

The Economist – 20/08/2012

Electricity taxes in Brazil

Untangling the custo Brasil

http://www.economist.com/blogs/americasview/2012/08/electricity-taxes-brazil?fsrc=scn/ln_ec/untangling_the_custo_brasil



Electricity pylons next to the Itaipu Reservoir

"I PAY so many different taxes: registration fees, union fees, social contributions, payroll taxes and taxes on profits," says Angela Sardelli, the boss of Vox, a Brazilian company that trains telemarketers for other businesses. The number and complexity of those taxes-municipal, state and federal-means even small firms have to get specialist accountancy advice. "If you don't do this, you're running a really big risk," she says. "If you make a mistake, fixing it means trekking between different government offices, and paying fees and fines." So many taxes have nothing to do with her cash flow that on occasion, she has had to take out bank loans to pay.

High and complex taxes are only some of the obstacles businesses face in Brazil: poor infrastructure, outdated labour laws and reams of red tape also trip them up. These difficulties are so longstanding that they have their own name: the custo Brasil, or "Brazil cost". So it is no surprise that with excess capacity in the rich world and the real, Brazil's currency, not far off its all-time high, the country's manufacturers are struggling to compete globally. Though domestic consumer demand is healthy, up 4.5% on last year, imports are soaking up most of the growth in demand. Exports now consist mostly of commodities, in which Brazil has a commanding natural advantage. Industry is flatlining.

Until now the government's response has been piecemeal and protectionist. Sales taxes have been cut on cars and white goods manufactured in Brazil, and payroll

taxes replaced by a lower tax on turnover for some of the country's least competitive sectors, such as textiles, plastics and the automotive industry. Further obstacles have been put in the way of manufactured imports, which already face high tariffs. That has helped local manufacturers in the short term-though at great cost to consumers, who end up paying prices far higher than those elsewhere. But shielded from fierce foreign competition, Brazilian industry has grown flabby. Outside the agricultural and mining sectors productivity, never one of Brazil's strong points, is falling-even while costs soar.

On August 15th the government announced a programme to cut the custo Brasil by turning to the private sector to improve infrastructure. That is a big policy shift: it has previously been hostile to anything akin to privatisation. Over time it should help cut costs and make businesses more productive. But the government has put off confirming the other half of its plans: long-signalled cuts to payroll taxes and electricity costs. With federal workers striking over pay, it is now afraid it cannot afford them.

The cost of electricity is an example in microcosm of the custo Brasil. Although 70% of Brazil's installed capacity is cheap hydropower-by far the largest share of any big economy-Brazilian consumers pay some of the world's highest bills. A study by Firjan, Rio de Janeiro's Federation of Industries, last year found that the cost per kilowatt-hour was 50% higher than the world average, and more than double that in other big emerging economies. (The real has fallen since then, but by nowhere near enough to close that differential.) That pushes energy-intensive industries to site themselves elsewhere. Aluminium smelters are looking instead at neighbouring Paraguay-which gets its electricity from the Itaipu dam that also supplies a fifth of Brazil's electricity, but where the end price is far lower.< /SPAN>

Those bills are pushed up partly by transmission costs (most dams are far from the big cities in the south-east), and theft (though smart meters are reducing illegal connections, a hefty 13% of all electricity is not paid for by its user). But the biggest culprit is tax. In a recent report **Acende Brasil**, a research institute, calculated that tax makes up a whopping 45% of the average electricity bill. For other products, the average is 35%. And not only are the taxes built into the cost of electricity high; they are astoundingly complex. There are 28, half of which fall solely on electricity production. Those 14 are calculated on eight different bases: units of energy sold; maximum power output; gross profit; net profit; and so on. There are four different taxes with green aims.

The government has proposed cutting three taxes on electricity, and has said it will consider getting rid of a fourth. Industries complain that it would be better to renegotiate existing concessions when they come to a close in a couple of years' time: the government plans to renew the concessions without a new round of auctions. But even so, the National Confederation of Industries estimates that the tax cuts would reduce bills for businesses by 10-20%. Consumers would benefit too.

But this is only a start. Brazilian energy will still be pricey, and its taxes absurdly complex. The tax burden has risen from 22% of GDP in 1988 to 36% today, as more taxes are added and none is cut. The World Bank's annual Doing Business

study finds that simply paying taxes in Brazil takes a medium-sized firm around 2,600 hours annually. The global average is 277.