tax bulletin

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The Administrative Council of Tax Appeals

Specific tax report nº 98 • Year IX • May 2016

Dear Readers:

The purpose of this **Tax Bulletin # Administrative Council of Tax Appeals** is to inform our clients and those interested in the main issues being discussed and decided in this court.

In this 98th edition of our newsletter, we will comment on a decision in which the Administrative Council of Tax Appeals ("CARF") canceled an assessment issued for the collection of IOF/Credit on checking account transactions between companies of the same economic group, as it viewed that such transactions may not be considered loans.

We have also analyzed an appellate decision in which the Administrative Panel canceled an assessment of Individual Income Tax ("IRPF"), recognizing the nullity by statutory defect arising from the failure to comply with the accrual basis regime for the taxation of earnings received cumulatively by an individual, highlighting, in addition, CARF's impossibility of redoing the assessment, which is an exclusive power of the Assessing Authorities.

To directly access the text referring to each of these topics, click on:

IOF – Non-Levy – Checking Account – Connected Companies

IRPF – Earnings received cumulatively – Statutory Defect – CARF's impossibility of reassessment

Schneider, Pugliese, Sztokfisz, Figueiredo e Carvalho Advogados is available to its clients should they have any questions on the decisions commented on in this newsletter.

Enjoy your reading!

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"IOF. CHECKING ACCOUNT BETWEEN CONNECTED COMPANIES. NON-LEVY. (...)
If the Tax Authorities do not prove that the transactions recorded in the Taxpayer's books must have their legal nature reassessed, since they would have characteristics of a "credit transaction corresponding to a loan", the presumption of veracity and legitimacy of the books must prevail, there being no IOF charged on commercial transactions recorded in the checking account between connected companies."

This decision deals with an Assessment Notice issued for the collection of the Tax on Financial Transactions, with reference to credit ("IOF/Credit"), levied on checking account transactions between legal entities of the same economic group.

According to the Tax Authorities, the transactions in question have the legal nature of financial loans and, under such classification, are subject to the charge of the IOF/Credit, pursuant to article 13 of Law no. 9,779/99.

The taxpayer filed an Administrative Defense against the Assessment Notice, claiming that the transactions recorded in the checking account do not evidence a credit transaction subject to the IOF charge, but a mutual availability of funds between companies belonging to the same economic group, not subject to the charge of the tax.

In the lower administrative court, the Administrative Defense was dismissed, which then led to the filing of a Voluntary Appeal.

When examining the Voluntary Appeal, the CARF fully cancelled the assessment, as it viewed that the checking account transactions did not have the alleged loan nature identified by the Tax Authorities and, for this reason, would not be subject to the IOF/Credit.

In the appellate decision, the distinct legal nature of checking account transactions and loan transactions loan stood out, and only on the latter could the IOF/Credit be levied. In fact, under the checking account contract, ruled by article 4, §2, letter "b", of Law no. 7,357/1985, the parties agree to make reciprocal remittances of amounts deriving from legal transactions, seeking the offsetting between credits and debits of the parties to verify, at the end of the contract term, the existence of any payable balance. Differently, the loan, regulated by article 586 of the Civil Code, consists of the loan of fungible items, which are to be returned in the same kind, quality, and quantity by the borrower to the lender.

Thus, the Rapporteur of the appellate decision stated that the use of a checking account does not imply the existence of loan transactions subject to the charge of IOF/Credit. Nevertheless, it should be verified that, in this specific case, the checking account was supposedly used to perform loans between the companies.

In this regard, in the case in question, it was evidenced that the accounting entries made as checking account corresponded to effective commercial transactions, service renderings, asset sharing and transfers between companies of the assessed taxpayer's economic group. Therefore, the Rapporteur then concluded that "there is no loan, since the amounts constitute the record of transactions between related companies, which have great synergy in relation to their commercial operations, leading to the need for checking account bookkeeping, so that such events may be properly identified, and are in no way classified under the elements that constitute a loan (article 586 and following articles of the Civil Code)."

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Still in this regard, the Rapporteur stressed the evidentiary force of the taxpayers' books and accounting records, which, in the case at issue, were not disregarded by the Tax Authorities, who did not devote much effort in demonstrating any irregularities in the recording of the checking account transactions.

Lastly, one of the members of the Administrative Court reinforced the differences between checking account transactions and a loan, pointing out the need to follow the concepts of Private Law in the interpretation of tax levy instances, thus concluding it is impossible to demand the tax in this specific case.

CARF then partially granted the Voluntary Appeal in order to fully cancel the IOF/Credit levied on checking account amounts.

"INDIVIDUAL INCOME TAX. EARNINGS RECEIVED CUMULATIVELY. ACCRUAL BASIS ACCOUNTING.
The Income Tax levied on earnings received cumulatively is to be calculated according to the tables and tax rates in force at the time the amounts should have been paid. Precedents of the STF and of the STJ in the system under articles 543¬B and 543¬C of the CPC.
CARF'S LACK OF JURISDICTION TO REDO THE ASSESSMENT. EARNINGS RECEIVED CUMULATIVELY. EXCLUSIVE JURISDICTION OF THE ADMINISTRATIVE AUTHORITIES.
The assessment adopted a mistaken and discordant legal criteria in relation to STF and STJ case law, impacting the identification of the tax basis, current tax rates, and consequently the calculation of the due tax, which characterizes a statutory defect. The CARF lacks jurisdiction to redo the assessment with other legal criteria."

In the decision at issue, CARF analyzed the Assessment Notice issued for the constitution of the IRPF relative to the fiscal year of 2010/calendar year 2009, on earnings received cumulatively by an individual.

The Tax Auditors verified the taxpayer's omission of earnings received cumulatively by a legal entity arising from a judicial action, recording the due tax on the assumption that they should have been taxed in the month they were earned (cash basis accounting).

In an Administrative Defense, the taxpayer then claimed, in sum, the right to IRPF exemption, pursuant to article 6, item XIV, of Law no. 7,713/88, also on the differences received in relation to administrative or judicial proceedings, as she suffers from a debilitating disease.

When hearing the Administrative Defense, the Federal Revenue Judgment Office ("DRJ") upheld the assessment, based on the submitted official medical report, which states as the date of start of the exemption being April 18, 2009, meaning that, as they were released in February 2009, the earnings received cumulatively were not supported by the exemption rule.

Dissatisfied with the decision, the taxpayer then filed a Voluntary Appeal, reiterating the arguments of the Administrative Defense.

When hearing the matter, CARF decided to cancel the assessment due to statutory defect, given the violation of article 142 of the National Tax Code ("CTN"), after identifying an incorrect calculation of the tax basis and, as a result, of the undue tax rate of the IRPF and of the assessed tax amount.

When rendering his vote the Rapporteur Councilor sustained that the assessment was based on the assumption that the earnings received cumulatively should have been taxed in the month they were received (cash basis accounting) and not according to the time in which they should have effectively been paid (accrual basis accounting).

Thus, he upheld that the assessment had adopted a totally mistaken legal criteria and in disagreement with case law of the STF and STJ, leading to the occurrence of a statutory defect, based on article 142 of the CTN.

The Rapporteur Councilor based his opinion on the position expressed by the STF in Extraordinary Appeal no. 614,406, within a General Repercussion case, and in the position of the STJ in Special Appeal no. 1,118,429/SP, subject to the Repetitive Appeal system, whose compliance is mandatory by the CARF, by regulation.

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Furthermore, the Rapporteur Councilor then stated that the correct distribution of the amounts every month, under the accrual basis accounting, would certainly reach fiscal years previous to the fiscal year of 2010/ calendar year 2009, object of assessment, demonstrating the need of a new ex-officio assessment, and not only the rectification of the original assessment.

However, he concluded that the CARF lacks jurisdiction to redo the assessment, since this is exclusive of the Assessing Authorities, who verify the occurrence of the taxable event of the corresponding liability, determine the taxable matter, calculate the amount of due tax, and identify the tax debtor, pursuant to article 142 of the CTN.

Thus, considering the incorrect calculation of the tax basis, the applicable tax rate, and consequently of the assessed tax amount, the members of the Panel unanimously granted the taxpayer's appeal, in order to fully cancel the assessment.

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