



International Tax

Brazil Tax Alert

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New position adopted on tax treatment of payments for technical services without transfer of technology

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Brazil's National Treasury Attorney's Office (PGFN) recently issued a significant opinion (PGFN/CAT No. 2,363/2013), in which it revisited the tax authorities' long-standing position on the interpretation of the business profits article in Brazil's tax treaties with respect to payments made abroad for services that do not involve an accompanying transfer of technology.

According to guidance issued in 2000 and 2011 (Declaratory Act COSIT 1/2000 (ADE 1/2000) and PGFN/CAT/No 776/2011, respectively), income paid for the provision of such technical services should be treated as "other income," rather than business profits under Brazil's tax treaties when the entity providing the services does not carry on business in the other contracting state through a permanent establishment situated therein. (Unlike the OECD model treaty, the other income article of Brazil's tax treaties allows both contracting states to tax the income.) As a result, such income would be subject to withholding tax at source.

The PGFN opinion was issued in response to a potential threat by the Finnish government to terminate the existing Brazil-Finland tax treaty if Brazil were to seek to exert taxing rights with respect to payments made by a Brazilian resident taxpayer for technical services rendered in Finland by a Finnish company. The opinion adopts a change in the government's interpretation and acknowledges that remittances abroad for technical services *without* an accompanying transfer of technology should fall within the scope of the business profits article of a treaty and, therefore, will not be subject to withholding tax.

The opinion provides as follows:

- The general tax treaty rule is that payments made abroad for technical services and technical assistance without an accompanying transfer of technology are treated as business profits, as they constitute a component of the profits of the foreign enterprise providing the services;
- If a treaty specifically allocates taxing rights to Brazil with respect to payments made abroad for technical services and technical assistance, such payments will be subject to the treatment in the royalties article;
- If a treaty allocates taxing rights to Brazil with respect to payments made

abroad for technical services and technical assistance rendered by an individual, such payments will be subject to the treatment in the independent personal services, where there is specific provision related to those technical activities; and

- The opinion will apply only in the context of a tax treaty.

This conclusion is consistent with decisions issued by Brazil's regional federal courts, as well as the Superior Court of Justice, all of which have ruled that the business profits article prevails over domestic legislation with respect to payments made for technical services that do not involve a transfer of technology.

The PGFN has recommended that the tax authorities revoke the 2011 guidance, which may indicate that the 2000 guidance also may be revoked.

Conclusion

The PGFN opinion represents a major shift away from the position on the taxation of outbound payments for technical services that the Brazilian tax authorities have held for 14 years. The opinion indicates that the business profits article generally should apply to such payments where there is no accompanying transfer of technology. Although the PGFN opinion is nonbinding, it is a strong indication that the tax authorities will issue new measures to reflect the interpretations in the opinion.

Affected taxpayers should monitor the possible issuance of new rules in line with the PGFN opinion and re-examine their outbound tax burden remittances involving technical services and technical assistance, taking into account the specific fact patterns at issue.

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