

# TAX REFORM AND M&A TRANSACTIONS IN BRAZIL

Constitutional Amendment No. 132/23 and Supplementary Law No. 214/25 ushered in a new tax era in Brazil, replacing the fragmented consumption tax framework (ICMS, ISS, PIS, COFINS and IPI) with a dual model consisting of a Goods and Services Tax (IBS) and a Contribution on Goods and Services (CBS), in addition to the Selective Tax (IS).

This new framework will impact the structuring and execution of M&A and other business combinations, requiring multidisciplinary teams fully attuned to the new landscape.

## IMPLICATIONS FOR VALUATION, CASH FLOWS, AND FINANCIAL MODELING

Tax reform effects should be incorporated into valuations, cash flows, and financial modeling, including:

- Equity adjustments for Purchase Price Allocation (PPA);
- Impacts on Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) multiples; and
- Effects on equity-based purchase price adjustment clauses.

In addition, metrics such as EBITDA, net debt, and working capital could be materially impacted by the update of the new tax model.

## LEGAL AND CONTRACTUAL ASPECTS IN M&A TRANSACTIONS

Due diligence should be expanded to capture risks specific to the transition period:

- **Tax credit mapping**, assessing the portability and liquidity of PIS, COFINS, and ICMS credit balances;
- **Tax classification** according to the Mercosur Common Nomenclature (NCM) and the Brazilian Services Nomenclature (NBS), which determine applicable tax rates and credit eligibility;
- **Exposure to legacy regimes**, mapping historical contingencies;
- **Tax incentives being phased out**, identifying current benefits and compensation mechanisms; and
- **Compliance and systems**, assessing ERP (Enterprise Resource Planning) maturity and investments required to adapt to the reform.

For contracts already executed, such impact must be assessed in advance to define approaches, contingency measures, clause renegotiation strategies and, if necessary, defensive measures.

For contracts under negotiation, a comparative and informed assessment will yield contracts better calibrated to the reform's effects, as outlined below.

## REPRESENTATIONS & WARRANTIES

Transaction agreements must include specific representations and warranties addressing the tax transition, particularly regarding the absence of known or likely contingencies due to the transition between tax systems.

## INDEMNITIES AND RISK ALLOCATION

The structure must provide for:

- legacy contingencies tied to taxes being phased out;
- loss of tax credits that cannot be utilized; and
- loss of tax incentives without adequate compensation.

Another recommendation is to establish smaller baskets for reform-related contingencies, caps with carve-outs for fraud and fundamental contingencies, and extended survival periods, given the long preemptive periods.

## PURCHASE PRICE ADJUSTMENT MECHANISMS

In deals where reform-related impacts are highly uncertain, parties may structure:

- **A tax earn-out** tied to the realization of credits, maintenance of incentives, and absence of deficiency notices;
- **A true-up of working capital** adapted to normalize tax credits and address split payment; and
- **Tax-focused material adverse change (MAC) clauses**, with specific reform-related triggers.

## CONTRACT REPRICING

Long-term contracts executed under the current tax system may become misaligned once the IBS and CBS take effect, particularly those with fixed prices or adjustment clauses that do not account for tax changes.

## COVENANTS, FINANCING, AND CAPITAL MARKETS

Changes stemming from the reform may lead to:

- unintended impacts on covenants (especially financial covenants) undertaken by the target, the acquirer, or their affiliates;
- acceleration events; and
- the need to update or clarify disclosures made by public companies or by entities subject to public reporting of their financials.

## IMPAIRMENT AND ACCOUNTING EFFECTS

The reform may require reassessing deferred tax assets and liabilities, as well as impairment testing of goodwill premised on tax benefits that are being phased out. The costs of adapting systems and the regime transition period (2026-2032) must be priced in. The shift to destination-based taxation alters location-driven planning strategies and may create opportunities to consolidate entities, redesign operating flows, and simplify corporate structures.

## COMPLIANCE AND INTEGRATION COSTS

The new tax system requires upgrades to ERPs and management systems.

## CONSOLIDATION AND TAX PLANNING

The shift to destination-based taxation, which is central to the IBS, fundamentally affects location-based tax planning strategies. Structures that benefited from reduced ICMS rates in specific states lose effectiveness. The reform may require a review of corporate structures established under assumptions tied to the previous system.