Tax Bulletin

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The Administrative Council of Tax Appeals

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Dear Readers:

This publication **Tax Bulletin # The Administrative Council of Tax Appeals** aims to update our clients and others interested about the main subjects that are being discussed and judged in this body.

In this 71st edition of our newsletter, we will comment on a decision in which the Superior Chamber of Tax Appeals ("CSRF") recognized the ITR exemption on a legal reserve area, whose registration took place after occurrence of the taxable event.

We also analyzed a decision in which the Administrative Council of Tax Appeals ("CARF") declared the nullity of the tax assessment due to substantive flaw, on account of the lack of a written order from a relevant authority for the performance of a second inspection on identical.

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

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

Enjoy your reading!

Souza, Schneider, Pugliese e Sztokfisz Advogados

"TAX ON RURAL TERRITORY PROPERTY – ITR
In order for the legal reserve area to be excluded from the tax basis of the ITR, it must be registered separately from the property's record. This obligation derives from a harmonious and joint interpretation of the provisions in Laws no. 3393, of 1996, and no. 4.771, of 1965 (Forestry Code), even if the registration is verified subsequent to the occurrence of the taxable event, but prior to the start of the tax proceeding."

This case deals with a Tax Assessment Notice issued for the collection of the Rural Territory Tax ("ITR") of the fiscal year of 1999, due to the rejection of the amounts declared on the basis of a legal reserve area.

In examining the case, the Third Chamber of the former Third Taxpayers' Council , rejected the Voluntary Appeal, through a casting vote, maintaining the requirement related to the legal reserve area. In this decision, the Council found that the legal reserve area should not be charged by the tax. However, the legitimacy of the declared and controversial legal reserve should be demonstrated by presenting the record of the rural property, with the respective registration stated prior to the occurrence of the taxable event of the ITR.

The taxpayer then filed a Special Appeal against this decision, seeking to rule out the mentioned requirement, claiming there was no obligation to register the legal reserve prior to the occurrence of the ITR's taxable event.

With regard to the above argument, the Reporting Councilor examined the applicable legislation (Law no. 9.393/96, which governs the ITR, and Law no. 4.771/75, which created the Forestry Code) and the doctrine on the matter, stating the existence of two doctrine currents that deal with the effect of the legal reserve registration for purposes of exemption of the ITR. The former current views that the effect of the registration is constitutional and that, therefore, the right to the exemption of the legal reserve area would only exist if it is registered separately from the property's record, prior to the date taxable event. The latter current, in turn, claims the declaratory effect of the registration, that is, that it would be unnecessary for supporting the ITR exemption relative to the legal reserve area, meaning it would be up to the taxpayer to prove the existence of the mentioned are through other evidence-finding procedures.

The position of the Reporting Councilor was that neither current would satisfactorily meet the purpose of the rule that requires the registration of the legal reserve area. According to him, this rule would have an extra-fiscal purpose of creating a burden on environment preservation, which would encumber the property.

Furthermore, Reporting Councilor also stated that in the tax legislation, there is no definition that the date of registration is a condition for the ITR exemption. He then voted for the need to register the legal reserve areas, which can be done after the occurrence of the taxable event of the tax, as long as it is before the audit procedure.

Thus, by majority vote, the CSRF granted the taxpayer's Special Appeal, so as to rule out the rejection of the amounts declared on the basis of the legal reserve area.

"MATTER: TAX ON CORPORATE INCOME TAX – IRPJ
Ascertainment period: 2002
TAX PROCEEDING WRIT – REOPENING OF TAX AUDIT. As the first Audit was closed without an examination, the second audit on the same period is not a mere sequence to the first one, but a new one. The second Audit started without there being a written order from the Superintendent, District Director, or from the Auditor of the Federal Revenue of Brazil, as required by law, stating the reason for the new Audit. Taking into account that article 906 of RIR/99, specific legislation, provides that the express authorization is a requirement for the existence of the new Audit, the lack thereof leads to its substantial nullity, notwithstanding the rule of nullity stated in article 59 of Decree no. 70.235/72, not providing for it expressly. This is a rule created by a specific law, which violates the entire audit procedure in an irreparable manner, since the authorization, as expressly stated in the law, cannot occur. Despite the assessment being formally perfect, there is nothing to be repaired. In turn, the nullity of the Tax Proceeding Writ which originated it is irreparable, since it is not possible to obtain an authorization retroactive from the start of the audit proceeding".

The decision in question deals with a tax credit requirement relative to the Corporate Income Tax ("IRPJ"), the Social Contribution on the Net Income ("CSLL"), Contribution to the Employee Profit Distribution Program ("PIS") and to the Contribution to the Social Security Funding ("COFINS"), referring to the calendar year of 2002. The assessment was formalized after the Audit had set the Taxpayer's profits, under the claim that the Taxpayer had failed to maintain the Ledger or forms used to summarize or total the entries, per account or subaccount, made to the Journal, in good order and in compliance with the recommended accounting standards.

The Tax Proceeding Writ ("MPF") that supported the audit leading to the issue of the tax assessment notice mentioned was the second to be issued to the Taxpayer in relation to the same period, as the previous audit had been closed without any result.

In an Objection, the Taxpayer clarified that it was undergoing a bankruptcy procedure and, for this reason, the documents requested by the audit were in possession of the bankruptcy court, preventing its submission. Nevertheless, the assessment was fully maintained by Federal Revenue Judgment Office ("DRJ").

The Taxpayer then filed a Voluntary Appeal with the Administrative Council of Tax Appeals ("CARF"), arguing that it had been the target of a previous audit and that, therefore, the requested documents had already been submitted to the Federal Revenue of Brazil. The Taxpayer further claimed nullity of the Tax Assessment Notice issued in the new audit for which there was no written order, since the Taxpayer had already been audited in relation to the IRPJ on the same ascertainment period, without nothing having been verified by the Tax Authorities.

When the case records were examined by the 2nd Ordinary Panel of the 1st CARF Section, the Reporting Councilor granted the Voluntary Appeal in order to declare Nullity of Assessment, based on article 906, of the Income Tax Regulation ("RIR"), which establishes that *"With regard to the same fiscal period, a second examination is only possible by way of a written order of the Superintendent, the District Director, or the Auditor of the Federal Revenue".*

Based on such, the Reporting Councilor found that as the audit supported in the first MPF was closed without any result, the second audit, which led to the issue of the tax assessment notices, was not the continuation of the first, but a new tax audit procedure. Thus, in order for a new audit to be opened in relation to the same period, it would be necessary to have a written order by one of the authorities mentioned article 906 of the RIR, which was not verified in this case. Thus, the rapporteur granted the Voluntary Appeal, so as to declare Nullity of Assessment due to procedural flaw.

The Appointed Drafter followed his vote as to the merits, but disagreed in relation to the nature of the flaw, which he characterized as substantive. According to him, the assessment is formally perfect, has no procedural flaws, and there is nothing to be repaired. In turn, he argued that the nullity of the MPF that caused it is irreparable, and that the tax proceeding is flawed, since there is no means of obtaining a retroactive authorization to the start of the audit procedure.

He further added that in addition to the authorization to start a second examination, it is necessary to state the reason for the new audit, which may not be the same as that of the first. He also affirmed that, as the express authorization is a requirement for the existence of a new audit, it lead to the nullity of the audit procedure in case it is not granted to the Tax Agent.

Lastly, the Councilor clarified that what is null may not produce any legal effects, and if it has done so, the recognition of the nullity removes such effects, given that the recognition has an *extunc* (from the outset) effect.

Due to such, the CARF granted the Voluntary Appeal in order to declare the nullity of the tax assessment for substantive flaw, cancelling it in full.

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Team responsible for preparing The Administrative Council of Tax Appeals Bulletin:

Igor Nascimento de Souza (igor@ssplaw.com.br)

Henrique Philip Schneider (philip@ssplaw.com.br)

Eduardo Pugliese Pincelli (eduardo@ssplaw.com.br)

Cassio Sztokfisz (cassio@ssplaw.com.br)

Fernanda Donnabella Camano de Souza (fernanda@ssplaw.com.br)

Diogo de Andrade Figueiredo (diogo@ssplaw.com.br)

Flavio Eduardo Carvalho (flavio@ssplaw.com.br)

Rafael Fukuji Watanabe (rwatanabe@ssplaw.com.br)

Rodrigo Tosto Lascala (rodrigo@ssplaw.com.br)

Laura Benini Candido (laura@ssplaw.com.br)

Marina Lee (marina@ssplaw.com.br)

Pedro Lucas Alves Brito (pbrito@ssplaw.com.br)

Viviane Faulhaber Dutra (viviane@ssplaw.com.br)

Maria Carolina Maldonado Mendonça Kraljevic (mmaldonado@ssplaw.com.br)

Tiago Camargo Thomé Maya Monteiro (tiago@ssplaw.com.br)

Flavia Gehlen Frosi (flavia@ssplaw.com.br)

Thomas Ampessan Lemos Da Silva (thomas@ssplaw.com.br)

Gabriela Barroso Gonzaga Ferreira Porto (gabriela@ssplaw.com.br)

Guilherme Almeida de Oliveira (goliveira@ssplaw.com.br)

Amanda Mateoni Salvestrini (amanda@ssplaw.com.br)

R. Cincinato Braga, 340 • 9º andar • 01333-010 • São Paulo • SP
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 • 70715-900
tel 55 61 3251 9400 • fax 55 61 3251 9429

www.ssplaw.com.br

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