

VGL NEWS

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MP 232/04 – Tax Law Amendments

Provisional Measure no. 232 (*Medida Provisória* - “MP 232/04”), dated December 30, 2004, was published in the Federal Gazette’s Special Edition of that same date, introducing important changes to Brazilian tax laws.

MP 232/04 established a new progressive table for the purpose of determining the Income Tax, due by individuals on a monthly and annual basis, with regard to the triggering events occurring as of January 01, 2005 (article 1):

Monthly Progressive Table

Tax Basis in R\$	Tax Rate %	Amount to Deduct from the Tax in R\$
Up to 1,164.00	-	-
From 1,164.00 to 2,326.00	15	174.60
Above 2,326.00	27.5	465.35

Annual Progressive Table

Tax Basis in R\$	Tax Rate %	Amount to Deduct from the Tax in R\$
Up to 13,968.00	-	-
From 13,968.00 to 27,912.00	15	2,095.20
Above 27,912.00	27.5	5,584.20

Other exemptions and deductions applicable to income earned by individuals were also restated, as follows: (i) the exempt portion of earnings deriving from retirement and pension paid by the Social Security, by any state-owned company or by complementary pension entities, for taxpayers who will be 64 years of age, was fixed at R\$ 1,164.00 per month; (ii) the monthly deduction amount of expenses incurred with dependents was increased from R\$ 106.00 to R\$ 117.00, with the consequent increase of the annual limit deductible from the Income Tax basis from R\$ 1,272.00 to R\$ 1,404.00, per dependent; (iii) the limit of individual annual deduction with expenses with the taxpayers’ education and such taxpayers’ dependents, carried out to educational establishments, was increased from R\$ 1,998.00 to R\$ 2,198.00; and (iv) the discount value for taxpayers opting for the simplified form of the Annual Adjustment Declaration (*Declaração de Ajuste Anual*) was altered to R\$ 10,340.00.

Furthermore, taxpayers, both individuals and legal entities, are now not obliged to deduct from amount corresponding to the Income Tax that will be refunded, the amount corresponding to the penalty for failure to deliver the declaration of earnings or the untimely delivery of such declaration, where such penalty will be carried out through a tax assessment proceeding carried out by the Federal Revenue Office (*Secretaria da Receita Federal*).

MP 232/04, by means of an amendment to article 30 of Law no. 10,833/03, established that payments made by legal entities to other private legal entities for the rendering of medical, engineering, transportation and advertising services, as well as those itemized in that law, are subject to withholding in relation to the Social Contribution Tax on Profits (*Contribuição Social Sobre o Lucro Líquido*), Contribution for Social Security Funding (*Contribuição para o Financiamento da Seguridade Social*) and the Contribution to the Employee Profit Distribution (*Contribuição para o Programa de Integração Social*). Such withholding will not be required from foreign transportation companies. On the other hand, regarding international transportation services carried out by domestic companies, only Social Contribution Tax on Profits shall be withheld.

Amounts paid or credited by legal entities to other private legal entities for the rendering of maintenance services for movable assets and real estate, as well as transportation services, medical services in general rendered under medical orientation, and engineering services are subject to the Withholding Tax (*Imposto de Renda Retido na Fonte*), at a 1.5% tax rate, and must be collected up to the third business day of the week after the occurrence of the triggering events.

The Withholding Tax rate levied on the amounts paid or credited by legal entities to other legal entities for the rendering of cleaning, conservation, maintenance, security, surveillance, transportation and labor contracting/rental services was increased from 1% to 1.5%.

The amendments dealt with in the previous three paragraphs, in view of the provisions of MP 237, dated January 27th, 2005, only apply to payments carried out as of March 1st, 2005.

Pursuant to article 9 of MP 232/04, the currency exchange variation of foreign investments held by legal entities and assessed by the equity pick-up method shall be a part of the taxable income and the tax basis for the Social Contribution Tax on Profits as revenue or financial expense.

MP 232/04 also established a percentage of 40% to be considered as Corporate Income Tax and Social Contribution Tax on Profits tax basis owed by legal entities opting for presumed profit (*lucro presumido*) on the following activities: (i) general rendering of services, except hospital-related services; (ii) business intermediation; (iii) management, leasing or assignment of movable assets, real estate and rights of any nature; (iv) cumulative and continuous rendering of services such as credit and market advisory, credit management, risk selection, management of accounts payable and receivable, purchase of credit rights arising from commercial sales carried out in an on credit basis or the rendering of services (factoring). Such increase shall be in effect for the Social Contribution Tax on Profits as of April 01, 2005, and for the Corporate Income Tax as of January 01, 2006.

Concerning tax administrative proceedings, several provisions of Decree no. 70,325/72 were amended, among which we highlight that the following cases may not be appealed: where the amount in dispute is lower than R\$ 50,000.00 (fifty thousand Reais), proceedings relative to penalty for non-compliance with accessory obligation, refund, reimbursement, off-set, reduction, exemption and immunity of taxes and contributions, as well as proceedings related to the *SIMPLES*.

Redemptions in complementary pension plans structured in the on a fixed-benefit (*benefício definido*) mode are also subject to Income Tax at a fixed rate of 15% (article 3 of Law no. 11,053/04), whereas the benefits remain subject to taxation based on the progressive table.

We highlight that with the revocation of article 36 of Law no. 10.637/02, as of January 01, 2005, the difference between the amount of the paid-up capital, resulting from the incorporation to the equity of another legal entity carrying out the subscription and pay-up, and the value of participation registered in the accounting record of the same legal entity, is now to be computed for the determination of the taxable income and the tax basis of the Social Contribution Tax on Profits.

As a last issue, we would like to point out that the Brazilian Congress (*Congresso Nacional*) is demonstrating a great resistance to approve this Provisional Measure, particularly with respect to the increase of the tax burden for service rendering companies.

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