BRAZILIAN TAX REGIMES

PART I

ACTUAL PROFIT METHOD
AND ARBITRATED PROFITS

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After long discussions to define your business model, exhaustive analyzes of the flow of consumers to choose the location of your points of sale or commercial establishments, recruit and train employees, take risks in the election of your partners, pilgrimage in search of initial capital or loans free from abusive interest rates, go through marketing studies to determine the name, logo and visual identity; designing the delicate ecosystem of partners and suppliers, going through the exhausting bureaucratic process of setting up and regularizing their business, the entrepreneur, in short, can proceed in the, on his own, challenging management of his company. However, without counting less than five steps on his new journey, he comes face to face with a new obstacle – this one insurmountable for many – the choice of the company's tax regime, whose decision will govern, probably for a long time, the life of the company, its tax efficiency and determine the survival or not of its activity.

But how to choose your tax regime? The Brazilian Tax Regime is the system for defining and measuring the basis of calculation that a company must use to measure the taxes that will fall on its income, based on factors such as the size of the business, the amount invoiced, the origin of its income, and the activity of the company. Depending on some factors, the company's adoption of a certain regime will be mandatory. Otherwise, the entrepreneur is free to choose the tax regime that offers the best tax efficiency for the moment of his company.

The tax regimes of the Brazilian system are:

1 **Actual Profit Method**

2 **Arbitrated Profit**

3 **Deemed Taxable Income**

4 **Simples Nacional**

The definition of the adopted tax regime is of great importance for the fiscal efficiency of the company, because of the different advantages and disadvantages that each regime presents, in addition to being the system that will define the calculation of some of the taxes with the greatest impact on the balance sheet of almost all companies – taxes levied on income, such as the Income Tax (IRPJ) or the Social Contribution on Net Income (CSLL); as well as taxes on revenue, such as the dreaded PIS/Pasep and Cofins.

1

Actual Profit Method

It is the system in which the taxation calculation is determined by the actual profit method calculated by the company (hence the "actual" in the name), subtracting the revenues raised during the fiscal year by the costs and expenses that are permissible for the legal deduction. It is the only regime whose adoption is mandatory, that is, if your company does not fit the items that require the adoption of the real regime (better explained below), it means that your company can adopt any other regime.

This system has two calculation modalities, that is, the tax calculation period: **quarterly** and **annual:**

A Quartely

Actual profit method calculated quarterly.

The tax calculation takes place four times a year (until the end of March 31, June 30, September 30, and December 31). The disadvantage of this system is that the company can only offset the tax loss (negative tax result) from previous semesters up to 30%. This means that if the company suffered a greater tax loss in the 2nd semester, it would not be able to fully offset such a negative balance in the 3rd semester in which it collected a good result of profits. Thus, such a regime presents probable distortions in the taxed result against what was accounted for. However, the positive side is that the taxes calculated on a quarterly basis can be paid in up to 3 installments, whose value will be determined (as opposed to the monthly payment by estimate, as occurs in the annual calculation). However, this "advantage" must be viewed with reservation since the monthly payment entails adding interest from the 2nd installment. .

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B Annual

Actual profit method calculated annually

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Despite the term "annual", the calculation of this system occurs, against all expectations, monthly.

Such calculation occurs in 2 ways:

B1 by estimate, in which a percentage falls on the taxable amount (which can vary from 1.6% to 32% of the observed profit, depending on the company's activity)[1]. The disadvantage of such a system is that, depending on the activity carried out (such as services in general, which have the highest rate), it may result in a higher tax than the accounting calculated for the year. On the other hand, the advantage is that such a system facilitates and speeds up the calculation of a company. In case the company develops diversified activities (which fall on each one, different rates), the percentage corresponding to each activity will be applied.;

B2 by partial real profit, in which suspension or reduction balance sheets are prepared, month by month, with the values of the actual results earned by the company, which may result in a tax reduction[2]. The advantage is that it is possible to reduce the tax amount for a month when it is verified that the amount paid in the previous months already compensates for the proportional tax expected for the year. The disadvantage is the cost for the company to draw up monthly balance sheets or the indeterminacy of the tax amount, which fluctuates from month to month according to the year-to-date results (unlike what happens, for example, in the monthly amount of the tax calculated quarterly, whose value is already determined).

If your company presents one or more of these characteristics, the adoption of the taxable profit regime will be mandatory, for an example[3]:

I

Whose total revenue exceeds BRL 78 million (or proportional, when the company has less than 12 months of activity);

II

Whose activities are financial institutions, banking or not, as defined by the Central Bank, factoring, securitization of real estate, financial and agribusiness credits, among others;

III

Who have profits, income or capital gains from abroad; and

IV

Enjoy tax benefits related to tax exemption or reduction.

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[1] The complete list of the different rates in the quarterly calculation by estimate is available at the following link, subject to changes in legislation after this article's publication date.

[2] It is "Suspension" when the balance sheet indicates that the amount of taxes on the company's fiscal result accumulated up to the date of issuance has already been effectively paid in the past months. A "reduction" when the amount of the tax, based on the accumulated for the year, already exceeds the amount effectively calculated, reducing the surplus in the following months.

[3] The complete list of items characterizing the mandatory real profit is available in the following **link**, subject to changes in the legislation after the date of publication of this article.

2 Arbitrated Profit

Arbitrated profit is the regime often mentioned but little explored, largely because it is an exception regime, which occurs, especially when the company, improperly or fraudulently, adopts an incorrect taxation regime and fails to register its accounting files or does not prepare the financial statements required by law, calculates its earnings improperly, and fails to comply with certain requirements issued by the tax authority.

It is a regime that features two:

A Sanitation

to correct the lack of compliance with its tax obligations

and / or

B Punishment

Punishing the company that used illegal artifices to evade, defer or fail to comply with its tax obligations.

In these cases, as the name implies, the Public Power will arbitrate – determine, without room for discussion – the amount of tax to be paid by the company, using metrics defined in laws, such as: increase in the determined gross profit, tax history of the company, and estimation using supplier payroll and pay. In addition to the risk of leaving the Public Power the unilateral establishment of its tax debt, the arbitration of profit does not exclude the application of various penalties for non-compliance with tax rules. Thus, it is paramount that the company keeps its accounting routine, bookkeeping, and tax files up to date and r egularly fulfills all its legal duties.

FORMS OF DETERMINATION

All the tax regimes here are presented to calculate the taxable income base – the amount on which the income tax rate will fall.
The Deemed Taxable Income, Actual Profit Method, and Simples Nacional will determine the basis for calculating the IRPJ and CSLL.
Thus, regardless of the regime adopted, 15% of the IRPJ (plus 10% on the calculated amount that exceeds R$ 20 thousand per month) will be levied, and 9% of the CSLL.

Our recognitions

Análise Advocacia (2021)

Chambers & Partners Brazil (2021 & 2022)

Leaders League (2021 & 2022)

Transactional Track Record (2021 & 2022)

The Legal 500 (2022)

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