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Brazil and OECD present the main features of the proposed new transfer pricing system in Brazil

At a joint event held on 12 April 2022 in Brasília, the Organization for Economic Cooperation and Development ("OECD") and the Brazilian Federal Revenue Service ("RFB") presented the key features of Brazil's proposed new transfer pricing ("TP") system. The proposed changes are the outcome of a joint project launched in February 2018 between OECD and RFB, in which the TP framework currently in place in Brazil was assessed as compared to the international consensus on transfer pricing (represented by the OECD TP Guidelines) and where a number of gaps and divergences were identified.

During the opening ceremony, Paulo Guedes – Brazil's Finance Minister – noted that the convergence of the Brazilian TP system with the international standard is not only an essential step towards Brazil's acceptance as an OECD member, but also a key measure to avoid double taxation, on the one hand, and to prevent tax evasion through profit shifting, on the other. In addition, Pascal Saint-Amans – Director of the OECD Centre for Tax Policy and Administration – emphasized that the alignment of the Brazilian TP legislation with the OECD TP framework is a transformational change that will support Brazil's development objectives and facilitate a smooth implementation of the Two-Pillar Solution to address the tax challenges of the digitalization of the economy, with significant revenue potential for Brazil.

Although the draft of the new Brazilian TP legislation is yet to be published for public consultation, general features and technical aspects that can be expected in the new TP system were presented by Brazil's General Coordinator of Taxation and representatives of the OECD's Center for Tax Policy and Administration at the event held on 12 April 2022. As anticipated, the core of the new Brazilian regulatory framework will be the incorporation of the arm's length principle, in line with the OECD TP Guidelines.

After being made available for public consultation and after the collection of comments and suggestions from different sectors of the economy, the expectation is that the bill will be officially presented to the Brazilian Congress for voting and approval. The highlights discussed at the meeting are summarized below.

Highlights

Among the most decisive topics discussed at the meeting is that the new legislation will give the taxpayer the possibility of applying all the TP methods currently recognized and accepted by the OECD TP Guidelines, including the transactional profit methods (i.e., transactional net margin method and profit split method), which currently have no parallel in the Brazilian regulation. Furthermore, the choice of method will follow the criterion of the most appropriate method, which is contrary to the current rule, under which the taxpayers may choose the method that brings the smallest possible adjustment.

A full comparability analysis will also be a key part of the new legislation, considering that such analysis is very limited in the current Brazilian TP rules. Another highly expected change by taxpayers concerns TP adjustments, as the current Brazilian rules do not foresee the possibility of end-of-year adjustments and the issuance of debit and credit notes to correct eventual distortions in the transfer prices. In this regard, different approaches regarding possible adjustments are envisaged by the new TP legislation.

As for documentation requirements, Brazilian taxpayers will be required to prepare TP documentation in accordance with the OECD TP Guidelines, such as the master file and the local file, in addition to the country-by-country report, the latter being already present in the current rules. Moreover, with the aim of simplifying and optimizing legal certainty, Brazilian tax authorities contemplate the possibility of entering into Advance Pricing Agreements ("APAs").

Other expected changes
Several other topics were prominent at the event held on 12 April 2022. This is the case, for example, of transactions involving intangibles. It is foreseen that the rules currently in force will be reformulated, not only to redefine the term "intangibles" in accordance with internationally accepted standards, but also to introduce the DEMPE concept (development, improvement, maintenance, protection, and exploitation of intangibles), which will be adopted as a basis for the valuation of intangibles (also for situations involving hard-to-value intangibles) and the definition of its allocation.

Another discussed topic was the pricing of intragroup services. As the current Brazilian rules aim at the valuation of goods, adaptations are commonly necessary for the valuation of transactions involving services. Therefore, the new Brazilian TP framework is expected to provide for specific rules regarding the pricing of services in general, as well as those with low added value, with the introduction of rules to simplify the evaluation of such transactions.

Further, the TP aspects of cost sharing agreements also pose a challenge due to the lack of regulation and potential conflicts with certain rules on the deductibility of expenses for Brazilian income tax purposes and ramifications in the tax laws. Thus, the new legislation should include contracts for the development of intangibles and services related to the provision of services, highlighting guidelines regarding compensation, participation rules, and definitions of an entity's attributions.

In addition, new regulation will be implemented in relation to the transfer pricing consequences of business restructuring, a subject which is not yet addressed by the Brazilian regulatory framework.

Finally, great expectations are placed on new rules for financial transactions. The current Brazilian legislation either does not allow for any assessments or rely on complex adjustments to calculation methods to enable analysis. Likewise, there is no regulation concerning cash pooling arrangements and intragroup guarantees. Not only new TP rules are awaited, but also general deductibility rules. The main issues concern the extent of financial operations covered and the need for changes in existing regulatory rules depending on the transaction under analysis.

Conclusion
Changes to the Brazilian legislation in relation to transfer pricing is not a matter of “if" but is rather a question of “when" they will occur. The latest discussions between the OECD and the Brazil's General Coordinator of Taxation have produced a strong momentum that is expected to ultimately result in changes to the Brazilian transfer pricing regulations in the near future. In an effort to anticipate these changes, taxpayers should already start brainstorming to determine how any potential changes to the Brazilian transfer pricing regulations might affect their existing transfer pricing policies and transfer pricing models in relation to their Brazilian subsidiaries. Deloitte Germany's Transfer Pricing team has set-up a *Brazilian Desk* which helps clients navigate through these expected changes by informing companies of the latest developments in the legislation process and offers specialized workshops to help companies identify key areas that might be affected by the proposed changes. Please contact our *Brazilian Desk* for any support needed.

References
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For a background of the OECD-RFB joint project, see: “Brazilian milestones towards convergence with the OECD Transfer Pricing standard", Deloitte Tax-News