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*Advogados Associados*

## VGL NEWS

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### "New Brazilian Year-End Tax Rules – WHT and IOF Rules relevant to nonresident investors"

In December 31, 2010, two different rules relevant for nonresident investors were published, one concerning Brazilian Withholding Tax ("**WHT**"); and the other one concerning Tax on Credit, Foreign Exchange, Insurance or Bonds' and Securities' Transactions ("**IOF**") – the type levying on foreign exchange ("**FX**") transactions ("**IOF/FX**"); and on Bonds and Securities ("**IOF/TVM**").

#### 1 – WHT

The Provisional Measure no. 517, of December 30, 2010, brought about, in its Article 1 and 3, relevant WHT rules for foreign investors (among other tax rules), determining the following:

#### **(a) Article 1: New Foreign Investors' Zero-WHT for Brazilian Private Bonds purchased under Public Distribution**

Income (as defined under item "a" of paragraph 2, of article 81, Law 8,981/95 – meaning earnings/remuneration of capital of any kind – herein denominated "**Income**") remitted, credited, paid, delivered to, or used by, a "**non-tax favorable jurisdiction foreign investor**" (foreign investor not resident in a country or jurisdiction that do not tax income or tax it at a maximum 20% rate), arisen from bonds or securities ("**Bonds**"):

- (a) issued by private legal entities not classified as financial institutions;
- (b) acquired as of January 1, 2011, under a public distribution;
- (c) regulated by the Brazilian National Monetary Council ("**CMN**") or by the Brazilian Securities and Exchange Commission ("**CVM**");

will be subject to zero percent rate of Brazilian withholding tax ("**Zero-WHT**").

In order for such Zero BR WHT to apply, the Bonds in question must cumulatively present the following features ("**Bonds' Conditions**"):

- <!--[if !supportLists]-->(i) <!--[endif]-->be remunerated by prefixed interests rate connected to price indexes or Brazilian Reference Rate (*Taxa Referencial* or "TR");
- <!--[if !supportLists]-->(ii) <!--[endif]-->have an weighted average maturity/term above 4 (four) years, which formula shall be determined by the CMN;
- <!--[if !supportLists]-->(iii) <!--[endif]-->be prohibited the repurchase of the Bond by the issuer in the first 2 (two) years after the issuance;
- <!--[if !supportLists]-->(iv) <!--[endif]-->not present any promise to resell the Bond assumed by the buyer/investor;

- <!--[if !supportLists]-->(v) <!--[endif]-->term for the periodic payment of income, if applicable, with minimum intervals of 180 (hundred and eighty) days;
- <!--[if !supportLists]-->(vi) <!--[endif]-->demonstrate proof that the Bonds are traded within securities' regulated markets;
- <!--[if !supportLists]-->(vii) <!--[endif]-->present simplified procedure (to be determined by the CMN) to demonstrate the intention to allocate the funds raised by the Bonds into investment projects.

Regarding Bonds invested by foreign investors before January 1, 2011, and as long as the Bonds' Conditions above are met, the respective foreign investor may opt (until June 30, 2011) to anticipate any WHT due on the Income as if any remittance, payment, credit, usage or delivery of the Income abroad was performed, being the Income earned as of the date of the WHT collection, subject to the beneficial Zero-WHT rule above-mentioned.

### **(b) Article 3: Investment Funds investing in Debentures issued by Special Purpose Entities ("SPE") – Zero WHT for the Funds' Foreign Investors**

Income remitted, credited, paid, delivered to, or used by, a "**non-tax favorable jurisdiction foreign investor**" holding shares of an Investment fund ("**Fund**") that, in its regulation, has the intention to invest ("**Condition**"), at any time of the Fund's existence, not less than 85% (eighty five percent) of the Fund's net equity value, in debentures issued by SPE incorporated to implement investment projects on the infrastructure area (considered as priory as regulated by the Brazilian Federal Government), shall be subject to Zero-WHT, *being such Income subject to the Zero WHT the one particularly connected with the debentures in question*. The Zero-WHT is also applicable for Foreign Investors holding shares of Funds investing at least 95% (ninety five percent) of its resources in shares of other Funds attending to the Condition above-mentioned. Funds or Funds investing into Funds' shares will have the following terms: (a) to comply with the Conditions, 180 (hundred and eighty) days as of the Funds' incorporation date; (b) 90 (ninety) days for any reclassification.

The lack of attendance by the Fund or by the Fund investing into the Fund of the Conditions provided in this rule will imply on the Fund's extinction or transformation/reclassification in another investment fund modality, as applicable. The reclassification shall be computed as of the date the Fund disobeyed to the Conditions. On the Fund's extinction or transformation/reclassification in another investment fund modality, the Income *connected with the debentures in question* will be subject to the regressive WHT rates of 22,5% to 15%, depending on the length of the investment.

The CVM and the Brazilian Internal Revenue Services will regulate the subject.

## **2 – IOF**

Decree 7,412, of December 30, 2010, changed some rules contained in Decree 6,306, December 14, 2007 (which approved the "**IOF Regulation**"), concerning both IOF/FX and IOF/TVM.

### **(a) IOF/FX**

Article 15 of IOF/Regulation was re-written (actually, the previous paragraph 1 of said article was substituted by the new version of article 15-A) and the following relevant changes on the IOF/FX rules were brought about:

- Introduction of new rules for the settlement of the following FX transactions hired as of January 1, 2011, being in all cases subject to IOF/FX at 2% (two percent rate):
  - (a) entered by foreign investors, for the entry of funds into Brazil (including via simultaneous FX transactions) for the acquisition of shares of Equity Investment Funds (named as "FIP"); investment funds of emerging legal entities ("FIEE") and investment funds investing in those investment funds, being all those investment funds incorporated according to pertaining CVM rules – "**FIP and FIEE Investments**";
  - (b) simultaneous FX for the entry of funds in Brazil by means of the cancellation of Depositary Receipts, for investing in stocks traded within stock exchange market – "**Cancellation of DRs**";

- (c) simultaneous FX for the entry of funds into Brazil deriving from the change of foreign investment regime, from direct investment dealt with Law 4,131/62, to investment in stocks traded in stock exchange market as regulated by CMN – **“conversion of 4131 Direct Investment into 2689 Capital Markets’ Investment”**.

The former rule (contained in the former item XII) regarding FX transactions’ settlement for the remittance of dividends and interest on net equity (*juros sobre capital próprio*) to a foreign investor under the transactions dealt with the former items XXIV, XXV, XXVI and XXVII (primarily the transaction *in the financial and capital markets*), subject to IOF/FX at zero percent rate, was changed (currently under Item X), excluding the express mention to the items concerning foreign investments in the financial and capital markets; only maintaining that such amounts must be “received by foreign investor”.

The former zero IOF/FX rule regarding foreign credit transactions (i.e. foreign loans and financing transactions) was only applicable to funds raised/entered into Brazil *as of October 23, 2008*; the new rule under new item IX excluded such date condition, being therefore applicable for the settlement of FX transactions for the entry of funds into Brazil and the remittance of funds abroad, relating to fund raised via foreign loans and financing.

#### **(b) IOF/TVM, also applicable to Foreign Investors**

Change on the IOF/TVM applicable for “Fixed Income Investments - Short-term transactions”: the former rule was applicable to any kind of fixed income transaction (including private bonds); the current rule only maintains the IOF/TVM levy for fixed income investments in federal, state and municipal public bonds; and for investments in investment funds (except stock funds).

As to the IOF/TVM of 1,5% applicable for the transfer/assignment of stocks by the stocks’ holder to the custodian bank in order to such stocks be the underlying asset of Depositary Receipts to be issued abroad: the new rule established criteria for such IOF/TVM levy, particularly for determining the IOF/TVM taxable basis. For public offerings, the taxable basis will be the price established under the book-building process or, if this is the case, the price determined by the offer under the public offering documents. If not under a public offering, the taxable basis shall be determined by multiplying the number of stocks transferred/assigned by its stock exchange closing quote on the date prior to the transaction or, if there is no trade on such date, by the last stock exchange closing quote available.

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