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NEWSLETTER



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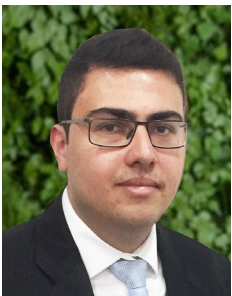
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Strategic view of transfer pricing in Brazil

1) History, concept and Brazilian rules of Transfer Pricing

The Brazilian transfer pricing rules were created in 1996 and had an anti-abuse purpose and supposedly inspired by the arm's length standard, according to the Explanatory Memorandum of the Provisional Measure that resulted in Law n. 9430/1996. The arm's length principle aims to treat the parts of multinationals as if they were different entities operating under market conditions. Along these lines, the Organization for Economic Co-operation and Development (OECD) maintains that member companies seek to replicate market dynamics in their transactions with each other.

Basically, the aforementioned Law is applicable to taxpayers who carry out commercial and financial transactions with related parties abroad, such as their head office, branch, controllers, subsidiaries or affiliates. In addition to transactions with related parties, transfer pricing rules are also applied in cases of transactions with countries that have favored taxation and a privileged tax regime.

The price charged by these persons connected in the transactions may be artificially stipulated and, consequently, diverge from the market price negotiated by independent companies. Therefore, it appears in order to avoid the transfer of profits (taxable in Brazil) abroad through manipulation of the prices of imports and/or exports.

2) Brazil x OECD

Currently, Brazil is not yet a member of the OECD, but it has actively participated in some OECD projects on tax matters, such as the Global Forum on Transparency and Information Exchange for Tax Purposes and the Project to Contain Base Erosion and Profit Transfer (known as BEPS).

As the OECD has the practice of fostering unity between fiscal practices among member countries, we know that Brazilian transfer pricing rules can create an obstacle to their entry into the organization. This is because Brazil adopts transfer pricing rules that are not in accordance with what is observed in international practice. This can hinder the business and economic development of Brazil and its trading partners.

It is possible to say that Brazilian law favored practicability, yielding to a stricter adoption of the arm's length principle. The best example of this is the fixed profit margins of the Resale Price Less Profit (PRL) method, as opposed to a func-

tional and case-by-case analysis to determine the profit margin, recommended by the OECD. The Brazilian model is more suited to developing countries, as it requires less tax revenue.

3) Strategic view of Transfer Pricing in Brazil

The purpose of transfer pricing rules is to combat the artificial transfer of profits. Thus, transfer prices must be controlled in certain transactions (imports, exports and loans) involving related parties or resident or domiciled in a country or dependency with favored taxation. Thus, the company will monitor the possibility of suffering with major adjustments in the calculation of the calculation basis of taxes levied on the income of legal entities.

In addition to the significant tax impact for the Brazilian branch, a company that does not observe transfer prices could make the business in Brazil unfeasible. A Brazilian branch needs competitive prices to make a local profit and consequently financial health. Part of this strategy is closely linked to the transfer price, because if the group decides to market a product in Brazil but leaves little or no profit margin for the Brazilian related company, that company will not prosper and will accumulate debt and successive loan operations.

Thus, the transfer price calculation is an important strategic tool for multinational companies that do business in Brazil.

The calculation and control are able to demonstrate whether the company will be profitable in Brazil, whether it will be competitive in the local market, as well as whether it will comply with Brazilian transfer pricing rules and will not suffer major tax adjustments.

The calculation must be presented to the tax authorities annually, within the ancillary obligation Corporate Income Tax Return (“ECF”). However, strategically many companies do the calculation and monitoring quarterly or semi-annually to track purchase prices (import) and sales prices in the local market. With this monitoring, it is possible to assess in advance whether the company is computing a profit and whether there will be an adjustment in income tax due to intercompany transactions. If a relevant adjustment is verified, the company may negotiate new prices with the headquarter to possibly avoid an impact on the local income tax.

This practice can be extremely beneficial for the business group, given that the company located in Brazil will be able to grow, be profitable and will not need successive loans or other subsidies from the group, keeping its level of indebtedness low. In addition to boosting the Brazilian economy, it can offer to open new businesses in South America.

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For companies that are thinking about starting a branch in Brazil, we believe that it is very important to carry out a tax model considering all taxes, as well as estimate the transfer price based on Brazilian legislation. This is a study of great importance to plan the future of the Brazilian branch.

As already informed, the transfer price calculation must be sent annually to the tax authorities through the accessory obligation Corporate Income Tax Return (“ECF”). If the company does not provide the calculation according to Brazilian rules, they will be exposed to a fine of 3% (three percent) of the omitted, inaccurate or incorrect amount. In the ancillary obligation, it is necessary to inform the value of intercompany import and export transactions, therefore, the fine will be calculated on the total value of all intercompany transactions carried out in the year.

Rödl & Partner Brasil has specialized professionals who can help define the procedures to be adopted for the transfer price in Brazil.

Autor der Publikationen **So geht's Besteuerung von Unternehmen in Brasilien*

Alle Inhalte dieses Newsletters obliegen der Verantwortung der jeweiligen Autoren und wurden von diesen sorgfältig recherchiert.

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