Recent increase in the Brazilian Presumed Profits Method cap allows more companies to elect the regime

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In brief

The Brazilian government recently published Provisional Measure No. 612 (PM 612), the provisions of which increase the gross revenue limitation for companies to elect the Presumed Profits Method (PPM) for computing Brazilian income tax. In accordance with the new rules, effective January 1, 2014, companies whose total gross revenues do not exceed BRL 72 million (approx. USD 35 million) may elect the PPM. The previous gross revenue cap of BRL 48 million (approx. USD 24 million) had not been adjusted since 2003.

This is an important change for US MNCs whose Brazilian subsidiaries either did not qualify for the PPM under the prior revenue cap, or that are seeking to invest in the country. The new limitation will allow more companies to elect the PPM. This may reduce bookkeeping and other administrative costs (i.e., because actual tax deductions are not relevant when determining taxable income) and, in certain cases, may result in a lower tax burden in Brazil.

In detail

The PPM

Brazilian companies may calculate and pay corporate income tax by electing one of two methods. The first method is the so-called actual profits (lucro real) method, pursuant to which tax payments are calculated based on actual net income (i.e., gross income less actual tax deductions). The second method is the PPM, which allows Brazilian companies to calculate tax payments based on a presumed taxable income base (i.e., gross income multiplied by statutorily provided margin percentages).

For purposes of the PPM, the margin percentages vary depending on the entity's activities:

- For corporate income tax purposes, the percentage is generally 8% for manufacturing companies and 32% for services companies.
- For social contribution tax purposes, the percentage is generally 12% for manufacturing companies and 32% for services companies.
- Note that other margin percentages may apply in certain cases.

Note that the computation of Brazilian PIS/COFINS taxes is generally different for companies that apply the PPM. Therefore, we recommend that taxpayers carefully model the corresponding indirect tax impact to assess whether they should elect the PPM. PIS/COFINS are taxes levied on gross income at the combined rate of 9.25%. Companies are entitled to PIS/COFINS credits after acquiring certain inputs and services (following a non-cumulative methodology similar to a value added tax). If the PPM is adopted, the PIS/COFINS combined rate is reduced to 3.65%, but the non-cumulative methodology is no longer allowed.

Some companies may not elect the PPM, for example: financial institutions; companies that earn profits, earnings or capital gains outside of Brazil; and companies utilizing certain tax exemptions/reductions.

The takeaway

The increase in the PPM revenue cap is a significant change that may impact Brazilian tax planning. US MNCs should consider whether and how the expanded revenue cap may affect the ability of their Brazilian affiliates to elect the PPM, and how they may effectively utilize the PPM in developing integrated global business structures that involve Brazil.

Let's talk

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