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4-1-1980

Brazil

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**Recommended Citation**

*Brazil*, 12 U. Miami Inter-Am. L. Rev. 482 (1980)

Available at: <http://repository.law.miami.edu/umialr/vol12/iss2/13>

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## LEGAL MEMORANDUM

The following is a brief summary of legal rulings and decisions recently enacted by the Brazilian Government:

### LEGISLATIVE AND ADMINISTRATIVE RULINGS

#### *Economic Package*

In view of the negative effects of Brazil's galloping inflation and balance of payment difficulties, the Government has issued a strong economic package consisting of various Decree-Laws, Decrees, and Resolutions. Basically, the package consists of eight major alterations in the areas of exchange, foreign trade, subsidies, and tax incentives.

The most important measure was the 30% devaluation of the cruzeiro in relation to the U.S. dollar. This will evidently stimulate exports and discourage imports and thus improve Brazil's balance of payments. But it should also attract a greater number of foreign investors. According to Government sources, this so-called "maxi-devaluation," although representing a break in the former policy of "mini-devaluations," is merely an extraordinary event which will continue to be followed by normal small devaluations at regular intervals.

Another measure taken was the elimination, as of January 1, 1980, of the prior deposit of presently 80% of the FOB price of imports. This deposit remained blocked for one year and made imports very costly. As the devaluation of the cruzeiro will already substantially increase the cost of imports, it was necessary to revoke the prior deposit requirement. The regulation that provided for this revocation was Resolution No. 584/79 of the Central Bank of Brazil. The same reason caused the issuance of Central Bank Resolution No. 585/79, which eliminated the prior deposit required for residents of Brazil to travel abroad.

#### *Deduction of Exchange Losses in Companies*

The 30% devaluation of the cruzeiro which occurred in early December would have caused companies with foreign loans to adjust the value of their indebtedness in accordance with the new exchange rate. This would apply to all companies with profits, and therefore, subject them to corporate income tax, thus causing a reduction in the taxable profit. This, in turn, would have deprived the Federal Government of considerable revenue. To mitigate this possibility,

the President of the Republic signed Decree-Law No. 1.733 of December 20, 1979. Corporate borrowers of foreign loans will thus be authorized to deduct from their taxable income in 1980 only the exchange loss referring to payments of interest and principal actually made in 1979. The same applies to the exchange losses of the following years. The exchange loss that does not refer to such actual payments but merely to accounting of exchange fluctuation may only be deducted within the limits of the official correction of Readjustable National Treasury Bonds (ORTNs), while any excess over these limits may be deducted in portions of 20% per year from 1981 to 1985 or added to the cost of the fixed assets.

### *Deduction of Exchange Losses in Financial Institutions*

In addition to the legislation enacted to deal with the exchange losses of companies as a result of the 30% devaluation of the cruzeiro, the Minister of Finance issued Portaria No. 1014 of December 27, 1979, to deal with the problem as regards financial institutions. Brazilian financial institutions that deal in repassing foreign loans to local borrowers have thus been authorized to repass the total exchange losses within the limits of the exchange losses actually suffered in connection with payments to the foreign lender. In the same Portaria, the Minister determined that commercial leasing companies may defer the exchange losses that exceed the official correction of Readjustable National Treasury Bonds (ORTNs).

### *Trading Companies*

According to the Government's policy of encouraging exports and thus strengthening trading companies, the Foreign Trade Department of Banco do Brasil, S.A. (CACEX) issued Communiqué No. 79/41 to determine that trading companies registered with CACEX for imports, or for both imports and exports, must have a minimum paid-in capital of Cr\$ 1,500,000 as of January 1, 1980.

### *Corporate Income Tax*

In the last months, successive Decree-Laws, Decrees, and Regulations have been issued by the Government to close the loopholes that taxpayers found under the new Company Law (Law No. 6.404 of 1976). More comprehensive regulations have now been issued on the matter in the form of Decree-Law No. 1.730 of December 17, 1979. This Decree-Law attempts to clarify the various changes that

have been introduced in corporate taxation by specifying them individually.

#### *Foreign Loans for Government Programs*

Brazil may only contract for foreign loans within prescribed limits established by law which are subject to adjustment. The President signed Decree-Law No. 1.756 of December 31, 1979, which increases the limits within which foreign loans may be sought and guaranteed by the Brazilian government. The limit for foreign loans to finance government works and services has been expanded to Cr\$ 250 billion, while the limit for the National Treasury to guarantee foreign loans taken by Brazilian States and Municipalities has been increased to Cr\$ 700 billion. These limits will be corrected each year according to the indexes applied to Readjustable National Treasury Bonds (ORTNs).

#### *Fiscal Rulings*

The Coordinator of the Taxation System issued Ruling No. 43 on December 18, 1979, to establish the procedure for applications for federal fiscal rulings. Such applications are to be made in the form of petitions addressed to the Federal Revenue Office of the taxpayer's domicile and are to be restricted to one tax. If the application refers to the tax classification of goods, it should not cover more than three products.

#### *Export Incentives*

Portaria 960 of the Minister of Finance, which was part of the economic package released at the end of last year, suspended the tax credit allowed on exports and consisting of the refund of IPI tax paid on domestic market operations. According to Portaria 19/80, the Minister of Finance has now determined that such suspension will not apply to: (a) exports contracted in cruzeiros and for which Export Licenses were issued prior to December 6, 1979; (b) exports for the construction of the Palmar hydroelectric plant; (c) sales of national machinery and equipment on the domestic market when made directly by a manufacturer entitled to an IPI tax credit premium; and (d) local purchases by shipbuilders of machinery and equipment.

The Minister of Finance also issued Portaria 20 establishing that the import duty and IPI tax exemption enjoyed by the producers of manufactured goods, when importing items limited in value to 10% of

their export increase in the previous year, will no longer be granted, effective 1980.

### *Tax Benefits*

In Portaria 16/80, the Ministers of Finance and Industry and Commerce established that applications for import duty and IPI tax reduction are to be submitted to the Export Incentives Commission (CIEIX) only until March 31, 1980. After that date, the authority for such tax benefits will be transferred to the Commission for the Concession of Tax Benefits to Special Export Programs (BEFIEIX).

### *Tax at Source*

When there is tax at the source, it is considered that the taxpayer is the beneficiary of the payment: the source is nothing but the intermediary who collects the tax due from the beneficiary and pays it into the Government coffers. Nevertheless, on some occasions, the source may be willing to accept the liability for the tax, and then the normal procedure is for the amount on which the tax is calculated to be grossed-up. In the case of payments to non-residents of Brazil, for instance, when the tax is normally 25% at the source and the payor agrees to accept the liability for the tax, the amount due, if the base amount is 100, is grossed-up to 133, so that the 25% due at the source will bring the net to 100. This grossing-up was not normally accepted in the past as an expense of the payor, with the tax authorities taking the view that the added amount was not due by local companies. The Coordinator of the Tax System has just reversed this ruling with the issuance of Normative Ruling No. 2 of January 15, 1980, which states that if the payor accepts the greater liability for the added amount, then the full amount of the tax paid should be considered as a normal business expense.

### *Compulsory Deposit of Foreign Loans*

Foreign loans that enter Brazil are divided into loans which may be negotiated without official accrediting (loans taken by private concerns), and loans which may only be negotiated with official accrediting (loans to government concerns). According to Central Bank Resolution No. 595/80, the foreign loans that may be freely negotiated shall, as of January 17, 1980, be subject to the compulsory deposit with the Central Bank of Brazil of 75% of the principal amount. This deposit is to be made in the form of Central Bank Resolution 432/77,

which permitted the funds of foreign loans to be deposited in foreign currency and withdrawn in the same amount of foreign currency. Of this 75% deposit, one-third will be released after sixty days, one-third after ninety days, and one-third after 120 days.

### *Price Control*

The Price Control Commission (CIP) has recently issued several Resolutions as follows: (a) Resolution No. 132/80, to revoke CONEP Resolution No. 19/68 which permitted the adjustment of the prices of ICM tax-paying products to the extent of the respective tax raise; (b) Resolution No. 133/80, submitting the prices of comestible oils to CIP control; (c) Resolution No. 134/80, submitting the prices of lubricant oils to CIP control; and (d) Resolution No. 135/80, providing that retail dealers of medicine and diet products may only acquire such goods from the manufacturers upon presenting price lists approved by CIP.

## JUDICIAL AND ADMINISTRATIVE DECISIONS

### *Assets Abroad*

All residents of Brazil must attach to their annual income tax statement a complete list of all their assets, whether in Brazil or abroad. A recent decision of the First Taxpayers Court indicates, in a short statement, that the taxpayer who has assets outside the country may not simply justify the use and the origin of declared income. It is essential to prove the actual existence of these assets and the transfer of their value to Brazil (Decision No. 102-17.456).

Pinheiro Neto & Cia.—Advogados  
São Paulo, Brazil  
February 11, 1980