

AN ALERT FROM THE BDO INTERNATIONAL TAX PRACTICE

# BDO KNOWS: INTERNATIONAL TAXATION

## ►SUBJECT

## PUTTING BRAZIL'S TAX SYSTEM IN PERSPECTIVE

The World Bank published a study<sup>1</sup> estimating the time spent by companies to comply with direct, indirect, and labor tax obligations in several countries. Among 185 countries, Brazil unfortunately ranked highest—with an average of 2,600 hours per year/per company to comply with tax filing obligations.

### Selected Country Listing (rank, country name, and number of hours to meet compliance requirements)

Ranking	Country	Hours (2013)
1	Brazil	2,600
24	Argentina	405
38	Mexico	334
124	United States	175
150	Canada	131

The 2,600 required hours is due to Brazil's complicated tax legislation and the number of tax returns required to be filed. Brazilian tax returns contain 100% of the sales and purchase information of the company including identification of its suppliers, customers and employees, and the amount of its purchases, inventory balances, etc. The tax return supporting documentation contains 100% of the accounting entries.

In addition to the complexity of the Brazilian tax rules, Brazilian tax authorities impose some heavy fines for filing incorrect or incomplete information. The fine can be 0.2% of the prior month's revenue per tax return.

## ►PROVISIONAL MEASURE 627/13

In 2008, Brazil adopted International Financial Reporting Standards ("IFRS"). A year later, Brazil created a transitory tax regime to ensure that the move to these new accounting standards did not affect a company's income tax calculation. As the transitory tax regime expires in 2015, Brazil issued a government decree, Provisional Measure ("MP") 627/13, bringing important changes in the corporate income tax legislation and controlled foreign corporation ("CFC") rules. Under Brazilian law a decree must be converted into law within 120 days.

<sup>1</sup> The study may be found at <http://data.worldbank.org/indicator/IC.TAX.DURS>.



## CONTACT:

**ROBERT PEDERSEN**, International Tax Practice Leader  
212-885-8398 / rpedersen@bdo.com

**HOLLY CARMICHAEL**, Partner  
408-352-1985 / hcarmichael@bdo.com

**SCOTT HENDON**, Partner  
214-665-0750 / shendon@bdo.com

**CHIP MORGAN**, Senior Managing Director  
310-557-7517 / cmorgan@bdo.com

**BRAD RODE**, Partner  
312-233-1869 / brode@bdo.com

**WILLIAM F. ROTH III**, Partner  
616-776-3761 / wfroth@bdo.com

**JERRY SEADE**, Principal  
713-986-3108 / jseade@bdo.com

**BOB BROWN**, Partner  
412-281-6018 / rmbrown@bdo.com

**FABRIZIA HADLOW**, Senior Manager  
312-239-9224 / fhadlow@bdo.com

MP 627/13 includes numerous changes to the income tax legislation, including how a company calculates its taxable income. The decree has more than 100 articles and 500 changes, including the following:

- Companies will be required to file a digital income tax return form, with a penalty not to exceed R\$5 million for failure to file such form.
- Goodwill will be calculated under the IFRS rules, and a company must register a report with the Brazilian authorities.
- Brazilian multinationals will be allowed to consolidate the profits and losses of their foreign subsidiaries to determine the taxation of their overseas earnings.
- CFC legislation allows for deferral of taxation on foreign profits, with the minimum tax of at least 12.5% per year.

The decree needs President Rousseff's signature and is expected to become law with substantially the same provisions as those approved by the Brazilian congress.

## ▶ TRANSFER PRICING

In addition to heavy compliance burdens, Brazilian transfer pricing requirements do not follow Organization for Economic Cooperation and Development or United States transfer pricing rules. Brazilian transfer pricing rules are unique, with fixed formulas and profit margin requirements that do not consider economic, risk, and functional analysis. For this reason, efforts to comply with Brazilian transfer pricing rules may be significantly greater than other jurisdictions around the globe.

## ▶ BDO BRAZIL: HIGHLIGHT OF TAX SERVICES

**Tax return validation:** As noted above, Brazil's tax compliance requirements average 2,600 hours per year per corporate entity and new rules are being introduced for the determination of a taxpayer's taxable income. To help clients navigate through the complexities in Brazil's tax rules, BDO Brazil has developed a software-based tool to cross-check the information included in several of the tax returns filed by companies. The software allows BDO Brazil to identify missing or incorrect information and provide advice on the best way to solve problems commonly found within the returns. This is an important service offering that increases the accuracy of Brazilian tax filings and reduces the risk of penalties for incorrect tax filings.

**Transfer pricing calculations and documentation:** Whether we assist clients by advising on transfer pricing matters, review transfer pricing documentation or prepare transfer pricing studies, BDO has the global transfer pricing expertise to assist clients with the unique demands the Brazil transfer pricing rules create. While working with clients to gather information, identify transactions with related parties, and identify transactions with persons located in tax-preferred jurisdictions, BDO will look for opportunities to apply methodologies to optimize their Brazilian and worldwide tax positions.

As the Brazilian tax legislation allows for the use of different methods for calculating intercompany pricing charges within the same transaction, companies may use the most suitable transfer pricing method applicable for the transaction. We assist clients in determining which method or methods can provide the best answer.

## ▶ HOW BDO CAN HELP

BDO USA, LLP, through its United States/Latin America Country Desk, has extensive experience in United States and Brazil cross-border structuring matters. BDO USA, LLP, BDO Brazil and the other members of the BDO International network can assist you in analyzing the effects these changes may have on your operations.

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