

2023

BRAZIL AT THE OECD

HLB TAX ADVISORY - LAW 14.596/2023

e-Book



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BRAZIL AT THE OECD

Brazil's adherence to the guidelines of the Organization for Economic Cooperation and Development (OECD) resulted in the promulgation of Law no. 14.596 of June 14, 2023, and other regulations issued by the Special Secretariat of the Federal Revenue of Brazil (RFB), bring a new scenario for the taxation of international operations.

In this study, we summarize the fundamental concepts and principles that international tax practitioners should consider when dealing with the Brazilian Transfer Pricing regulations, especially during the transition period for those who opt for the 2023 calendar year, and in full from 2024 onwards.

We hope that this material will be useful in helping you to understand the new legislation.

We remain at your disposal,

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Tax Partner, Transfer Pricing



Leandro Arnoni Scalquette

Lead partner of the Transfer Pricing practice from FILB Brasil.

With more than 25 years' experience in tax consultancy focused on Transfer Pricing, he has solid knowledge of the subject acquired throughout his career in companies such as KPMG, EY, PWC and Grant Thornton, as well as speaking at events in Brazil and abroad on Corporate Taxes and Transfer Pricing.

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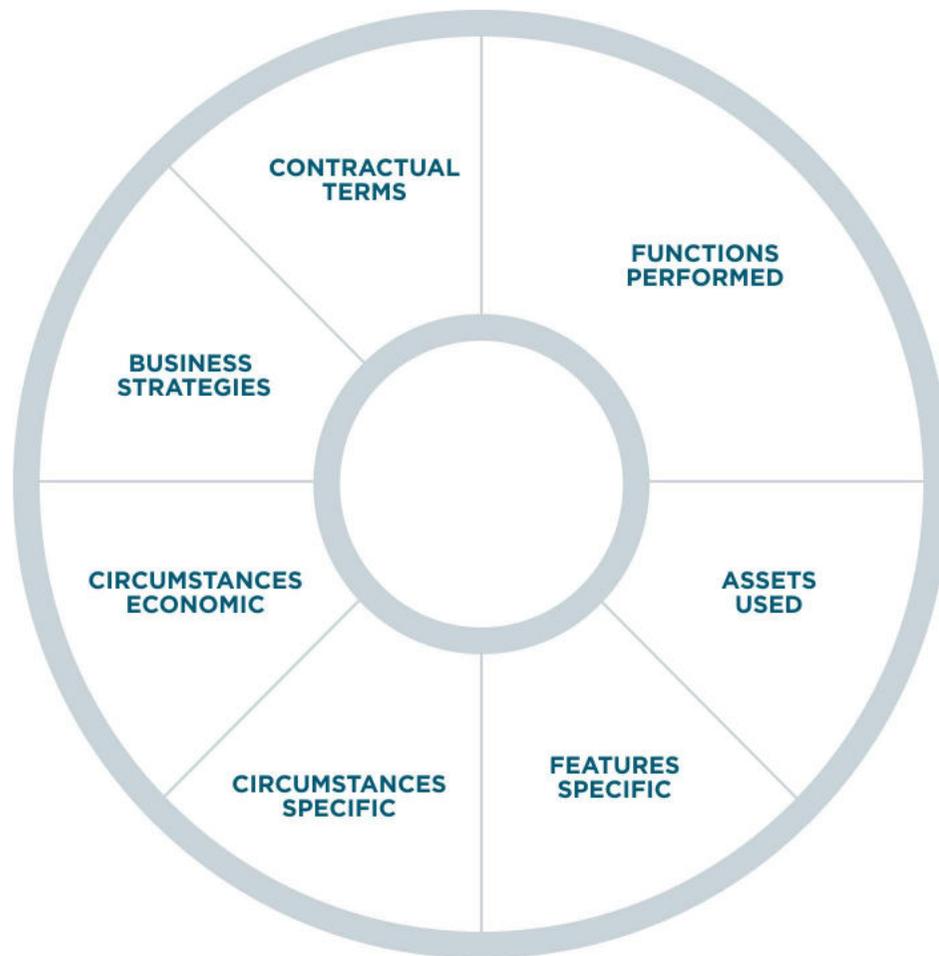
APPLICATION OF THE ARM'S LENGTH PRINCIPLE

CONTROLLED TRANSACTION	RELATED PARTY	OUTLINING THE TRANSACTION	COMPARABILITY ANALYSIS
<ul style="list-style-type: none"> Any type of transaction, regardless of how it is carried out/formalized (direct or indirect). It includes practices, understandings, actions or omissions, even though they are, or are intended to be, legally enforceable and the terms and conditions of such transaction are formally documented. The definition of a related party does not only apply to entities abroad. 	<ul style="list-style-type: none"> The term "influence" should be understood from its effects. The complementary list seeks to simplify the analysis of situations in which the TP rule should be applied. The definition of related party does not only apply to entities abroad. 	<ul style="list-style-type: none"> Analysis of the facts and circumstances of the transaction. Analysis of the evidence of the parties' actual conduct. Identify the trade and financial relations between related parties and the economically relevant characteristics associated with these relations. 	<ul style="list-style-type: none"> Compare the terms and conditions of the controlled transaction with the terms and conditions that would be established between unrelated parties in comparable transactions.
<h2>ARMS' LENGTH PRINCIPLE</h2>		<h2>METHOD + APPROPRIATE</h2>	<h2>ADJUSTMENTS</h2>
<ul style="list-style-type: none"> The terms and conditions of a controlled transaction will be established in accordance with those that would be established between unrelated parties in comparable transactions. 		<ul style="list-style-type: none"> TRADITIONAL <ul style="list-style-type: none"> PIC PRL MCL PROFITABILITY <ul style="list-style-type: none"> MLT MDL 	<ul style="list-style-type: none"> Spontaneous Compensatory Primary

OUTLINING THE TRANSACTION

ART. 7°

- Based on the analysis of the facts and circumstances of the transaction and the evidence of the actual conduct of the parties, with a view to identifying: the trade and financial relations between related parties and the economically relevant characteristics associated with these relations



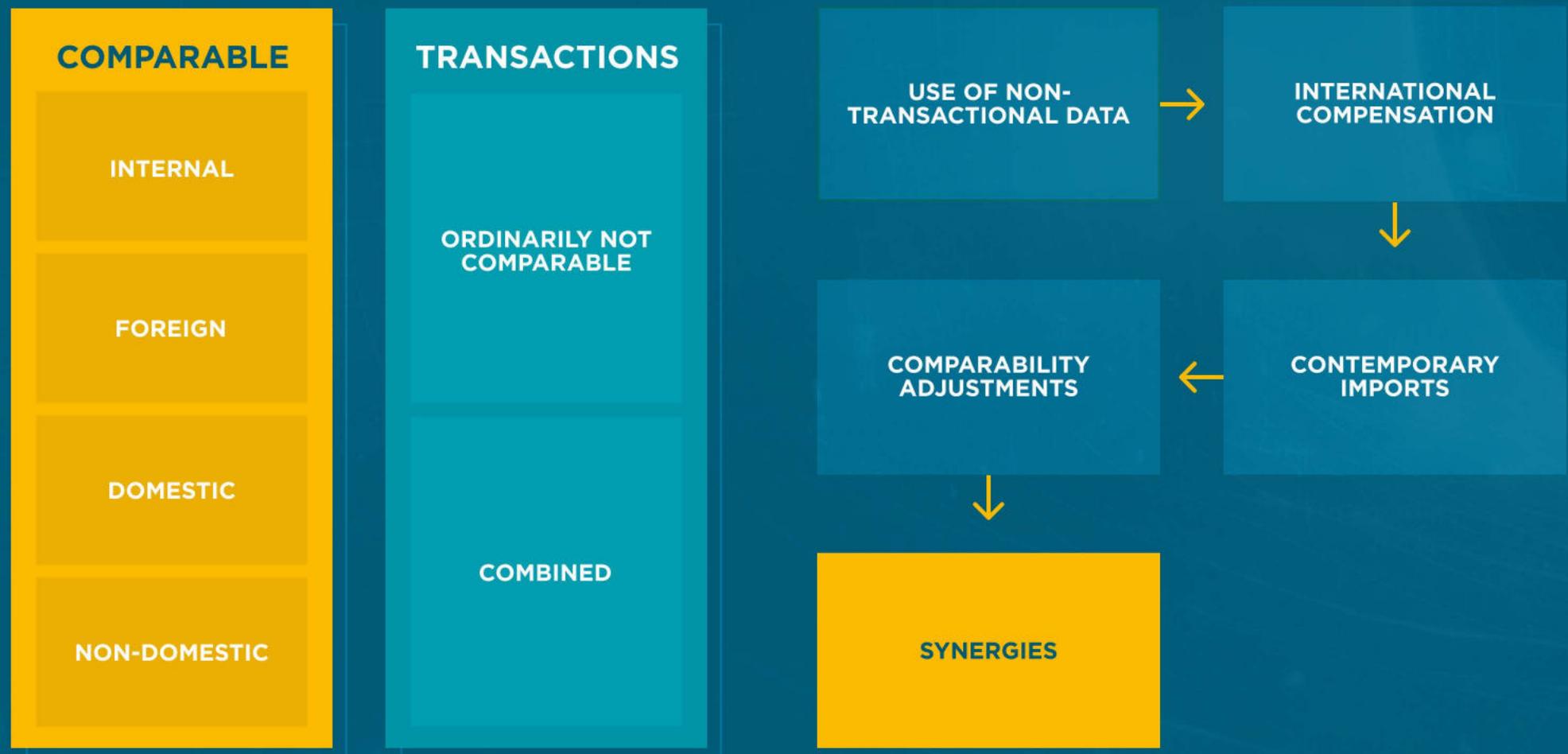
OUTLINING REQUIRES AN UNDERSTANDING OF:

- the economic activities of the multinational group and the factors that affect the commercial transaction performance;
- of the multinational group's organizational structure;
- the functions, assets and risks assumed by the entities that are part of the multinational group; and
- of the supply chain and its added value for each entity in the multinational group.

COMPARABILITY ANALYSIS

ART. 9º

- The comparability analysis will be carried out with the aim of comparing the terms and conditions of the controlled transaction, outlined in accordance with the provisions of Article 7 of this Law, with the terms and conditions that would be established between unrelated parties in comparable transactions



METHODS

PIC

- Compares the price or value of the consideration for the controlled transaction with the prices or values of the consideration for comparable transactions between unrelated parties.

PRL

- Compares the gross margin that an acquirer of a controlled transaction obtains on the subsequent resale to unrelated parties with the gross margins obtained on comparable transactions between unrelated parties.

MCL

- Compares the gross profit margin obtained on the supplier's costs in a controlled transaction with the gross profit margins obtained on the costs in comparable transactions carried out between unrelated parties.

MLT

- Compares the net margin of the controlled transaction with the net margins of transactions comparable transactions between unrelated parties, both calculated on the basis of an appropriate profitability indicator.

MDL

- Division of profits or losses, or part thereof, in a controlled transaction in accordance with what would be established between unrelated parties in a comparable transaction, taking into account the relevant contributions provided in the form of functions performed, assets used and risks assumed by the parties involved in the transaction.

METHOD HIERARCHY RULE

- In the event that the PIC, PRL and MCL methods and the MLT and MDL methods **can be applied with equal reliability**, the PIC, PRL and MCL methods will be preferred.

→ Degree of comparability between controlled and non-controlled transactions

→ Fewer adjustments

→ Reliability of adjustments

+ STRENGTH

- PIC - The most direct and reliable way to apply the test in a transaction ballot box.
- PRL - Less comparability is required than with the PIC method.
- MCL - Less comparability is required than in the PIC method / Well suited to manufacturing and service activities.
- MLT - Simple / In practice, the most used / Less comparability required.
- MDL - Adapted when both parties to the related party transaction have made significant and unique contributions.

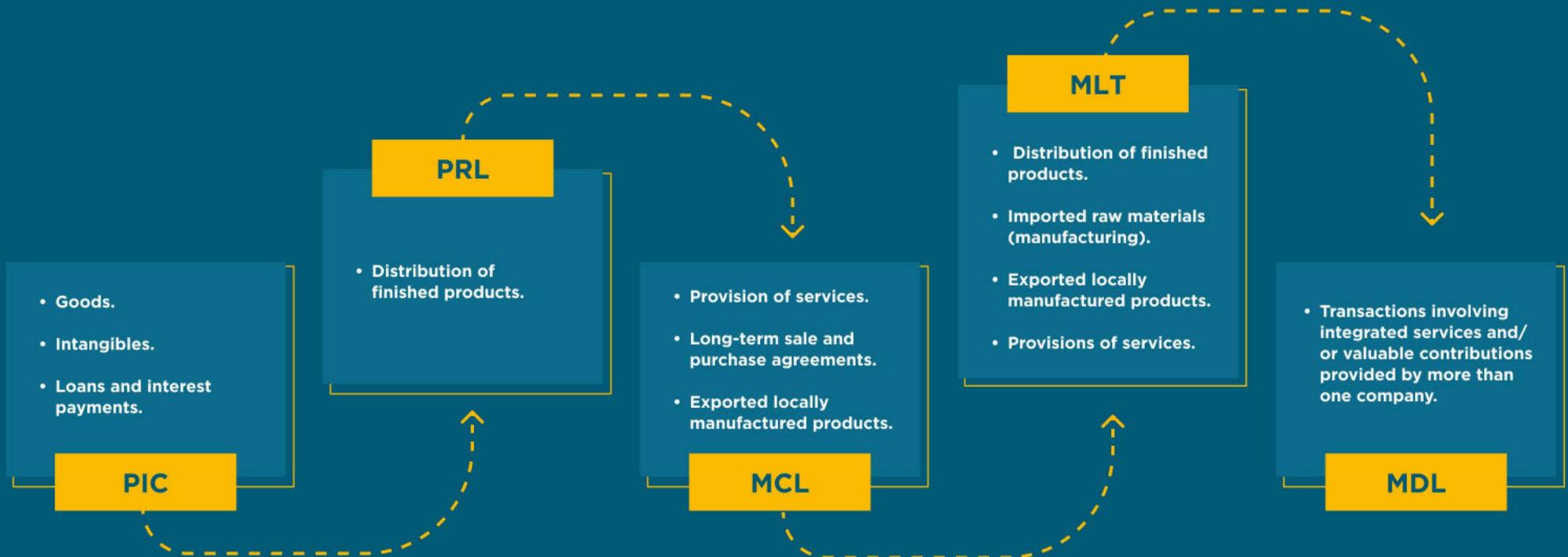
- WEAKNESS

- PIC - Requires high comparability. Lack of publicly available data.
- PRL - Financial data (gross profit) from comparable companies may not be available / Consistency of accounting standards.
- MCL - Lack of publicly available data / Consistency of accounting standards.
- MLT - The net margin can be impacted by non-TP related tactics.
- MDL - Complex / Not applicable to all transactions.

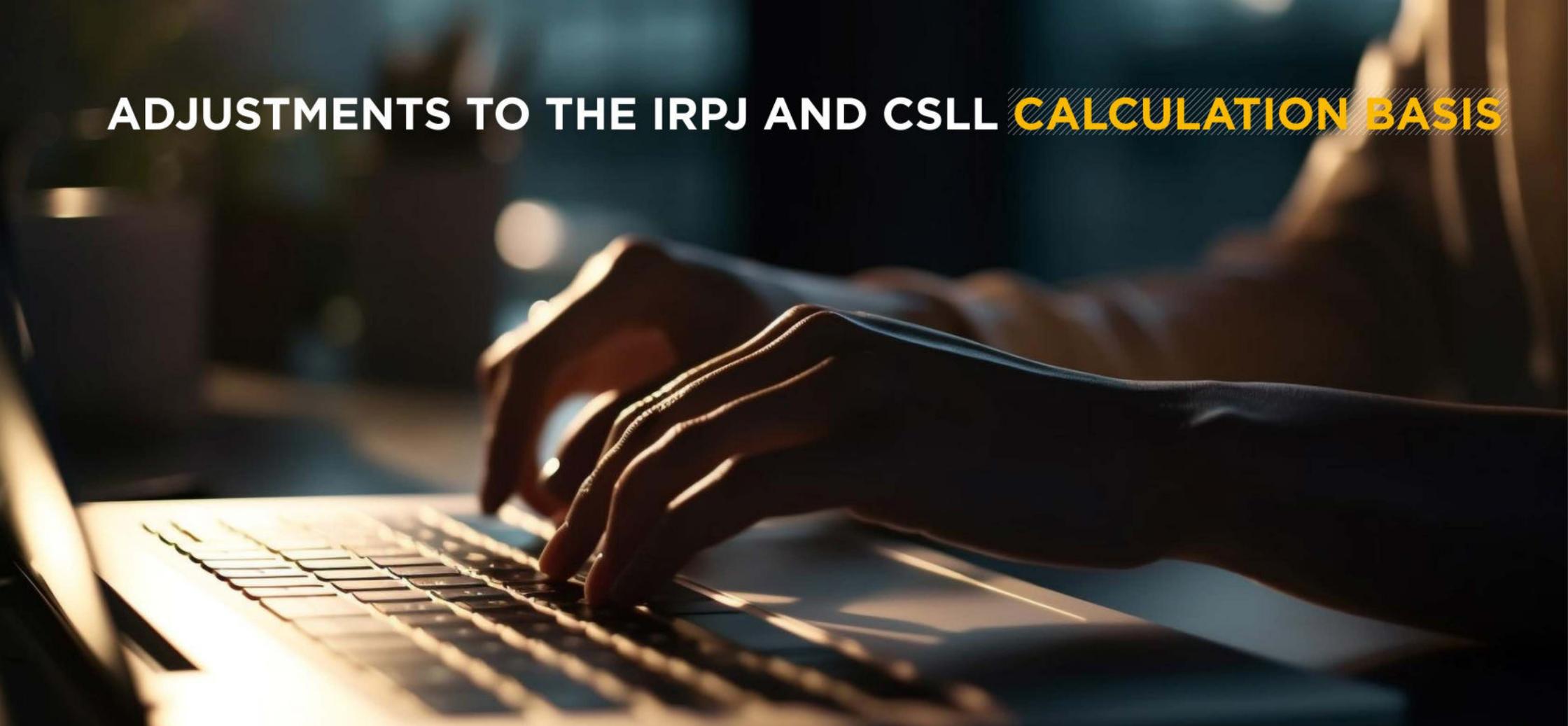
SELECTION OF METHODS

✓ Most appropriate method

- *The most appropriate method is that which provides the most reliable determination of the terms and conditions that would be established between unrelated parties in a comparable transaction.*



ADJUSTMENTS TO THE IRPJ AND CSLL **CALCULATION BASIS**



IT WILL NOT BE ALLOWED ADJUSTMENTS THAT:

- Reduce the IRPJ and CSLL calculation basis
- Increase the value of the IRPJ tax loss or the CSLL negative calculation basis

THIS PROHIBITION DOES NOT APPLY IN THE FOLLOWING CASES:

- compensatory adjustments
- of results agreed in dispute settlement mechanisms provided for in international agreements or conventions to eliminate double taxation

ADJUSTMENTS TO THE IRPJ AND CSLL **CALCULATION BASIS**

TAXPAYER WILL PAY THE ADJUSTMENT



DIFFERING TERMS AND CONDITIONS

THE
CALCULATION
BASIS WILL BE
ADJUSTED

SPONTANEOUS ADJUSTMENT

That made by the legal entity domiciled in Brazil **directly in the calculation of the IRPJ and CSLL calculation basis**

- i. The spontaneous adjustment must be computed in the IRPJ and CSLL calculation basis for the fiscal year of December 31st, even if the calculation regime is quarterly. Except in the case of incorporation, merger, spin-off or closure of activities, in which case the adjustment will be made on the date of the special event;
- ii. When opting for annual taxable income, the adjustments do not apply when calculating basis for calculating estimated tax payments.

COMPENSATORY ADJUSTMENT

That made **by the parties to the controlled transaction** up to the end of the calendar year in which the transaction is carried out in order to adjust its value so that the result obtained is equivalent to what would have been obtained if the terms and conditions of the controlled transaction had been established in accordance with the ALP.

ADJUSTMENTS TO THE IRPJ AND CSLL CALCULATION BASIS

✓ COMPENSATORY ADJUSTMENT

It may be determined up to the time of submission of the Tax Bookkeeping, provided that its accounting record is made in the bookkeeping of the legal entity for the calendar year relating to the calculation period to which the controlled transaction refers.

- It must be carried out symmetrically in the bookkeeping of the legal entity domiciled in the country and the other parts of the controlled transaction, observing the same value and nature of the transaction.

- It must be based on the issue of debit or credit notes or tax and commercial documentation capable of proving the nature and amount of the adjustment.

- It must be ratified by a declaration from the legal representative of the other parties to the controlled transaction, which states that it has made the adjustment in the same amount as that made by the legal entity domiciled in the country, attested to by the latter's representative.

The implementation of this adjustment does not require prior authorization from the RFB, without prejudice to the possibility of its subsequent verification in a tax audit procedure.

ADJUSTMENTS TO THE IRPJ AND CSLL **CALCULATION BASIS**

TAXPAYER WILL PAY THE ADJUSTMENT



DIFFERING TERMS AND CONDITIONS

**THE
CALCULATION
BASIS WILL BE
ADJUSTED**

● PRIMARY ADJUSTMENT

The tax authority will make the primary adjustment (the one made by the tax authority in order to add to the IRPJ and CSLL calculation basis).

The primary adjustment must be computed in the IRPJ and CSLL calculation basis for the fiscal year of December 31st, even if the calculation regime is quarterly. Except in the case of incorporation, merger, spin-off or closure of activities, in which case the adjustment will be made on the date of the special event.

DOCUMENTATION

- §Art. 56 (Normative Instruction). The taxpayer will submit the Global File and the Local File in Digital Process, through the service available at the RFB's Virtual Service Center (e-CAC), within three (3) months of the deadline for transmitting the ECF for the corresponding calendar year.
- § 1 Part of the information provided for in arts. 59 and 60 will also be provided in the ECF, considering the definitions and instructions contained in the Layout Guidance Manual of the ECF, published by the General Inspection Coordination through an Executive Declaratory Act (ADE) published in the Federal Official Gazette (FOG).
- § 2 - For the calendar year 2024 or, if the option provided for in art. 45 of Law no. 14.596 of 2023, for the calendar year 2023, the deadline for submission of the Global File and the Local File will be the last business day, respectively, of the calendar years 2025 and 2024.

DECLARED COUNTRY TO COUNTRY

GLOBAL
ALLOCATION OF
REVENUES, ASSETS
AND INCOME TAX
PAID BY THE
GROUP

ECONOMIC
INDICATORS

GLOBAL FILE

GROUP
STRUCTURE

THE ACTIVITIES OF
THE GROUP TO
WHICH IT BELONGS
AND THE OTHER
ENTITIES THAT MAKE
UP THE GROUP

FILE LOCAL

CONTROLLED
TRANSACTIONS; AND

PARTIES
RELATED PARTIES
INVOLVED IN
CONTROLLED
TRANSACTIONS

The submission of the Country-to-Country Declaration will comply with the provisions of RFB Normative Instruction No. 1681 of December 28th, 2016.

ART. 57 AND § 1 - LOCAL FILE AND GLOBAL FILE:

- It will be waived if the total value of the taxpayer's controlled transactions, before transfer pricing adjustments, in the calendar year prior to the calendar year to which the Local File refers is less than R\$ 15,000,000.00 (fifteen million reais).

PENALTIES

ART. 35º

- **Failure to comply with the provisions of Art. 34 of this Law shall result in the imposition of the following penalties, without prejudice to the application of other sanctions provided for in this Law:**

I. as to the submission of the declaration or other specific accessory obligation established by the Special Secretariat of the Federal Revenue of Brazil for the purposes of the provisions of art. 34 of this Law, regardless of the form of its transmission:

a) fine equivalent to 0.2% (two-tenths percent), per calendar month or fraction thereof, on the value of the gross revenue for the period to which the obligation refers, in the event of failure to submit it on time - **GLOBAL AND LOCAL FILE;**

b) a fine equivalent to 5% (five percent) of the value of the corresponding transaction or 0.2% (two-tenths percent) of the value of the multinational group's consolidated revenue for the year prior to the year to which the information refers. In the case of accessory obligations established to declare the information referred to in items III and IV of the caput of art. 34 of this Law, in the event that the information submitted is inaccurate, incomplete or omitted - **GLOBAL FILE;** or

c) a fine equivalent to 3% (three percent) of the gross revenue for the period to which the obligation refers, in the event of submission without complying with the requirements for submitting an accessory obligation - **GLOBAL FILE AND LOCAL**

II. In the case of failure to present information or documentation requested by the tax authority during a tax procedure or other prior inspection measure, or other **conduct that impedes inspection during the tax procedure**, a fine equivalent to **5% (five percent) of the value of the corresponding transaction.**

§ 1º The fines referred to in this article will have a minimum value of R\$ 20,000.00 (twenty thousand reais) and a maximum value of R\$ 5,000,000.00 (five million reais).

§ 2º For establishing the value of the fine provided for in subitem "c" of item I of the caput, the maximum value provided for in § 1º of this article will be used:

I. if the taxpayer does not inform the value of the multinational group's consolidated revenue in the previous year; or

II. when the information provided has not been duly substantiated.

§ 3º The fines referred to in this article will have a minimum value of R\$ 20,000.00 (twenty thousand reais) and a maximum value of R\$ 5,000,000.00 (five million reais).

§ 4º The maximum value provided for in § 1º of this article shall be used to establish the value of the fine provided for in subitem "c" of item I of the caput:

I. if the taxpayer does not inform the value of the multinational group's consolidated revenue in the previous year; or

II. when the information provided has not been duly substantiated.

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