

# Tax Newsletter

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## First Swiss-Brazilian DTA becomes reality

The double taxation agreement (DTA) between Switzerland and Brazil has come into force on 16th March 2021 and will apply as of 1st January 2022. Both Swiss and Brazilian taxpayers will benefit from an enhanced tax environment which will boost cross-border investments.

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Almost three years after Switzerland and Brazil signed a double taxation agreement (DTA) on 3 May 2018, the Brazilian senate approved the DTA and it has come into force on 16th March 2021 and will apply as of 1st January 2022. The presidential decree, still outstanding as yet, is a mere administrative act and the Brazilian President Jair Messias Bolsonaro is expected to affix his signature in due course.

### Economic background

The currently low Brazilian Real and the huge potential of the by far biggest Latin-American country - by size and population - opens tremendous investment opportunities. Besides offering a domestic market with over 210 million inhabitants, Brazil is also a major producer and exporter of commodities and agricultural products. Switzerland, on the other hand, is not only a prime commodity trading hub, but also one of the world's largest investor countries. Moreover, Switzerland is leading in innovation and technology.

Already now, Brazil is the most important trading partner for Switzerland in Latin America, while Switzerland is the sixth largest investor in Brazil, whereby Swiss direct investments reached a volume of CHF 10.5 billion in 2018 alone. The DTA will further enhance Switzerland's attractiveness for Latin American investments and provide investors with legal certainty in tax matters.

### Key features

The DTA has been drafted in line with the recommendations of the Organization for Economic Co-operation and Development (OECD) and is aligned with the Base Erosion and Profit Shifting (BEPS) actions. Specifically, it provides for anti-abuse provisions, a mutual agreement clause (without an arbitration clause) as well as an exchange of tax information upon request in accordance with the current international standard.

The DTA, of course, includes typical provisions to facilitate international cross-border investments and financial transactions:

- Compared to 35% withholding tax (WHT) on dividends stipulated by Swiss domestic law, the residual Swiss WHT on dividends is limited to 10% under the DTA, provided that an interest of at least 10% has been held directly in the company for at least one year, and 15 per cent in all other cases. As an additional benefit, any WHT reduced thereby will be creditable against the recipient's income tax. Even though profits/dividends distributed by a Brazilian entity to resident or non-resident beneficiaries - individuals and/or legal entities - are not subject to IRRF at present (the Brazilian term for withholding income tax), the planned introduction of a respective WHT on Brazilian source dividends will extend the benefits of the DTA to Swiss recipients.
- The residual withholding tax on interest payments generally amounts to 15%. It is lowered to 10% in respect of interest payments on specific bank loans and to 0% in respect of interest payments to certain pension funds and government agencies. Given the 15% domestic Brazilian WHT rate on interest, there will be no decrease for the majority of the Swiss resident recipients, but they should be entitled to WHT credits.
- As regards royalties, the residual withholding tax is 15% on trademarks and 10% in all other cases.
- The protocol to the DTA also contains a most favourable clause for WHT on interest, royalties and technical services fees.

- The DTA generally exempts capital gains on the sale of shares (unless real estate companies are involved) in the country where the company is located. Thus, Swiss investors will no longer be subject to Brazilian taxation on capital gains earned on the disposal of shares in Brazilian companies.

### Particularities

Deviating from recent other double taxation agreements concluded by Brazil, this DTA includes the following provisions:

- The DTA explicitly applies to the Brazilian net profit social contribution (“contribuição social sobre o lucro líquido”).
- A residual 10% Brazilian withholding tax could be applied to fees paid out of Brazil for technical services rendered from Switzerland.

### How can double taxation be avoided?

Based on Article 23 of the DTA, Brazil eliminates potential double taxation by applying the credit method, whereas Switzerland applies either the credit or the exemption method, depending on the source of income. In line with the recommendations of the OECD, the DTA does not contain any tax-sparing or tax-matching clauses.

### Rules on tax residency

The DTA provides certainty on tax residence in the event of dual residency for individual and corporate taxpayers. The tie-breaker rule in Article 4 is in line with OECD standards. The tax residency of individual taxpayers is determined in a cascade based on the centre of their vital interests, their permanent home, usual abode and finally their citizenship. This includes Swiss resident individuals having a Brazilian investor visa and dual resident individuals by all other means. For corporate taxpayers, the place of effective management rather than the place of incorporation is decisive for their tax residency.

### Way forward

Once the new Swiss-Brazilian DTA is applicable, investors and corporate groups will be given an effective tool for identifying structuring opportunities, which will allow both the optimisation of existing structures and international expansion. This may also apply to corporate groups having their headquarters in third countries, but already running or planning to run substantial operations in both Brazil and Switzerland.

Walder Wyss is very well connected with Brazilian international tax and legal specialists and we are happy to assist you in all related matters.

The Walder Wyss Newsletter provides comments on new developments and significant issues of Swiss law. These comments are not intended to provide legal advice. Before taking action or relying on the comments and the information given, addressees of this Newsletter should seek specific advice on the matters which concern them.

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