memorandum to clients

10.25.2017

ICMS Covenant No. 106/2017 – Imposition of ICMS on software sales by download

The ICMS Covenant No.106/2017, dated of October 5, 2017, sets forth the imposition of ICMS regarding operations with digital goods traded in the electronic commerce.

The above mentioned covenant enables all Federation States to impose ICMS on the sale of standardized software, electronic games, apps, digital files and similar products, despite the possibility of customization by download or streaming, as of April 1st, 2018.

According to the Covenant, the ICMS will be due to the State where the customer resides. The taxation will cover all operations with digital data that are marketed on websites or digital platforms, despite the existence of periodic payment.

In order to meet the new obligations stablished by the Covenant, companies must register in all the States Taxpayers' Register, where they perform internal sales or import operations. In addition, the States may stablish certain requirements to validate the company's register. Apart from that, all States may also exempt companies from registering. When exempted from registration, companies must collect taxes using the National Payment Form for State Taxes ("Guia Nacional de Recolhimento de Tributos Estaduais – GNRE") or another tax payment form fixed in the State's law.

The ICMS Covenant No. 106/2017 also allow the States to transfer the collection obligation to the following third parties; (i) the one who, due to the marketing contract, perform the merchandise offer, trade or delivery; (ii) the financial intermediary, including the credit card administrator, or any other payment method; (iii) the acquirer of the digital good, in the hypothesis in which the taxpayer is not registered in the State where the product is destined; and (iv) the debit card administrator or financial intermediary responsible for the currency exchange in import operations.

In addition, it also states that operations with digital merchandise by download or streaming prior to the sale to final consumers will be exempt of ICMS taxation.

Please note that this is not the first attempt of Confaz publishing an agreement allowing ICMS taxation on software. ICMS Covenant No, 181 dated of December 28, 2015, authorized the granting of reduction on the ICMS's taxable basis so that the tax burden would correspond to, at least, 5% (five percent) of the software or similar operation value, traded by any mean, including electronic data transfer.

São Paulo State, even before the publishing of ICMS Covenant No. 181/2015, had already published the State Decree No. 61.522/2015 in order to change the prior provision that only allowed the taxation of twice the media value, to state that the ICMS would be imposed on the whole operation value.

Later, after questionings from taxpayers regarding the above mentioned Decree, the State of São Paulo suspended the ICMS taxation on software and similar sales until the definition of the place where taxable event will deemed to be occur, according to the ICMS Agreement No. 181/2015.

The State of São Paulo, aligned with the current understanding of Confaz, published the Normative Decision CAT No. 4, dated of September 20, 2017, reaffirming its jurisdiction to tax ICMS on digital standardized goods and establishing that as soon the place where the tax event is deemed to be occurred is stablished, it would start taxing it.

schneider, pugliese,

On the other hand, the Municipal Secretary of the Treasury of Municipality of São Paulo has recently edited the Regulatory Opinion SF No 1, dated of July 18, 2017, indicating that the licensing and assignment of the rights of use of software, either by physical support or download, or even when installed from an external server ("Software as a Service – SaaS"), being it either a customized software on demand or a standardized ("off the shelf") software is subject to the ISS (Municipal Tax on Services).

Due to this situation, a new harmful tax competition between the State and City of São Paulo is established, disregarding the consolidated decision of the Supreme Court (STF) in the RE 176.626-SP, which stated that: (i) software manufactured in large scales and in physical support (named "off the shelf software") are only taxed by ICMS; on the other hand (ii) the software that do not have a physical support, which is, the ones that are understood as incorporeal goods, are only taxed by ISS, since they are defined as "licensing or assignment of the right to use a software".

Regarding the taxation on software via download, STF does not have a consolidated understanding yet. There is only one precedent under analysis by the Supreme Court's Plenary under ADI 1945/MT, which analyzes the constitutionality of Mato Grosso's State Law 7.098/98. By a majority vote, in a preliminary decision, it was decided that software via download should be given the same tax treatment of software contained in a physical support. The final decision on the case awaits definitive ruling by STF.

Notwithstanding the above, we highlight that the ICMS Covenant 106/2017 may be subject to questionings. According to Section 146 of the Federal Constitution, only Complementary Laws can solve tax jurisdiction conflicts between States and Cities, in addition to stablish the taxable event, the taxable basis and the taxpayers responsible for the tax collection. For that reason, it would be necessary the edition of a Complementary Law in order for the States establishing its taxation.

Nonetheless, the changes brought by ICMS Covenant 106/2017 are yet to be ratified by the States, which will make public State Decrees internalizing such provisions to regulate the taxation and the ancillary obligations regarding the above mentioned operations.

The Schneider, Pugliese, Sztokfisz, Figueiredo e Carvalho Advogados Team (contato@schneiderpugliese.com.br)

r. Cincinato Braga 340 , 9º andar
São Paulo , SP , Brasil , 01333-010
tel +55 11 3201 7550 , fax +55 11 3201 7558

Brasília Shopping , SCN quadra 5
bloco A , Torre Sul , 14º andar , sala 1406
Brasília , DF , Brasil , 70715-900
tel +55 61 3251 9400 , fax +55 61 3251 9429

schneiderpugliese.com.br