

# Indirect Tax Alert

News from Americas Tax Center

## Brazilian tax authorities rule on manner in which companies may exclude ICMS from PIS/COFINS tax basis

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The Brazilian tax authorities have ruled (Tax Ruling #13/2018 (23 October 2018)) that companies may exclude the monthly state Value Added Tax payable (i.e., ICMS included in the tax basis of PIS and COFINS (social contributions)) from the tax basis of the social contributions.

### Background

This Tax Ruling responds to the Federal Supreme Court's ruling in an Extraordinary Appeal (RE #574.706) on 15 March 2017. The Court decided that ICMS should not be included in the tax basis of the PIS/COFINS, when they are levied on revenue. The Court's decision is binding on all courts.

The final text of RE #574.706 is still pending due to a motion for clarification from the Office of the Attorney General of the National Treasury (PGFN). The two issues on which the PGFN seeks clarification are: (i) the effective date of RE #574.706; and (ii) the method taxpayers should use for excluding the ICMS from the tax basis of PIS/COFINS (the matter is controversial, as both ICMS and PIS/COFINS may be creditable for the taxpayers).

Despite uncertainties around those outstanding issues, companies began calculating the amount of their overpaid social contributions as soon as the Court decided RE #574.706. In most cases, companies calculated the overpaid amounts over the past five years, which is the Brazilian statute of limitations,

and based the overpaid amounts on the ICMS reported on the sales tax invoices (i.e., the gross amount of ICMS reported in the “Nota Fiscal”, in Portuguese).

### **Tax Ruling #13/2018**

In Tax Ruling #13/2018, the Brazilian tax authorities state that the amount to be excluded from the social contributions' tax basis is the monthly ICMS payable (which already takes into consideration any credits that companies may have used, or tax incentives from which the taxpayer may benefit, for example). The ruling provides details on the method for calculating the mentioned “ICMS payable” amount to be considered when calculating the recoverable PIS and COFINS.

The tax authorities' method for calculating the overpaid PIS/COFINS is contrary to the method that most companies have been adopting (i.e., companies focus on the gross ICMS reported in the invoice, whereas tax authorities focus on the net ICMS effectively paid). The tax authorities' method reduces the amount companies may recover. Through Tax Ruling #13/2018, the tax authorities limit the Supreme Court's decision by restricting the ICMS amount that may be excluded from social contributions to the ICMS amount paid.

The ruling leaves many questions open, including:

- ▶ Is Tax Ruling #13/2018 the best interpretation of the Supreme Court's decision in RE #574.706?
- ▶ How binding is Tax Ruling #13/2018?
- ▶ What are the ruling's effects on taxpayers that accumulate positive ICMS credit balances (and consequently are not collecting ICMS monthly), such as exporters?
- ▶ For taxpayers that benefit from ICMS presumed credits (i.e., tax incentives granted by Brazilian states that reduce the amount of ICMS payable), what amount would be excluded from the PIS/COFINS tax basis?

As demonstrated, based on the recent interpretation issued by the tax authorities, taxpayers should discuss with their tax advisers on how Tax Ruling #13/2018 affects them. EY Brazil has experience to support taxpayers in these analyses, considering all the complexity, technical and financial relevance that this subject presents.

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