

MEMORANDUM TO CLIENTS

08.28.2014

STOCK-FOR-STOCK MERGER – IMPOSITION OF IRPF

On August 22, 2014, it was published the Response to Inquiry no. 224, issued by the General Tax Coordination of the Brazilian Revenue Service (“COSIT”). Such Response provides the moment in which the Individual’s Income Tax (“IRPF”) is levied on the capital gain realized on a stock-for-stock merger, by the individual Stockholder.

The COSIT explains that *“in the stock-for-stock merger transaction, a company acquires all of the shares of the other, but the latter is not extinguished, continuing to have rights and obligations”*. Under Article 252 of Law no. 6.404/76, the acquiring company (“**Company A**”) will increase its capital, pursuant to the stockholders’ resolution, which shall be subscribed by the stockholders of the target company (“**Company B**”) by transferring the target company’s stocks.

Thus, the stockholders of **Company B** will receive stocks of **Company A** in exchange for the stocks held by them in **Company B**, becoming stockholders of **Company A**; this company, in turn, will become the sole stockholder of **Company B**, its wholly owned subsidiary.

According to the understanding of COSIT, the capital contribution by individuals through the transfer of assets is considered a sale for IRPF purposes, if any capital gain is assessed on such transaction, i.e., if the appraised value of the stocks that are being contributed exceeds its book value declared in the Stockholder’s Income Tax Return.

Thus, COSIT understands that if any capital gain is realized when the stockholder contributes the stocks of **Company B** into **Company A** and, consequently, receives shares in lieu of the stocks previously held, then the IRPF will be due on such transaction.

Lastly, COSIT clarified that the tax treatment applied to the stock-for-stock merger doesn’t apply to merger transactions, since they are distinct corporate transaction. In company mergers, the absorbed company loses its legal personality, and the surviving company becomes responsible for all duties and obligations of the absorbed company.

Should you require any further information on the above matter, please feel free to contact us.

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