS

PIS - Contribution toward the social integration program levied monthly on the gross income of corporate entities. Current rates are 0.65% and 1.65%, the former being cumulative and the latter non-cumulative, in accordance with criteria as set forth in law.

Export goods are exempted from PIS, and non-profitable legal entities contribute with payment of 1% on the monthly payroll.

6.4. PIS & COFINS Importation

PIS & COFINS - Contribution toward the social integration program (PIS) and social contribution for funding social security (COFINS), levied on imports, assessed on the customs value of goods or the price paid for services, including applicable taxes. The general rates are 1.65% for PIS/PASEP, and 7.6% for COFINS, aside from other specific rates.

6.5. INSS & FGTS

INSS - Payroll charges for social security contributions levied on the monthly payroll.

Employers must withhold this charge on behalf of their employees at a rate which varies from 8% to 11%, and at the rate of 11% from self-employed individuals. In both cases, the basis for calculation of this charge is limited to R$ 3,416.54 (Feb/2010).

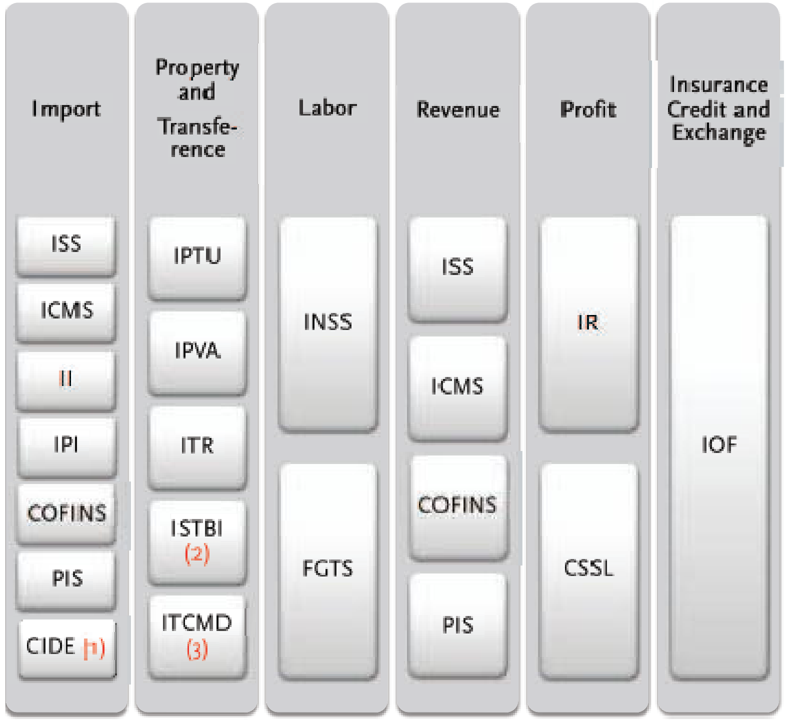

Fig. 23 Main Transactions x Taxation

Notes:

(1) Special contribution may be created at any time for the purposes of protecting some domestic industries. CIDE for gas imports, software imports and film imports and some remittances abroad are examples of CIDE currently charged in Brazil.

(2) ISTBI or ITBI - If the transfer results from a purchase, it will be charged by the Municipality where the property is located.

(3) ITCMD or ITC - If the transfer results from donation or inheritance, it will be charged by the State where the property is located.

Companies pay INSS at the rate of 20% on payments to individuals for services performed, with no ceiling, plus work accident insurance contributions charged at a variable rate (1% to 3%) with another 5.8% going to autonomous federal social services (SESI, SESC, FNDE, SENAR, SEBRAE), culminating in a total of 28.8%.

See the chapter on Labor and Charges for more details on these contributions.

6.6. CIDE

CIDE- Contributions to intervene in the economic domain are due in a variety of different instances. One of them is fuel imports and trading in the domestic market, which is charged at specific "CIDE-Gas" rates. Another example is the "CIDE-Remittance" applied at a rate of 10% to remittances to foreign individuals for royalties or technology transfers and administrative services.

Similarly, CIDE is due at the rate of 10% on remittances of royalties or compensation deriving from technology transfers, in cases where the withheld income tax is applied. This does not apply to profits and dividends, which are exempt from withheld income tax.

7 Federal Fees

Union federal fees encompass other categories of fees ranging from passport issue to registering a business with the regulatory agencies.

One example of the latter is the R$10,000.00 fee charged by the Union to "authorize" each graduation course in private universities.

8 International Tax Treaties

In the field of tax-related international trade issues, Brazil has signed, ratified and incorporated into its domestic law a variety of international tax agreements.

8.1. Treaties for the Avoidance of Double Taxation

Argentina
Austria
Belgium
Canada
Chile
China
Czech Republic
Denmark
Ecuador
Finland
France
Hungry
India
Israel
Italy
Japan
Korea
Luxembourg
Mexico
Norway
Netherlands
Philippines
Portugal
Slovakia
South Africa
Spain
Sweden
Ukraine

Source: Receita Federal do Brasil, Oct 2009

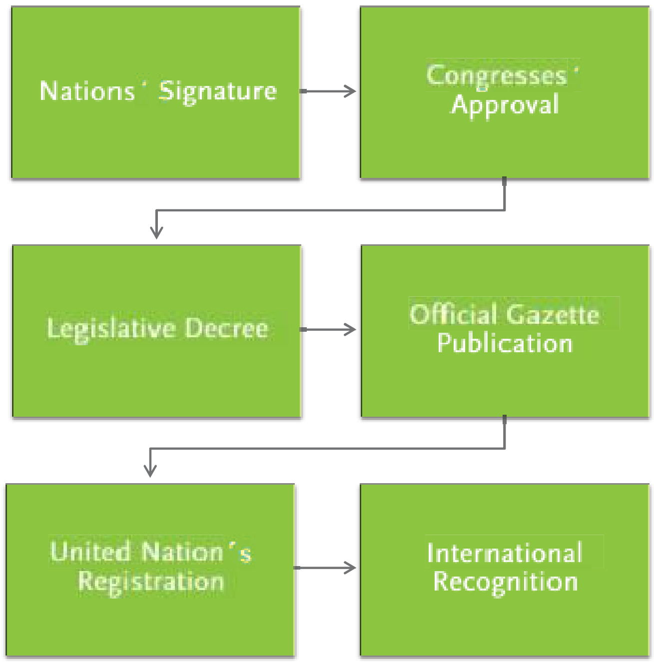

Fig. 24 International Treaty Recognition

Please see the next chapter on how Foreign Treaties and Trades operate in Brazil