

BRAZILIAN TAX REFORM APPROVED BY THE CHAMBER OF DEPUTIES

b/luz



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INTRODUCTION

At the beginning of the year, a Tax Reform Working Group, comprised of 12 deputies, was created within the Brazilian Chamber of Deputies (House of Representatives).

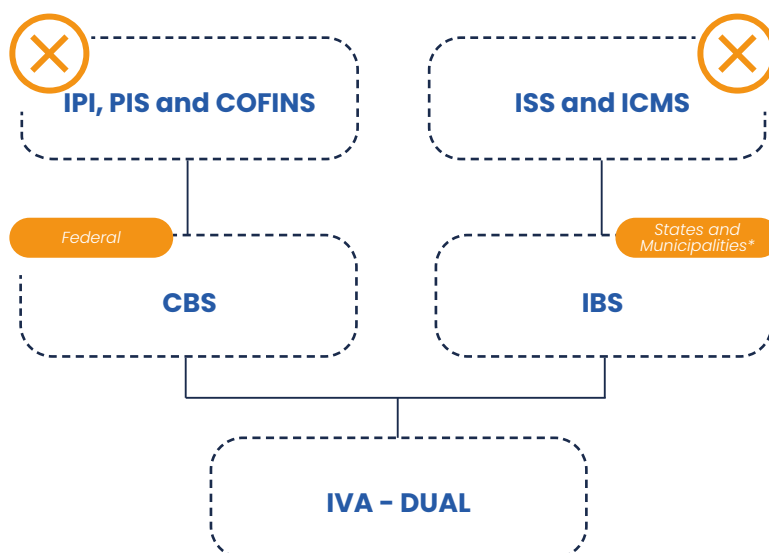
Based on the report prepared by the Working Group, a preliminary replacement draft (substitutivo) for the Constitutional Amendment Proposal ("PEC") No. 45/2019 was presented on June 22, 2023. The text was approved by the Chamber of Deputies on July 6, 2023 and will now proceed to be voted on in the Federal Senate.

Although the text does not provide the standard tax rate for the new taxes, the overall expectation is that the new tax system will increase the tax burden on the service sector, which is currently subject to the Tax on Services (ISS), and decrease the tax burden on the industrial sector, which is currently subject to the Tax on Circulation of Goods (ICMS) and Excise Tax (IPI).

Check out the summary that the Tax team at b/luz prepared, with the main points of the tax reform approved by the Chamber of Deputies:

SIMPLIFICATION OF THE TAX SYSTEM. CREATION OF A TWO-TIER VAT ("IVA-DUAL")

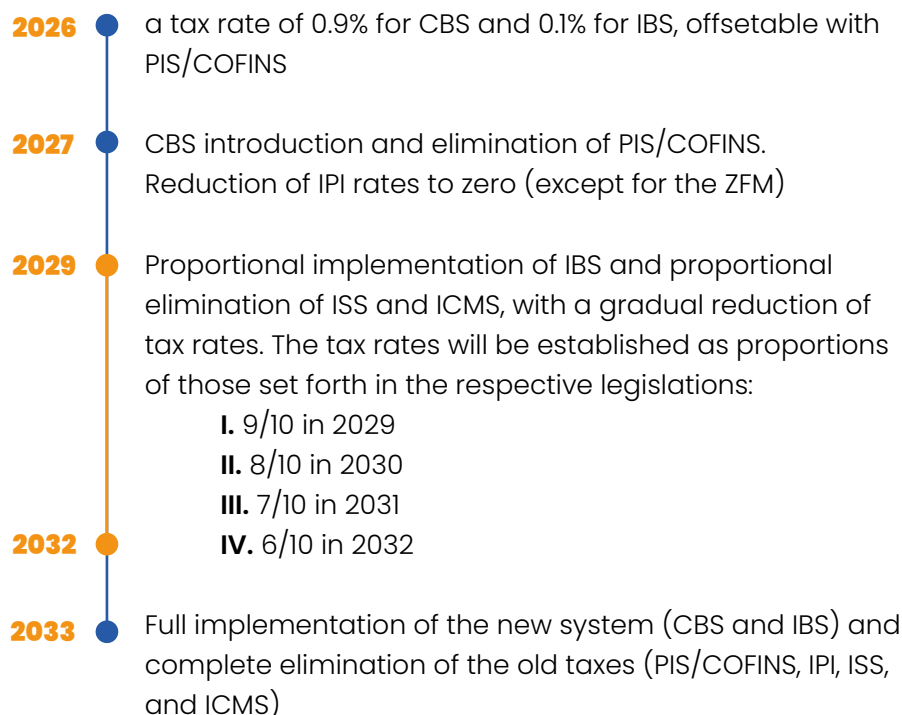
/ Elimination of five taxes (IPI, ICMS, ISS, PIS, and COFINS) and creation of a Dual VAT, comprising a federal-level Contribution on Goods and Services ("CBS"), and a Tax on Goods and Services ("IBS"), under the responsibility of States and Municipalities.



*Federative Council of IBS: it will be comprised of representatives from states, the Federal District, and municipalities, with the objective of managing of the IBS.

TRANSITION TO THE NEW TAX REGIME

The transition from the old system to the IVA-Dual will span eight years, as follows:



Note: The federative transition to the destination principle will occur gradually until 2078.

IVA-DUAL: TWO-TIER VAT MAIN FEATURES



Tax Rate: Each federative unit will establish its own specific tax rate by law, which will be applicable to all goods and services. The tax rate for CBS will be uniform throughout the national territory, whereas the tax rate for IBS will be the sum of the rates set forth by the destination State and Municipality. The PEC does not specify the standard tax rate.



Tax base: the tax reform adopts a broad tax base, levied not only on transactions involving "goods" or "services" but also on transactions involving intangibles and any other rights.



Taxation at the destination: tax due at the destination of the transaction, as defined by a Complementary Law. Depending on the transaction, the destination can be the place of delivery, availability, or location of the goods; the provision or availability of the service; or the domicile or location of the purchaser of the goods or services.



No tax cascade or "tax on tax": the consolidation of taxes into a Dual VAT tax eliminates the possibility "cascade effect" of taxes. It also prevents the "tax on tax" base, which occurs when a tax is included on its own (or another tax's) taxable base.



Credit offsetting: a Complementary Law will establish cases in which the use of the credits for offsetting purposes will be conditioned to the verification of the actual payment of the tax on the transaction.



Cashback: a Complementary Law will set forth cases for tax refunds to individuals, including the limits and beneficiaries, with the aim of reducing income inequalities.



Responsibility of intermediaries (marketplaces, payment facilitators, etc.): a Complementary Law may define as a taxpayer the person who contributes to the completion, execution, or payment of the transaction, even if they are resident or domiciled abroad.

FAVORABLE TAX TREATMENTS



A Complementary Law may establish favorable tax rates and treatments



They must be uniform throughout the national territory



Adjustments to the standard rates may be required, in order to rebalance the tax revenue of the federative units:

/ Farmers, whether individuals or legal entities, with annual revenue below R\$ 3,600,000.00 (three million six hundred thousand Brazilian Reals) can opt out from CBS and IBS.

/ 60% reduction in the total tax rate (CBS and IBS) for:

- I. Education services;
- II. Healthcare services;
- III. Medical devices and accessibility devices for people with disabilities;
- IV. Medicines and basic menstrual health care products;
- V. Urban, semi-urban, or metropolitan public transportation services;
- VI. Agricultural, fishing, forestry, and natural plant extraction products in their raw state;
- VII. Agricultural inputs, food for human consumption, and personal hygiene products;
- VIII. National artistic, cultural, news, and audiovisual productions

/ Exemption from CBS and IBS for urban, semi-urban, or metropolitan public transportation services.

/ Possibility of applying a full exemption (100% reduction) in the total tax rate (CBS and IBS) for::

- I. Medicines and basic menstrual health care products;
- II. Horticultural products, fruits, and eggs;
- III. Operations carried out by integrated producers (article 2, II of Law No. 13,288/2016).
- IV.

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/ 100% reduction in the CBS tax rate for: Services benefiting from the Emergency Program for the Recovery of the Event Sector (PERSE) until February 28, 2027 and Higher education services (PROUNI).

/ Deemed credits may be granted to the acquirer of:

- I. services provided by self-employed individuals who are not taxpayers of the tax;
- II. waste and other materials intended for recycling, reuse, or reverse logistics, from individuals, cooperatives, or other forms of grassroots organization;
- III. used movable goods (from non-taxpayer individuals) for resale.

/ National Basic Food Basket: basic food basket products will be granted full exemption (i.e. the total tax rate of CBS and IBS will be reduced to zero). A Complementary Law will define the products that will compose such basket.

⚠ IMPORTANT: The benefits of the Manaus Free Trade Zone and the tax treatment of companies classified under the Simples Nacional simplified tax regime are maintained.

DIFFERENTIATED TREATMENTS

A Complementary Law may establish differentiated treatments as indicated below:



Fuels and lubricants: the tax will be levied only once, and the rates will be uniform throughout the national territory. Credits will be granted to the acquiring taxpayer of the tax.



Financial services, real estate transactions, health insurance plans, sports betting, hotel services, amusement parks, theme parks, restaurants, and regional aviation: possibility of implementing modifications in the tax rates and credit rules, and creating a revenue-based taxation system.



IMPORTANT:

Financial services remunerated through fees and commissions will not have differentiated treatment. The rule will only apply to credit transactions.

Real estate transactions include: construction and real estate development; land subdivision and sale of real estate; leasing and renting of real estate; and real estate administration and intermediation.



Government purchases: the tax will not be levied, and credits arising from previous stages of the supply chain will be allowed.

FEDERATIVE COUNCIL OF THE IBS

The Federative Council of the Tax on Goods and Services will be made up of representatives from the Brazilian States, the Federal District, and municipalities, with the goal of managing the IBS.

The States and the Federal District will have 27 members each, while the municipalities and the Federal District will be represented by 27 members: 14 elected based on the equal votes of these entities, and 13 based on the votes of each municipality, weighted by the respective populations. The resolutions of the Federative Council will be approved if they obtain, cumulatively, the votes:

I. with regard to the group of States and the Federal District:

- a.** an absolute majority of its representatives, and
- b.** representatives corresponding to more than 60% of Brazil's population; and

II. with regard to the group of municipalities and the Federal District, the absolute majority of their representatives.

SELECTIVE TAX ("IS")



A federal tax, the Selective Tax will be levied on the production, sale, or importation of goods or services harmful to health and the environment. The list of products subject to the Selective Tax is not specified in the text. This list must be set forth by a Complementary Law and cannot include goods and services that benefit from a reduced tax rate.





MOTOR VEHICLE PROPERTY TAX (IPVA)

/ IPVA may be progressive based on the environmental impact, value, type, and use of the vehicle.



IMPORTANT! It will also be levied on the ownership of aircraft and boats, excluding:

- a. aircraft used in the provision of air services to third parties
- b. vessels owned by a legal entity providing water transport services or by persons (either individuals or legal entities) engaged in industrial, artisanal, scientific, or subsistence fishing.
- c. self-propelled water-going platforms.



INHERITANCE AND GIFT TAX (ITCMD)

The PEC authorizes the levy of the tax in the following situations, regardless of the enactment of a Complementary Law:

/ When the donor has domicile or residence abroad; or

/ When the deceased had assets, was a resident or domiciled, or had its estate processed abroad.

- Gift or inheritance of immovable property will attract the jurisdiction of the state where the property is located.
- If the donor has a domicile abroad, the tax will be due to:
 - I. the state where the donee has a domicile or to the Federal District; or
 - II. to the state where the property is located or to the Federal District, if the donee is a non-resident.
- Regarding the assets of the deceased, even if located abroad, to the state where he/she was domiciled, or if domiciled or resident abroad, to the state where the heir or legatee has a domicile, or to the Federal District.



ITCMD is not applicable to donations destined for non-profit institutions with public and social relevance purposes, including charitable and assistance organizations of religious entities and scientific and technological institutes, subject to the conditions established by a Complementary Law. The exemption encompasses both donations to and donations made by these entities, in the pursuit of their social goals.

COMPENSATION FUNDS

Regional Development Fund

Goal: To reduce regional and social inequalities through the allocation of resources to states and the Federal District for investment in:

- I. infrastructure studies, projects, and works;
- II. promotion of productive activities with high potential for job creation and income generation, including the granting of economic and financial subsidies; and
- III. promotion of actions aimed at scientific and technological development and innovation.

It will be effective as from 2029, with no end period.

⚠ IMPORTANT! This is one of the sections of the proposal that is still under discussion, as government officials expect an increase in the amounts allocated to the Fund.

Tax Benefits Compensation Fund

Goal: to compensate, until December 31, 2032, legal entities benefiting from exemptions, incentives, and tax or financial-fiscal benefits granted for a certain period and under conditions.



INCOME TAX REFORM

The Executive Branch must submit to the National Congress, within 180 days after the Constitutional Amendment, a bill that reforms the taxation of income, complemented by the studies/forecasts of budgetary and financial impacts.



Our Tax team is available to answer any questions you may have on the subject via email at:

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Find out more – visit our website or follow us on social media.



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