Clarification on Transfer Price Charged in Brasil

Carlos Antonio Da Silva Moura

Accountant, economist and lawyer post graduate degree in Tax Law from Fundação Getulio Vargas, Diamond Offshore Drilling Inc, Administrative Manager, Rio de Janeiro, Brasil

Accepted 15th October, 2015

In Brazil the Transfer Price, widespread as "Transfer Price" was regulated by Federal Law No. 9,430 / 96. Which provides for the federal tax law, contributions to social security, the administrative consultation process and other measures, including the general rules of the Transfer Price is emphasized in the research assignment to control prices between individuals or related legal and effective tax assessments in commercial or financial transactions. These operations are carried out between related parties based in different tax jurisdictions, particularly when one party is based in a tax haven or when the country's domestic law to determine secrecy to disclosure of information in connection with the corporate constitution of legal entities and to prevent the distribution disguised profit among companies in the same group.

Key words: Transfer Pricing, Legislation, Taxation, Ley N ° 9430/96.

INTRODUCTION

This work has the main goal to spread the rules of the transfer price used in Brazil and dictated by the Department of the Treasury Internal Revenue Service of Brazil since the publication of Law 9,430 / 96 in 1996 to the present day. Importantly, the transfer price system in Brazil is quite different from the basic rules applied in other countries as well as with the rules dictated by the Organization for Economic Cooperation and Development - OECD. As regards the OECD defines equal treatment to companies belonging to multinational groups and independent companies, so as to avoid tax advantages which the transfer price is based on the principle of arm's length, ie the one which would have been agreed between unrelated parties involved in the same transaction or similar transactions under the same conditions or similar market conditions in order to provide equal treatment to companies belonging to multinational groups and independent companies in order to avoid tributary benefits arising from economic power concentration .

The fiscal control of transfer price in Brazil is imposed due to the need to avoid the loss of tax revenue in the face of any artificial allocations of revenues and expenses in operations with sale of goods, rights or services, between people of different tax jurisdiction when there is a connection between them. Another aspect to consider would be the Covert distribution of profits that may occur through the apportionment of costs and expenses between companies of the same group when the appropriation of costs and expenses to be deducted from the taxable income of the Brazilian company. The analysis of cost-sharing contracts and expense, where the leader conducts expenses for the benefit of all or part of the other members of group companies through reimbursement of costs incurred. From the standpoint of the transfer price should be considered the circumstances in which the activities take place in view of the possible occurrence of activity that cannot justify that certain group company to cover costs when no private or do not require these services. The fact that certain services are intended only to one company of the group in the allotment of contract costs and expenses should be reflected in the cost allocation criteria, in order to observe the Principle of arm's length, considering that the contribution of each company should be consistent with the expected individual benefit or received effectively find inappropriate the Transfer Price outline the Brazilian tax system in relation to world economic order since the difficulties of pricing of intergroup exchanged values may lead states to redirect its collection , creating an uneven tax burden.

In Brazil, the main objective of the Brazilian Tax System regarding the practice of Transfer Pricing routines is to try to prevent the transfer of results of multinational companies operating in the Brazilian market to other countries, avoiding at all costs the invoicing of outgoing operations and overpricing in entry operations, seeking to nullify the possibility of the occurrence of assumptions that lead to Disguised Profit Distribution companies within the same group, associated or correlated in some way. The term 'transfer price' has been used to identify controls to which commercial and financial

Corresponding Author: lucidalv@yahoo.com.br
operations conducted between related parties headquartered in different tax jurisdictions, or when one of the parties is located in a tax haven. By reason of the peculiar circumstances that exist in the operations conducted between these two parties, the price charged in these operations may be artificially stipulated and, therefore, differ from the market price negotiated by independent companies in identical conditions - a price based on the arm's length principle. The transfer price fiscal control is imposed in keeping with the need to avoid the loss of fiscal revenues. This reduction is seen in face of the artificial allocation of revenues and expenditures in property, claims or services sale operations between two parties located in different tax jurisdictions, when a connection between them exists, and even if they are not connected to each other, but provided on of them is located in a tax haven - a favored taxation country or dependent state or whose internal legislation imposes secrecy on the disclosure of information regarding the make-up of or title to legal entities.

Several countries have been instituting this control as a safeguard measure for the fiscal interests, in view of the proven price manipulation by interdependent counties in international transactions, with the unmistakable purpose of enjoying more favorable tax system. Thus, the income transfer occurs from one State to another that offers lower rates or grant exemptions, by means of manipulating prices charged in the export and import of goods, services and claims.

They are required by the Brazilian law to observe the transfer price rules:

- Individuals or legal residing or based in Brazil that conduct operations with individuals or legal entities residing or based abroad and deemed connected even if by means of an intermediary.
- Individuals or legal entities residing or based in Brazil that conduct operations with any individual or legal entity, though not connected, either residing or based in a country that does not tax income or tax it at a rate below 20% (twenty percent), or whose internal legislation imposes secrecy regarding the make-up or or title to legal entities.

A company based abroad is considered to be under the following types of control:

- Common partnership when the same individual or legal entity, regardless of the location where he/she resides or is based, holds the title to partner's rights in each of the said companies, that permanently ensure him/her preponderance in those partnership discussions and the power to elect most of its administrators;
- Common administration, when:

b.1) The position of chairman of the board or chief executive officer of both is held by the same person;
b.2) The position of chairman of the board of one and of chief executive officer of another is held by the same person;
b.3) The same person holds a direction position with decision-making power in both companies.

In case of consortia or condominiums entered by the companies, they are deemed connected only during the term of association with the consortium or condominium. A country with favored taxation according to article 24 under Law # 9,430 of 1996 with the amendments introduced by articles 3 and 4 under Law # 10,451 of 2002 is a country or dependent state. 

- That does not tax income or tax it at a rate below 20% (twenty percent). The tax legislation of the said country must be considered, applicable to the individuals or legal entities according to the nature of the party with which the operation took place, and the taxation of labor and capital must be considered separately, as well as the dependent states of the country of residence or the head office.
- Whose internal legislation imposes secrecy on the make-up of or title to legal entities?

The concept of the favored taxation country must be applied to the taxpayer on an individual basis (Law # 9,430 of 1996, article 24 § 1 and Regulatory Instruction by the Brazilian Revenue Service (IN SRF) # 243, article 39 § 1). For the purpose of transfer price control, an intermediary is the party that liaises operations between connected parties (IN SRF # 243 of 2002, article 2 § 5); therefore the operations that a legal entity based in Brazil conducts with the intermediation of a trading company, whether it is based in Brazil or not, are subject to transfer price control. Note that the trading company, as a legal entity, that enjoys exclusivity as an agent, distributor or grantee for the purchase and sale of goods, services or rights is considered bound to the legal entity based in Brazil in the form of IN SRF # 243 of 2002, article 2, item IX). Likewise the trading company, as a legal entity based in Brazil, that enjoys exclusivity as an agent, distributor or grantee for the purchase and sale of goods, services or rights is considered bound to the legal entity based abroad in the form of IN SRF # 243 of 2002, article 2, item X).

The baseline price is the price ascertained by means of transfer price methods under the Brazilian legislation, which will be used as reference in the comparison with the price that was effectively applied by the company. If a difference arises, the taxpayer shall proceed as listed below:

**EXPORTATION**

When the baseline price ascertained by the exportation methods is higher than the export price charged, it means that the taxpayer acknowledged a lower revenue. Therefore the difference over and above the amount already allocated in the company's bookkeeping should be added to the net income to determine the taxable income and be included in determining the presumed or arbitrated profit and in the CSL (Social Contribution on Net Income) calculation basis. Up to the calendar year of 2001 it must be added to the net income for the exploration profit calculation (IN SRF # 32 of 2001, article 20). Starting in the calendar year of 2002 the portion to be added to the exploration profit should be included in the amount of respective revenues, whether enjoying a tax benefit or not (IN SRF 243 of 2002, article 21, paragraph).

**IMPORTATION**

When the parameter price ascertained by the importation methods is lower than the import price charged, it means that the taxpayer acknowledged an amount as cost or expense higher than what it should have been and therefore this difference should be taxed. Up to the calendar year of 2001 the amount corresponding to the excess cost or expense and included in the company's net income must be added to the taxable income and to the CSL calculation basis (IN SRF # 32 of 2001, article 5, item I).

Starting in calendar year of 2002, pursuant to the provision in article 45, Law # 10,637, 2002 and paragraphs 1 to 4 under article 5, IN SRF # 243 of 2002, in case an excess
cost is ascertained in the acquisition of goods, rights and services imported from connected companies and it is considered non-deductible in the determination of the actual profit or calculation basis for the social contribution on net income assessed in the form of article 18, Law # 9,430 of 1996, upon the end of the assessment period the legal entity should adjust the excess cost determined by one of the methods provided in the legislation accounting-wise by means of a debit entry in accrued net income account and credit to:

- The asset account where the goods, rights or services acquisition was entered and that remains recorded there at the end of the assessment period; or
- A proper cost or expense account for the assessment period that records the amount of the goods, rights or services in case these assets have already been written off the assets account where their acquisition was recorded.

In case of goods classifiable in permanent assets that have generated depreciation, amortization or depletion quotas in the calendar year of the importation, the excess acquisition price amount in the importation should be credited to the assets account where their quotas have been charged as a counterpart to the accrued income account. In case the legal entity opts to add, in determining the actual profit and the social contribution on net income calculation basis, the excess amount assessed in each assessment period only upon the sale or write-off for whatever reason of the good, right or service acquired, the total excess amount assessed in the acquisition period should be excluded from the net worth for the purpose of determining the calculation basis for the interest on the company's own capital addressed by article 9, Law # 9,249 of 1995. In this hypothesis the legal entity should record the total amount of the excess acquisition price in a subsidiary of that account in which the good, service or right acquired abroad is recorded.

The operations listed below are subject to transfer price control when conducted with individuals or legal entities residing or based abroad and deemed connected, including those performed through a middle party, or yet if not connected but residing or based in a country or dependent state considered a tax haven:

- The importations of goods, services and rights;
- The exportations of goods, services and rights;
- or interests paid or credited in financial operations when arising from a contract not registered at the Central Bank of Brazil;
- or interests earned in financial operations when arising from a contract not registered at the Central Bank of Brazil;

These are methods established by law, for the purpose of ensuring that the prices considered to assess the taxable income, whether presumed or arbitrated, and the calculation basis for the social contribution on net income are as close to market prices as possible. Each of the methods has its respective readjustment, whose objective is to allow the comparison between the prices by which identical or similar goods, services and rights are sold/bought, even when traded under different conditions. Therefore the Compared Independent Prices Method (PIC);

- Resale Price Less Profit Method (PRL Resale), with a 20% (twenty percent) profit margin;
- Resale Price Less Profit Method (PRL Production), with a 60% (sixty percent) profit margin;
- Production Cost Plus Profit Method (CPL), with a 20% (twenty percent) profit margin.

In exportation

- Export Sale Price Method (PVEx):
- Wholesale Price in the Country of Destination Less Profit Method (PVA), with a 15% (fifteen percent) profit margin;
- Retail Price in the Country of Destination Less Profit Method (PVV), with a 30% (thirty percent) profit margin;
- Acquisition or Production Cost Plus Tax and Profit Method (CAP), with a 15% (fifteen percent) profit margin.

For interests arising from a loan not registered at the Central Bank of Brazil: LIBOR rate for deposits in U.S. dollars for a six-month term, plus three percent per annum as a spread, pro-rated in keeping with the period to which the interests refer. Cost or price charged by the company is the weighted arithmetic average of the prices for which the company bought or sold a particular product during the calendar year. It must be calculated product by product. Average calculated cost or price, or baseline price, is the weighted arithmetic average of prices charged in operations between independent companies collected and adjusted according to a method defined in law, chosen by the taxpayer. It must also be calculated product by product. The annual period ending on December 31 shall also be considered (even though the company ascertains the taxable income on a quarterly basis) or the period between the beginning of the calendar year and the activities closing date. Consequently the eventual adjustment shall be made on December 31 or on the activities closing date, except in case of suspected fraud.

As defined in the DIPJ 2003 completion instructions, a good, services or rights import or export operation shall comprise the ensemble of transactions of the same nature. It is understood as ‘same nature’ the transactions whose traded goods, services or rights have the same specifications in the DIPJ ‘Description’ field. This field is completed with the description of each group of transactions in order to allow its perfect identification, including with information related to make, type, model, kind, etc. Let it be emphasized that only one classification exists per Common Mercosur Nomenclature (NCM) for operations with goods. The goods, services or rights import or export operations must be grouped by identical products. Similar products may be included, provided the similarity adjustments provided in article 10, article 13 § 6 and in article 17 under IN SRF # 243 of 2002. Eventual exchange variations occurring in the same base period cannot be adjusted, since the exchange variation equally influences the baseline price and the price charged. Taking into account that in order to calculate the price changed in the import or export operation all operations performed during the calendar year must be considered, if the calculation of the baseline price the operations performed by the independent companies, that occurred along the same calendar year are also considered, the exchange variation shall have influenced both prices to be compared the same way.
On the other hand, the exchange adjustments arising from the comparison with operations performed during periods before and after must be made according to the provisions in articles 11 and 18 under IN SRF #243 of 2002. When it is possible to identify the dates when the operations took place, the exchange rate for the respective dates must be used, as shown in the two previous questions. If it is not possible, use the average exchange rate for the calendar year disclosed by the Federal Revenue. For example, in applying the PIC - Compared Independent Prices method, if utilized in goods importation operations performed by independent companies (under IN SRF # 243 of 2002, article 8, paragraph, item III), the sell exchange rate for the second business day immediately preceding the goods importation declaration registration date must be used. If the CPL - Production Cost Plus Profit method is utilized to ascertain the baseline price, considering that the make-up amounts were formed along with the calendar year, the average exchange rate for the year must be used. To ascertain the baseline price based on the PVA - Wholesale price, in the Country of Destination method, the exchange rate for the dates the respective sales took place must be used. Brazil is not a country member of OCDE. Therefore the methods to be applied are limited to those provided in the Brazilian legislation. The agreements signed by Brazil to prevent double taxation do not provide for the utilization of transfer price methods. The percentages addressed by the PRL (20% and 60% margins), CPL, PVA, PVV and CAP methods and the provision in article under IN SRF # 243 of 2002 may be officially amended or in compliance to a class entity request or the party concerned itself. The requests shall be made according to the rules applicable to consultation proceedings (IN SRF # 2 of 1997) and shall contain schedules and documents enclosed to support the plea (IN SR # 243 of 2002, articles 32 and 34; and Administrative Rule MF # 95 of 1997).

For the purposes of analyzing the subject matter, it is understood as 'operation' the ensemble of transactions of a particular good, service or right performed along a calendar year. In this hypothesis the price readjustments should be performed operation by operation for the same good, service or right considered, and the offset of the prices considered is not allowed if the operation involves different goods, services or rights (IN SRF # 243 of 2002, article 5, § 5 , and article 20, paragraph). The legislation does not establish a legal price and cost sampling concept. Considering that in order to calculate the price charged in the import or export operations all operations performed in the calendar year must be considered, if all the operations performed by independent companies taking place along the same calendar year are also considered, the sample shall be consistent, thereby preventing eventual distortions in relation to the exchange variation occurring in the period and facilitating the growing conviction regarding the prices by the Tax Auditors in charge of the verification. The rules on transfer prices do not apply in case of royalties and technical, scientific, administrative assistance and alike, mentioned in articles 352 to 355 under RIR/1999, in compliance with the definitions under article 22, Law # 4.506 of 1964 (IN SRF # 243 of 2002, article43).

The performance of maintenance services, services that do not involve technology or process transfer, as well as the revenues received by the author or creator of the good or work (copyrights) are subject to transfer price adjustments. The following operations are subjected to baseline price ascertainment:

- Those performed by related parties, even if performed by means of intermediaries, residents or based abroad;
- Those performed by connected parties or not, residing or based in a country or dependent state with favored taxation, or whose internal legislation imposes secrecy on the make-up of legal entities or title thereto.

Whenever possible the comparison should be itemized, considering that similar products may be classified under the same NCM for comparison purposes; for comparison purposes, when similar products are used, the similarity adjustment should be performed in the terms of article 10 under IN SRF # 243 of 2002. On one hand, let it be stressed that the NCM classification only exists for goods, but in case of services and rights the comparison with similar ones may also be done, provided that the proper adjustments are made in the terms of the aforementioned article. The weighted arithmetic average of the prices charged to unconnected parties must be calculated according to the provisions in article 6 under IN SRF # 243 of 2002. The weighted arithmetic average of the price to be compared with the one charged and entered in the income account shall be determined as follows: The prices obtained will be multiplied by the quantities regarding the respective operation and the ascertained income will be added and divided by the total quantity. § 3 under article 13 of IN SRF # 243 of 2002 allows the utilization of data regarding the producing units of other companies located in the country of origin of the good, service or right, in cases in which they are not necessarily their suppliers. Therefore the CPL may be also applied in this case, provided the other producing unit authorizes the opening of cost data.

The production cost must be ascertained in compliance with the generally accepted accounting principles and pursuant to the provisions in the Brazilian legislation, provided it falls in the situations established in § 4, article 13 under IN SRF #243 of 2002. If the legal entity does not have information on freight and insurance itemized byproduct, it is possible to pro-rate it by product according to the methodology used in the company's cost accounting. The excess price paid in the importations, subject to transfer price control, should only be taken into account in the IRPJ (corporate income tax) and CSLL calculation bases when the corresponding goods were entered as costs. However the amount resulting from the excess cost, expenses or burdens, which is considered nondeductible in determining the taxable income and the CSLL calculation basis, shall be adjusted accounting-wise by entering it as a debit in the net worth accrued income account and credit to:

- The asset account where the goods, rights or services acquisition was entered and that remains recorded there at the end of the assessment period; or
- A proper cost or expense account for the assessment period that records the amount of the goods, rights or services in case they have already been written off the assets account where their acquisition was recorded.

In case the legal entity opts to add, in determining the actual profit and the CSLL calculation basis, the excess amount assessed in each assessment period only, upon the sale or write-off for whatever reason, of the good, right or service acquired, the total excess amount assessed in the acquisition period should be excluded from the net worth for the purpose of determining the calculation basis for the interest on the company's own capital addressed by article 9, Law # 9,249 of.

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1995. In this hypothesis the legal entity should record the total amount of the excess acquisition price in a subsidiary of that account in which the good, service or right acquired abroad is recorded (IN SRF # 243 of 2002, article 5). In order to convert the foreign market price amounts to the national currency, the exchange rate for that currency, corresponding to the second business day immediately before the goods import declaration registration submitted to consumption order must be used (IN SRF #243 of 2002, article 7, line 1, with the wording provided by IN SRF #321 of 2003, article 1). Provided that the importation of the good does not imply costs or expenses that may be deductible from taxable income and CSLL taxation purposes. Let it be stressed that the mandatory return of the good must be observed, as previously established, and its utilization for other purposes other than what was initially adjusted between the parties is not allowed.

In case of importation of identical goods, services and rights, only adjustments related to the following shall be allowed to be made:

- Payment term;
- Traded quantities;
- Warranty requirement of the good operation, or service or right applicability;
- Requirement of public promotion of the good, service or right by means of advertisement and publicity;
- Requirement of quality, services standard and cleanliness, condition inspection costs;
- Intermediation costs in the purchase and sale operations conducted by unconnected companies, considered for price comparison purpose;
- Packing;
- Freight and insurance. (IN SRF #243 of 2002, article 9).

The gross income make-up does not include non-cumulative taxes (such as IPI - excise tax) charged from the buyer or contractor, of which the seller of the goods or service provider are merely trustees. Non-cumulative tax is where the tax amount charged in previous operations is deducted at each operation. Likewise the IPI must not be included in the goods and raw materials acquisition cost, which will be recovered in a sales operation later. Therefore, in ascertaining the baseline price - based on the Resale Price Less Profit (PRL) Method with a 20% (twenty-percent) profit margin - the IPI is not included upon the goods outflow because they are not part of the Gross Income. Thus, when comparing the baseline price with the price charged on the importation, the IPI must be excluded from the acquisition price. The statement must comply with all provisions established in article 13, IN SRF # 243 of 2002.

The proper documents to support the production costs of imported goods and services may be copies of the documents that were the basis of the records entered in the accounting books, such as acquisition commercial invoices for raw materials and other goods or services used in the production, labor cost pro-ration spreadsheets and copies of payrolls, proof of costs of rent, maintenance and repair of the equipment used in the production, utilized percentage statements for depreciation, amortization and depletion and burdens, and for allocated breakages and losses, in compliance with the provision under § 4, article 13, IN SRF # 243 of 2002 A copy of the income tax statement submitted to the federal revenue of the other country, equivalent to DIPJ in Brazil must also be presented. We clarify that any document from abroad must be translated to the national language in order to have legal effects in Brazil and be enforceable before third parties or in Federal, State, Federal District, Territory and Municipal Offices or in any jurisdiction, court or tribunal. In addition, it must be legalized in its country of origin, that is, notarized, consularized and recorded at the Title and Document Recording Office (Law # 10,406 of 2002, article 224 under the New civil Code, Code of Civil Procedure, articles 129 and 148; Law # 6,015 of 1973; and PN CST # 250 of 1971).

As a rule of thumb an evaluation should be performed according to the transfer price method. As subsidy item II under article 21, Law # 9,430 of 1996 provides for the possibility of using researches done by a technically acknowledged price verification company or institution. Documents normally issued by companies in purchase operations are also considered. Packing or re-packing does not imply the production of another good, service or right. The same method must be used for each identical or similar good, service or right, regardless of the country subject of the transaction. Provided that the importation has been done by a connected party, even if by means of an intermediary or a party domiciled in a country or dependent state with favored taxation, or whose internal legislation imposes secrecy regarding the company make-up or title thereto. Any goods importation operation performed by a connected party domiciled abroad, with a party residing or domiciled in a country or territory with favored taxation, or whose internal legislation imposes secrecy regarding the company make-up or title thereto, or by means of an intermediary must be subjected to the price transfer legislation.

The deductibility of the expenses arising from Cost Sharing contracts, even if signed between connected parties in regard to Research and Development cost sharing, that fall within the royalties and technical assistance, scientific, administrative or akin concepts, in the terms of article 22 under Law 4,506 of 1964, and that involve technology transfer operations are not subjected to transfer price control. Such operations are subject to the limits established in articles 352 to 355 under RIR/1999, to income tax withholding of the amount paid, delivered or remitted in the terms of articles 708 and 710, under RIR/1999 and the Economy Domain Intervention Contribution (Cide), in the terms of Law # 10,168 of 2000. (Law # 9.430 of 1996, article 18, § 9 and IN SRF # 243 of 2002, article 43).

The paragraph under article 8 under IN SRF # 243 of 2002 establishes that, for the baseline price calculation based on the PIC method, only the prices of identical or similar goods, services or rights shall be considered, without any priority order:

- Sold to the same export company to unconnected resident or non-resident legal entities;
- Bought by the same import company from unconnected resident or non-resident legal entities;
- In purchase and sale operations performed between other unconnected resident or non-resident legal entities.

First of all it must be ascertained if the service performance in Brazil implied a technology transfer. In the hypothesis the technology transfer is proved and consented by the National Institute of Industrial Property (INPI), the transaction would not be subject to the transfer price rules as established by article 43 under IN SRF # 243 of 2002. In this hypothesis the deductibility of such expenses are subject to the limits established by articles 352 to 355 under RIR/1999. If a technology transfer does not exist, these services become
subject to the transfer price rules (Law # 9,430 of 1996 and IN SRF # 243 of 2002). The PRL method with a sixty percent margin shall be utilized in the case of imported goods, services or rights applied to production. In this hypothesis the baseline price of the imported goods, services or rights shall be ascertained by excluding the value added in Brazil and 60% (sixty percent) profit margin according to the following methodology:

- **Net sale price**: The weighted arithmetic average of the sale prices of the goods produced, less the unconditional discounts granted, taxes and contributions on the sales and commissions and brokerages paid;
- **The participation percentage of the imported goods, services and rights in the total cost of the produced good**: The percentage ratio between the value of the imported good, service or right and the total cost of the good produced, calculated according to the company cost spreadsheet;
- **Participation of the imported goods, services and rights in the sale price of the produced good**: The application of the percentage participation of the imported good, service or right in the total cost, ascertained according to item 'b', on the net sale price calculated according to item 'a';
- **Profit margin**: The application of a rate of 60% (sixty-percent) on the participation of the imported good, service or right in the sale price of the produced good, calculated according to item 'c';
- **Baseline price**: The difference between the participation of the imported good, service or right in the sale price of the produced good, calculated according to 'c', and the 60% (sixty percent) profit margin, calculated according to item '4'.

The expression 'consistently per good' is considered as the impediment of using more than one method in the event the good has the same specifications. This consistency is not required if the specifications are different. In order to find the baseline price for a vehicle make X, 2.0, 4 doors, and one method may be utilized; for a vehicle with the same specifications, but 2 doors, another method may be utilized. The term 'arbitration' contained in article 14, IN SRF # 243 of 2002 conveys the obligatory submission of the revenues earned in export operations - subject to transfer price control - to the baseline price calculation according to the methods established by the transfer price legislation. Article 14 under IN SRF # 243 of 2002, provides for the utilization of prices charged on the sale of identical or similar goods, services and rights in the Brazilian market during the same period and under similar payment conditions, which should be subject to the similarity adjustments provided in article 17 under IN SRF # 243 of 2002.

The methods must be consistently applied per good, service or right, and the utilization of more than one method in determining the baseline price for the same good, service or right is not admitted.

Export operations are not subject to transfer price control when:

- The legal entity proves having ascertained a net income, before the social contribution on net income and income tax, arising from sale revenues from exports to connected companies, amounting to the equivalent to at least 5% (five percent) of those total revenues (IN SFR # 243 of 2002, article 35);
- The net export revenue does not exceed 5% (five percent) of the total net revenue in the same period. (IN SRF #243 of 2002, article 36);
- The average sale price of the exported goods, services or rights during the respective income tax calculation basis determination period is equal or greater than ninety percent of the average price charged on the sale of the same goods, services and rights in the Brazilian market, during the same period and under similar payment conditions (IN SRF #243 of 2002, article 14);
- The exports to a connected company aim at a market share increase in another country for the goods, services and rights produced in Brazilian territory, provided the conditions established in article 30 under IN SRF # 243 of 2002 are observed.

**NOTE:**

Let it be clarified that the acknowledgment revenue amounts based on the price charged in hypotheses 1 and 2 do not imply final acceptance, and it may be rejected - if improper - in an official proceeding by the Federal Revenue Secretariat (IN SRF # 243 of 2002, article 37, item I). In the calculation of the 5% (five percent) rate in the hypothesis in item 'a', the goods, services and rights sales operations, whose profit margins in the export methods provided in articles 24, 25 and 26 under IN SRF #243 of 2002 that have been amended by determination of the Ministry of Finance in terms of articles 32, 33 and 34 under IN SRF #243 of 2002 may be excluded. (IN SRF #243 of 2002, article 35, with the wording provided in IN SRF #321 of 2003, article 1). The benefits of hypotheses 1, 2 e 4 do not apply to sales made to connected companies established in countries with favored taxation or whose legislation imposes secrecy, as defined in article 39 under IN SRF #243 of 2002 (IN SRF #243 of 2002, article 37, item I, and article 30, § 4).

The Brazilian legislation on transfer prices allows the free choice of method. There is no restriction to applying the PVEK, PVA and PVV methods provided the conditions stipulated for the utilization of each method are observed. If other methods provided in the legislation cannot be applied for lack of a market that charges independent prices, which allows the evaluation of consistent prices, the utilization of the CAP method would be recommended in these cases. The statement segregating the operations performed with connected companies must contain the information required to determine the export price charged. Likewise the statement with the sales operations performed with independent companies must contain the information required to ascertain the baseline price, according to appropriate adjustments to the chosen method. In regard to the supporting documents, copies of the Export Declarations, Export Records, outflow invoices, commercial invoices and other documents proving the operations and prices effected, as well as the covenanted contracts. However, let it be stressed that in lack of evidence deemed sufficient or useful, the Federal Revenue may order other documents be presented, and apply one of the methods described in the legislation in effect, pursuant to the provisions in the paragraph under article 40, IN SRF # 243 of 2002. Obtaining proof of the price charged in the wholesale and retail market is paramount.

It should be conveniently reminded that according to the PVA Method the export sales revenue may be determined, based on the arithmetic average of identical or similar good sales prices charged in the wholesale market in the country of destination (IN SRF #243 of 2002, article 24); and based on
the identical or similar goods sale prices charged in the retail market in the country of destination, in case of ascertainment according to the PVV Method (IN SRF #243 of 2002, article 25). The 'country of destination' is to be considered the final destination of the good. Company’s equity are the rights recorded in the company's Assets. Therefore, its sale to a connected party in the terms of article 2, IN SRF # 243 of 2002 or to a party residing or domiciled in a country or dependent state with favored taxation or whose internal legislation imposes secrecy on company equity, as defined in article 39, IN SRF # 243 of 2002, shall be subject to the transfer price rules. Articles 35 and 36 under IN SRF # 243 of 2002, which address the exemption of proof, contemplate export operations only. In addition, the discrepancy margin of up to 5% (five percent) allowed by the SRF, both in exports and in imports, assumes the price calculation adjusted by the transfer price rules and its subsequent comparison with import and export documents, which is a collation not provided in the mentioned articles.

The conditions established in article 30, IN SRF # 243 of 2002 must be observed in full. The fact that a company has its products subordinated to minimum prices control by Secex does not eliminate its responsibility regarding the compliance with the transfer price tax legislation. Therefore, if the operation is performed with a connected party by means of an intermediary or is intended for a country or dependent state with favored taxation or whose internal legislation imposes company equity secrecy, as defined in article 39, IN SRF # 243 of 2002, the company must comply with the provision in articles 19 to 24; Law # 9,430 of 1996; and PN CST # 243 of 2002. The financial burden included in term sales may be adjusted in order to minimize the effects caused on the prices to be compared, as provided in §§ 1 and 2 under article 15, IN SRF # 243 of 2002. It is hereby clarified that the interests earned in operations performed with connected companies, or those established in a country or dependent state with favored taxation or whose internal legislation imposes secrecy regarding the company make-up or title thereto, are subject to the limit established in § 1 under article 27, IN SRF #243 of 2002. Finally, we clarify that Regulatory Instruction # 1395 of September 13, 2013 amends Regulatory Instruction RFB # 1,312 of December 28, 2012 that provides for the prices to be charged on goods, services and rights purchase and sale operations performed by an individual or legal entity residing or domiciled in Brazil with an individual or legal entity residing or domiciled abroad and deemed connected. Yet Law # 12,715 that provides for the prices to be charged by companies in import and export operations with head offices, branch offices or subsidiaries abroad or other companies when headquartered in fiscal havens is very strict.

The main objective of 'Transfer Pricing' in Brazil is to prevent a fraudulent transfer of profits to connected companies abroad, by means of goods, services and rights import and export operations, in addition to interest paid or received between companies. In relation to the operations performed with connected companies located abroad, the legislation establishes maximum prices in import operations and minimum prices in goods, services and rights export operations.

REFERENCES


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