

TAX DEVELOPMENTS

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1. AMENDMENTS TO BRAZILIAN CORPORATION LAW – ACCOUNTING RULES

The Law No. 11.638 was published on December 28, 2007, which amends the Law No. 6.404/76 (known as Brazilian Corporation Law), in particular in relation to the provisions concerning the accounting, aiming at updating the accounting rules of the Brazilian corporations to the international practices, and it amends the Law No. 6.385/76 (which regulates the market and Securities and Exchange Commission).

We emphasized the main amendments:

- Statements of cash flow and value added: The “Statement of Cash Flow” has been added to the list of statements to be prepared by stock corporations in lieu of the “Statement of Source and Application of Funds”, so as to allow for submitting better the financial position of the corporation, and also in the event of a publicly-held company, the “Statement of Value Added”.
- Large Corporation: The provisions applicable to stock corporations about the accounting and preparation of financial statements and the requirement of an independent audit carried out by an auditor registered with the Exchange Commission - CVM also apply to large corporations, even though they are organized as limited companies. The company, or a group of companies holding, under common control, the total assets more than two hundred and forty million Brazilian reais (R\$240,000,000.00) or an annual gross revenue more than three hundred million Brazilian reais

(R\$300,000,000.00) for the prior fiscal year is deemed to be large corporation.

There is no express mention in law as to whether a large corporation is required to publish such financial statements, thus resulting in adverse opinions by attorneys-at-law. CVM issued a Notice stating that the publication of said financial statements is not required, emphasizing, however, that when a large corporation discloses them voluntarily or to satisfy any specific requests (of creditors, suppliers, customers, etc.), it shall do so with the due degree of transparency and according to the new law.

- Privately-held Companies: The privately-held companies may elect to perform the financial statement rules issued by the Exchange Commission (CVM) to publicly-held companies.
- Intangible Assets: The subgroup of intangible assets has been inserted into the permanent assets account, in which the rights to the intangible assets allocated for the maintenance of the company or exercised for such purpose, including the acquired goodwill, will be recorded. The tangible assets allocated for the maintenance of the company's activities are recorded in the subgroup of fixed assets, including when the benefits, risks and controls of such assets are transferred, even if the property of such assets is not transferred.
- Extinction of Revaluation Reserve: In lieu of the "Revaluation Reserve account", the "Assets Evaluation Adjustment account" has been created in the shareholders' equity, in which the considerations for the increase or decrease in assets and liabilities shall be recorded due to the respective

evaluation at fair market value, including the evaluation of financial instruments (the rating and evaluation rules of which have also been provided by the new law) and the adjustments of exchange variation of investments overseas.

According to the new law, the companies may elect to retain the balances outstanding on the revaluation reserves until they are effectively realized or reverse them until the end of the fiscal year of 2008.

- Corporate reorganization upon transfer of control: According to the new law, in the event of corporate reorganization (upon merger, incorporation and split-off), involving parties independent and associated with the transfer of control, the assets and liabilities shall be recorded at the fair market value.
- Permanent evaluation to recover the values of the Fixed Assets: The company shall review the recovery of the properties recorded on the fixed assets, the intangible and deferred assets from time to time for the purpose of recognizing the losses resulting from the capital expenditures and the adjustments of estimated useful life of the assets.
- Equity Method: The word “relevant” has been extracted from article 248 of the Brazilian Corporation Law, which determined that the investments considered to be relevant by law would be evaluated at equity value of the invested company. With the exclusion of this word, the record of investments so evaluated was increased.

2. INDUSTRIALIZATION BY ORDER MAY BE CONSIDERED TO BE PROVISION OF SERVICE

The Interpretative Declaratory Act - ADI No. 20 as of December 13, 2007 was recently published by the Brazilian Revenue Service - **RFB**, establishing that for the purposes of computation of the Corporate Income Tax - IRPJ and tax basis of the Social Contribution on Net Income - CSLL, **the industrialization operations by order are considered to be provision of services when the costs of inputs provided by the ordering party are higher upon the composition of total cost of the industrialized product inputs.**

The logical consequence from such understanding reflects from this year on legal entities electing the estimated income taxation system, since they will have to pay the IRPJ and CSLL four times more.

This is due to the fact that said “industrialization by order” will be classified as provision of services. This is to say that the tax rate of 8% fixed to the company electing the estimated income taxation system will be 32%, which is the percentage fixed for provision of services.

Another very important factor is that if such legal entities elect to move from the estimated income taxation system into the taxable income system, they will be automatically transferred into the non-cumulative PIS and COFINS system and the rate of such taxes will be increased to about six percent, without having practically the option to avail itself from the contributions within the production chain.

In order to avoid a possible confusion from the change of activity, from industrialization into provision of services, the ADI provides that such rule is for IRPJ and CSLL purposes. However, there is always the concern that the municipal governments begin to levy the Services Tax – ISS on such legal entities based on the statement by the Brazilian Revenue Service.

3. FINANCIAL INSTITUTIONS SHALL FILE THE DIMOF

As informed in our Tax Developments dated January, 2008, the Federal Government found out rapidly ways to supply the inspection instruments extinguished upon the termination of CPMF, since the Brazilian Revenue Service – **RFB** determined that financial institutions shall file information on a semi-annual basis relating to any financial transactions, such as deposits, payments, checks issued, redemption of deposits and loan agreements, in which the operated global amount on each semester is more than R\$5,000.00 to individuals and R\$10,000.00 to corporations.

For that purpose, the Normative Ruling No. 811 as of January 28, 2008 was published, by which the Declaration of Information on Financial Operation – **DIMOF** was created, the submission of which will be obligatory by any banks, credit cooperatives and saving and loan associations.

For purposes of computing the amount indicated above, the sum of the credits assessed for the month in case of deposits and of the debits assessed for the month associated with financial transactions in any other cases shall be taken into account, without giving the due regard to the values relating to book reversing entries of interests paid or credited as saving account earnings, as well as the values transferred between checking account and saving account of the same

account holder, and the insertion of information that might identify the source or allocation of the funds is forbidden.

By means of the **DIMOF**, the Brazilian Revenue Service – **RFB** will have access to the financial transactions carried out by its users identified by the Individual Taxpayer Registry – CPF and Corporate Taxpayer Registry – CNPJ number. The **DIMOF** shall be filed by digital means using the application made available on website of the Brazilian Revenue Service – **RFB**, and in the event of failure, unreasonably delay to file the **DIMOF** or untrue information, the financial institution shall be subject to penalties.

4. SOCIAL SECURITY CONTRIBUTIONS ON REWARD CARDS

In a recent judgment, the Taxpayers Council (the Administrative Federal Court) decided for the first time that the amounts usually allocated by some companies to their employees as reward for production, which normally occurs by means of the called reward cards shall be subject to the Social Security Contributions.

By judging the appeals filed by Farma Service Distribuidora Ltda., the Taxpayers Council has considered that this incentive bonus amount for production is allocated as salary, by which the contribution salary of the rewarded employees (the tax basis of the Social Security Contributions) must be an integral part and shown in declarations filed by the companies to the Brazilian Revenue Service – **RFB** by means of the Government Severance Indemnity Fund Deposits – **GFIP**.

5. STATE CADIN

The Register of Information on Unpaid Credits to State Entities and Agencies – **State CADIN** was created by the Government of São Paulo State in accordance with Law No. 12.799, as of January 11, 2008, aiming at gathering into an only database the information related to debtors before State entities and agencies. Thus, the name of the individuals and corporations in default will be included in Federal CADIN and **State CADIN**.

The **State CADIN** will serve as an instrument so that the Government of São Paulo State may recover any unpaid credits. In addition, it will contribute for the payment of all values due to the State, allowing thus for the allocation of a higher number of funds to other important programs.

The **State CADIN** will be managed by the Control and Evaluation Department - DCA of the Treasury Secretary of the State of São Paulo, which, among other functions, is in charge of including and excluding the names of debtors from the register.

Awaiting for the regulation of said Law by the Executive Department.

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