

Considerations on the Double Tax Treaty executed between Brazil and Switzerland

On 1 January 2022, the new treaty to avoid double taxation between Brazil and Switzerland (“DTT”) entered into force.

Considering that Brazil is Switzerland's most important trade partner in Latin America¹, the DTT will certainly contribute to the further development of bilateral economic and trade relations. It does not only seek avoiding double taxation between Brazil and Switzerland, but also, more generally speaking, increases legal security for companies and individuals doing business in both countries.

The DTT only applies to persons resident in Brazil, Switzerland or in both countries (with tie-breaker rules in the latter case). The DTT provides for restrictions on tax transparent entities that would otherwise unduly benefit from its provisions.

The taxes covered by the DTT are both Brazilian and Swiss income taxes, including also Brazilian Social Contribution on Profits (CSLL) and Swiss cantonal and communal income taxes.

One of the main benefits of the DTT is the reduction of the Brazilian withholding income tax (“WHT”) rates in the following cases:

Payment of Royalties

- In case a Brazilian taxpayer were to pay royalties to a Swiss resident person, the DTT reduces the Brazilian WHT from 15% to 10%, except when the remittance relates to royalties for the use (or right to use) of industrial or commercial trademarks, in which case the standard rate of 15% remains applicable.

Payment for Technical Services

- In case a Brazilian taxpayer were to pay a fee to a Swiss resident person in consideration for consulting, technical or management services, the DTT reduces the Brazilian WHT from 15% to 10%. Technical services are defined as services which (i) depend on specialized technical knowledge; or (ii) involve administrative assistance; or (iii) involve consulting; or (iv) result from automated structures with clear technological content; all provided by independent contractors or employees.

Payment for Non-Technical Services

- In case a Brazilian taxpayer were to pay a fee to a Swiss resident person in consideration for so-called non-technical services, the DTT eliminates the WHT altogether, provided that there is no permanent establishment of the Swiss resident in Brazil. Non-technical services are all services that do not fit in the technical services definition.

¹ <https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-70663.html>.

Payment of Interest on Loan

- In case a Brazilian taxpayer were to pay interest on a loan to a Swiss financial institution in the context of a long-term loan (i.e., duration of at least 5 years) for the purchase of equipment or within the context of investment projects, the DTT reduces the Brazilian WHT from 15% to 10%. In other cases, the standard rate of 15% remains applicable.
- In addition, in case a Brazilian taxpayer were to pay interest on a loan to a Swiss pension fund, the Swiss government or a Swiss bank, taxation may only occur in Switzerland if certain conditions are met.

Payment of Dividends

- At present, the payment of dividends from a Brazilian entity to a Swiss resident is not subject to Brazilian WHT. However, the Brazilian legislator has been discussing tax reform proposals in recent times which could, if turned into law, eventually result in a Brazilian WHT on dividends. The following WHT rate limits in the DTT will therefore impact owners of Brazilian companies only if dividends paid by Brazilian companies become subject to WHT in Brazil in the future. The DTT limits the applicable WHT rate on dividends as follows: (i) 10%, in case of dividends paid to a shareholder with a “qualified participation” (i.e., at least 10% company participation and minimum holding period of the shares of 365 days); (ii) 0%, in case of dividends paid to pension or sovereign funds, if certain conditions are met; and (iii) 15%, in all other cases.

Additionally, the DTT also eliminates double taxation through the application of general and specific tax elimination methods:

General Methods (applicable to income in general, but not to dividends, interest, royalties and technical service fees)

- Income taxation in Switzerland, payment from Brazil to Switzerland: No Swiss income tax may be levied on income that is subject to taxation in Brazil.
- Income taxation in Brazil, payment from Switzerland to Brazil: Any Swiss income tax payments may be deducted from the income tax due in Brazil, limited to the total amount of the Brazilian tax levied on the payment from Switzerland.

Specific Methods (applicable to dividends, interest, royalties, and technical service fees)

Income taxation in Switzerland, payment from Brazil to Switzerland:

- Deduction of the WHT paid in Brazil from the income tax due in Switzerland, limited to the Swiss tax levied on the amount of the payment from Brazil.
- Reduction of the Swiss income tax in certain cases.

- Partial exemption of the Swiss tax that is at least equivalent to the income tax paid in Brazil.
- A Swiss company that receives dividends from a Brazilian company benefits from the same reduction of Swiss tax levied on such dividends as if it received the dividend from another Swiss entity.

It is also worth mentioning that the DTT expressly states that the payment of “interest on net equity” by a Brazilian company to a Swiss shareholder shall be treated as a payment of interest - and not as a payment of dividends². This provision, which does not exist in most DTTs signed between Brazil and other countries, aims to prevent Brazilian companies from classifying the payment of interest on net equity to Swiss shareholders as a payment of dividends with the Brazilian Central Bank in order to avoid taxation (considering that dividends are currently exempt from taxation in Brazil, as mentioned above). Its objective is also to bring Brazil closer to fulfilling the OECD’s Base Erosion and Profit Shifting (“BEPS”³) requirements.

The DTT provides for a most-favored-nation clause: in case the income tax rates on interest, royalties, and technical services in another treaty executed by Brazil with a member of the OECD following the DTT are lower than the ones in the DTT, those lower rates shall apply to the DTT as well.

Switzerland is not considered a low-tax jurisdiction under Brazilian law. However, certain Swiss company setups may be considered as so-called “privileged tax regimes” under Brazilian legislation. This is, in particular, the case of Swiss companies incorporated (1) as holding companies, domiciliary companies, auxiliary companies, mixed companies and administrative companies whose tax treatment in Switzerland results in the levy of corporate income tax at a rate lower than 20%, considering federal, cantonal and communal taxes; or (2) as other legal forms by means of rulings issued by Swiss tax authorities that result in the levy of corporate income tax at a rate lower than 20%. Privileged tax regimes are subject to certain restrictions under Brazilian tax legislation. However, the DTT benefits are also applicable to privileged tax regimes.

We trust you find the above considerations on the DTT useful and are available in case you have any questions, comments, or thoughts.

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² By means of article 9 of the Protocol of the DTT.

³ BEPS is a project of the Organization for Economic Cooperation and Development (OECD), supported by the G20 countries, which aims to avoid the transfer of profits to low tax countries.