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Deloitte Doing Business : Regional Incentives

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Regional Incentives



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Manaus Free Trade Zone (Zona Franca de Manaus)

The Manaus Free Trade Zone, regulated by Decree-Law No. 288/1967, is a free import and export trade area where special fiscal incentives apply. It was set up with the objective of creating in the Amazon Region an industrial, commercial and agricultural center under economic conditions that allow its development, given local factors and the great distance separating it from its markets.

Today, around fifty years after it was founded, the Manaus Free Trade Zone represents a virtuous Brazilian government development model that has managed to make a socio-economic base in the Amazon region feasible, promote the better productive and social integration of the region with the rest of Brazil, and guarantee national sovereignty over its borders.

During its historical evolution, the Manaus Free Trade Zone has enabled three economic hubs to be developed: industrial, commercial and agricultural. The first of these, represented by the Manaus Industrial Sector (PIM), is considered the foundation stone that sustains the model.

The Manaus Free Trade Zone has a set of tax and other incentives available especially to attract and keep investments in its area of influence. These incentives have been made available by a joint action between the Federal and State Governments, offering:

• Federal Taxes Incentives

Import Duty Reduction (II): 88% reduction for consumables used in industrialization;

Excise Tax Exemption (IPI):

Corporate Income Tax Reduction (IRPJ): 75% reduction of Income Tax and Non-Refundable surcharges, exclusively for reinvestments. Common to all the Legal Amazon.

Social Integration Program Tax (PIS) and Social Security Contribution (COFINS) Exemption/Reduction: Exempt for imported goods and internal sales between industries within Manaus Free Trade Zone, and reduction for 3.65% aliquot – rather than 9.25% – on finished goods sales to the rest of the country.

• State Taxes Incentives

State Value Added Tax Reduction (ICMS): Reduction from 55% up to 100% of the ICMS, depending on the investment project. In all cases, to use the incentives, companies must contribute with funds for financing high education, tourism, R&D, and small and micro-companies.

• Other Incentives

As well as the tax incentives, the Superintendence of the Manaus Free Trade Zone provides land for investors for a subsidized price, with urbanized road system, water supply network, telecommunications network, sanitary sewer and rainwater drainage.

To be eligible for MFTZ's incentives the produced goods must meet the Brazilian PPB (Basic Productive Process), which determines the level of nationalization required for each type of product, since the initiative aims to encourage the national industry. The PPB is defined by joint decree of the Ministry of Science, Technology and Information and the Ministry of Development, Industry and Trade.

Northern and northeastern Brazil

Before the 1930s – Brazilian development policy was based primarily on exports, but in the late 1930s, Brazil implemented a development policy based on import substitution. As a result of this action, South and Southeast Regions increased their share of the industrial provision at the expense of the other Regions (North, Northeast and Midwest), leaving those regions far behind.

In the 1960s – Brazilian government implemented policies to counterbalance the Regional development by stimulating investments, consequently, economic growth on the lagging regions. As a result of these policies, Development Agencies were established in the North (Superintendence for the Development of the Amazon - SUDAM) and Northeast (Superintendence for the Development of the Northeast) regions with the purpose of coordinating the development funds and granting tax incentives.

This tax incentive mechanism intends to benefit investments in the North and Northeast regions, in the State of Mato Grosso and in some municipalities in the northern region of Minas Gerais and Espírito Santo, in activities considered vital for Brazilian

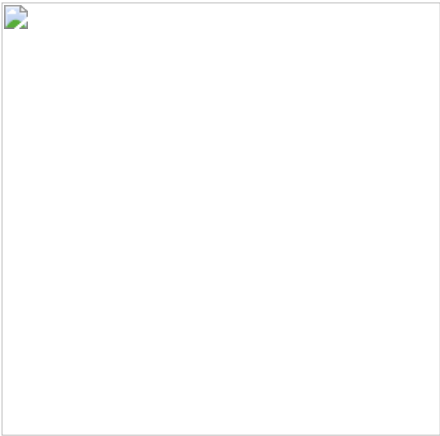
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development.

Historically, the vast majority of foreign investment has been concentrated in the country's Southern and Southeastern states. However, recent data suggests that this dynamic is changing. In order to achieve a competitive edge and access markets with incredible growth potential, multinationals are beginning to look to investment opportunities outside the traditional investment centers.

The North and Northeast regions are being seen as potential destinations. These two regions have tremendous room for future growth and investors are starting to realize these opportunities.



MAIN TAXES INCENTIVES OFFERED BY SUDAM AND SUDENE

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Tax incentives in Brazil

For the sake of regional development, or to develop special industries considered strategic by the Government, the Brazilian tax system may allow for tax incentives. Tax incentives in Brazil may take several forms, from normal tax cuts, to mere reductions in indirect taxes or kickbacks.

The government and most states seek to promote and attract new investment, generally in all types of industry, and provide assistance to investors seeking to obtain financing and advisory services. Therefore, tax incentives are commonly negotiable and are granted at federal, state and municipal levels.

Foreign investors are generally eligible for available incentives. That is to say: local and foreign investors are generally treated equally as regards investment incentives and tax concessions, and there are no special federal tax incentives to attract foreign investors.

Special federal programs reward investments in the poorer North and Northeast regions, including reductions in federal income tax. States that are covered by such incentives are:

In the Northeast: Alagoas, Bahia, Ceará, Espírito Santo, Maranhão (part), Minas Gerais (part), Paraíba, Pernambuco, Piauí, Rio Grande do Norte, Sergipe. The organ that supervises incentivized growth in that region is SUDENE – Secretaria de Desenvolvimento Econômico do Nordeste.

In the North: Acre, Amapá, Amazonas, Maranhão (some parts), Mato Grosso, Pará, Rondônia, Roraima and Tocantins. The organ that supervises incentivized growth in that region is SUDAM – Secretaria de Desenvolvimento Econômico da Amazônia (and here they mean the “legal region” of the Amazon, comprising all these states above mentioned).

Eligibility for Tax Incentives in Brazil

In general, incentives are available to both local and foreign-controlled companies. However, the granting of incentives depends on approval by the federal government agencies SUDENE and SUDAM in respect of the implementation of new industrial projects or the planned expansion, diversification or improvement of an existing industry. SUDENE and SUDAM evaluate not only a project’s technical and economic feasibility, but also its suitability as part of the region’s overall economic development.

Type of Tax incentives

For the Northeast and Amazon regions, the investment incentive plans administered by SUDENE and SUDAM, respectively, offer certain fiscal benefits to companies operating approved projects. These are as follows:

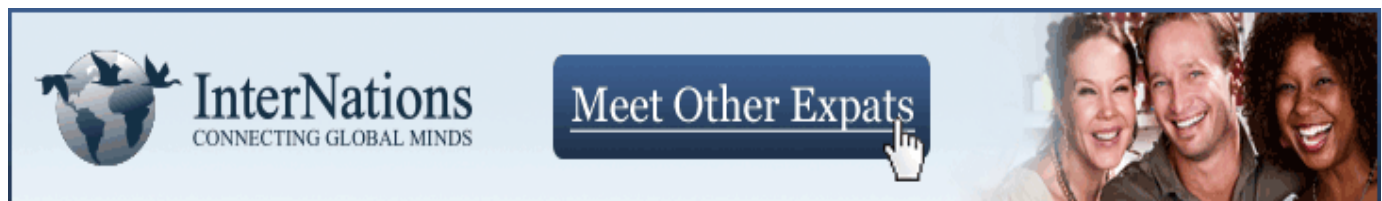
• Silicon Metal

- 75% reduction of the income tax and non-refundable surcharges due on operating profit (lucro de exploração), for a maximum period of ten years, for implementation, expansion, diversification and improvement projects submitted and approved from August 24, 2000, to December 31, 2018, relating to economic segments considered to be a priority for the development of these regions;
- 5% reduction of income tax and non-refundable surcharges. This benefit was valid only from January 1, 2009, until December 31, 2013, for legal entities which maintain economic enterprises that participate in the development of these regions. Legal entities which own such projects may apply for the abovementioned reduction of 75%, within a period of ten years, provided that their activities fall into economic segments considered by the government to constitute a priority for the development of these regions;
- The corporate income tax reduction cannot be distributed to the company's quotaholders/shareholders and must be booked and kept as a subsidy reserve (capital reserve), to be used only for capital increases or offsetting existing losses;
- Certain state VAT (ICMS) incentives are also made available to certain businesses, depending on the nature and peculiarities of the project.

Non-tax incentives

For companies in the Northeast and Amazon regions, low-cost loans or loan guarantees are granted by government development banks, such as the Bank of Northeast Brazil (BNB), the Amazon Bank (BASA) or the National Bank for Social and Economic Development (BNDES).

There are no specific incentives for establishing holding companies and regional administrative offices, and there are no tax havens or offshore financial facilities. There is a free-trade zone in Manaus and fiscal benefits apply in areas of the Western Amazon region (see Free-trade zones below). Brazilian tax system also has incentives for the promotion of exports in general.



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