TAX

ENACTMENT OF LAW NO. 7,988/18 RJ - DISREGARD OF LEGAL ACTS AND DEALS BY THE RIO DE JANEIRO STATE REVENUE OFFICE

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State Law No. 7,988/18 - RJ, published on June 15, revoked Article 75-A of Law No. 2,657/96 (the ICMS Law) in order to establish new rules regarding the procedures that the tax auditor of the Rio de Janeiro state revenue office must observe in order to disregard legal acts or transactions carried out for the purpose of concealing the occurrence of a taxable event or the nature of the elements giving rise to a tax obligation.

The attempt was to implement new elements to allow the application of article 116, sole paragraph of the National Tax Code, a controversial provision known as the "anti-avoidance clause". It would give power to the tax authorities to draw up tax assessments, levies, and penalties for the taxpayer, even in situations where the occurrence of a taxable event is not clearly found, on the grounds that, through subterfuge, its occurrence had been disguised.

Legal scholarship severely criticizes the validity of these provisions in the Brazilian tax law precisely because there is a conflict between this article and the principles and guarantees of the taxpayer, such as the principle of legality, the prohibition on taxation by analogy, and legal certainty.

There is also a certain consensus that this is a rule of limited effectiveness, because it depends on regulations by law. As no federal law has been issued regulating the application of the anti-avoidance clause, the federal tax authority avoids using it as a legal basis in assessments, even though it may sometimes rely on it as grounds for lack of a business purpose, abuse of form, or lack of substance.

With the enactment of State Law No. 7,988/18, the State of Rio de Janeiro seeks to remedy this lack of regulations in order to enable the application of the sole paragraph of article 116 of the National Tax Code.

The law establishes that the act of disregard will be done by drawing up an infraction notice, which must be based on the elements or facts that demonstrated the concealment, as well as the acts or deal to be taxed, therein indicating the respective standards applicable. Therefore, prior to the issuance of the infraction notice, the tax auditor should:

1. Subpoena the taxpayer to provide clarifications and information within 30 days about the facts, causes, reasons, and circumstances that led to the undertaking of the legal act or deal with "indicia" of concealment (failure to comply with the subpoena or the presentation of incomplete information or clarification will result in disregard);

1. If the clarifications are not enough, or do not convince the tax authority, an infraction notice will be drawn up and administrative litigation regarding the infraction notice will follow, with right to an adversarial proceeding and full defense.

It should be noted that there is no definition in the rule of what is meant by "act or deal undertaken for the purpose of concealing the occurrence of the triggering event." This opens a wide margin of discretion so for the state tax authority to assign to certain situations a finding of concealment, even those in which a taxable event does not occur.

An attempt has already been made to create a federal law to regulate the application of an anti-avoidance clause by Presidential Decree No. 66/02. In this case, the Presidential Decree brought in even more elements regarding the concepts to be used in disregarding the legal act or deal, therein expressly mentioning the lack of a business purpose and abuse of form, and assigning their respective meanings in the legal text itself. The rule also required that the tax assessment be accompanied by evidence gathered by the auditor. Even so, these provisions were broadly rejected and ended up not being part of the text of the law that resulted from the conversion of the Presidential Decree.

Another attempt was made at the federal level with the enactment of Presidential Decree No. 685/15. It provided that the taxpayer would be required to make a prior annual declaration to the Federal Revenue Service of legal acts or deals (i) that had no relevant non-tax reason; and (ii) whose adopted form was not usual, was an indirect legal deal, or had a contractual provision that was not typical for contracts. These statements would be submitted as consultations to the Federal Revenue Service, which would express its opinion on the validity of the acts and possible disregard of them. Again, these provisions have not been converted into law.

Therefore, taxpayers in the State of Rio de Janeiro should be attentive, since the enacctment of Law No. 7,988/18 is inserted into a context of various legal controversies, which brings in uncertainty regarding its application by the tax authorities and uncertainty as to the position that will be adopted in any discussion in administrative and judicial courts.

The enactment of the law conveys the message that the state revenue service intends to use this type of anti-

avoidance argument more frequently in order to prepare new tax assessments, which will certainly require even greater attention from taxpayers who intend to show that the tax assessment is unfounded.