BRAZIL

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INTERNATIONAL DEVELOPMENTS

1. WHAT ARE RECENT TAX DEVELOPMENTS IN YOUR COUNTRY WHICH ARE RELEVANT FOR M&A DEALS AND PRIVATE EQUITY?

On 16 March 16 2016, the Brazilian government enacted Law 13,259, which establishes a new progressive capital gain taxation method that is into force since January 2017 (rates may vary from 15% to 22.5%) and reaches Brazilian individuals tax resident and non-Brazilian tax residents investing in Brazil outside the Brazilian financial and capital markets. In this sense, Brazilian Federal Revenue Service ("RFB") issued Normative Instruction ("NI") 1,455 establishing the acquirer shareholder (or its legal representative if the acquirer shareholder is a non-Brazilian tax resident) is the responsible party for withholding the income tax levied on the capital gain verified by the non-Brazilian tax residents upon the sale or disposal of the Brazilian assets (e.g. Brazilian legal entity's shares).

Capital gain verified by non-Brazilian tax residents shareholders corresponds to the positive difference between (i) sale or disposal price and (ii) acquisition cost suitable. There are some discussions if the capital gain amount must be calculated in Brazilian currency (which may lead to the taxation of any positive foreign exchange variation verified by the non-Brazilian tax residents shareholders) or in foreign currency. Although the RFB consolidated its understanding in the sense that this capital gain amount must be calculated in Brazilian currency, there are possibilities to sustain at Brazilian judicial tax courts that the capital gain involving the non-Brazilian tax residents shareholders must be calculated in foreign currency. This is an open subject in the Brazilian case law.

As a rule, the acquisition cost amount should be proved by the non-Brazilian tax residents through suitable and proper documentation.

Besides that, the Brazilian tax legislation provided two options to determine the acquisition cost amount for calculating non-Brazilian tax residents' capital gain taxation in situations where there was no suitable and proper documentation: (i) based on the amount of foreign capital registered with Brazilian Central Bank ("BACEN") or (ii) the acquisition cost equals to zero. As of October, 2016 the NI 1,662 has eliminated the first option to determinate the acquisition cost amount. This change has given rise to the need for non-Brazilian tax residents to obtain and keep proper and suitable documentation in order to support the acquisition cost for calculating the capital gain on the sale or disposal of the Brazilian assets (e.g. Brazilian legal entity's shares).

The main key tax consideration associated with private equity investments in Brazil is the tax benefit available to investments on Brazilian Private Equity Funds ("FIPs"). The most relevant tax advantage in connection with FIPs are the following: (i) the tax-exemption status of their portfolio on income and gains from investments, as taxation is deferred to redemption of shares by the FIP investor; and (ii) provided certain requirements set forth in tax regulations are met, non-Brazilian tax resident investors holding shares in FIPs may also be exempt from income tax upon redemption of FIP's shares (generally levied at a 15% rate, in this case).

2. WHAT IS THE GENERAL APPROACH OF YOUR JURISDICTION REGARDING THE IMPLEMENTATION OF OECD BEPS ACTIONS (ACTION PLANS 6 AND 15 SPECIFICALLY) AND, IF APPLICABLE, THE AMENDMENTS TO THE EU PARENT-SUBSIDIARY DIRECTIVE AND ANTI-TAX AVOIDANCE DIRECTIVES?

Brazil is engaged in the OECD discussions, few references have been formally made to BEPS in Brazilian tax legislation – e.g. a formal indication of compliance with Action 12 in the proposal of Provisional Measure 685 (revoked by the Congress) and with Action 5 in the reasoning for the issuance of Normative Instructions No. 1,634 and 1,689 regarding the disclosure of the beneficial owner.

Besides that, on April 15, 2016 was published the Legislative Decree No. 105/2016 in the official gasette to implement the 2010 protocol to the OECD Convention. On 1 June 2016, Brazil deposited its instruments of ratification with the OECD, and announced that the OECD Convention will enter into force on 1 October 2016. On 30 August 2016, Brazil's Federal Revenue Service ("RFB") announced the enactment of Decree No. 8842/2016, which further implements the OECD Convention.

Brazil signed on October, 2016 the Multilateral Competent Authority Agreement on the Exchange of Country-by-Country Reports ("CbC MCAA") and on 28 December 2016, RFB published NI No. 1,681 to implement annual country-by-country ("CbC") reporting in Brazil as of the tax year of 2016.

In respect the BEPS Action 6, until April 2017, there is no known implementation measure yet. Regarding the BEPS Action 15 Brazil participated in the ad hoc Group for the development of the multilateral instrument, but the expected timing for its implementation is not known yet.

GENERAL

3. WHAT ARE THE MAIN DIFFERENCES AMONG ACQUISITIONS MADE THROUGH A SHARE DEAL VERSUS AN ASSET DEAL IN YOUR COUNTRY?

A. Share deal

Tax advantages:

Tax losses and other tax attributes of the target company may be carried over. Minimisation of tax impacts of an asset deal, especially for Brazilian indirect taxes (IPI, ICMS, PIS, COFINS and ITBI purposes). Depending on how the transaction is structured, the buyer may be able to obtain a better tax result by acquiring the relevant shares, instead of acquiring the assets directly. The benefit is that acquiring shares could allow for the recovery of the purchase goodwill (part of acquisition price exceeding net worth and fair value of target's assets) through tax deduction of such goodwill. There is no need to transfer or terminate employment relationships in course, which avoid the labor and tax costs of termination of employment contracts.

Tax disadvantages:

Pre-acquisition tax, legal and labour liabilities of the target remain with the purchased legal entity. In principle, the acquisition of part of the target's business is not allowed. Pre-acquisition structuring steps may take some time to be implemented.

B. Asset deal

Tax advantages:

The buyer usually obtains a step-up on the book value of the assets. If the acquired assets constitute a going concern / establishment, the buyer may obtain certain benefits of tax credits and certain other tax attributes, especially those associated with indirect taxes, such as IPI and ICMS. It often helps to minimise the risk of tax, legal and labor liabilities. It may take less time to implement.

Tax disadvantages:

Tends to result in a more tax burdensome transaction when compared to a share deal (especially for Brazilian indirect taxes – IPI, ICMS, PIS, COFINS and ITBI purposes). It may prevent the buyer from acquiring the target's tax losses and other tax attributes. Depending on the assets or businesses acquired, acquiring assets may require new registrations for tax, labor and other regulatory purposes. In the case the assets transferred constitute a going concern / establishment, the risk of tax, legal and labor liabilities cannot be avoided.

BUY-SIDE

4. WHAT STRATEGIES ARE IN PLACE, IF ANY, TO STEP UP THE VALUE OF THE TANGIBLE AND INTANGIBLE ASSETS IN CASE OF SHARE DEALS?

The rules of Purchase Price Allocation ("PPA") could step up the value of tangible and intangible assets of the acquired company. However, in some cases, Brazilian corporate income taxes could be levied on such increase of value.

5. WHAT ARE THE PARTICULAR RULES OF AMORTISATION OF GOODWILL IN YOUR COUNTRY?

Current tax legislation determines that the goodwill paid on local transactions (involving non-related parties) must be allocated according to IFRS: goodwill must be allocated first to the fair value of assets/liabilities and intangibles and the remaining portion could be allocated as deductible goodwill for tax purposes (based on future profitability). Tax amortisation of the goodwill (excluded previous allocation on the fair value of assets/liabilities and intangibles) was preserved, complying with the maximum limit of 1/60 per month. As a condition for the tax deduction of the goodwill, a PPA report must be prepared by an independent expert and filed with the Brazilian Federal Revenue or the Register of Deeds and Documents within 13 months.

Goodwill tax deduction is still allowable, provided certain conditions are met, mainly that an independent report is prepared and filed with the tax authorities or the Register of Deeds and Documents and that the deal is not carried out between related parties.

6. WHAT ARE THE LIMITATIONS TO THE DEDUCTIBILITY OF INTEREST ON BORROWINGS IN THE CASES OF ACQUISITION OF SHARES AND ASSETS?

The Brazilian legislation establishes requirements for the deductibility of interest expenses arising from debt operations with related parties or lenders located in low-tax jurisdictions or under a privileged tax regime. Generally, for tax purposes, the debt cannot be higher than: (i) two times the amount of the participation of the related lender located anywhere outside Brazil (except for lenders located on low-tax jurisdictions or under a privileged tax regime) in the net equity of the borrower and (ii) 30 percent of the net equity of the borrower if the lender is located in a low-tax jurisdiction or under a privileged tax regime (whether it is a related party or not).

This rule also applies for any kind of debt operation where a foreign related party acts as guarantor, co-signer or intervening party of the debt contract. The legislation also defines specific requirements that taxpayers must meet to deduct payments to beneficiaries located in a low-tax jurisdiction or under a privileged tax regime. These requirements include identifying the beneficial owner and determining the operational capability of the foreign party to carry out the operation agreed with the Brazilian party.

In addition, the Brazilian transfer pricing legislation sets forth certain limits regarding the deductibility of interest expenses arising from debt operations with related parties.

Brazilian BEPS Action implementations are not known yet in this respect.

The deductibility of interest expenses arising from debt operations with non-related parties is allowed once the transaction is carried out at normal market conditions and such expenses seem necessary for the business activities of the borrower.

7. WHAT ARE USUAL STRATEGIES TO PUSH-DOWN THE DEBT ON ACQUISITIONS?

In most situations where the purchaser intends to push-down debt on acquisitions, the legal entity that acts as the borrower is a Brazilian vehicle or holding company. Following the purchase, this legal entity is merged into the acquired operational legal entity.

Other structures may involve (i) back-to-back loans on the same terms and conditions, or (ii) obtaining a new loan at the level of the acquired company so that it can pay off the original loan. These structures may be feasible if the entire capital stock of the legal entity is purchased. Others structures may also be feasible subject to a case by case analysis.

Brazilian BEPS Action implementations are not known yet in this respect.

8. ARE THERE ANY TAX INCENTIVES FOR EQUITY FINANCING?

Brazilian tax rules do not provide a specific tax treatment for private equity financed transactions. However, Brazilian legal entities have available a deductible instrument for remunerating shareholders for the capital invested in companies: interest on net equity, calculated by reference to the net equity accounts, considering the official Brazilian long-term interest rate. The upper limit on interest on net equity is determined as the higher of: (i) 50% of the net income for the year, before deduction of the interest on net equity and deduction of the

provision for corporate income tax, but after the deduction of the social contribution on net income, and (ii) 50% of retained earnings plus profit reserves. Besides treating these payments as a tax deductible expense, Brazilian tax law also requires them to be taxed at source at 15%, even if the recipient is a nonresident.

9. ARE LOSSES OF THE TARGET COMPANY(IES) AVAILABLE AFTER AN ACQUISITION IS MADE?

In general, tax losses are kept by the acquired company, but the income tax regulation provides for some exceptions, including the following: (i) on a merger, the tax losses of the absorbed company cannot be used by the surviving entity and thus are essentially lost, (ii) in a spin-off, the tax losses of the target entity are lost in proportion to the net equity transferred; (iii) carried forward tax losses are forfeited if the company's ownership and main activity change between the tax period in which the losses are generated and the tax period in which they are used.

Income tax regulation provides that tax losses generated in 1 year can be carried forward indefinitely. However, the use of tax losses carry forwards is limited to 30 percent of the taxable income generated during the year.

Further, non-operational tax losses carryforwards may only be used against non-operational taxable income. The 30 percent limitation applies here as well. A gain or loss from the sale of inventory generally is treated as ordinary or operational activity, while a gain or loss from the sale of the machinery and equipment, buildings, land and general intangibles is treated as a non-operational (capital) activity.

10. ARE THERE ANY ITEMS THAT SHOULD BE INCLUDED IN THE SCOPE OF A TAX DUE DILIGENCE THAT ARE VERY SPECIFIC TO YOUR COUNTRY?

Tax compliance in Brazil is an important point to be considered in due diligence, since Brazilian companies are subject to many levels of taxation (federal, state and municipal) and are required to file several ancillary tax obligation (tax returns, accounting and tax electronic bookkeeping). Tax authorities have five years counted from the taxable event to collect or question the payment of taxes, reason why a good and deep due diligence shall be done with regard to payment of taxes, in order to verify any possible materialised or non-materialised (i.e. potential) tax contingency involving all taxes regarding the last 5 years. In addition, corporate reorganisations with the sole purpose of tax efficiency can be questioned by tax authorities and may be considered fraudulent. In this sense, not only past corporate reorganisations shall be evaluated, but also it is important to consult specialists before implementing any corporate reorganisation on the target companies.

11. IS THERE ANY INDIRECT TAX ON TRANSFER OF SHARES (STAMP DUTY, TRANSFER TAX, ETC.)?

There is no Brazilian stamp, issue, registration or similar tax or duties payable by shareholders on transfer of shares. There is no Brazilian inheritance or gift tax applicable to the ownership, transfer or disposition of shares, except inheritance or gift tax imposed by Brazilian states on inheritances or gifts by individuals or entities domiciled in Brazil or abroad.

12. ARE THERE ANY RESTRICTIONS ON THE CORPORATE TAX DEDUCTIBILITY OF ACQUISITION COSTS?

Please see the answer to question 5.

13. CAN VAT (IF APPLICABLE) BE RECOVERED ON ACQUISITION COSTS?

As a general rule, VAT is not levied on acquisition costs related to share deals. Assets deals could be taxed for VAT purposes in Brazil and the recovery of relevant VAT could occur, depending on applicable legislation, facts and circumstances.

In Brazil, VAT has a very particular system when applied at federal or state level. Federal VAT, referred to as Excise Tax ("IPI"), is levied on manufactured products. IPI is payable at varying rates on nearly all sales and transfers of industrialised products. Normally, it is charged at an ad valorem rate according to the classification of the product based upon the Harmonised Tariff Schedule, with rates ranging from zero to a maximum of 330%.

State VAT ("ICMS") is levied on communication services, inter-state and inter-municipal transportation services and also the circulation of goods. ICMS inter-state transactions are subject to rates of 12%, 7% and 4%. Intra-state transactions are subject to an average rate of 18% on goods and 25% on communication services.

In Brazil, establishments or business units are generally treated as independent taxable persons for VAT purposes. There are no such provisions for VAT grouping, whereas cross-border transactions performed with a Brazilian entity or a Brazilian branch of a foreign entity may be taxed, if the transaction is subject to VAT in Brazil.

Value added tax (VAT) credits may be transferred where an establishment is acquired as a going concern/establishment.

14. ARE THERE ANY PARTICULAR TAX ISSUES TO CONSIDER IN THE ACQUISITION BY FOREIGN COMPANIES?

Please see the answer to question 1 regarding the rules of capital gains involving foreign shareholders.

15. CAN THE GROUP REORGANISE AFTER THE ACQUISITION IN A TAX NEUTRAL ENVIRONMENT THROUGH MERGERS OR A TAX GROUP?

Depending of applicable legislation, facts and circumstances, it is possible to carry out a tax neutral environment through mergers based on book values. Brazil does not admit any consolidation for tax purposes and does not have a tax group.

16. IS THERE ANY PARTICULAR ISSUE TO CONSIDER IN CASE OF TARGET COMPANIES OF WHICH MAIN ASSETS ARE REAL ESTATE?

Considering that the target companies' main activities involve the purchase and sale of real estate properties, besides regulatory and other tax matters, the main issues refer to the levy of Municipal Real Estate Transfer Tax (ITBI). The ITBI is a municipal tax payable by the buyer on the acquisition of real estate and the rate varies depending on the relevant Municipality. The basis calculation is the market value of the property or its appraised value, whichever is higher.

In addition, a presumed profit method for corporate income taxes could be interesting to decrease the tax burden of legal entities that deal with real estate transactions.

17. IS FISCAL UNITY/TAX GROUPING ALLOWED IN YOUR JURISDICTION AND IF SO, WHAT BENEFITS DOES IT GRANT?

Brazil does not admit any consolidation for tax purposes.

In Brazil, establishments or business units are generally treated as independent taxable persons for VAT purposes. There are no such provisions for VAT grouping.

SELL-SIDE

18. HOW ARE CAPITAL GAINS TAXED IN YOUR COUNTRY?

The amount of capital gain realised as a result of a direct sale of shares issued by a Brazilian company equals the excess of the amount realised on the sale of the shares over its acquisition cost. That is, when earned by a Brazilian legal entity, the capital gain is subject to corporate income tax at a combined rate of 34%. When earned by a Brazilian tax resident individual, the capital gain is subject to progressive rates ranging from 15% to 22,5%.

A non-Brazilian legal entity or tax resident individual who sells assets located in Brazil are subject to WHT at rates that may vary from 15% to 22,5%, or 25% if they are resident or domiciled in a tax heaven jurisdiction. As mentioned on the answer to question 1, the method for the determination of the acquisition cost basis of non-Brazilian legal entities or tax resident individuals is not completely clear and is subject to different interpretations.

19. IS THERE ANY FISCAL ADVANTAGE IF THE PROCEEDS FROM THE SALE OF SHARES ARE REINVESTED?

Brazilian legislation does not provide for any fiscal advantage if the proceeds from sales are reinvested in Brazil.

20. ARE THERE ANY LOCAL SUBSTANCE REQUIREMENTS FOR HOLDING COMPANIES?

On September 14, 2016 was published in the Official Gasette the Normative Instruction RFB No. 1,658/2016 that has clarified that a holding company is deemed to have "substantial economic activity" when, in its residence country, it presents an operational capacity suitable to its purpose, evidenced, among other factors, by the existence of skilled employees in sufficient number and adequate facilities for management and effective decision-making relating to: (i) the development of activities aimed at obtaining income derived from its assets or and (ii) the management of the equity stake aimed at obtaining income arising from the distribution of dividends and capital gains.

As per Normative Instruction RFB No. 1,658/2016's provisions, in order to identify the existence of economic substance, RFB is focusing more on the activity carried out by the holding company (rather than its corporate format).

21. ARE THERE ANY SPECIAL TAX CONSIDERATIONS REGARDING MERGERS/SPIN-OFFS?

Mergers, spin-offs and transfer of assets are also not in any case subject to indirect taxes or value-added taxes and there is also no tax on net worth of companies or individuals. Such transactions will, however, be subject to certain fees payable to commercial registries, and notarial offices (real estate and documents).

As far as spin-offs are concerned, like in the case of mergers, tax losses of the spun-off company and merged company cannot be off-set by the successor company. In case of a partial spin-off the tax losses of the spun-off company could remain available for offset by the spun-off company in proportion to the equity that remains after the spin-off.

MANAGEMENT INCENTIVES

22. WHAT ARE THE TAX CONSIDERATIONS IN YOUR JURISDICTION FOR MANAGEMENT INCENTIVES?

Brazil does not have attractive instruments for management incentives. However, for managers who are employees of a Brazilian legal entity, there are some tax benefits regarding labor duties and tax and social security taxes regarding Profit Share Programmes, once certain conditions and requirements are met by the legal entity.

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