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Brazil approves supplementary law, taking a big step toward Brazilian tax reform

- *Congress has approved a supplementary law regulating Brazilian tax reform.*
- *Passage of the new law brings the country closer to introducing a tax on goods and services and contribution on goods and services.*
- *This Alert highlights these changes and their implications for businesses.*

After many months of discussion in the upper and lower houses of Congress, one of the supplementary laws that regulates new taxes under the Brazilian tax reform was approved on 17 December 2024. The new law paves the way for introducing the tax on goods and services referred to as IBS (for *Imposto sobre Bens e Serviços*) and the contribution on goods and services referred to as CBS (for *Contribuição sobre Bens e Serviços*) in 2026 as predicted in the Brazilian Constitution. After receiving the changes proposed by the Senate, the Brazilian Congress disregarded most of the alterations and decided to keep the law mainly as it was.

What is the tax reform?

In December 2023, the Congress and Senate passed a constitutional amendment regarding tax reform in Brazil. This bill revoked the indirect taxes that are currently applicable (PIS/COFINS, ICMS, ISS and IPI)¹ and created new taxes that are calculated more in line with the Organisation for Economic Co-operation and Development (OECD) rules for value-added tax (VAT). The new taxes are:

- CBS, which would replace PIS/COFINS
- IBS, which would replace ICMS and ISS
- Imposto Seletivo (excise tax), which should levy on operations with goods that are considered a threat to the environment and to human health

Although the tax reform is intended to simplify the current tax system, it will also generate a wide range of changes in markets and relative product prices, considering that currently applicable taxes are embedded in prices and affect business investment decisions, such as the allocation of investments between Brazilian states. In this regard, the tax reform might also reduce the "weight" of tax factors in allocation decisions for productive and commercial investments, affecting not only the tax department but also other corporate departments (procurement, finance, marketing, strategy, supply chain, systems, etc.).

Where are we now?

Although congressional approval of the first supplementary law was a big step, there is still a long way to go toward regulation. One more supplementary bill (Bill #108) needs to be approved by the upper and lower Houses, and numerous other laws and complementary regulations are still pending discussion. In summary, the legislative steps are:

- Constitutional amendment (the basis for the tax reform): The bill was approved in December 2023.
- Supplementary laws (general regulations for the new taxes): Bill #68, which contains the general rules for the new taxes (IBS, CBS and excise tax), was approved on 17 December 2024. Bill #108, which contains regulations for the transition period and rules of operation for the IBS Committee, is still under discussion and expected to be approved early in 2025.
- Other laws and regulations (providing operational details on how the system will actually work): These items await discussion in 2025. It is important to note that some e-invoicing regulations were already issued, clarifying how the new taxes must be informed in the invoices and the new tax codes that will apply from 2026 onward.

What were the “surprises” in the approved bill?

Despite that the general rules of the new indirect tax system were already included in the Brazilian Constitution, there were a few surprises in the text of the approved supplementary law.

The first “surprise” is the adoption of intelligent split payment as a rule in the first years of the transition period. Split payment in Brazil is proposed to be like no other system in the world — it will apply to all payment operations (except payments in cash) and include a consultation system, in which the financial operator must access and consult tax authorities’ systems to determine whether the tax reflected on a particular invoice was (or was not) already paid. Implementing such a robust system will require technological changes and investments from banks and other similar companies.

The other surprise is the credit-deduction condition — i.e., for the buyer to have the right to deduct the credit, the supplier must pay the taxes informed on the invoice. In the current system, the VAT credit can be deducted the moment the buyer receives the invoice (and the goods and the services linked to it). In the future, taxpayers will have to wait until the supplier effectively pays the taxes to deduct the credit, which will generate accounting issues, require the establishment of new controls and have cash flow implications.

Challenges to be faced in 2025: what's next?

The first challenge: timing

For the transition period to commence in 2026, as predicted, all discussions regarding the other laws and regulations must occur early in 2025, so companies will have time to adapt. Otherwise, companies will face significant challenges with regard to system and process changes, considering that the first invoices for IBS and CBS must be issued in January 2026.

The second challenge: 2025 will be focused on processes adjustments and IT

Many Brazilian companies have not yet begun to analyze the changes that will be needed from a process and systems perspective to implement the tax reform. Internal processes must be reviewed to optimize company resources (considering the increase in workload, mainly during the transition years) and to adapt these resources for the new taxes' calculation. From a systems perspective, although most of the enterprise resource planning (ERP) providers and software houses will adjust the main features of the systems to adapt to the tax reform, each company must review customizations, specific parameterizations and tax parameters, amounting to considerable work for tax and information technology (IT) departments in 2025.

What is beyond?

Finally, although there is much work to be done with systems and tax processes in 2025, likely driving tax departments' agendas in the new year, it is important to remember that the tax reform is a transformational journey, affecting the way companies do business in the country and the region. In this sense, actions like working on current tax credit monetization, reviewing the supply chain network, and reviewing pricing policies and strategies, among other business priorities, cannot be forgotten and must be addressed as part of the journey toward simplification.

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Endnote

¹ Specifically, the new taxes replace the state and federal VATs (ICMS — *Imposto sobre a Circulação de Bens e Serviços* and IPI — *Imposto sobre Produtos Industrializados*), the Tax on Services (ISS — *Imposto sobre Serviços*) and the federal social contributions known as the Program of Social Integration (PIS) and Contribution for the Financing of Social Security (COFINS).

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