tax bulletin

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The Administrative Council of Tax Appeals

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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 100th edition of our newsletter, we will comment on a decision in which the Superior Chamber of Tax Appeals ("CSRF") ruled for the prevalence of the new general rule over the more specific previous rule; and on the possibility of concomitance between the separate fine, for failure to collect monthly estimates as advance, and the voluntary fine, for the failure to collect the definitive tax.

We also analyzed an appellate decision in which the Administrative Council of Tax Appeals ("CARF") upheld the charge of the Corporate Income Tax ("IRPJ") and the Social Contribution on the Net Income ("CSLL") on profits earned through a Spanish company controlled by a Brazilian company, as it viewed that there was no violation of article 7 of the Treaty for the Avoidance of Double Taxation on Income ("TDT") entered into between the two countries.

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

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.

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"IRPJ PROFITS OF EXPORTS WITH INCENTIVES OF ABUNDANT MINERALS. SPECIFIC TAX RATE. INAPPLICABILITY. As Law no. 9.249, dated 1995, established an indistinct tax rate of 15% for the ascertainment of the IRPJ (with an additional 10%), repealing provisions determining otherwise, the specific tax rate of 18% for the profits of the exports with incentives of abundant minerals is not applicable (without any additional rate), provided for in Law no. 7.988, dated 1989, there being no prevalence of the previous special rule over the subsequent general rule.

PROSPECTIVE EFFECTS OF CLAIM PRECLUSION. CHANGE OF LEGAL CIRCUMSTANCES. The alteration to the factual or legal supports existing at the time the judicial decision is rendered, focusing on the discipline of continuous tax legal relations, causes, from then on, the cessation of the binding effectiveness emerging therefrom due to its final and definitive status. The final and unappealable decision ruling out the application of the specific IRPJ tax rate provided for in Law no. 8.034, dated 1990, to the Taxpayer's profits of exports with incentives of iron ore, in which the tax rate provided for in Law no. 7.988, dated 1989, remains applicable, has no effects for taxable events occurring in 2007 and 2008, pursuant to Law no. 9.249, 1995, which established an indistinct tax rate of 15% (with an additional 10%).

FINE FOR FAILURE TO COLLECT MONTHLY ESTIMATES. CONCOMITANCE WITH THE VOLUNTARY FINE. LEGALITY. The voluntary fine imposed for the lack of payment of the IRPJ ascertained at the end of the calendar year and the separate fine charged for the lack of collection of monthly estimates of IRPJ constitute sanctions with specific legal provisions (items I and II of article 44, respectively, of Law no. 9.430, date 1996), applied to different violations and calculated on different tax bases, where its simultaneous (or concomitant) application is possible."

The decision in question deals with a Special Appeal filed by the Attorney General Office of the National Treasury ("PGFN"), granted by the Superior Chamber of Tax Appeals ("CSRF"), in order to overturn the decision of the Administrative Council of Tax Appeals ("CARF"), which had partially granted the Taxpayer's Voluntary Appeal and dismissed the Ex-Officio Appeal. As a result, the CSRF restored the following: (i) the application of the IRPJ tax rate at 15%, as well as the additional 10% rate on the exceeding portion of the tax basis of R$ 20,000.00; and (ii) the concomitant application of the separate fine, for the non-collection of monthly estimates, with the voluntary fine, applied on the unpaid IRPJ debt after the annual adjustment.

In the case at issue, which refers to the ascertainment periods of 2007 and 2008, the Taxpayer was supported by a final and unappealable decision that removed the charge of the IRPJ increase created by Law no. 8.034/90 – expressly subjecting this decision to the taxation under Law no. 7.988/89, which provided for a specific IRPF of 18%, without any additional rate, for its activity. For the PGFN, however, as the Tax Assessment Notice was issued with the IRPJ tax rates contained in Law no. 9.249/95, which was not object of the judicial action at the time it was filed, there would be no judicial approval for the case under analysis.

Within this context, the Treasury resorted to the provisions of PGFN/CRF Opinion no. 492/2011, which established that "in case the facts existing at the time the decision is rendered are modified or in case the right then applicable to this case is altered, there is thus a new legal relation of substantive law".

In addition, the National Treasury claimed that there would be autonomy between the fines, which would be independent sanctions, on distinct violations, and there would be no impediment to its concomitant application.

For the Taxpayer, due to the fact that the judicial decision was rendered after the enactment of Law no.

9.249/95, it would then cover it; defending that the Treasury should have expressed its position in relation to the judicial action, opposing to the application of Law no. 9.249/95, losing its right to do so later, pursuant to the rule of the Brazilian Civil Code of Procedure.

Moreover, the Taxpayer claimed that Law no. 7.988/89 would not be part of the list of repealed rules contained in Law no. 9.249/95 and that that former Law would have a special nature, since it specifically mentions the activities whose taxation it rules. Therefore, as there is no express revocation, the more specific rules of the former Law would prevail over the general rule of the new Law.

Lastly, the Taxpayer stated the impossibility of concomitance of the fines, because at the end of the calendar year there would no longer be the possibility of making collections related to the advance of tax on the basis of estimates due during the calendar year, as they were replaced by the definitive tax. So, the possibility of collecting the separate fine charged on the estimates would be substituted by the possibility of assessment of the voluntary fine on the definitive tax that was not collected. For the taxpayer, the estimate would be part of the definitive tax, so that the simultaneity of both fines would constitute bis in idem.

When examining the IRPJ tax rates matter, the First Panel of the Superior Chamber of Tax Appeals viewed that: (i) as Law no. 9.249/95 was not dealt with in the judicial action, the substantive claim preclusion arising from that action did not support the Taxpayer as to the effects of this law; and that (ii) with the enactment of Law no. 9.249/95, the lawmaker repealed all the previous provisions determining otherwise, including Law no. 7.988/89 – the list of revoked rules stated in article 36 of Law no. 9.249/95 being a mere exemplification.

For the CSRF, this is confirmed when observing that the exception of the IRPJ tax rate of Law no. 7.988/89 was not included in Decree no. 3.000/99 (Income Tax Regulation), unlike other cases of distinguished tax rate existing at the time of enactment of this Regulation.

As to the fines, the Superior Chamber considered the concomitant application of the separate fine and of the voluntary fine is valid, as there would be a provision in the legal system for its simultaneous application. Along these lines, CARF Precedent no. 105 was ruled out under the claim that its applicability is limited to periods prior to the effectiveness of Provisional Measure no. 351/2007, which amended the text of Law no. 9.430/96 concerning the fines, among other topics.

According to the opinion passed by the Rapporteur Councilor, “with the legislation amendment to article 44 of Law no. 9.430, of 1996, there is a new situation regarding the application of these fines. In fact, the tax basis of the fine was no longer the ‘tax totality or difference’, but the ‘monthly payment amount’ on the basis of estimate, in addition to a reduction of its percentage to 50%”.

Thus, it was understood that as the Precedent’s text expressly refers to the separate fine that was provided for “in article 44 § 1, item IV of Law no. 9.430, dated 1996” and that today the equivalent sanction provision is found in item II of said article 44, the application of CARF Precedent no. 105 does not apply to facts occurring after this change to the text of Law no. 7.430/96. Therefore, for the CSRF, the separate fines on estimates and ex-officio fines on the definitive tax are currently imposed on different violations, provided for in different legal provisions, whose validity the administrative courts would not have jurisdiction to reject.

Thus, through a casting vote, the Special Appeal of the PGFN was fully granted in order to restore the Assessment Notice, applying the tax rate of 15% to the IRPJ (with an additional 10%), established by Law no. 9.249/95 and the concomitant application of the voluntary fine and the separate fine.

“PROFITS ABROAD. NATURE OF TAXATION. DOUBLE TAXATION AGREEMENTS. COMPATIBILITY. Regardless of its scope, article 74 of MP no. 2.15835/01 conforms to the rules created in several countries in line with the international fiscal transparency phenomenon. These are specific anti-avoidance rules whose purpose is to avoid the deferral of the taxation of profits of companies qualified as controlled foreign corporations (CFC). The law taxes a fictitious income of the Brazilian legal entity itself (the resident company). In other words, it views the resident company and, considering the fact that it has ownership interest in another company that ascertained profits abroad, it assumes that there is income availability and determines that a certain amount estimated based on the ascertained profits by the company abroad is to be taxed as profits of the Brazilian company. This is not the case of “presumed dividends”. For this reason, there is no violation of the double taxation agreements, both with regard to the provisions dealing with the profits of companies and to those dealing with dividends.

PROFITS ABROAD. OFFSETTING OF LOSSES. The offsetting of losses ascertained in a subsidiary abroad against the profits of this same subsidiary is conditioned to the recording of its financial statements with accounts and subaccounts translated into Portuguese and with their amounts converted into reais, classified according to the rules of the Brazilian commercial legislation, and its safeguard by the statute of limitations period and transcription into the accounting journal.”

The decision in question refers to a Tax Assessment Notice issued for the collection of the Corporate Income Tax (“IRPJ”) and the Social Contribution on the Net Income (“CSLL”) charged on profits earned by a company resident in Spain, controlled by a company resident in Brazil.

According to the Tax Authorities, the profits abroad should be added to the taxable income and to the tax basis of the CSLL ascertained by the Brazilian company, and were considered to be available to the holding company on the date of the balance sheet relative to the period in which they were ascertained by the foreign subsidiary. It is of note that the case occurred prior to the enactment of Law no. 12.973/2014, which introduced a new law referring to the worldwide taxation system applicable to legal entities resident in Brazil.

Against the Tax Assessment the Taxpayer then filed an Opposition, claiming that the collection would violate the provisions of article 7, item 1, of the Treaty for the Avoidance of Double Taxation on Income (“TDT”) entered into between Brazil and Spain, which determines that the profits earned by a company resident in one of the Contracting States will only be taxable in the State of residence of the company. Furthermore, the taxpayer claimed that in the event the profits were advanced dividends, distributed in favor of the Brazilian holding company, article 23, item 4, of the mentioned TDT would be violated, which provides for the exemption of taxable dividends in Spain earned by residents in Brazil (participation exemption). Lastly, the taxpayer defended the lack of grounds of the assessment, given that the Spanish subsidiary holds accumulated losses, which, when offset against the profits it ascertained in the base year subject matter of the assessment, would not result in payable IRPJ and CSLL.

In the lower administrative court, the Federal Revenue Judgment Office (“DRJ”) of Rio de Janeiro upheld the assessments. In turn, when examining the Voluntary Appeal filed by the taxpayer and the Ex-Officio Appeal filed by the National Treasury, the CARF also upheld the collections.

In the appellate decision rendered by the CARF, the Rapporteur pointed out that the Brazilian legislation that determines the taxation of profits, earnings and capital gains ascertained through subsidiaries or associate companies abroad does not intend to tax the profit earned by the foreign legal entity but rather the fictitious income earned by the Brazilian legal entity abroad.

In fact, according to the Rapporteur, the Brazilian legislation considers the fact that the company resident in Brazil has ownership interest in the company that ascertained the profits abroad and, by fictitiously assuming this income as being available on the date of ascertainment of the balance sheet, it determines that a certain amount estimated based on the ascertained profits by the company abroad is to be taxed as profits of the Brazilian company. This assumption would be compatible with the concept of income adopted in Brazil, supported by the theory of equity increase.

The appellate decision also expressed the position that the Brazilian legislation does not violate the provisions in article 7, item 1, of the Brazil-Spain TDT, since, according to the Rapporteur, the provision in question consists of the "form that the Model Conventions chose to say that the country of source may only tax the profits of its non-resident if the latter exercises an activity in this country through a permanent establishment". Therefore, article 7, item 1, of the TDT would not prevent the adoption of rules of controlled foreign corporations ("CFC Rules"), which are instruments to protect the local tax basis, which would be possible to infer from the comments to the Organisation for Economic Co-operation and Development ("OECD") and from the final report released in Action 3 of the Base Erosion and Profit Shifting ("BEPS") project.

Furthermore, the Rapporteur stated that it is not possible to regard the system adopted by the Brazilian law as a sort of taxation of "presumed dividends", owing to the incompatibility with the concept of dividend provided for in the Brazilian corporate legislation, and to certain aspects of the method of relief of the legal double taxation based on credit adopted by Brazil. Therefore, the Brazilian taxation on profits abroad would also not mean any violation of the participation exemption provided for in article 23, item 4, of the Brazil-Spain TDT.

Lastly, although he recognizes that, for purposes of determining the taxable income in Brazil, the Brazilian legislation provides for the possibility of absorbing the previous losses, accumulated by the subsidiary or associate company abroad, by the profits ascertained by this same subsidiary or associate company, the Rapporteur understood that, in the case at issue, the taxpayer had failed to meet the accounting and document requirements in order to prove the results abroad, provided for in Normative Rule no. 212/2002. According to the Rapporteur, the offsetting of the losses accumulated abroad has an exemption nature and, therefore, there would be no room to increase or reject the conditions imposed for its application.

In conclusion, the CARF partially granted the Voluntary Appeal filed by the taxpayer and dismissed the Ex-Officio Appeal of the National Treasury, upholding the requirement of the IRPJ and CSLL on the profits earned by the subsidiary in Spain.

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