tax bulletin

91

The Administrative Council of Tax Appeals

Specific tax report n° 91 • Year VIII • October 2015

Prezados Leitores:

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 91st edition or our newsletter, we will comment on a decision in which the Administrative Council of Tax Appeals ("CARF") reduced an ex-officio fine from 150% to 75%, due to the lack of requirements leading to its determination, as it was understood that the Taxpayer's act, when rectifying its Federal Tax Debts and Credits Statement ("DCTF") in order to remove the information of taxes originally stated as due, does not represent an intention to prevent the Tax Authorities' from identifying the occurrence of the taxable event of its tax liabilities, mainly when the debts were duly stated in the Social Contribution Ascertainment Statement ("DACON") and Corporate Economic and Tax Information Statement ("Corporate Economic and Tax Information Statement").

We also commented on a decision in which the CARF upheld the assessment of the Corporate Income Tax ("IRPJ") and the Social Contribution on the Net Income ("CSLL") on the undue premium amortization based of future profitability, as it viewed that the tax planning failed to present a business purpose and to prove the future profitability at the time of the investment.

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

IRPJ, CSLL, PIS, COFINS – Rectifying DCTF- Disregard of Ex-Officio Fine – Lack of Willful Intent, Fraud or Evasion

IRPJ and CSLL – Premium –Future Profitability – Undue deduction

O escritório **Souza, Schneider, Pugliese e Sztokfisz Advogados** encontra-se à disposição dos clientes para esclarecer quaisquer dúvidas acerca dos julgados aqui relatados.

Esperamos que tenha uma boa leitura!

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tax bulletin 91

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"MATTER: ADMINISTRATIVE TAX PROCEEDING
Calendar year: 2009, 2010
EVASION, FRAUD or COLLUSION. CHARACTERIZATION. PUNITIVE FINE.
The filing of Federal Tax Debts and Credits Statements ("DCTF"), in which the tax debtor states the inexistence of debts relative to Corporate Income Tax ("IRPJ"), Employee Profit Distribution Program ("PIS") and Contribution to the Social Security Funding ("Cofins"), and to the Social Contribution on Net Income ("CSLL"), does not characterize the practice of evasion, fraud or collusion, requirements for determining the ex-officio fine, when the sum of such taxes is correctly stated in the corresponding Corporate Economic and Tax Information Statements ("DIPJ") and Social Contribution Ascertainment Statements ("DACON").
These case records have been examined and discussed.
Members of the panel, by majority vote, have agreed to partially grant the voluntary appeal, in order to reduce the 150% fine to 75%, in disagreement with the Rapporteur's opinion. Councilor Marcelo Cuba Netto was appointed to draft the winning part, and Councilor João Carlos de Lima Júnior followed the divergence by the conclusions."

The decision in question deals with a Tax Assessment Notice issued for the establishment and collection of the IRPJ, CSLL, PIS and Cofins taxes related to the calendar years of 2009 and 2010, plus late payment interest and an ex-officio punitive fine of 150%.

In the examined case, the Taxpayer filed the DIPJs, DACON and DCTFs, stating certain amounts of those taxes as being due, and later filed rectifying DCTFs, stating the inexistence of the debts informed previously.

In the audit procedure, it was viewed that the Taxpayer's conduct would represent a willful intention to prevent the Tax Authorities from being informed of the occurrence of the taxable event of the tax liabilities, by the reiterated rectifications of the DCTF that canceled the payable balance of the taxes.

The Taxpayer then filed its Opposition, seeking to disregard the fine, claiming (i) there would be an error in the filling in of the rectifying DCTFs information, by mistake of the service provider hired to manage its accessory bookkeeping obligations, which mistook the Taxpayer's information for that of other clients; (ii) that there was never any intention of preventing the Tax Authorities from knowing about the occurrence of the taxable event of the mentioned taxes, since the original statements were correctly filled in, meaning there was no willful intent on the part of the Taxpayer; and (iii) that, when the same error was verified in the periods not comprised by the Audit, it made the respective corrections.

Alternatively, the Taxpayer sought the right to settle the assessed amounts with the inclusion only of the late payment fine (which is limited to 20%), fully cancelling the ex-officio fine.

The Opposition was dismissed by the Federal Revenue Judgment Office ("DRJ") and the 150% fine was maintained. Due to this decision, the Taxpayer then filed a Voluntary Appeal, reiterating the claims stated in its Opposition.

When analyzing the arguments, the CARF viewed that the ex-officio fine could not be completely canceled so that only the late payment fine would be applied, since this possibility is limited to cases in which the Taxpayer spontaneously pays the overdue tax, in other words, prior to any audit procedure, unlike what occurred in this case.

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As to the determination of this ex-officio fine, the CARF understood that with the rectification of the DCTFs only –upholding, however, the original DIPJs and DACONs, that is, including the information that was eliminated from the DCTF through rectification – it would not be possible to affirm that the Taxpayer sought to prevent the Tax Authorities from knowing of the occurrence of the taxable event, taking into account the statement of the taxes in other accessory bookkeeping obligations.

In fact, the Councilors, except for the Rapporteur, viewed that the Taxpayer's intention was only for the debts not to be promptly recorded as collectible, since the statement in the DCTF implied debt acknowledgment. Thus, it was then decided that, as there was no willful intention of the Taxpayer to prevent the identification of the taxable events by the Tax Authorities, this was not characterized as evasion, fraud or collusion – which, under the legislation (articles 71 to 73 of Law no. 4,502/64), are acts of willful intent capable of leading to an ex-officio fine.

Along these lines, given the lack of such requirements for applying the sanction, the panel partially granted the Voluntary Appeal, reducing the ex-officio fine from 150% to 75%.

"CORPORATE TAKEOVER. PREMIUM AMORTIZATION AT THE ACQUISITION OF SHARES. UNDUE DEDUCTION.
Premium amortization is allowed in situations in which a legal entity absorbs assets from another legal entity, as a result of a takeover, in which it holds the ownership interest acquired with the premium, including in case of a takeover of the holding company by its subsidiary. In this case, the amortization is undue, as the corporate transactions sought to abusively build, shape, and materialize the levy event of the rule of tax enjoyment of the premium, with the utilization also of an ephemeral company, of brief existence, which was not engaged in any other corporate activity. The defense, in an attempt to rule out the mentioned abuse of law, comprised in the seeking of tax economy, predominantly, failed to prove that the corporate engineering was justified in the optimization of operating results, and to prove this cause and effect relation.
PREMIUM. PROVE OF ITS FORMATION. NECESSITY. At the time of the ownership interest, the recording of the premium is to be based on the demonstration that the taxpayer will file it as bookkeeping proof. In this specific case, there is no timely proof of payment of the premium based on future profitability, other than the fact that there is no evidence of the performance of internal studies, having the taxpayer attached a type of report, written in English, without any date of preparation or signature, and lacking the elements that confirm the adopted assumptions. In the event the defense theory prevails, even spreadsheets without signature, therefore lacking the requirement of the existence of declaration of intent stated therein, or information provided by the Director of the investor himself, lacking the minimum substantiating evidence, could be accepted, in full compliance with the legislation in force. The legislation allows the amortization of the paid premium, provided that the taxpayer proves its economic fundamentals based on reliable evidence elements, without any reason for doubts. (...)"

The decision in question deals with a Tax Assessment Notice issued for the collection of the IRPJ and CSLL, related to the period from 2007 to 2009, as well as result of the rejection of premium amortization based on future profitability arising from the acquisition of investments in ownership interest.

In this case, in May 2006, a purchase and sale agreement of shares was entered into among a holding company of a Brazilian financial institution, its partners (individuals), and a company domiciled abroad, whose object would consist of the transfer of ownership of shares representing the totality of the controlling

interest of the mentioned financial institution to the latter company.

The disposal at issue involved a number of corporate transactions carried out in a short period.

First, the shareholders of the financial institution resolved on the takeover of the holding company and, on the same date, the totality of the financial institution's controlling interest was assumed by the acquirer domiciled abroad. There was a down payment for the ownership interest and the remainder was deferred, pursuant to the executed agreement.

Thereafter, the acquirer increased the capital of a company domiciled in Brazil ("Company A"), established a few months earlier, with the acquired ownership interest.

Next, the totality of the shares of Company A was transferred to another investment company domiciled in Brazil ("Company B"), set up on the same date as that of Company A. Two months later, Company B was taken over by the financial institution, meaning the premium generated in the initial investment was then used for fiscal purposes.

When carrying out the audit procedure, the Tax Agent viewed that the mentioned corporate restructuring only sought a tax economy, without any business purpose. The reason is that the only purpose of the corporate events carried out within few days seemed to be the exclusion, at the ascertainment of the tax bases of the IRPJ and CSLL, of the premium amortization amounts generated in the investment. Moreover, there could only be an amortization of the portion of the effectively paid premium.

Due to such, the Tax Agent rejected the amortization of the premium in the tax bases of the IRPJ ad CSLL, assessing the tax differences, plus interest and an ex-officio fine.

When examining the matter, the Federal Revenue Judgment Office ("DRJ") approved the opposition in relation to the amortization of the premium, as it viewed that the basic assumptions for the use of the premium were not met (there was no business purpose in the transactions and the effective payment of the premium). The appellate decision was then object of a Voluntary Appeal filed by the Taxpayer.

In the trial of the Appeal, the Councilor who rendered the concurring opinion upheld the assessment under the following arguments, among others: (i) only the effectively paid value of the premium could be used for fiscal purposes; (ii) there was no evidence of any extra-fiscal business purpose for the transactions (i.e., no operating gain was verified), and the verification of the dates on which the corporate transactions were performed evidence the abusive nature of the tax planning carried out; (iii) an operating company was utilized exclusively to allow for the fiscal use of the premium; (iv) there was no evidence of the performance of previous studies, based on legitimate documents, in order to substantiate the amortization of the premium based on future profitability, since the Taxpayer had submitted an internal report lacking the date on which it was prepared and/or signature and a report prepared by independent auditors after the completion of the transactions.

Through vote explanation, one of the dissented Councilors upheld the non-applicability of the business purpose in Brazil, the possibility of amortization at the payment of the remaining balance of the premium, and the sufficiency of the assessment report prepared after closing the transactions in order to prove the existence of the premium's economic fundamentals.

Due to aforesaid, with regard to the premium amortization issue, the CARF, through a casting vote, dismissed the Voluntary Appeal in order to maintain the tax credit assessment.

tax bulletin

91

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