

TP - expanded definition of low tax jurisdiction introduced in Brazil

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On 23 June 2008, the Brazilian Congress enacted Law 11,727/2008, portions of which contain some potentially significant changes to Brazilian domestic tax law.

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The new law has an impact on the application of Brazil's transfer pricing rules as it expands the concept of what may constitute a low tax jurisdiction.

Brazil's transfer pricing rules, which became effective on 1 January 1997, do not adopt the internationally accepted arm's length principle. Rather, the intention of Brazil's transfer pricing rules has been to prevent multinational companies from transferring taxable income abroad. Therefore, Brazil's transfer pricing rules apply to transactions conducted with a foreign resident, even if unrelated, that is domiciled in a country that does not tax income or that taxes income at a rate of less than 20%, or is in a jurisdiction with internal legislation allowing secrecy with regard to corporate ownership. Under the prior law the concept of a low tax jurisdiction referred only to countries, with many of the countries that have become synonymous with the investment management industry, such as Hong Kong, Isle of Man, Channel Islands, Cayman Islands and United Arab Emirates, being included on an inclusive list of tax havens issued by the Brazilian tax authorities.

The new law (11,727) expands the concept of a tax haven jurisdiction in the context of Brazil's transfer pricing rules to include regions within countries, which may include states, provinces and cities.

In the increasingly global world of both traditional and alternative investment management, the extension of Brazil's transfer pricing rules to include unrelated parties located in the newly defined low tax jurisdictions may have implications for companies with operations in Brazil. There is also a question as to whether the newly expanded definition of tax haven may apply in the context of determining the appropriate withholding tax rate. For example, the withholding tax rules relating to service payments directly reference the new definition of tax haven while the rules relating to interest and royalties do not. Careful consideration should be given to the application of the new rules.

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