BMA
ADVOGADOS

Did Constitutional Challenge ADI 2446 solve tax planning controversy?

29.06.2022 3 min read

Authors

Vivian Casanova

Related areas

Tax

Topics

Tax BMA Review

Tax planning is a controversial topic both in the courts and among tax specialists, which news were expected to arise from the judgement of the Constitutional Challenge ADI no. 2446, by the Brazilian Supreme Federal Court (STF – *Supremo Tribunal Federal*).

The Constitutional Challenge proceeding was filed in April 2001, immediately following publication of Complementary Law 104/2001, which added a new paragraph to article 116 of the National Tax Code that allows tax authorities to assess taxes based on the disregard transactions carried out by the taxpayer. ADI 2446 challenged the constitutionality of the new provision.

Judgment on the Constitutional Challenge was finally rendered in April 2022, more than 20 years after the proceeding was filed. By a majority, the STF held that the provision was constitutional, adopting the reasons in the lead opinion given by Justice Cármen Lúcia.

In her opinion, Justice Cármen Lúcia stressed a number of important points:

- the provision is intended to prevent abusive tax planning (tax evasion), and is aimed at situations where, after a taxable event has occurred, the taxpayer carries out acts and transactions designed to disguise or conceal the event;
- the provision does not prohibit lawful tax planning (tax avoidance), and taxpayers have the right to seek tax savings through legitimate means;
- in itself, the provision has limited effect, since "the full effect of the provision depends on ordinary legislation to establish the procedures to be followed."

Contrary to expectation, therefore, the STF's judgment does not make any significant contribution to the debate over tax planning, since it simply underlined the distinction between tax avoidance and tax evasion without addressing the question of what constitutes valid or lawful tax planning. Furthermore, in concluding that the provision seeks to prevent illicit tax evasion, it adopts reasoning based on sham transactions, which is already sufficient grounds for tax authorities to disregard acts and transactions, without having to rely on the sole paragraph of article 116 of the Tax Code.

The inconclusive nature of the STF's decision can be seen in the fact that both the Tax Prosecution Service (PGFN – *Procuradoria-Geral da Fazenda Nacional*) and taxpayers are "celebrating" the outcome:

- The taxpayers are satisfied because the STF confirmed that the provision does not apply in cases of tax avoidance, so tax planning to avoid the occurrence of taxable events is permitted, even when the only objective is tax savings, without an independent business purpose;

- The PGFN is satisfied because the “anti-avoidance” (the term used in the summary of the STF’s decision) provision was held to be constitutional and has unrestricted application, since the provision that it applies only to cases of tax evasion is a mere obiter dictum.

Despite the PGFN’s views, the distinction between tax evasion and tax avoidance in the application of the provision was the main reason that the court ruled in favor of the constitutionality of the sole paragraph of article 116 of the National Tax Code, and it was precisely that distinction that led eight other members of the court to concur in Justice Cármen Lúcia’s opinion. *Obiter dictum* or not, the distinction must be taken into account in interpreting the court’s ruling in ADI no. 2446.

In the end, without guidance from the STF as to the limits of valid tax planning, such transactions will continue to be subject to a case-by-case analysis by the Courts, with the concomitant lack of legal certainty for taxpayers. The difficulty is that tax planning structures are generally complex, and it is not always easy to distinguish between tax avoidance and tax evasion.

› PROFESSIONALS

Professionals who combine legal insight and market perspective

Vivian Casanova