Brazil’s Measures Concerning Discriminatory Taxation and Charges for Automobiles, etc.

<Outline of the Measure>
In September 2011, the Brazilian government announced that 30% would be added to the existing IPI (Imposto sobre Productos Industrializados) tax on domestic and imported automobiles, in order to protect the domestic industry, and it became effective in December of the same year.

However, an additional IPI tax is exempted for automobiles which were produced in Brazil, Mercosur or Mexico and fulfill certain requirements, and those manufacturers must meet the following three requirements and become a “certified enterprise,” in order to qualify for the exemption:
1) to purchase 65% or more of supplies sourced from within Mercosur
2) to conduct more than 6 out of 11 production processes, such as assembly and press, in Brazil
3) to invest 0.5% of gross sales (gross income after tax deduction of the entire company) into research and development (R&D)

This system was set as a tentative measure, to expire in December 2012, but in October 2012, the Brazilian government announced a new automobile policy (the Inovar-Auto Policy) to replace the system. The new system maintains the increase of IPI on automobiles by 30% for five years from 2013 to 2017 and reduces IPI by up to 30% under certain conditions. In order to participate in the Inovar-Auto Policy, automobile manufacturers need to become a “certified enterprise” by (1) achieving the prescribed fuel efficiency standards by 2017 (fuel efficiency of new cars in 2017 would be reduced by 12% compared to that in 2012), and participating in the vehicle labeling program; (2) investing a certain amount in domestic research and development, innovation, or engineering etc.; and (3) carrying out certain manufacturing processes such as assembly and pressing in Brazil (replacing “more than 6 out of 11 production processes” in (2) above with “8 out of 12 production processes by 2013 and 10 by 2017”). Accredited companies are granted IPI credits that can be used for IPI reduction according to the amount of purchases of domestic parts and other expenditures in Brazil (details of conditions and tax incentives differ depending on the status of corporate activities ((1) domestic manufacturer, (2) import and sales corporate, (3) corporate with investment plans)). Also, a 30% IPI reduction is applied to imports of automobiles from Mercosur and Mexico by accredited companies.

Not only in the field of automobiles, but also in other fields including information and communications, Brazil has introduced measures for drastic reductions or exemptions from indirect taxes on products based on such requirements as carrying out the production process called “basic production process” (PPB) (manufacturing of certain parts and assembly of final products) in Brazil. As a result, the difference between effective tariff rates for imported products and those for domestic products has arisen.

<Problems under International Rules>
This measure recognizes drastic reductions or exemptions from indirect taxes only on products manufactured in Brazil and certain other countries, and provides an incentive for companies manufacturing automobiles, etc. in Brazil to preferentially use domestic parts over imported parts in order to benefit from tax reductions or exemptions. Also, it treats imported parts unfavorably. Moreover, the auto reduction tax is only approved for automobiles produced in Mercosur or Mexico.
under the Inovar-Auto Policy. Automobiles imported from countries other than Mercosur and Mexico are treated unfavorably in relation to not only domestically-produced automobiles but also automobiles imported from Mercosur or Mexico. This may be a violation of GATT Article I (general most-favored nation treatment) Article III (national treatment on internal taxation and regulations), TRIMs Article 2 (national treatment and quantitative restrictions) and WTO Agreement on Subsidies Article 3.1 (b).

<Recent Developments>

Japan has repeatedly expressed concerns on the abovementioned policies\(^1\), but no efforts to improve the policy have been observed. In addition to automobiles, there has been an effort to expand preferential taxation measures that are linked to a wide range of sectors, including telecommunications network devices and chemicals (fertilizers). The EU made a request for consultations with Brazil in January 2014, and then requested the establishment of a panel in October of the same year (not only the automobile policy and the preferential taxation measures in the information and communications technology sector but also the preferential taxation measures for specific exporting companies were set within the scope of the panel). The panel was established in December of the same year, in which Japan participated as a third party. Furthermore, Japan also made a request for consultations with Brazil in July 2015, and then requested the establishment of a panel in September of the same year. The panel was established in the same month (The EU’s preceding panel proceedings and Japan’s panel proceedings were consolidated).

On August 30, 2017, the panel accepted the claims made by Japan and the EU, and found that the preferential taxation measures in the automobile sector and the information and communications technology sector are inconsistent with GATT Article I (most-favored nation treatment) and Article III (national treatment), TRIMs Article 2 (national treatment) and WTO Agreement on Subsidies Article 3.1 (b). In addition, the panel accepted the claim by Japan and the EU, and found the preferential taxation measures for specific exporting companies inconsistent with WTO Agreement on Subsidies Article 3.1 (a).

Brazil appealed, thus Japan, together with the EU, will take action to ensure that this case will be settled appropriately in the Appellate Body proceedings consistently with the WTO Agreement and will continue making necessary actions while paying attention to how Brazil will deal with this measure.

### Protection of Intellectual Property

#### Licensing Regulations on Patents and Know-How

No specific actions have been taken for solving problems. For more, including specific problems, please see pages 172-173 of the 2017 Report on Compliance by Major Trading Partners with Trade Agreements -WTO, FTA/EPA and IIA-.

\(^1\) For details of bilateral and multilateral consultations carried out before the request of WTO consultations, please see page 172 of the 2017 Report on Compliance by Major Trading Partners with Trade Agreements -WTO, FTA/EPA and IIA-.