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Tax implications of talent mobility – cross-border movement of employees: Brazil

The Brazilian tax system is known for its complexity and having a large number of rules. Therefore, cross-border talent mobility involving Brazil demands careful attention to the country's tax and social security legislation. An individual's residency status affects the application of the tax regime and gives rise to several obligations. This article aims to explain the main impact on both employers and employees when foreign talent establishes residence and carries out work in Brazil.

1. Overview of the tax system

Regarding the taxation of an individual's income, Brazil adopts a model in which the tax bases vary substantially depending on the taxpayer's residence status, with contrasting approaches taken to those deemed to be a tax resident and those with an income source in Brazil. Individuals who are considered to be tax residents in Brazil are taxed on their worldwide income, namely all of the income they receive from both Brazilian and foreign sources is subject to income tax locally. Non-residents, on the other hand, are taxed only on income derived from Brazilian sources, generally through withholding taxes applied at fixed rates, which can be reduced in situations where a tax treaty applies. This distinction is the starting point for any analysis of international mobility involving the country.

2. Taxation of employment income

The first step in analysing the taxation of foreign employees in Brazil is the need to determine their tax residency status. Under Brazilian law, a foreign individual entering Brazil with a permanent visa, or with a temporary visa linked to a local employment contract, is considered a tax resident from the date of their arrival in the country. For those entering Brazil with other types of visas, tax residency is established if they stay in the country for more than 183 days, whether such days

are consecutive or not, within a 12-month period. Once an individual's tax residency is established, the individual becomes subject to progressive income tax rates, which range from 7.5 per cent to 27.5 per cent, and they must file and pay taxes on their worldwide income.

For employees who are non-residents but who earn income from Brazilian sources (for example, an executive located abroad who receives compensation from a subsidiary in Brazil), the system is different. Their employment income is subject to exclusive withholding tax at a flat rate of 25 per cent and they are not entitled to the legal deductions available to Brazilian tax residents, such as those concerning medical and education expenses.

2.1 Scope of taxable income

Under the Brazilian tax system, a taxable event for individual income tax purposes is governed by the cash basis method. This means that income is taxed at the moment it is received or made available to the individual, regardless of whether the paying source is located in Brazil or abroad.

Direct compensation, which includes an individual's base salary, bonuses, performance bonuses and other benefits, is fully taxable and subject to the relevant income tax bracket, with a maximum rate of 27.5 per cent. Income tax is withheld at the source by the employer. Any compensation received from abroad must be reported and the tax paid by the expatriate through the mandatory tax payment system, known as '*Carnê-Leão'*.

Allowances, such as housing and transportation-related payments, payments made towards school tuition fees and benefits in kind, among others, are taxed at the same rates as the individual's salary. The Brazilian tax authorities generally have a broad view of income: any financial benefit or advantage granted by the employer which, under normal circumstances, would be borne by the employee themselves, is considered to be indirect remuneration. As such, these types of payments must be added to the expatriate's basic salary for the purpose of calculating the income tax due.

Employees may claim certain tax deductions allowed by law, provided that the strict requirements regarding documentary evidence are met. It is possible to deduct specific expenses relating to legal dependents, medical expenses (medical expenses incurred abroad are also accepted, provided they are duly translated and substantiated) and education expenses (according to an annual limit stipulated by law). In addition, contributions to Brazilian private pension plans may be deducted up to a limit of 12 per cent of the individual's gross taxable income, depending on the type of pension plan involved. However, as a rule,

contributions made to foreign pension plans are not deductible for tax purposes in Brazil.

Regarding equity compensation, the level of taxation applied depends on the type of equity plan involved: for example, after discussions in Brazilian courts over many years, it has now been recognised that stock option plans are strictly commercial in nature, rather than being a form of compensation, provided that the employee effectively pays for the stock options and takes on the relevant risk. Consequently, taxation does not occur at the moment of granting the shares, but only upon the sale of the shares (generally after a vesting period). The profit earned from the sale of stocks is subject to taxation as capital gains, with more favourable tax rates ranging from 15 per cent to 22.5 per cent.

Conversely, restricted stock units (RSUs) are taxed as compensation, since RSUs are granted without any form of payment by the employee. Consequently, the market value of RSUs is taxed based on the individual's income tax bracket at the time the vesting conditions are met and the stocks become available to the employee.

2.2. Source of income rules

Employment income is considered to be locally sourced when it is paid by a local company or individual. Remuneration paid by a Brazilian entity (salary, bonuses, benefits) is subject to withholding tax, in the same way as local employees, using progressive income tax rates.

If the expatriate is a non-resident, a flat rate of 25 per cent is applied. Withholding tax in this context is exclusive and definitive in nature and, as such, no deductions are allowed.

Income source-related taxation may be waived under the terms of a tax treaty. Article 15 of the tax treaties entered into by Brazil concerning dependent professions provides for taxation exclusively in the employee's country of residence, unless the remuneration is paid by a permanent establishment (PE) situated in the source country.

Nevertheless, some treaties signed by Brazil also provide for taxation in both countries when the work is being carried out in the territory of the other contracting state, provided that: (1) the employee stays in the other state for more than 183 days in any 12-month period; and (2) the remuneration is paid by an employer who is not resident in the country where the work is being carried out and is not attributable to a PE in the country where the work is being carried out.

It is important to note that Brazil allows individuals to hold dual residency. In cases where there is a tax treaty, tiebreak rules on residence, as provided for in Article

4, may be applied. In situations where there is no applicable tax treaty, Brazil will not consider tiebreak rules and will instead apply objective criteria to establish residency, namely concerning an individual's entry into the country with a temporary or permanent visa, or a period of stay exceeding 183 days.

Regarding social security contributions, the Brazilian system requires that every person engaged in paid employment in the country is, by law, compulsorily insured, regardless of their nationality or tax residency status. When applied to cross-border professionals, this rule may result in the application of double social security taxation. This is why international social security treaties play an important role in this context.

If a cross-border professional comes to work in Brazil on a secondment from a company based in a country with which Brazil has a tax treaty (eg, the United States, Portugal or Germany), he or she can apply for a certificate of temporary relocation in their country of origin. This certificate confirms that they remain affiliated with their home country's social security system. Upon presenting this certificate in Brazil, both the employee and the Brazilian company are exempt from paying social security contributions in regard to the individual's remuneration for the duration of the validity period stipulated in the agreement (usually between two and five years, extendable).

Where there is no applicable treaty, registration with the national social security agency is mandatory. The company must withhold the employee's social security contribution according to the set tax brackets (up to 14 per cent) and pay the employer's contribution (generally 20 per cent of the total remuneration, in addition to other contributions made to third parties). If the individual's country of origin also requires the payment of social security contributions, double taxation will be unavoidable and will increase the overall cost of the expatriation package.

3. PE risks

Although the term is included in the tax treaties signed by Brazil, domestic legislation does not provide a definition of a PE. The concept is also rarely applied by local tax authorities, given that, historically, the Brazilian government has always preferred to implement taxation through withholding tax rather than the designation of a PE.

For this reason, a company intending to operate/provide services in Brazil must register with the Federal Revenue Service (*Receita Federal do Brasil* or RFB), obtain a company taxpayer ID and, consequently, they will be taxed in the same way as other domestic entities.

When it comes to an agent or sales-related PE, the Brazilian Income Tax Regulations provide that where sales are made in Brazil by non-residents through their agents or representatives, the income derived from such transactions shall be taxable in accordance with domestic tax rules. Furthermore, compliance with ancillary obligations, as well as the payment of taxes on these transactions, must be carried out by the Brazilian agent or representative.

As in many countries, the key criteria for designating an agent PE are the authority to enter into contracts and conclude transactions on behalf of the foreign company employing the agent.

4. Exit tax/departure rules

The Brazilian tax system does not apply an exit tax. Legislation does not assume that a taxpayer's assets are realised upon his or her departure. Therefore, no tax is levied on the mere appreciation in value of assets that have not actually been sold/alienated.

Until 2025, when an individual departed Brazil after being a tax resident, his or her local assets were deemed to have been realised, even if they remained in the country. The realisation of local assets in this context used to take place at the moment the individual's tax status changed from resident to non-resident. In such a scenario, the individual would be required to notify the bank of his or her new residence status. Following this, the relevant assets would then be realised and, therefore, the gains would be subject to taxation.

From January 2025 onwards, due to a new regulation issued as part of the national monetary system, existing investments do not need to be realised. Instead, they may be retained until they mature or until the individual wishes to redeem them.

In regards to departure proceedings, the individual must fill out and submit a notice of permanent departure to the RFB, which runs from the date of their departure until the last working day of February in the following calendar year. In addition to notifying the tax authorities of their departure, he or she must notify in writing all their paying agents in Brazil (banks, brokers, landlords, former employers) of their new residence status, so that the relevant entities apply the applicable withholding tax rules for non-residents.

In addition to submitting a notice of permanent departure, the individual must also fill out and submit the declaration of permanent departure by the same deadline as the annual income tax return, usually in May. By means of such a declaration, he or she is required to declare and pay income tax on all of their income earned

from 1 January until the date of his or her departure. The tax calculated on this return must be paid in a single instalment.

5. Recent developments and case law

Historically, Brazil has only heard a few cases on the taxation of international mobility, but there has been an increase in recent years, both before the administrative and judicial courts.

With respect to equity compensation, the Superior Court of Justice recently decided in favour of the taxpayer. In its ruling in Repetitive Case 1.226 (September 2024), the Court held that stock option plans have a commercial nature, rather than being compensatory, provided they are not granted as cost free for the employee.

This decision rules out the levy of individual income tax at the time the option is exercised (vesting/exercise), deferring taxation solely to the time of the sale of the shares, in the form of capital gains tax (15 per cent to 22.5 per cent). However, the decision is limited to personal income tax. The debate regarding the levy of social security contributions on stock options still awaits a binding resolution, and the administrative court continues, in many cases, to impose fines on companies on the grounds that stock options have a compensatory nature, since they are directly linked to the employment relationship.

Administrative case law has also been established concerning the levy of social security contributions on some types of bonus payments (which are called ‘profit-sharing plans’ in Brazil). According to the relevant case law, for social security contributions to be waived, Brazilian legislation requires that (1) the profit-sharing agreement must previously define, with clear and objective rules, the targets, outcomes and deadlines to be fulfilled by the employees for the bonuses to be paid; (2) such agreement must be filed and registered before the local competent labour union; and (3) payment of the bonuses must comply with the legal frequency requirement, which is a maximum of two payments per year, with a minimum interval between them of at least three months.

Regarding dual tax residence, the administrative courts have reinforced the application of the tiebreak rules set out in Article 4 of the tax treaties signed by Brazil to determine the sole tax residence of individuals who are considered to be residents of both Brazil and a foreign country, thereby avoiding double taxation of income. The judgments examined both the relevant objective criteria and the centre of vital interests to determine the residency status of the taxpayers involved.

6. Key takeaways

To summarise, an outline of the key takeaways, the main risks and guidelines for effective tax planning are provided below.

The key takeaways are as follows:

- the residency dichotomy: tax residents in Brazil are taxed on their worldwide income; non-residents are taxed exclusively at source on income of Brazilian origin;
- the tax residency criteria: tax residency in Brazil is established upon an individual's entry into the country on a permanent or a temporary visa linked to local employment or by physically staying in the country for more than 183 days (consecutive or not) within a 12-month period;
- scope of the tax base: the RFB considers salaries, bonuses and most allowances to be taxable income;
- equity compensation: stock options with an exercise price have a commercial nature (taxed as capital gains on sale). RSUs (granted free of charge), on the other hand, are taxed as remuneration; and
- leaving Brazil: there is no exit tax on unrealised gains, but formal notification (notification and declaration of permanent departure) is mandatory to cease the application of universal taxation.

The main risks are as follows:

- for the employer: risks arise in regard to split payroll arrangements where the employer's social security contributions are not deducted from the portion of the remuneration paid abroad. The provision of benefits without including them in the payroll attracts a 35 per cent withholding tax. Social security contributions are levied on bonuses and stock options; and
- for the employee: the failure to pay income tax or to formalise their permanent departure may result in double taxation, the imposition of severe fines and the cancellation of the individual's Brazilian tax ID (which is still relevant if the non-resident has assets in the country). There are risks related to dual residency and double social security contributions in the absence of a tax treaty involving Brazil.

Things to note when planning for tax purposes:

- pre-immigration: prior to an individual's arrival in Brazil, it is important to obtain a temporary relocation certificate to avoid double taxation on social security contributions;

- structuring the package: contracts must distinguish between salary, benefits and allowances. Any equity plans must be reviewed to ensure compliance with Brazilian rules; and
- repatriation: returning to another country requires compliance with the relevant RFB deadlines, formal notification to local paying agents and the conversion of the individual's bank accounts to non-resident status.