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Doing Business in Brazil

Abstract
[Excerpt] Imports into Brazil are subject to government controls from at least three sources: the Secretary of Foreign Trade (SECEX), which supervises registration and licensing, the Central Bank of Brazil, which approves the payments for financed imports, and the IRS, which supervises valuation for customs purposes. According to the new import regulations there are two kinds of importation: "automatically licensed importation" and "non-automatically licensed importation." In principle, goods submitted to the "automatically licensed importation" do not need any authorization from Brazilian authorities prior to their shipment to Brazil and clearance through customs.

Keywords
Brazil, foregn investment, trade, commerce, business, law, imports

Disciplines
International Business

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Doing Business in Brazil

Brazil

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2004

Doing Business in Brazil:

A Legal Brief 2004

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Importing into Brazil

Import Licensing

Imports into Brazil are subject to government controls from at least three sources: the Secretary of Foreign Trade (SECEX), which supervises registration and licensing, the Central Bank of Brazil, which approves the payments for financed imports, and the IRS, which supervises valuation for customs purposes.

As of January 1, 1997, a new system was created for purposes of controlling and authorizing imports, through the "SISCOMEX." The SISCOMEX is a computer system, which involves a network between the IRS, the Central Bank and SECEX, previously employed for Brazilian export, and as of January 1, 1997, used for imports as well. As the first step in the importation process, the proposed importer must register with the SISCOMEX.

According to the new import regulations there are two kinds of importation: "automatically licensed importation" and "non-automatically licensed importation." In principle, goods submitted to the "automatically licensed importation" do not need any authorization from Brazilian authorities prior to their shipment to Brazil and clearance through customs.

The "non-automatically licensed" importation, on the other hand, subjects the importation to the prior examination and special control by certain governmental agencies. The importer, before shipping the goods from abroad, or before customs clearance of the goods (at the discretion of SECEX), must secure SECEX registration of the importation. The cases of "non-automatically licensed" importation are provided for in Comunicado No. 37/97 and in the SISCOMEX.

Certain products are subject to approval and special control by particular governmental agencies. Such products include arms and ammunition (Military Ministry), herbicides, pesticides and beverages (Agriculture Ministry), and narcotic substances, human blood and food (Health Ministry).

SECEX may deny an import license whenever there is reason to believe that the effect of the importation may be to interfere unduly with free trade, to manipulate prices to the detriment of the Brazilian balance of trade, to constitute dumping or unfair competition or to pose a risk to the national economy. SECEX may also refuse to issue a license for products imported from countries that discriminate against Brazilian products.

Price Control

If an importer sets too low an invoice value on its goods for import, the government is deprived of its rightful share of duties and taxes; if it sets too high a value, the result may be an excessive remittance of foreign currency, in violation of exchange controls. For these reasons, SECEX strictly monitors the prices of imported products.

Accordingly, SECEX requires the Brazilian importer to submit the foreign exporter's price lists and catalogs. If no catalogs or price lists are published by the exporter, SECEX may accept a "pro forma" invoice. If SECEX believes that the prices quoted are not commensurate with international prices, it may require a statement from the exporter that the prices are in fact normal in the exporter's market.

SECEX will compare prices submitted by the exporter with prior import prices (if the products have previously been imported into Brazil) and with information provided by branches of the Banco do Brasil S.A. If SECEX determines that the importer is consistently over- or under-invoicing, SECEX may apply

penalties to the importer, ranging from suspension to cancellation of registration, thereby effectively preventing the importer from obtaining further import licenses.

In addition, if SECEX's price evaluation indicates that the prices are below normal international market levels prevailing under similar circumstances, it may set the price for customs duties and taxes at a higher level, as determined by SECEX's information sources.

Agents

Commission agents may be paid either in Brazil in the national currency, or abroad as part of the import price. No minimum or maximum percentage is set on commissions, although they seldom exceed 10 percent of the import value.

Local Similarity Test

To qualify for special tax or financial benefits or incentives, an import must meet the "local similarity test" *(teste de similaridade nacional*). This test is met when SECEX confirms that a similar product is not available in Brazil.

Imports of Used Products

Although used products may be imported, SECEX subjects them to very strict scrutiny to avoid fraud in connection with obsolete products. Moreover, used products may only be imported if the same or similar products are not available from Brazilian producers, and if their importation is of interest to the national economy.

Temporary Admission Regime

According to Law No. 9,430 of December 30, 1996, goods imported under temporary admittance will be subject to taxes levied on importation, based on the period the respective goods remain in the country. This provision is regulated by Decree No. 2,889 of December 21, 1998.

Bonded Warehouse

Importers may also deposit imported goods in public bonded warehouses. The product will remain in custody of the customs officials. The importer will pay no customs duties (but storage fees only) until the product leaves the bonded warehouse for consumption in the domestic market. The importer will pay no customs duties if the product is re-exported.

Leasing

International leasing is acceptable to SECEX under special financial conditions approved by the Central Bank of Brazil.

Exchange

Once the SECEX-approved products are effectively imported, the Brazilian importer will be allowed to exchange local currency for the currency agreed upon with the exporter and to pay the import price through regular banking channels. Imports payable according to terms longer than 360 days are subject to registration by the Central Bank of Brazil, through the "*Registro de Operações Financeiras*" ("ROF").

Taxes on Imports

Taxes or duties on imports consist of: import tax (II), due on the CIF import price at selective rates; excise tax (IPI), due on the import price grossed up by the import tax and based on selective rates; state sales tax (ICMS), due on the import price grossed up by the import tax, IPI and ICMS itself (rates of ICMS are eighteen percent (18%) in most states); and maritime transport fee (AFRMM), due on the value of freight [usually at the rate of twenty-five percent (25%)].

Taxes are based on the price negotiated between exporter and importer and approved by SECEX, plus import costs. Customs agents may question the tax basis, demand a higher basis for tax purposes and impose penalties on the importer, depending upon the circumstances.

Under-invoicing and over-invoicing are subject to a penalty of 100 percent of the under-/over-invoiced difference. Whenever the price quoted varies less than 10 percent from the normal value of the products, the customs agent may ignore this difference and not impose any penalties. If the price varies more than 10 percent from the normal value and does not constitute a case of fraudulent invoicing, the agent may impose a fine of 50 percent of the tax difference.

Freight

As a general rule, transportation for imports entering Brazil may be contracted with non-Brazilian flag carriers. There are some exceptions to this rule (e.g., importation with tax exemptions), in which cases the transportation must be contracted with Brazilian vessels.

Insurance

Coverage of imported goods must be provided by insurance companies established in Brazil. Brazilian importers may only contract FOB or C&F terms, not CIF or C&I, because the amount corresponding to the insurance may not be transferred abroad.

Latin American Integration Agreement

(LAIA or ALADI). Brazil is a member of the Latin American Integration Association (LAIA or ALADI), instituted by the Treaty of Montevideo of August 12, 1980. ALADI members grant preferential duty treatment to one another. The ALADI community includes Argentina, Bolivia, Brazil, Colombia, Ecuador, Mexico, Paraguay, Peru, Uruguay and Venezuela.

Southern Cone Common Market (MERCOSUL)

Brazil is also a member of the Southern Cone Common Market, or *Mercado Comum do Sul* (MERCOSUL). MERCOSUL is currently functioning as a free trade zone and a customs union. By the year 2006, it is expected to become a truly integrated common market. MERCOSUL now allows most goods and services to circulate among its members exempt from tariff and non-tariff barriers, and provides for a common external tariff *(tarifa externa comum*, or TEC) for most products that the member countries import from non-MERCOSUL countries. At this point, TEC does not yet apply to certain products such as computers, automobiles and capital goods. However, schedules for gradual harmonization of the tariffs have been agreed upon and should lead to a uniform TEC by target year 2006. MERCOSUL members are renegotiating bilateral treaties with other ALADI countries and negotiating treaties with the European community and with NAFTA. Eventually, other countries such as Bolivia, Chile and Venezuela may become participants in MERCOSUL.

Brazilian-Argentine Binational Corporations

On June 29, 1992, Brazil and Argentina executed the Treaty to Establish Brazilian-Argentine Corporations. The objective of this treaty is to provide economic integration between the two countries at the corporate level. This arrangement permits the free transfer of profits and employees between member states. Qualifying Binational Corporations and their subsidiaries and affiliates are treated as national entities of both Brazil and Argentina with respect to their legal rights and access to domestic sources of credit, financing and tax incentives. A Binational Corporation must be controlled by Brazilian and/or Argentine capital. Currently, local officials are directed to observe the treaty so as to permit Binational Corporations to operate in Brazil.

Manaus Free Trade Zone

The free trade zone of Manaus is designed to encourage manufacturing for export and local sales. Raw materials, parts and components imported into the Manaus free trade zone enjoy deferment of customs duties and exemption of federal excise tax (IPI). These benefits apply only to merchandise entering the free trade zone by Manaus Airport or Manaus Harbor. They do not apply to the importation of weapons and ammunition, perfumes, tobacco products, beverages or automotive vehicles.

Exporting from Brazil

Export License

Exports are also supervised by the Secretary of Foreign Trade (SECEX) and by the Central Bank of Brazil. SECEX is in the process of simplifying legal requirements for exporting. Currently, exporters must be registered on SISCOMEX, in an approved list of exporters supervised by SECEX. Once listed, an exporter may export by simply reporting the transaction to SECEX, with no need of further approvals.

Export Incentives

The Program for the Financing of Exports (PROEX) provides financing to exporters. Exporters may also benefit from exemption from the federal excise tax (IPI), immunity from the state sales tax (ICMS) and exemption from the social welfare taxes (COFINS and PIS). In addition, exporters may claim rebates for the amount paid for these social welfare taxes at the time when the raw materials were acquired.

Drawback Incentive

Another export incentive is available under the Drawback System (Comunicado SECEX No. 21 of July 11, 1997). This benefit takes the form of a deferral or exemption from taxes on importation of raw materials, semi-finished and finished products, parts and components utilized in the manufacturing of products for export.

Intellectual Property - Protection, Enforcement and Licensing

Introduction

The Industrial Property Law ("the IP Law") is the primary law in the area of patents, trademarks, industrial designs and geographical indications, and regulates registration thereof with the Brazilian Patent and Trademark Office ("INPI").

The IP Law is a modern statute, adapted to the most recent requirements of the World Trade Organization legislation related to industrial property rights (commonly referred to as TRIPS). In addition to affiliation to the WTO, Brazil is a member of several international conventions and agreements for the protection of industrial property rights, such as the Paris Convention and the Patent Cooperation Treaty, among others.

Patents

Patent Categories.

The IP Law provides for two types of patents: inventions and utility models. An invention is an original concept that represents a solution for a specific technical problem and may be industrially manufactured or used. An utility model is a new form introduced into a known product with practical purpose, improving its use or manufacture thereof.

Non-patentable Inventions and Utility Models.

Inventions and Utility Models. Inventions and utility models that are immoral, contrary to good practices or to public safety, order and health are not patentable. Likewise, substances or products of any kind resulting from the transformation of the atomic nucleus are not patentable. Besides, living beings, in whole or in part, are not subject to patent protection either, except for transgenic microorganisms which present the prerequisites of patentability and provided that they are not merely a discovery.

Prerequisites.

There are three prerequisites for the patentability of a creation: novelty, inventive activity and applicability for industrial use. In order to be granted patent protection, the invention must be considered new, i.e. not included in the state of art. The state of art comprises everything that has been made available to the public, either by written or oral description, by usage or any other means, in Brazil or abroad, before the filing date of the application. The requirement of inventive activity will be complied with whenever to an expert on the subject the invention does not result in an evident or obvious manner from the state of art. As a third prerequisite for patentability, the invention must be capable of being applied (i.e., used or produced) in the industry.

Priority.

A right of priority shall be granted to the application filed in a country which has entered into a treaty with Brazil or which is a member of an international organization of which Brazil is also a member, during the terms provided therein, such as the Paris Convention. According to the Paris Convention, the priority term is of one year for a patent of invention, and of six months for an utility model.

Validity.

The patent for inventions is valid for twenty years; and the patent for utility models, for fifteen years, counted as of the date of filing of their respective applications.

Scope of Protection

The patent provides its owner protection against unauthorized manufacture, use, marketing, sale or importation of the patented product, or of the process or product directly obtained from a patented process, by third parties, except when the unauthorized use is for non-commercial or experimental purposes that do not harm the patent owner's economic interests.

Compulsory Licenses

According to the IP Law, patents may be subject to compulsory licensing to be granted by the INPI or by the Federal Government in the following circumstances:

(i) if the patent holder exercises his rights in an abusive manner or exercises, through the patent, economic power abuse, which must be evidenced by an administrative or Court decision;

(ii) in case the patent is not fully exploited in Brazil within three years after the patent grant, due to any reasons other than lack of economic viability;

(iii) if the sale of the patented product or product obtained through a patented process does not meet the market's needs;

(iv) in case of a dependent patent that represents substantial technical progress vis-à-vis the original patent; or

(v) in case of national emergency or public interest (including interests related to public health and environmental protection), declared by the Federal Government, if the patent holder or licensee does not fulfill such needs.

Such compulsory licenses may be requested by any interested third party, provided that such third party is technically and economically qualified to carry out the efficient exploitation of the patent. The products resulting therefrom must be earmarked mostly for the Brazilian domestic market. Compulsory licenses will be granted only on a non-exclusive basis.

Certificate of Addition

The IP Law also provides protection for an improvement or development introduced into the subject matter of an invention by granting a Certificate of Addition, which is added to the patent's certificate. The certificate's validity shall be the same validity of the corresponding patent.

Extinction of Patent Rights

In addition to the extinction of the patent protection due to expiration of its validity term, the waiver, lack of payment of any annual fee, forfeiture for failure to cure the abuse or misuse of the patent or the lack of appointment of an attorney in Brazil to receive summons, will cause the extinction of the patent.

Industrial Designs

Creations Susceptible of Registration

An industrial design is a bi-dimensional representation (ornamental assembly of lines and colors) or tri-dimensional object (ornamental plastic form) that may be applied to a product, affording a new and original look in its external configuration and which may be used for industrial production.

Prerequisites

The prerequisites for the registration of an industrial design are novelty and originality. The definition of novelty is the same applied to patents. The prerequisite of originality shall be met if the industrial design has an original and distinct visual configuration when compared to other previously known objects. A common or ordinary form of an object, or those determined by technical or functional considerations, are not considered industrial designs. Immoral designs do not qualify for registration.

Validity

The registration is valid for ten years and may be renewed for three successive periods of five years each, and a fee must be paid each five years.

Trademarks

Signs Susceptible of Registration as Trademark.

Any visually perceptible, distinctive sign not prohibited by law qualifies for registration as a trademark. The IP Law has permitted registration of tridimensional trademarks but audio or olfactory trademarks do not qualify for trademark protection in Brazil.

Signs not Susceptible of Registration as Trademark

The following, among others, cannot be registered as trademarks: any expression or sign which is immoral, offensive or discriminative; signs commonly used to describe the nature of a product or service; advertisement slogans and colors; false indications of geographical origin; civil names or signatures, except upon consent of the holder of the right; technical terms used in connection with the product or service; reproduction or imitation of a mark belonging to a third party for identical, similar or related products; common or necessary form or packaging of the product; and the reproduction or imitation of a mark that cannot be ignored by those that work in the field of activity in which the trademark is used.

Trademark Categories

Trademarks are divided into three categories: (i) products or service marks used to distinguish a product or service; (ii) certification marks, used to assert the compliance of the product or service with certain standards of quality or technical specifications; and (iii) collective marks, used to identify products or services originated from members of a certain group.

Validity.

Trademarks are registered for a ten-year period, renewable for identical terms.

Prerequisites

Any individual, private or public entity may apply for the registration of a trademark in Brazil, provided that the applicant may only claim classes related to the business activity in which he is engaged, directly or through controlled companies. The applicant for a collective mark must be a legal entity that represents the collectivity, and the applicant for a certification mark may only be a person without commercial or industrial interest in the certified product or service.

Priority.

A right of priority will be granted to the application filed in a country which has entered into a treaty with Brazil or which is a member of an international organization of which Brazil is also a member, during the terms provided therein. The priority term provided in the Paris Convention for trademarks is of six months.

Famous and Well-Known Marks

Special protection shall be afforded to a registered trademark deemed famous in Brazil, covering all classes of products and services. The trademark considered well-known in the field of activity in which it is used, pursuant to the Paris Convention, is also afforded special protection, regardless of whether it has been previously filed or registered in Brazil. This also applies to service marks.

Geographical Indications

According to the IP Law, the following qualify for protection as geographical indication and may be registered with INPI: (i) geographical names of countries, cities or regions which became known as centers for extraction, production or manufacture of a certain product or rendering of a certain service; or (ii) geographical names used to designate products' or services' qualities or features due exclusively or essentially to the geographical environment. The name of a geographical region commonly used to designate a product or service will not be considered a geographical indication. Only those manufacturers or services provider that are actually established in the geographical area shall be allowed to use the corresponding geographical indication.

Copyrights

Scope of Protection and Requirements

The Brazilian Copyright Law provides for the protection of intellectual works arising out of human creation and expressed in any physical media, such as literary, artistic, scientific or photographic works, architectural projects, designs, paintings, among many others. The protection of copyrights in Brazil does not depend on registration of the work with any governmental authority. Notwithstanding, the author may register the work to indicate, among others, the date of creation of the work. Copyrights in Brazil comprise the economic rights of author and the moral rights. The moral rights cannot be licensed, transferred or waived. As to the economic rights of author, the protection of copyright lasts for seventy years as of January 1st of the year following the author's death or as of the work's first publication, in case of anonymous or pseudonymous works, audiovisual and photographic works.

Limitations to the Author's Rights.

According to the Copyright Law, the following actions, among others, do not represent infringement of copyright: (i) reproduction in the daily press of news or articles previously published, provided that the author's name (if signed) and the original publication are mentioned; (ii) reproduction, in only one sample, of small parts of the work for private use of the person who made the copy, provided that the copy is made by himself with no profit purposes; (iii) use of literary, artistic or scientific works, phonograms and television and radio transmission in commercial establishments, exclusively for the purpose of demonstration to customers, for establishments that commercialize the equipment or supports that allow such use of the works.

Software

Scope of Protection and Requirements.

The Software Law grants software copyright protection and defines computer program as "the expression of an organized set of instructions in natural or codified language, contained in a physical media of any kind, and necessarily applied in automatic machines for information processing, devices, peripheral instruments or equipment, operated under digital or analogue techniques which make them work in a certain way and for a certain purpose". In spite of the same protection regime applied to copyright, the Software Law provides that the moral rights of author do not apply to computer programs, except for the right of the software creator to assert its authorship and to oppose unauthorized alterations of the software that may damage his honor and reputation. The protection of software does not depend on registration of the program and lasts for fifty years, as of January 1st of the year following the publication or creation of the software. The author may however register the software and, in this case, the application for registration must be filed with INPI. In case of any transfer of technology of software, registration of the related agreement with INPI is then required and the delivery of the complete documentation, source code and additional information by the supplier to the technology recipient is mandatory under the law.

Limitations to the Author's Rights.

According to the Software Law, the following actions do not represent infringement of the copyright holder over the software: (i) reproduction of one copy of the software, by the one who acquired a legal and regular program, for back-up or electronic storage; (ii) citation of part of the software for educational purposes, provided that the protected work and its author are indicated in the citation; (iii) similarity between computer programs, arising from functional characteristics of their application or from the compliance with legal and technical requirements; (iv) integration of the software with an application or operational system that is technically essential for the user's needs, provided that the software's basic characteristics are maintained and that the integration is for the sole use of the person who carried it out.

Enforcement of Intellectual Property Rights in Brazil

The intellectual property laws also include provisions pertaining to crimes and violations of rights and provide for remedies in case of infringement of intellectual property rights. Below are examples of the most useful remedies available:

Extra-judicial cease-and-desist letter.

The purpose of the cease-and-desist letter is to make the infringing party aware of the corresponding violation and it may also constitute an effective mean of obtaining a settlement between the parties.

Judicial cease-and-desist letter.

The purpose of such cease-and-desist letter is also to make the infringing party aware of the violation. However, the judicial cease-and-desist letter may be a more effective tool to obtain a settlement with the infringing party, due to its official and judicial character.

Administrative Appeals.

The administrative appeals are used during the period of examination of applications for registration of industrial property rights with INPI, or immediately after such rights are granted. The competent agency to receive and decide on said appeals is INPI.

At the administrative level, a patent, trademark or industrial design may be declared null and void in the event of any formal flaw in the registration proceedings. The INPI may initiate the nullity proceeding itself or upon request of any third party having a legitimate interest, within a term of six months counted from the date of grant (for patents and trademarks) and five years from the date of grant (for industrial designs). The industrial property owner may reply to such declaration and the President of INPI shall decide the appeal, closing the administrative level.

In addition to such nullity proceedings, legal nullity action may be pursued before a Federal Court, as you may see in the next item below..

Preliminary Search and Seizure procedures

The owner of an intellectual property right (either copyright and software, or industrial property rights - i.e., trademarks, patents and industrial design) has two different avenues to obtain a search and seizure order regarding the infringing products: (a) the criminal procedure, in which the seizure will be limited to the number of samples of the counterfeit product sufficient to allow a technical examination, in the cases of crimes against intellectual property rights and unfair competition. In cases of crimes against copyright and trademark (when the imitation of the trademark is obvious), all the products illegally produced or reproduced are object of the seizure; and (b) the civil procedure, in which the seizure will include all the counterfeit material, related manufacturing equipment, molds, packaging and advertising materials.

Injunctions.

It is possible for intellectual property rights owners to obtain injunctions against infringers so that they are forced to cease the manufacturing, launching, use, reproduction, offering for sale, sale or import of the infringing products in the market, either in order to prevent irreparable harm caused by the infringement and the delay in having a final court decision, or to anticipate the effects of the final decision in view of strong evidence that plaintiff's claim is well-grounded. In both cases, strong evidence of the alleged infringement and of potential irreparable harm to the plaintiff must be submitted to the judge.

Ordinary Civil Lawsuit.

An ordinary civil lawsuit is usually filed against the infringing party for three purposes: (i) discontinuance of any unauthorized use of the corresponding intellectual property right; (ii) imposition of a fine for noncompliance with the discontinuance of the use thereof; and (iii) compensation for losses and damages caused by reason of the counterfeiting.

With regard to the collection of losses and damages, the IP Law establishes that the loss of profits is determined by the following criteria, whichever is most favorable to the industrial property right owner: (i) the profits that would have been obtained by the industrial property right owner if the infringement had not taken place; (ii) the profits obtained by the infringing party; or (iii) the compensation that the infringing party would have paid to the industrial property right owner for a license that would have allowed it to lawfully exploit the object of the rights.

Crimes against Industrial Property and Unfair Competition

The IP Law provides for the following criminal penalties in case of violation of industrial property rights: (i) imprisonment from three months to one year, or a fine, in case of (a) unauthorized use or manufacture of products subject matter of a patent; (b) reproduction or alteration of a trademark; and, (c) manufacture of products subject matter of industrial design; and (ii) imprisonment from one to three months for other cases such as use of trademark or advertisement expression to indicate false origin of a product, or use of false geographical indication. Such penalties may be increased when the violating party is a sales representative/agent; an authorized individual, company, partner or employee of the industrial property owner or its licensee, and also if the violated trademark is famous, well-known, certified or collective mark.

The IP Law also treats as crimes certain unfair competition practices, such as the disclosure or employment of fraudulent means or false statements for the purpose of obtaining an advantage via-à-vis a competitor; the diversion of clientele; the deliberate misleading of the consumer; the unauthorized use of a third party's corporate name or confidential information, and other fraudulent actions. The IP Law provides for a penalty of imprisonment of three months to one year, or a fine. The above-mentioned actions, as well as other actions of unfair competition not defined as crimes, are subject to civil lawsuits and may entitle any competitor harmed by such practices to losses and damages.

In such crimes, the prosecution of the infringer depends on the request of the holder whose rights were violated.

Crimes against Copyrights

The Criminal Code establishes that the partial or total reproduction of a copyrighted work with economic purpose, without express authorization of the author, constitutes a crime and subjects the agent to a penalty of two to four years of imprisonment. The same penalty applies to the one who distributes, sells, offers for sale, rents, introduces in the country, acquires or keeps in storage, original or copy of a copyrighted work reproduced in violation to the author's rights. In both cases, the Public Attorney may initiate the criminal

claim, taking into account the relevant public interest involved in the issue, regardless of the initiative of the victim.

A penalty of two to four years of imprisonment is applied to the one who offers, without the author's or performer's express authorization, to the public any the copyrighted work by means of cable, optical fiber, satellite, waves or any other system.

The Software Law also establishes that the violation of software copyrights is a crime, and shall subject the infringer to a penalty of imprisonment from six months up to two years or fine. In case such violation consists in the unauthorized reproduction of the software (or part thereof) for purposes of resale, the penalty shall be of imprisonment from one to four years and penalty..

Parallel Imports into Brazil.

"Parallel import" is the non-authorized importation of an original product covered by a patent and/or trademark by a third party other than the legitimate holder of such patent and/or trademark or authorized licensees or distributors.

The Brazilian IP Law has adopted the national exhaustion of rights, that is, the owner of a Brazilian patent cannot impede the sale or use of a patented product or a product manufactured under a patented process if such product was placed in the Brazilian market by the patent owner or with his consent.

The same principle applies with regard to trademarks. The IP Law sets forth that the trademark owner cannot prevent the free circulation of a product bearing its trademark, if such product was introduced in the Brazilian market by the trademark owner or by a third party, with the trademark owner's consent (except for certain specific situations regarding patented products subject to compulsory license or which manufacture in Brazil is not economically feasible).

Therefore, in case of parallel import, *i.e.* if the owner of the patent or trademark has not imported nor consented with the importation of a legitimate product into Brazil, manufactured under his patent or bearing his trademarks, the patent or trademark owner or authorized licensee may prevent the importation, seize the imported products and/or claim damages, depending on the factual verification.

Customs' Control

The IP Law establishes that products bearing false, modified or imitated trademarks or that bear false indications of origin may be seized by customs officers at the time of clearance, or upon the request of an interested party.

A different situation encompasses "gray market" products, which are those products resulting from parallel import. As these products are not counterfeit, their import into Brazil does not constitute a crime, and consequently the customs officers cannot seize these products without a specific judicial order for this purpose.

Intellectual Property Licenses and Transfer of Technology

Types of agreements subject to registration with INPI

Supply of Technology Agreements

Agreements that imply in transfer of technology must be registered with INPI to be effective vis-à-vis third parties. INPI does not accept technology licenses and understands that the technology is permanently

transferred to the Brazilian recipient. In view of that, INPI usually imposes certain restrictions in connection with the confidentiality and term of the agreements, among others.

Brazilian laws limit the tax deduction of payments remitted in consideration for supply of technology. This limit varies according to the industry involved, reaching a maximum of 5%, calculated upon net sales of the products manufactured or the services rendered under the agreement, and includes payments in consideration for the transfer of technology, rendering of technical assistance and licensing of patents and trademarks in aggregate. In case of an agreement entered into with a foreign related company, the same percentage applies as a limit for remittance of payments.

Specialized Technical Services and Technical Assistance Agreements.

This category includes agreements for the rendering of services that involve technology transfer (technical assistance agreements for the incorporation/absorption of the technology by the recipient company), or services related to the main industrial activity of the recipient company (specialized technical services in connection with the engineering project for a manufacturing facility, start-up of a production line or assembly and installation of industrial equipment, among others). They are also subject to registration with INPI. Specialized technical services agreements entered into with a related company headquartered abroad are subject to the Brazilian transfer pricing rules.

Patent License Agreements

Agreements for the license of patents applied for or granted in Brazil must be registered with INPI to be effective vis-à-vis third parties. The deduction and remittance caps mentioned above for supply of technology agreements also apply to the remittance of payments abroad in consideration for patent licenses.

Trademark License Agreements

Agreements for the license of trademarks registered or applied for in Brazil are subject to registration with INPI. Tax deduction of royalty payments for trademark licenses is capped at 1% of the licensee's net sales. In case of trademark license agreements entered into with a foreign related company, INPI will only allow the remittance of royalties in consideration for the trademark license provided that the use of the trademark is not directly connected to products or services manufactured and/or rendered under a supply of technology, technical assistance and/or patent license agreement (in force) between the parties.

Franchise Agreements

Franchise has been legally defined as the system through which a franchisor grants to a franchisee the right to use his trademarks or patents, along with the exclusive or semi-exclusive right to distribute products or services and, in some cases, also with the right to use the technology for the implementation and management of specific businesses or operating systems developed by the franchisor. Franchise Agreements are subject to registration with INPI to be effective vis-à-vis third parties. The Franchise Law sets forth franchisor's obligation to convey to the potential franchisee the corresponding franchise offering letter with certain information on the franchise, which must be delivered to the franchisee at least ten days before the execution of the contract (or letter of intent) or before any payments from the franchisee to the franchisor.

In case of an agreement with a foreign licensor or supplier of technology, the registration with INPI is also a condition precedent for the remittance of payments abroad and deduction of payments by the Brazilian licensee or recipient. After registration with INPI, such agreements must also be registered with the Central Bank of Brazil, as they call for payments in foreign currency.

Types of agreements not subject to registration with INPI

Professional Services Agreements

Agreements for the rendering of professional, consulting, administrative, financial or managerial services are not subject to registration with any Brazilian Governmental authority. Payments thereunder may be remitted at the floating rate of exchange through any commercial bank authorized to perform exchange operations upon presentation of the Agreement, its translation into Portuguese and the corresponding invoice. In order to qualify as professional services, these services cannot involve any license of intellectual property, transfer of technology or production of intellectual (scientific) knowledge. Professional services contracted abroad between related companies are subject to the deductibility limits established by the Brazilian transfer pricing rules.

Copyright Agreements

Except for certain specific cases, copyright agreements (such as editing agreement, agreement for assignment of rights, production agreement, agreement for future work of art, representation and execution agreement, among others) are not subject to registration with any Brazilian governmental authority, and the applicable copyright fees may be remitted abroad without any registration. The regulation for such remittance is less strict than the rules covering the remittance of royalties and technical assistance fees, although the amount of the remittances may be reviewed by the Central Bank of Brazil as part of foreign exchange controls and by tax authorities. Certain types of copyright fees must be approved by governmental agencies, such as those related to audiovisual works. Copyright agreements contracted abroad between related companies are subject to the Brazilian transfer pricing rules.

Software Agreements

Software may be licensed in Brazil either (i) directly by the holder of the rights on the software or authorized licensor to end users or (ii) through a reseller, distributor or other similar vendor. In both cases, registration of the relevant agreement is not required.

Software license, maintenance and customization fees may be remitted abroad without any specific approval. There is no limit for the fees that may be remitted abroad under software agreements, provided however that, if the agreement is entered into between related companies, Brazilian transfer pricing rules shall apply.

Relevant Tax Burdens on Intellectual Property-Related Transactions

Withholding Income Tax

Payments made to non-residents in consideration for the license of patents and/or trademarks, technology transfer, technical assistance and specialized technical services, as well as in consideration for consulting and/or professional services that do not involve transfer of technology, license of software and/or copyrights are subject to the withholding income tax, currently levied at a general rate of fifteen percent (except for Treaties to avoid Double Taxation entered into between Brazil and other countries that set forth a lower rate). The remittance of certain types of fees may be subject to different tax rates, such as fees for professional services that do not qualify as administrative assistance, which are subject to a twenty-five percent rate. The foreign company/recipient of payments abroad is the legal taxpayer of the withholding income tax, and the Brazilian company or individual is responsible for the payment. However, it is possible to establish in the agreement that the Brazilian company or individual shall bear the costs of such tax by grossing up the fees.

Contribution for Intervention in the Economic Domain ("CIDE")

Payments made to non-residents in consideration for: (i) supply of technology, (ii) technical assistance (technical assistance services and specialized technical services), (iii) technical services, administrative assistance and other similar services, (iv) trademark license and assignment, and (v) patent license and assignment are subject to the Contribution for Intervention in the Economic Domain ("CIDE"), levied at a rate of ten percent. CIDE is due by the Brazilian Company or individual and may not be deducted from such remittances of payments. Brazilian laws grant a credit of CIDE solely for remittances of payments under trademark and/or patent license agreements, to be used in future CIDE payments. Such credit is of seventy percent until 2008 and thirty percent until 2013. The scope of incidence of CIDE has been controversial with regard to remittances of payments abroad in consideration for software and copyright licenses, and depending on the circumstances, the Federal Revenue authorities understand that CIDE shall apply to such remittances as well.

Service Tax ("ISS")

The Service Tax is a Municipal Tax, levied and regulated by each city, but under a common umbrella of Federal legislation, that lists the services that trigger the ISS. ISS shall be levied on services rendered in Brazil and on "importation of services", i.e. services originating from abroad or which rendering was initiated abroad. The exportation of services shall not be subject to ISS, except for services developed in Brazil, which results occur in Brazil, even if the payer is a foreign resident. In what regards intellectual property-related transactions, the most relevant services currently on the list are: information technology and similar services; research and development services of any nature; license of the right to use trademarks and slogans; installation and assembly of devices, machines and equipment; programming and visual communication; biotechnology services; services related to art works made for hire; and broadcasting of music, films, musicals and similar. The levy of ISS on some of the items of the list, e.g. trademark license, may give rise to questioning, on the grounds that in principle they do not qualify as rendering of services (which is the basis for collection of the ISS tax). ISS rates may vary from two percent to five percent.

Contribution to the Social Integration Program and Contribution for Social Security Financing on Importation ("PIS/COFINS Import")

The PIS/COFINS Import Law, effective as of May 1, 2004, provides for the levy of the PIS/COFINS Import on the import of goods and services, as a general rule, at a total rate of 9.25%. Pursuant to the PIS/COFINS Import Law, the triggering event for payment of such taxes shall be (i) entrance of foreign goods into the national territory, as well as the (ii) payment, credit, delivery, use or remittance of amounts abroad in consideration for services rendered. As a general rule, the PIS/COFINS Import is due by the Brazilian company or individual that contracted the services or imported the goods. The contributions apply on the total value of the imported goods including State Value-Added Tax ("ICMS") and the amounts of the contributions themselves (PIS and COFINS Import). In cases of importation of services, the contributions apply on the amount paid, credited, delivered, used or remitted abroad, calculated before the Withholding Income Tax, plus the ISS and the amounts of the PIS and COFINS Import as well. Unlike the ISS, the PIS/COFINS Import Law does not provide for a list of the services subject to such contributions, and there is still no official understanding from the tax authorities. Notwithstanding, at least in principle PIS/COFINS Import may be applicable on certain intellectual property-related transactions, especially software and trademark licenses, as they are already deemed services for purposes of the ISS Law.

Contribution for Development of National Cinematographic Industry ("CONDECINE")

Aiming at promoting Brazilian movie industry, the Contribution for Development of the National Cinematographic Industry is levied at a rate of eleven percent, on payments made to non-residents in

consideration for the exploitation, acquisition or importation of cinematographic and videophonographic works. CONDECINE is also levied once every five years, at a varying rate calculated according to the market segment and the scope of exhibition of audiovisual works, on the exhibition, production, licensing and distribution of cinematographic and videophonographic works with commercial purposes.

Financial Tax ("IOF")

Previously, a financial tax of twenty-five percent was imposed on the net remittance of royalties, copyrights, software, technology, technical assistance and professional services fee payments to a foreign company. The IOF tax rate has been reduced to zero as of June 1997 for payments made under all said agreements.

Other Intellectual Property Rights

Brazilian Biological Diversity And Traditional Knowledge.

Brazil is a party to the Convention on Biological Diversity, and the Brazilian Government enacted a Provisional Act in 2001 to regulate the Brazilian biological diversity and incorporate the principles and purposes of the Convention. The Provisional Act establishes that the access to any genetic resource existent in Brazil and to any traditional knowledge associated thereto for purposes of scientific research, technological development or biodiversity prospecting is subject to the prior authorization of the Brazilian Genetic Heritage Management Council ("Conselho de Gestão do Patrimônio Genético - CGen").

Such access shall only be authorized to Brazilian public or private institutions, which perform research and development activities in the biological field and alike. The participation of foreign companies in expeditions to collect samples of any component of the Brazilian genetic heritage and to access any traditional knowledge associated thereto shall only be authorized if it occurs jointly with a public national institution, that must coordinate the activities.

Additionally, if there is any perspective of commercial use of the genetic resource and/or the traditional knowledge associated thereto, it is also necessary to execute an "Agreement for Use of Genetic Heritage and Benefit-Sharing". The Agreement must establish, among other things, a fair and equitable share among the parties of benefits arising out of the economic exploitation of the product or process resulting from the access. The benefit-sharing may be made by the sharing of profits, the payment of royalties, the access and transfer of technology, the license, free of charge, of products and processes, among other means. In cases the Brazilian Government is not party to the Agreement, it shall also be entitled to receive a part of said benefits. In order to be effective, the Agreement of Use of Genetic Heritage and Benefit-Sharing must be submitted to the CGen for approval and registration purposes.

The economic exploitation of products or processes developed from samples of any component of the Brazilian genetic heritage or associated traditional knowledge accessed in violation of the provisions of the Provisional Act shall subject the infringer to the payment of damages corresponding to, at least, twenty percent of the gross revenues obtained in the commercialization of the relevant product or of the royalties obtained from third parties due to the licensing of the relevant product, process or use of the technology, in addition to the applicable administrative and criminal penalties.

Domain Names.

Domain names at the top level ".br" are granted by the Research Support Foundation of the State of São Paulo ("FAPESP"), by delegation of the Managing Committee for Internet of the Ministries of Communication and Science and Technology. FAPESP created several top level domains corresponding to certain types of activity, such as ".com.br" for commercial purposes, ".ind.br" for industries, ".org.br" for non-profit organizations, etc. The registration of ".br" domain names is conducted electronically.

Brazil adopts the "first-to-file" system. Therefore, apart from official names, offensive names and a very limited list of notorious trademarks, any combination of at most twenty-six words and numbers may be registered at the top level domain name "br". Any individual or entity may register an unlimited number of domain names at the same top-level domain. However, FAPESP sets forth additional requirements for foreign individuals or entities, such as the obligation of a foreign entity to initiate its activities and establish a local presence in Brazil within one year as of the registration of the domain name.

Plant Varieties.

The protection of intellectual property rights related to plant varieties is accomplished by the granting of a Plant Variety Protection ("PVP") Certificate. For purposes of legal protection, the plant variety must be a superior vegetable variety of any type or species, clearly distinguishable from other known plant varieties by a minimum number of features, and must also have a distinguishing denomination and be homogeneous and stable with regard to its features throughout successive generations.

In order for a plant variety to be granted legal protection, it must be new or essentially derived from another variety.

The government agency responsible for the protection of plant varieties (National Service for Plant Varieties Protection - SNPC, of the Ministry of Agriculture and Supply) shall gradually publish the vegetable species and the minimum features necessary for an application for plant variety protection.

The PVP Certificate is valid for fifteen years, counted as of the date of granting of a provisional certificate of protection by the SNPC, except for vines, fruit trees, forest and ornamental trees, for which the term of protection shall be eighteen years. After the expiration of the Certificate's validity term, the variety's ownership will become public. The PVP Certificate provides protection against the unauthorized growing of the material, propagation of the variety for commercial purposes, as well as against marketing or offers for sale without authorization of the owner. However, such exclusive rights of the owner of the protected plant variety shall not be deemed infringed in case one: (i) stocks or cultivates seed for his own use; (ii) uses or sells the product obtained from the plantation of the variety as food or raw material (except for reproduction purposes); (iii) uses the variety as basis for variation in genetic improvements or scientific researches; or (iv) is a small rural producer and multiplies seeds for donation or exchange, exclusively for other small rural producers, within the scope of financing or supporting programs for the benefit of small rural producers, conducted by public entities or non-governmental agencies authorized by the Public Administration.

Trade Secrets.

In Brazil the protection of trade secrets does not grant the owner proprietary rights over the information: the protection exists to prevent the trade secret from being disclosed, exploited or used without authorization. This conduct may be characterized under Brazilian law as unfair competition. The IP Law characterizes a trade secret's unauthorized disclosure, exploitation or use as an unfair competition crime that entitles its legitimate holder to claim for losses and damages arising therefrom. Nevertheless, if a third party, by its own independent means, develops the same trade secret, it will also be its legitimate holder.

The nature of the information constituting a trade secret is not relevant for legal protection in Brazil, as the term "trade secret" is not defined by law. The information can be of technological, commercial, administrative, economic, fiscal or whatever nature, provided that it has economic value. Certain kinds of information cannot qualify as trade secrets, such as information obtained illegally by the owner, information of an unlawful nature or information that is obvious to a person skilled in the art or already in the public domain.

Trade secret protection is granted by the Brazilian Courts on a case-by-case basis. The central issue is usually the characterization of the disclosed information as a trade secret. For that purpose, the value of the information derives from its secrecy. Thus, the company's internal policies on the handling and confidentiality of its relevant information are of utmost importance.

Genetically Modified Organisms.

Brazilian Biosafety Law establishes a set of rules aiming at controlling the use of genetic engineering techniques for the development, breeding, handling, transportation, marketing, consumption, release and discharge of Genetically Modified Organisms ("GMOs") into the environment, for the protection of human, animal and plant life and health, as well as the environment. For purposes of said law, a GMO is any organism which genetic material has been modified by any technique of genetic engineering.

The Biosafety Law determines that the release of any GMO into the environment shall be subject to a prior authorization from the Brazilian National Technical Committee for Biological Safety - CTNBio. Further to said authorization, any company willing to develop activities in connection with biotechnology in Brazil, including research, development of technology and industrial production, must obtain a Certificate of Biosafety Quality and create an Internal Committee for Biosafety.

The importation of GMOs or product containing GMO into Brazil is subject to the authorization of the Ministry of Agriculture, which, in turn, depends on a technical opinion to be issued by the CTNBio. In order to import genetically modified vegetables or plants, the importer must also obtain from CTNBio a Certificate of Biosafety Quality and submit an import request to the Vegetal Inspection and Protection Department of the Ministry of Agriculture, detailing the exact quantity of such GMO's to be imported and the place in which research will take place. As soon as the GMOs enter into the country, they must be sent to the National Center of Genetic Resources and Biosafety for laboratory tests prior to their release to the importer.

Additionally, some environmental licenses may be required, such as the License for Operation in Research Areas, among others.

Forms of Doing Business

Introduction

As a general rule, Brazilian law does not prohibit or restrict the participation of foreign investment in business activities. Except for certain limitations, foreign investors are free to establish any business in Brazil.

Those few areas in which foreign investment is either totally prohibited or limited to a certain minority interest include certain telecommunications services and media. In these restricted areas, foreign investors are required to enter into joint venture types of arrangements with Brazilian companies or individuals or organize a subsidiary company under the Brazilian laws. Foreign investors sometimes adopt joint venture arrangements even in situations that are not restricted, for instance, when they seek the experience and expertise of locals in the domestic market.

A business presence in Brazil may, at least in principle, take the form of either (a) a branch, representative office or agency of a foreign business entity, or (b) a company organized under the laws of Brazil.

Branch, Representative Office or Agency of Foreign Business Entity

Though permits to establish branches of companies organized under the Brazilian laws are freely granted, the prior authorization of the President of Brazil is required to establish a branch of a foreign company. The granting process is entirely discretionary and lengthy (more than six months). In addition, adverse liability and tax consequences render this choice not advisable in most cases.

Local Business Entity

The establishment of a business entity in Brazil generally does not require any prior governmental approval. Most non-resident investors have found advisable to organize it according to the following two forms of companies: (a) *sociedade anônima* ("S.A."), in which liability is limited to the amount of the capital invested; and (b) *sociedade limitada ("limitada*"), which may be a more flexible form of a limited liability company, where the liability is limited to the total amount of the company's capital.

The basic requirements of a S.A. are as follows:

Shareholders: There must be at least two; no residency or nationality requirement applies.

Capital: At least ten percent (10%) of the stated capital must be paid in with cash at the time of incorporation. No minimum is required except to carry out certain regulated activities, e.g., banking, insurance and trading companies. The capital of a S.A. is divided into shares. According to the rights attributed to their holders, the shares may also be qualified as common or preferred. The number of preferred shares without the right to vote or with restrictions on the exercise of such a right shall not exceed 50% of the total number of shares issued by the company. As per S.A.'s law provisions, holders of preferred shares may not have voting rights, or they may have their voting rights restricted. However, the holders of preferred shares with no or restricted voting rights are entitled to certain financial rights, such as the priority (i) to receive dividends; (ii) to receive the reimbursement of capital, with or without bonus; or the accumulation of these aforementioned advantages. For publicly-held companies, the corporate legislation provides more protecting rules for the minority shareholders of preferred shares.

Management: The S.A. must be managed by at least two officers (*diretores*) who shall be residents in Brazil. Residency can be obtained for expatriates to be appointed as officers of a Brazilian S.A. A Board of Directors (*conselho de administração) is not required,* unless the S.A.: (a) trades its shares in the stock exchange or in the over-the-counter markets; (b) issues debentures at the market; or (c) has an authorized capital. Brazilian residence is no longer a requirement to take office in the position of member of the Board of Directors, provided that an attorney-in-fact resident in Brazil be appointed and vested with powers to receive services of process on behalf of a non-resident Director. According to the law, the Board of Directors must have at least three members, who shall hold at least one share.

Audit: The By-laws of the S.A. must provide for a shareholders' auditing committee *(conselho fiscal)*, which may be installed at a shareholders' meeting. If the auditing committee is so installed, its annual report to the shareholders must be published together with the S.A.'s financial statements, except if the conditions mentioned in the following item are complied with.

Meetings and publications: Shareholders' meetings must be held annually (e.g., to approve the financial statements) within the first four months after the end of the company's fiscal year. Calls for meetings must be published unless all shareholders attend or are represented at the meeting when the call is waived. The minutes of the meetings shall also be published. Special meetings (e.g., to amend the By-laws) shall follow the same procedure. Balance Sheets and Financial Statements must be published .Closely held S.As. with fewer than twenty (20) shareholders and with a net worth up to R$1,000,000.00 (one million Reais) are not required to publish their financial statements, balance sheets, auditing committee's annual reports and

certain other information, provided that certified copies thereof are filed with the Commercial Registry together with the minutes of the general meeting containing the decisions thereto.

The Brazilian Civil Code effective as of January 11, 2003 introduced significant changes in the corporate legislation, especially in connection with the *limitadas*. The *limitadas* lost some of their main advantages, as to simplicity of organization and flexibility granted to the partners to structure the company according to their needs. The Civil Code grants to minority partners more rights, including new quorum to amend the articles of organization (3/4 of the corporate capital) and to appoint administrators, with rules stricter than those provided for the S.A.'s.

The basic characteristics of a *limitada (sociedade limitada)* are as follows:

Partners: There must be at least two; no residency or nationality requirement applies.

Capital: No minimum is required either upon organization or to carry out business, except for specific activities. The *limitada* is not qualified to carry out certain regulated activities such as banking and insurance. The capital of a *limitada* is divided into quotas that, unlike the S.A. shares, are not represented by stock certificates, but are simply noted in the *limitada's* articles of organization. The capital may be increased only after all subscribed quotas have been paid-in.

Management: The *limitada* may be managed by the partners themselves, if residents and individuals, or by one or more officers appointed by the partners. Non-resident and legal entity partners must appoint Brazilian resident individuals. If the articles of organization authorize the management of the company by third parties (not partners), the managers' appointment shall depend upon approval of (i) all partners, if the corporate capital is not fully paid-in or (ii) partners representing 2/3 of the corporate capital if the capital is fully paid-in. When the officer is a partner, the appointment shall depend on the approval of at least 3/4 of the company's capital for appointment in the articles of organization, or of more than half of the corpo rate capital for appointment through a separate document.

Audit: None is required. However, the Civil Code authorizes the creation of an Audit Committee (*conselho fiscal*) composed of at least three (3) members.

Meetings and publications: The Civil Code establishes that the partners' decision shall be taken in a meeting or assembly, as provided in the articles of organization. The partners' assembly is required if the company has more than 10 partners. The partners' assembly is subject to more formalities than the meeting, such as calling, quorum, annual general partners' assembly and publications.

The Brazilian Federal Revenue Department issued the Normative Rulings No. 200, dated September 13, and No. 190, dated August 9, 2002, according to which legal entities and individuals domiciled outside Brazil must be enrolled with the Ministry of Finance's General Taxpayers' Registry ("CNPJ") and Individuals Taxpayers' Registry ("CPF"), respectively. This new requirement is applicable to all legal entities and individuals holding assets and rights subject to public registration in Brazil, including: real estate, vehicles, vessels, aircrafts, equity interest in Brazilian companies, bank accounts, investments in the financial market, investments in the

Exchange Controls

Introduction

Law No. 4,131 of 1962, as amended, regulates foreign investments in Brazil. This law requires that foreign investments be registered with the Central Bank of Brazil ("Central Bank") to entitle the foreign investor to receive abroad dividends and funds related to repatriations of capital. The law establishes broad rules governing the reinvestment of profits and the payment of royalties and technical assistance fees.

Investments

Foreign investments under the law include:

- Items imported as capital contributions (e.g., machinery, equipment);
- Capitalization of credits in foreign currency which are remittable abroad (capitalization of credits require prior registration with the Central Bank); and
- The transfer of foreign currency funds to Brazil.

As a general rule, a foreign investor may organize a subsidiary in Brazil to carry out any kind of business permitted by law, except for areas where foreign ownership is limited, such as media, domestic vessel transportation, banking and insurance.

Restrictions to foreign ownership of media companies have recently been reduced by the Constitutional Amendment No. 36 of May 28th, 2002, which authorizes, under certain conditions, the participation of foreign companies in up to 30% of the total and voting capital of newspaper and radio broadcasting, sound and image companies.

Foreigners are also limited as to the amount of rural land they may own.

Registration of Investments in Foreign Currency

Central Bank issued on August 15, 2000, Circular 2,997 (in force since September 4, 2000) that changed the foreign investment registration method in place at the time, by establishing the declaratory electronic registration system (the so-called RDE-IED "Registro Declaratório Eletrônico de Investimentos Externos Diretos"), which will be carried out through the Central Bank's computer system ("SISBACEN"). Thus, after the foreign currency funds are exchanged in Brazil for local currency or the machinery is imported, as the case may be, the Brazilian beneficiary company must register the investment electronically with the Central Bank, in the currency in which the funds were actually remitted to Brazil or the currency of the investor in the case of machinery. This registration is necessary for the remittance of dividends to the investor, for obtaining additional registration upon the reinvestment of profits and for the repatriation of the capital in foreign currency.

Registration of Investments in Brazilian Currency

Circular 2,997 also introduced the registration of capital contributions made in Brazilian currency by foreign investors. Investments made in Brazilian currency will be registered by the Central Bank provided that the relevant funds arise from a bank account maintained in Brazil by the foreign investor, according to the regulations in force.

Reinvestments

After profits are taxed, if they are not remitted abroad to the foreign investor, they may be reinvested in the same company. The reinvestment is also registered electronically with the Central Bank and, as a general rule, in the currency of the investor's country.

To compute the amount of foreign currency to be registered as reinvestment, the Central Bank applies the exchange rate applicable to commercial transactions in effect on the date on which the capitalization of profits was made.

Remittance of Profits

Law 4,131 of 1962, as amended, does not restrict a Brazilian company from remitting abroad the amount of profits attributed to the foreign investor.

Repatriation of Capital

When the foreign investor sells shares or quotas in the Brazilian venture or when the Brazilian company reduces its capital or is liquidated, the foreign registered investment can be repatriated in the relevant foreign currency free of taxes up to the amount of foreign currency registered with the Central Bank.

In the event the foreign investor sells its shares or quotas of the Brazilian venture locally (i.e., for Brazilian currency) for an amount exceeding the one registered with the Central Bank, the amount exceeding is considered a capital gain and taxed by the withholding income tax. Nevertheless, the exceeding amount may be, in principle, remitted abroad.

Loans

On February 22, 2001, the Central Bank issued Circular 3,027, which states that all registrations related to foreign loans (either in foreign or Brazilian currency) must be obtained through a declaratory electronic registration system (the Registration of Financial Operations – "ROF"), which will be carried out through the SISBACEN. The ROF must set forth the main financial terms and conditions of the loan, and interest charged on the loan may not be deemed excessive according to Central Bank's policies in force at the time. Until 2001, the Central Bank, used to issue a Certificate of Registration after analyzing and approving the transaction (instead of the "ROF" declaratory registration). All loans registered by Central Bank under the prior regulation should have been registered in SISBACEN through the ROF until May 31, 2002. Those loans that have not been transferred to ROF shall be registered upon the borrower's request to Central Bank.

Importation of products

The Central Bank of Brazil often changes the regulation related to importation of goods/equipment. Currently, some import transactions, such as financial lease, operational lease with payment terms longer than 360 days and financing for importation of goods also with payment terms longer than 360 days must be registered with the Central Bank of Brazil.

Taxes

Tax Treaties

To provide relief from double taxation on international transactions, Brazil has executed numerous tax treaties with other countries. The tax treaties provide for tax reductions on income such as royalties, interest, remuneration, dividends and profits. To date, Brazil has executed treaties with Argentina, Austria, Belgium, Canada, China, Czech Republic and Slovakia Republic, Denmark, Ecuador, Finland, France, Germany, Hungary, India, Italy, Japan, Korea, Luxembourg, the Netherlands, Norway, the Philippines, Portugal, Spain and Sweden.

Local Taxation

Introduction

Historically, Brazilian tax regulations have been complex. Although the government is engaged in reducing and simplifying the Brazilian taxation system, at this time an extensive body of tax regulations still applies. This section summarizes the most significant taxes that affect businesses in Brazil, as well as the major aspects of Brazilian taxation of personal income, which affect non residents, particularly expatriates.

Corporate Income Taxes

Most business entities are required to pay corporate income taxes (IRPJ). The IRPJ is computed at fifteen percent (15%) rate on adjusted net income. Annual net income in excess of R$ 240,000.00 is also subject to a surtax of ten percent (10%).

According to Law No. 9,430, of December 30, 1996, taxpayers may opt to calculate the IRPJ on a quarter or annual basis. If the IRPJ is calculated quarterly, it is also payable on a quarterly basis. Over the quarter net income, it is applied a fifteen percent (15%) rate, plus a ten percent (10%) surtax on net income exceeding R$ 60.000,00 per quarter. If the IRPJ is calculated annually, taxpayers are required to anticipate monthly payments of IRPJ, calculated over estimated income. For most companies, the monthly estimated income corresponds to eight percent (8%) of the total monthly gross revenues plus capital gains and other revenues and positive results incurred by the company. Over this tax basis, the fifteen percent (15%) rate applies, plus the ten percent (10%) surtax on estimated income exceeding approximately R$ 20,000.00 per month. When the annual method of calculation is adopted, with payment of monthly anticipations, at the end of the year, the entities must either pay or request reimbursement for the difference between the amount paid monthly and the amount calculated on annual income.

Another used method of calculating income tax is the presumed method. In this case the income tax is calculated on a quarterly basis and for most activities the tax basis corresponds to eight percent (8%) of gross revenues. There are other applicable rates to calculate presumed income related to certain specific activities (*e.g.*, thirty-two percent (32%) for most service activities). Over the presumed income, it is applied the income tax rates: fifteen percent (15%) and ten percent (10%) surtax levied on presumed income exceeding R$ 60.000,00 per quarter. If the presumed method of taxation is adopted, the taxpayer is <u>not</u> subject to any adjustment according to annual actual income.

Some requirements for eligibility to adopt the presumed method are (i) revenues earned in the previous taxable year must not exceed R$ 24,000,000.00; (ii) profits, capital gains or other earnings cannot be originated abroad (*e.g.*, from export transactions), and (iii) financial institutions or equivalent entities, as provided in Brazilian law, are not eligible to adopt the presumed method of taxation; (iv) companies cannot have tax benefits under authorization of the Brazilian tax law (*e.g.*, tax exemption or income tax

reduction); (v) companies cannot have paid the income tax calculated on a monthly and estimated basis, and (vi) factoring companies are not allowed to adopt the presumed method. Until 1.998, companies directly owned by foreign entities were not eligible to adopt the presumed method. In 1999 this restriction was revoked.

Net operating losses ("NOL") generated in a given period can offset taxable income of the subsequent period, limited to thirty percent (30%) of taxable income (i.e., for each R$ 1.00 of income, R$0.70 must be subject to taxation, regardless of the existing amount of NOL). Tax losses may be carried forward, without statute of limitation.

Prior to 1996, any dividends and profits distributed to non-residents were subject to a fifteen percent (15%) withholding income tax (IRRF), except for distribution to residents of Japan, in which a Brazilian tax treaty provides for a 12.5 percent rate.

According to Law No. 9249, of December 26, 1995, profits realized after January 1, 1996 are no longer subject to the IRRF when distributed. Profits and dividends realized prior to January 1, 1996 are still subject to the IRRF at the rates effective in the year the profits have been generated.

Interest on Equity

Law No. 9,249/95 provides that a Brazilian legal entity can pay or credit its equity holders interest on equity, provided that the company has retained or current-year earnings. The total amount of interest that can be paid or credited must not exceed fifty percent (50%) of the company's retained or current-year earnings. Basis for calculating the amount of interest on equity includes reserves in addition to contributed capital, but excludes fixed assets revaluation, special monetary correction of fixed assets, and real estate and intangibles revaluation reserves.

The interest is based on the government-monitored long-term interest rate TJLP (Taxa de Juros de Longo Prazo), calculated on a *pro-rata* basis. The expenses with interest on capital are considered operational deductible expenses for income tax and for social contribution on net income. A fifteen percent (15%) withholding income tax is levied on the amount of interest paid, accrued to the equity holders, or capitalized.

Withholding Income Tax on Payments Abroad

In general, payments made to non-residents are subject to withholding income tax in Brazil. Until December 31, 1998, payments to non-residents for services rendered to Brazilian residents and payments to non-resident individuals for work remuneration were subject to the general withholding income tax rate of fifteen percent (15%).

Beginning January 1, 1999, Law No. 9,779, of January 19, 1999, Article 7, has increased the previous rate of fifteen to twenty-five percent (15-25%). The higher twenty-five percent (25%) rate for payment of services does not apply to interest on loans, and other types of payments, which are not classified as services, and are subject to specific legal provisions. For these types of payments, the lower withholding rate of fifteen percent (15%) is still in place.

In addition, due to the creation of the new Contribution for the Intervention in the Economic Domain ("CIDE"), starting January 1st, 2002, Law No 10.332 reduced the income tax rate applicable to technical services, administrative assistance and other similar services that do not involve transfer of technology to fifteen percent (15%). In addition, the payments remitted abroad for these services will be subject to the ten percent (10%) CIDE.

Law No. 9,779, Article 8, increased the previous withholding tax of zero or fifteen to twenty-five percent (15-25%) for all payments of income, with few exceptions, made to nonresidents established in a low tax jurisdiction. The Brazilian Federal Revenue Department has listed some locations considered to be low tax jurisdictions for Brazilian tax purposes (Treasure Ruling No 33/01). These are American Virgin Islands, Andorra, Anguilla, Antigua, the Netherlands Antilles, the Bahamas, Bahrain, Barbados, Barbuda, Belize, Bermuda, Cyprus, Costa Rica, Djibouti, Dominica, Gibraltar, Granada, Cayman Islands, Cook Islands, Madeira Island (Portugal), Isle of Man, Channel Islands (Jersey, Guernsey and Alderney), Marshall Islands, Mauritius Islands, Turks and Caico Islands, British Virgin Islands, Labuan, Liberia, Liechtenstein, Malta, Monaco, Monserrat, Nauru, Nieui, Nevis, Panama, San Marino, Samoa Island, Saint Kitts, Saint Vincent, Santa Lucia, Seychelles, Tonga and Vanuatu. Thus, for example, interest payable on loans to a low tax jurisdiction is currently subject to the greater twenty-five percent (25%) withholding rate, unless there is legal provision regulating the withholding tax on the specific type of loan contracted.

Social Contribution Tax

Most entities are required to pay social contribution on net income (CSLL). This is a true corporate income tax surcharge, at the rate of eight percent (8%). Starting January 2000, the CSLL will levy on a worldwide basis, meaning that all the company's foreign source income will be subject to the CSLL. On May 1, 1999, the eight percent (8%) rate temporarily increased to twelve percent (12%). However, from May 5, 2000 this rate was reduced to nine percent (9%) and it is expected to reduce again to eight percent (8%) from December 31, 2002 onwards. The reason it is levied separately from the corporate income tax is because it is paid to the social security system, and not to the Federal Administration.

Tax basis for the CSLL is net income specifically adjusted for CSLL purposes. Similarly to the IRPJ, taxpayers may opt to calculate CSLL on a quarter or annual basis. In the latter case monthly payments must be made on an estimated basis. Law No. 9,316, of November 22, 1996, provides that the CSLL is no longer deductible from net income for purposes of calculating IRPJ.

Negative basis of CSLL (tax loss for CSLL purposes) can be used to offset taxable income from subsequent periods, although limited to thirty percent (30%) of taxable income. Similar to tax losses for IRPJ purposes, negative basis of CSLL may be used to offset future taxable income without statute of limitation.

Together with the maximum rate for IRPJ purposes, the overall income tax rate (*i.e.*, Federal Income Tax plus Social Contribution on Net Income) is currently thirty-four percent (34% from May 5, 2000 to December 31, 2002).

Contribution for Intervention in the Economic Domain ("CIDE")

This is a contribution due by companies that own licenses for the use of rights, acquire technological knowledge, or are parties in agreements which imply in transfer of technology, executed with foreign residents. As of January 1st, 2002, the CIDE is also due by companies that render technical services, administrative assistance and other similar services that do not involve transfer of technology. The CIDE is levied on the amounts paid, credited, delivered, used or remitted, in each month, to nonresident beneficiaries, as royalties of any kind and remuneration under the following agreements: (i) supply of technology; (ii) technical assistance (technical assistance services and specialized technical services); (iii) trademark license and assignment; (iv) patent license and assignment; and (v) agreements for the rendering of technical services, administrative assistance and other similar services that do not involve transfer of technology.

The rate is ten percent (10%) of the amount paid, credited, delivered, used or remitted monthly to nonresident beneficiaries of the items listed in the preceding paragraph. The contribution is due by the last

business day of the fortnight following the month the royalty or fee was paid, credited, delivered, used or remitted abroad.

The contribution was created to support a new social program *(Programa de Estímulo à Interação Universidade-Empresa para o Apoio à Inovação)* for the interaction between universities and companies to stimulate technological development in Brazil. The program will be carried out through scientific and technological research programs between universities, research centers and the productive sector.

Contribution for the Development of the National Cinematography Industry ("CONDECINE")

This contribution is levied on the exhibition, production, licensing and distribution of motion pictures and video phonographic works with commercial purposes, per market segments and is calculated based on the length of the work at fixed amounts. This contribution will not levy on the months of January to May of 2002.

The CONDECINE is also levied at an eleven percent (11%) rate on amounts paid, credited, remitted, delivered or used by local agents to foreign producers as a result of the exploitation of audiovisual works in Brazil or their importation, at a fixed price. This contribution will not be levied in the months of January and February of 2002.

Contribution for Intervention in the Economic Domain ("CIDE") on Fuels

This contribution is levied on the importation and commercialization of certain types of fuel (oil, diesel, aviation kerosene and other types of kerosene, fuel-oil, liquefied petroleum gas, including the one derived from natural gas and from naphtenate and alcohol fuel) at fixed amounts in Reais.

The CIDE shall be paid by the producer, blender or importer of fuels. The Taxpayer is allowed to deduct the CIDE from the PIS and COFINS contributions levied on sale of fuels, subject to limits of deduction provided for in the applicable legislation. This contribution shall not be levied on the income derived from the exportation of the products mentioned above.

Federal Welfare Taxes

Two types of federal welfare taxes, COFINS, at a rate of three percent (3%), and PIS, at a rate of 0.65% are due on monthly gross revenues of any kind, with a few exceptions established by the tax legislation.

Import Duty

An import duty (II) is due upon customs clearance of imported products on an *ad valorem* basis. The rate varies, depending on the tariff classification of the product imported. Imports are also subject to the IPI and ICMS (as described below). These taxes, along with II, are calculated as follows: the II is levied on the CIF value of the imported product; the IPI is levied on the CIF value plus II; and the ICMS is levied on the CIF value plus II, IPI and ICMS itself.

Export Tax

An export tax (IE) is due at the time of export. The tax applies on an *ad valorem* basis to a limited list of products. The tax rate varies, depending on the type of product exported.

Excise Tax

The Federal Excise Tax (IPI) is a federal value added tax levied on industrialized products as they leave the plant where they are manufactured. The IPI is also due on imported industrialized products, upon

importation and resale by the importer. IPI rates may vary depending on whether the type of product is regarded as essential or not.

The IPI is levied at each production stage of manufactured products and on the import of manufactured products. This tax is paid on the acquisition or importation of raw materials and intermediate products, parts, components, etc, and can offset the IPI due on subsequent transactions. The net effect is a tax on the value added at each stage of production.

Financial Transactions Tax

A financial transactions tax (IOF) is imposed on foreign currency exchange transactions effected to remit payments abroad for services, including technical assistance fees and royalties for the use of trademarks and patents. The local party who remits the funds abroad bears the responsibility for payment of IOF. The tax is collected by the commercial bank in Brazil at the time of the transaction. Currently, however, a zero rate applies to most cases.

The IOF is also due on currency exchange transactions intended to extend loans to Brazilian residents and/or to make certain investments in Brazil. Currently the IOF rate is five percent (5%) on loans extended to Brazilian entities with maturity term of less than 90 days. The law establishes a limit of 25 percent for increase of this tax. On exchange transactions made by credit card administrator in order to cover expenses made by their clients abroad the applicable rate is two percent (2%).

In addition to currency exchange transactions, an IOF is applied to financial transactions involving credit, insurance and securities.

Provisional Tax on Banking Transfer (Contribuição Provisória sobre Movimentação ou Transmissão de Valores e de Créditos de Natureza Financeira - "CPMF")

Law No. 9,311, of October 24, 1996, created the CPMF tax under temporary application. In 1999 the effects of this tax were extended until June 2002. The CPMF applies at a 0,38% rate to all banking transfers and withdraws of currency, such as the cashing of checks. Currently the Brazilian Government is trying to extend again the effects of the CPMF and the legislation related this tax is pending approval of the Brazilian Congress.

State Value Added Tax on Sales and Services (ICMS)

Similar to the IPI, the ICMS is another value added tax on sales and services, payable upon importation of a product into Brazil and sale or transfer within Brazil, or as to certain communication and intra and interstate transportation services, at the time the service is rendered.

ICMS rates and tax benefits vary from state to state and they also depend on the type of transaction (e.g., intra or interstate sale of goods, communication or transportation services, etc.). Currently, ordinary rates in the State of São Paulo are twelve percent (12%) on transportation services, eighteen percent (18%) on products imported, sold or transferred, and twenty-five percent (25%) on communication services. According to Constitutional Amendment No. 33/01, the ICMS shall be levied on importation carried out by legal entities as well as by individuals, even if they are not considered as taxpayers for ICMS purposes, at an eighteen percent (18%) rate. Other rates may also apply, according to the specific product or service. Rates may also vary with respect to interstate transactions (normally seven percent (7%) or twelve percent (12%) depending on the state of destiny of goods and services).

Similar to the IPI and to the VAT existing in most European jurisdictions, the ICMS system permits a given taxpayer to offset the ICMS paid in acquired goods and services against the ICMS due on

subsequent taxable transactions (*e.g.*, sale of goods and services subject to ICMS tax). The difference is the amount owed to the State government.

Since November 1, 1996, importers/purchasers may take a credit for the ICMS paid on imports and local purchases of fixed assets (which was not permitted until November 1, 1996). Nevertheless, Complementary Law No. 102/00 introduced a new systematic for the appropriation of the ICMS credits upon the acquisition of fixed assets, so that the taxpayer is allowed to register the mentioned credits at a monthly rate of 1/48. As of January 1, 2003, the taxpayer will be allowed to take a credit for the ICMS paid on acquiring goods (other than raw material, intermediate products and packaging material) self-consumed in the taxpayer's activities.

For taxpayers with excess of ICMS credits, some State regulations provide for alternatives that permit the taxpayer to transfer such credits. In the State of São Paulo, for example, the State regulations provide three alternatives through which the taxpayer with excess of ICMS credits can use the tax (besides offsetting ICMS debits). They can (i) transfer ICMS credits to any of its branches or offices located within the State of São Paulo; (ii) transfer the credits to an interdependent company, as defined in the regulations; or (iii) use the credits to pay the purchases to a supplier of raw material or and certain fixed assets. Other State regulations may provide for other alternatives to use excesses of ICMS credits.

Tax on Transmission of Assets by Donation or *Mortis Causa (ITCMD)*

The ITCMD is a state tax that levies on the transmission of movable or immovable assets as a result of donation or death. Currently in the State of São Paulo the ITCMD levies at a four percent (4%) rate on the appraised value of the movable asset, real estate or transmitted rights.

Municipal Services Tax

Federal regulations list specific services to which a municipal services tax (ISS) applies. Rates vary from zero to five percent (5%), depending on the type of service and the particular municipality in which the party rendering the services is located.

Real Estate Property Tax

The real estate property tax (IPTU) is a municipal tax levied annually at progressive rates according to the appraised value and use of the real estate in the Municipality of São Paulo.

Real Estate Transfer Tax

The ITBI, also known as SISA, is a municipal tax on the transfer of real estate. The rates may vary according to the actual value of the transaction or the appraised value of the property, whichever is higher. In the Municipality of São Paulo, however, a fixed rate of two percent (2%) applies. The ITBI/SISA does not apply to real estate transfers pursuant to corporate mergers or contributions of paid-in capital.

Personal Income Taxation

Brazilian tax law distinguishes individual residents from nonresidents. Generally speaking, a Brazilian national is automatically a resident while legally domiciled in Brazil or, if not domiciled in Brazil, upon his or her election to be treated as a resident for tax purposes.

Payments for individual's work

As a general rule payments for services from a Brazilian source to non-resident individuals may be subject to a fifteen percent (15%) or twenty five percent (25%) withholding tax rate depending on the specific case.

Visas

Beginning January 1, 1999, temporary visa holders are considered residents for tax purposes from the moment they enter the country to work under an employment contract. Accordingly, they must deliver an annual tax return including their worldwide income and payments are subject to the progressive income tax at rates of fifteen percent (15%) or twenty-seven and half percent (27.5%) (maximum rate).

Also under the new rules, holders of temporary visas entering the country for any reason other than under an employment contract are considered residents for tax purposes after a period of 183 days of stay, during a period of twelve months from any entrance.

Non-Residents

Expatriates treated as nonresidents are subject to Brazilian income tax only on income received from Brazilian sources, *i.e.*, from Brazilian residents, whether individuals or legal entities. Brazilian source income from salaries and wages are subject to the standard 25% withholding income tax, while capital gains are subject to the 15% withholding income tax. This taxation may be reduced if a tax treaty is applicable. The tax is generally based on gross payments (i.e., without any deductions), and is due when the funds are credited, made available, used on behalf of, or effectively remitted to, the nonresident, whichever occurs first.

Residents

Brazilian residents are subject to Brazilian income tax on their worldwide income, at progressive rates, which vary depending on the specific bracket of their net overall taxable income. The current rates are as follows: fifteen percent (15%) for income between R$ 1.058,01 and R$ 2,115.00, per month, and twenty seven and a half percent (27,5%) for income that exceeds R$ 2,115.00. Nevertheless, under certain conditions and provided the expatriate's country grants reciprocity, resident expatriates are allowed to offset their Brazilian tax liability with federal taxes paid abroad on foreign source income.

Transfer Pricing

Introduction

As of January 1, 1997, Brazil introduced specific transfer pricing rules (Articles 18 to 24 of Law No. 9,430) aiming at preventing undue allocation of income in international commercial transactions between related parties. The system adopted is one of determining the maximum amounts of deductible expenses, and minimum amount of taxable income, for Brazilian entities engaged in transactions with related parties outside of Brazil.

The transfer pricing rules provide for three methods to determine maximum deductible expenses, costs and charges related to goods, services or rights imported from a related party. The three methods are the following:

- Comparable Uncontrolled Price;
- Resale Price Less Profits;
- Production Cost Plus Profits.

For exports, taxpayers will be subject to adjustments whenever the average sales price in such transactions is lower than ninety percent (90%) of the average sales price in the Brazilian market during the same period and according to similar payment conditions. If the average price with related parties is lower than

ninety percent (90%) of that used with unrelated parties, the export income will be adjusted according to one of the following methods:

- Average Price of Export Sales;
- Wholesale Price in the Destination Country Less Profits;
- Retail Price in the Destination Country Less Profits;
- Acquisition or Production Cost Plus Taxes and Profits.

On April 30, 1997, transfer-pricing regulations were issued through Treasury Ruling No. 38/97. In 2000, new provisions and regulations were issued dealing particularly with the Resale Price Less Profit method for imports of products subject to manufacturing processes in Brazil (Provisional Measure No. 1924 – converted into Law No. 9959/2000 and Treasury Ruling No. 113/2000).

Brazil's official gazette of March 30, 2001 published Treasury Ruling No. 32, which consolidates provisions of Laws Nos. 9430/96 and 9959/00 and Treasury Rulings Nos. 38/97 and 113/2000. The new Treasury Ruling does not bring significant changes to the methods and usual application of transfer pricing in Brazil in comparison to the old Treasury Ruling No. 38/97, but clarifies some aspects that so far had been unclear.

In any event the taxpayer has the burden of proof to demonstrate compliance with transfer pricing rules, otherwise the tax administration may start a case. The costs and average prices to which Law No. 9,430 refers must be based on either official information or reports from the importing or exporting country or research conducted by companies or institutions with notorious technical expertise.

For goods, services and rights imported from a related party, the taxpayer must prove that the corresponding costs, expenses and charges do not exceed at least one of the three methods set forth by Law No. 9,430. Otherwise, the tax authorities may challenge the exceeding deduction. The exceeding amount shall be added back as taxable income and will thus be subject to the corporate income tax at the rate of fifteen percent (15%) plus a surtax of ten percent (10%). The nine percent (9%) social contribution on adjusted income also applies on the exceeding amount.

Although Law No. 9,430 does not provide for adjustments to compare the taxpayer's prices with prices adopted by other Brazilian companies that import or sell identical or similar goods, services or rights in the Brazilian market, Treasury Ruling No. 38, now Treasury Ruling 32, establishes some guidelines for comparison purposes.

- The regulations define "similar goods" as those that, simultaneously:
- Have the same nature and the same function; and
- Can mutually replace each other in the function for which they are made;
- Have equivalent specifications.

Related parties for transfer pricing purposes

The following parties are deemed as a related party of the taxpayer for transfer pricing purposes:

- Its parent company, domiciled abroad;
- Its branch or agency, domiciled abroad;

- The person or legal entity, resident or domiciled abroad, whose interest in the capital of the Brazilian taxpayer characterizes it as controlling shareholder or affiliate party, as defined in the Corporate Law;
- The legal entity domiciled abroad that is characterized as a controlled entity or an affiliate party of the Brazilian taxpayer, as defined in the Corporate Law;
- The legal entity domiciled abroad, when such an entity and the Brazilian taxpayer are under the common corporate or administrative control or when at least ten percent (10%) of the capital of each entity is owned by the same person or legal entity;
- The person or legal entity resident or domiciled abroad that, together with the Brazilian taxpayer, holds interest in the capital of a third legal entity, which sum characterizes them as the latter's controlling shareholders or affiliate parties, as defined in the Corporate Law;
- The person or legal entity, resident and domiciled abroad, that is associated, in the form or a consortium or condominium, as defined by the Brazilian law, in any enterprise;
- The person resident in Brazil who is a relative up to the third family degree, (as defined in the Brazilian Civil Code), the spouse or companion of the Brazilian company's management or direct or indirect controlling shareholder;
- The person or legal entity, resident or domiciled abroad, which has exclusive rights, as agent or distributor, to purchase and sell goods, services and rights of the Brazilian entity;
- The person or legal entity, resident or domiciled abroad, which has the Brazilian entity as exclusive agent or distributor to purchase or sell goods, services or rights.

Pursuant to Treasury Ruling No. 32, taxpayers need to inform in their annual tax return ("DIPJ") the existence of any relationship with related individuals or legal entities domiciled abroad and are also required to report transactions subject to the transfer pricing rules.

Methods Applicable to Imports of Goods, Services or Rights

Comparable Uncontrolled Price Method

This method is defined as the arithmetical average of sales price of goods, services or rights, either identical or similar, prevailing in the Brazilian or foreign markets, on transactions of purchases and sales, under similar payment conditions. In other words, the taxpayer shall compare its costs, expenses and charges of goods, services or rights acquired from a related party, during a given period of time, with such arithmetical average. If the costs, expenses and charges incurred by the taxpayer exceed the arithmetical average, the exceeding amount shall then be added back as taxable income.

Although Law No. 9,430 is silent, Treasury Ruling No. 32 provides for some adjustments between controlled and uncontrolled prices. For identical goods, services and rights, Treasury Ruling No. 32 permits adjustments related to:

- Payment conditions;
- Quantities negotiated;
- Obligations related to warranty for the good, service or right;

Obligations related to promotion of the good, service or right by means of marketing and advertising;

- Obligations for quality control, standard of services and health conditions;
- Agency costs in purchase and sale transactions carried out by unrelated parties;
- Packaging;
- Freight and insurance.

For similar goods, services or rights, besides the adjustments listed above, the regulations permit the taxpayer to make adjustments relating to physical differences between the goods, services or rights taken into consideration for comparison purposes.

Still with respect to the arithmetical average, only transactions carried out between unrelated purchasers and sellers will be taken into consideration for purposes to calculate such average. In addition, it is important to note that neither Law No. 9,430 nor Treasury Ruling No. 32/01 elects a preferred jurisdiction, whether local, state or foreign, in which "uncontrolled prices" are adopted in transactions between unrelated parties. Thus, a taxpayer may take into account, for purposes to calculate the arithmetical average price of goods, services or rights, "uncontrolled prices" adopted in either local, state or nationwide markets, or in import/export transactions, as well as in transactions carried on outside the Brazilian territory.

Resale Price Less Profits Method

Under the old rules and regulations enacted in late 1996 and in mid-1997, importers could not use the resale price method when imported goods or rights were subject to another manufacturing process that would result in a new product. In these cases, the importer had to use one of the two remaining methods that is, the comparable uncontrolled price method or (foreign) cost-plus method.

On October 7, 1999, the President of Brazil issued Provisional Measure No. 1.924/99 (Law No. 9.959/2000) introducing some changes to Brazil's transfer pricing rules. The most relevant change is the adoption of a new resale price method for imports of goods or rights that will be subject to another manufacturing process in the country. Under the new rules, there is a bifurcation of the resale-price-less-profit method, depending on whether the importer will submit the imported products to manufacturing process within Brazil.

For imported goods or rights to be subject to a further manufacturing process by the importer or a related entity, the resale-price-less-profit method is defined as the arithmetical average of resale prices of goods or rights (in Brazil) less:

- Unconditional discounts granted1;
- Taxes and contributions imposed on sales; or commissions and brokerage fees paid2;
- A profit margin of 60 percent, calculated over the resale price after deducting the above three items and the value added in the country.

For goods or rights imported into the country and not subject to a manufacturing process locally, the old rules continue to apply. In this case, the resale-price-less-profits method is defined as the arithmetical average of resale prices of goods or rights (in Brazil) less:

- Unconditional discounts granted;
- Taxes and contributions imposed on sales;

Commissions and brokerage fees paid; and

- A profit margin of 20 percent, calculated over the resale-price-profit margin of 20 percent, calculated over the resale price.

It is important to note, however, that when the 20 percent profit margin applies, the rules are silent as to any deduction from the resale price over which the profit margin is calculated. One could construe that no deduction from the resale price would be allowed to calculate the 20 percent margin — that is, that the margin would be calculated over the total resale price with no deduction whatsoever). However, the existing regulations, although based on the old rules, provide that the 20 percent margin should apply over the total resale price, less the unconditional discounts only. If the regulations are not changed in the future, unconditional discounts could be subtracted from resale price to calculate the 20 percent margin.

Unlike when the 60 percent profit margin applies (that is, when there will be a manufacturing process), the base to apply the 20 percent profit margin is greater. In other words, this means that the taxes, commissions, and brokerage fees enumerated above must always be added back to the transfer price to calculate the 20 percent margin.

The resale price to be considered for purposes of this method is the price adopted by the taxpayer in the wholesale or retail markets with unrelated purchasers with either individuals or legal entities. Differences in payment conditions can be adjusted according to the interest rate adopted by the taxpayer in its regular sales. If the taxpayer does not adopt a specific interest rate consistently, the adjustments in payment conditions should be made according to interest rates provided for in the regulations.

The costs of freight and insurance borne by the Brazilian importer and also the unrecoverable taxes paid on imports (e.g., import duties) must be included to determine the cost of the goods under the Resale Price Less Profit method. The wording of the old regulations seemed to consider the inclusion of these costs as an option. The new regulations make clear that the inclusion is mandatory;

Finally, as regards the profit margins, the regulations accept profit margins other than those set forth in the specific methods, provided the taxpayer proves them based on publications, surveys or reports prepared by foreign governments, foreign tax authorities, or companies or institutes of notorious technical knowledge.

Production Cost Plus Profits Method

The third method used to determine arm's length prices for imports of goods, services or rights is the production cost plus profit. It is defined as the average production cost of goods, services or rights, either identical or similar, in the country where they have been originally produced, and the taxes levied on exports in such a country and a markup of 20 per cent, calculated over the production cost.

According to the regulations, the following items can be computed in the (production) cost for purposes of this specific method:

Acquisition costs of raw materials, intermediary products and packaging material used in the production of the good, service or right;

The costs of other goods, services or rights used or consumed in the production of the relevant good, service or right;

The cost of the personnel used in the production of the good, service or right, including those for production supervision, maintenance and security of production facilities and corresponding social charges;

Costs of rents, leases, maintenance and repair, and depreciation and amortization charges of the goods, services or rights used in the production of the relevant good, service or right;

Reasonable losses in the production process, since admitted by the tax legislation in the foreign country.

Therefore, to determine the maximum deductible costs, expenses and charges according to this method, the taxpayer is required to prove they do not exceed the production cost, plus taxes and a twenty percent (20%) profit margin in the country the goods, services and rights have been produced. The profit margin of twenty percent (20%) applies over the production costs before the taxes levied on exports.

Methods applicable to exports of goods, services or rights

Average Price of Export Sales Method

This is the first method to determine the minimum taxable income in exports of goods, services or rights with a related party. The taxpayer must show that the export price in a transaction with a related party is higher than ninety percent (90%) of the average sales price adopted in the Brazilian market with unrelated parties. Therefore, this is the first condition for the taxpayer to avoid allocation of income based on the methods set forth by the transfer pricing rules.

For this purpose, the sales price in the Brazilian market shall be considered net of unconditional discounts, ICMS tax, ISS tax and the social contributions of gross receipts (i.e., the PIS and the COFINS). The export price shall be considered net of insurance and freight expenses borne by the exporter.

In case the export price does not exceed ninety percent (90%) of the average sales price in the Brazilian market, the taxpayer is required to compute a taxable income equal to one of the four methods provided by transfer pricing rules.

The Average Price of Export Sales method is defined as the arithmetical average of export prices adopted by the taxpayer or another exporter of goods, services or rights, either identical or similar, with unrelated parties, during the same period of calculation of the corporate income tax and under similar payment conditions.

If the taxpayer does not export goods, services or rights to unrelated parties, the tax authorities may compare the taxpayer's export prices with those adopted by third parties that export identical or similar goods, services or rights. The concept of "similar goods" for exports is the same as the one described to imports.

If the taxpayer does not carry out sales in the Brazilian market either, the regulations allow to take into consideration sales prices adopted by third parties. In an extreme situation, the taxpayer may face allocation of income based on comparisons made with exports prices and sales prices in the Brazilian market both adopted by third parties.

Wholesale Price in the Destination Country Less Profits Method

The second method for exports carried out with a related party is the wholesale price in the destination country less profit method. It is defined as the arithmetical average of sales of goods, either identical or similar, adopted in the wholesale market in the country of destination, with similar payment conditions, after deducting (i) the taxes computed in the sales price, charged in such a country, and (ii) a profit margin of fifteen percent (15%) over the wholesale price.

Retail Price in the Destination Country Less Profits Method

This method is similar to the preceding method, except for the fact that it takes into consideration the retail price instead of the wholesale price. It is defined as the arithmetical average price of goods, either identical or similar, adopted in the retail market in the country of destination, with similar payment conditions, after deducting (i) the taxes computed in the sales price, charged in such a country, and (ii) a profit margin of thirty percent (30%) over the wholesale price.

Production Cost Plus Profits Method

This is an authentic cost plus method. Such method requires the Brazilian seller to recognize, at least, a profit margin of fifteen percent (15%) (plus the costs incurred) for income tax purposes. It is defined as the arithmetical average acquisition or production costs of goods, services or rights exported, including the taxes levied on exports in Brazil and a profit margin of fifteen percent (15%) over the sum of costs and taxes. Pursuant to the regulations, the amounts paid by the foreign entity as freight and insurance shall be included to determine the acquisition costs for purposes of this method.

One of the relevant questions to be yet defined is whether services rendered by Brazilian service renderer within our territory, to a foreign related party, would in fact constitute (or not) an exportation under the transfer pricing rules, or whether the latter concepts/principles should only be applicable, for instance, to services rendered outside the Brazilian boundaries, representing, therefore, a clear and actual exportation.

Application for Lower Profit Margins

Treasury Ruling No. 32 also permits taxpayers to apply for a change of profit margins set forth in the transfer pricing regulations. The Regulations provide that this proceeding shall follow the general rules for Request for Rulings set forth in the current legislation.

To change profit margins, the taxpayer must file an application with the Treasury and provide certain documents. The Treasury Ruling also requires the taxpayer to indicate the term within which the new profit margin will be adopted. The reason is yet unclear, particularly because the taxpayer has the opportunity to change the current to a better transfer pricing method at the beginning of each fiscal year (in Brazil, January 1). As the application is filed, the Treasury analyzes the proposed profit margin, the term within which it will apply and the documents the taxpayer presented. The Ruling authorizes the Treasury to request further information and documents, if necessary.

The request for change in profit margins can now be supported by official reports and publications of foreign countries, studies and reports prepared by independent third parties with notorious technical expertise and also researches prepared by the World Trade Organization and the OECD. The former regulations allow the use of such reports, studies and researches as an element of evidence, but not specifically as a support when applying for lower profit margins.

If the Treasury does not accept the profit margin proposed, it notifies the taxpayer. No appeal is available. If the Treasury accepts the profit margin and the term, the application is sent to the Ministry of Finance who notifies the taxpayer by means of an Ordinance. If the Treasury accepts the profit margin but does not accept the term, it shall propose a new term that the taxpayer must follow. Again, no appeal is available.

Market Penetration

Transfer pricing regulations provide for special treatment when a Brazilian exporter will start selling its products in a new marketplace. In this case, the regulations permit an exporter to adopt lower sales prices than ninety percent (90%) of the average sales price in the Brazilian market.

The Brazilian exporter, however, can only benefit from these special provisions if, in addition to a previously approved "exportation plan" presented to the Treasury, the exporter complies with certain legal conditions.

Intercompany Loans

Also in connection with transfer pricing, Law No. 9,430 sets forth the minimum (taxable) and maximum (deductible) interest rates charged in intercompany loans falling outside the Central Bank of Brazil's jurisdiction: LIBOR for six months plus three percent (3%). Brazilian borrowers can only deduct a maximum interest rate of LIBOR plus three percent (3%) paid to a non resident related party, while Brazilian lenders must recognize as taxable income, at least, the same interest, in loans extended to foreign related parties.

"Safe harbors" (applicable to exports only)

Treasury Ruling No. 32 set forth two unclear provisions, which some have interpreted as "safe harbor" situations. The first case provides that the taxpayer that has a net profit originating from export sales to related parties, before income tax and the nine percent (9%) social contribution on adjusted income and, of at least five percent (5%) over such sales, can demonstrate its compliance with the transfer pricing rules only with the documents of the relevant transactions with related parties. The second case provides for the same consequence when the taxpayer shows net export revenues originating from transactions with related parties equal or less than five percent (5%) of its total net revenues. Such situations cannot characterize as true "safe harbors", particularly because the tax authorities have the power not to accept the amount of revenues recognized by the taxpayer.

Low Tax Jurisdictions

In addition to the rules applicable to transactions between related parties, the transfer pricing regulations set forth that such rules also apply to international transactions carried out with a person or legal entity, whether related or not, located in the so-called low tax jurisdictions. For transfer pricing purposes, a low tax jurisdiction is deemed to be the country that taxes income at a maximum rate below twenty percent (20%). The same list of countries considered to be low tax jurisdictions for the withholding income tax purposes is valid for transfer pricing purposes (Treasure Ruling 33/01).

Immigration

Business Visa

Under current legislation, foreign businesspersons may apply for business visa valid for a term of up to five years. The length of any one stay in Brazil is, however, still limited to an initial period of up to 90 days. This period may be extended, at the discretion of the federal police, for an additional 90 days.

Temporary Visa

If a longer stay is necessary, a temporary visa and work permit may be available for foreigners entering to work for a Brazilian company either under contract or pursuant to a technical assistance agreement. Unless otherwise noted, the temporary visa is valid for a term of two years, or the duration of the agreement or contract if less than two years, and is renewable for an equal period, unless specific stipulation is made to the contrary within the agreement or contract.

There are two forms of the temporary visa and work permit: (i) the expatriate will be included in the Brazilian company's payroll, under a work contract (in this case, his or her worldwide income will immediately become subject to Brazilian taxation); and (ii) the Brazilian company and the foreign company will sign a technical assistance agreement, registered with the Brazilian Institute of Intellectual Property (INPI). In this case, the expatriate will work for the Brazilian company, but remain on the foreign company's payroll.

In both cases, the executive must receive a work permit in order to receive a temporary visa. Each of the above-mentioned visas involves a different relationship between the employer/Brazilian company and the executive, and should be discussed in turn.

In case a foreigner needs to enter Brazil in an urgent basis, in order to render any kind of technical assistance, there is an alternative visa, which does not require a work permit. Normative Resolution No. 34/99 allows for the issuance of a temporary visa in case of emergency for those petitioning under the temporary visa category to provide technical assistance. The visa may be issued by the Brazilian Consulate having jurisdiction over the applicant, and is valid for 30 days with no renewals allowed. In addition, the emergency temporary visa may only be granted one time within a period of six months to each foreigner.

Permanent Visa

Permanent visas related to work permits are available only to foreigners who are appointed to management positions in Brazil, as evidenced by the articles of association of the Brazilian company sponsoring the visa. With a permanent visa and work permit, as well as in the case of the temporary one (in case the foreigner is included in the Brazilian company's payroll), the expatriates' worldwide income will immediately become subject to Brazilian taxation.

Restrictions on Brazilian Companies

Brazilian companies are not allowed to hire expatriates who do not hold the proper visas and work permits. Violation of this rule may subject the Brazilian company to fines and the company's officers to criminal sanctions.

Brazilian companies may obtain a temporary visa and a work permit for expatriates only if at least two-thirds of their employees are Brazilians and at least two-thirds of their total payroll goes to Brazilians. For a permanent visa, there is a required minimum investment in Brazil equivalent to US$ 200,000, corresponding to each work permit to be granted.

Application Process

An application for a work permit is filed with the Immigration Coordination of the Labor Ministry. When the work permit is approved (after review of the Brazilian company's qualification to hire expatriates), the Immigration authorities will instruct the Brazilian Consulate with jurisdiction over the applicant's domicile to issue the visa to the applicant and his or her dependents, if any.

The next step in the process is for the applicant and family to appear at the Brazilian Consulate with passports, marriage certificate and birth certificates along with a detailed list of personal assets and household goods to be shipped to Brazil. If the applicant already happens to be in Brazil, a trip back to the appropriate Brazilian Consulate in the home country is required.

The Consulate will stamp the visa in the passports and approve the list of items to be shipped. Expatriates may bring personal assets, not including cars, into Brazil without tax.

Upon arrival in Brazil, the applicant has a 30-day term to file application for a Brazilian identity card, taxpayer registration number and labor card. Once the identity card and labor card are issued, the applicant may be added to the Brazilian company's payroll.

Applicants may enter Brazil during the application process on a business visa either to render services on behalf of the foreign company or to make arrangements for the transfer (e.g., to secure housing and schools), but they may not work for the Brazilian company or be included in the payroll until the work permit is issued. Nor may applicants open bank accounts or lease property in Brazil until the proper visa is secured.

Brazilian Citizenship

A foreigner may qualify for Brazilian citizenship after four continuous years of residence in Brazil (or less, in special circumstances). Reasonable stays abroad not to exceed an aggregate of 18 months do not jeopardize this right.

The foreigner must fulfill the following conditions: (a) have reached majority of age; (b) read and write the Portuguese language; (c) exercise a profession or own capital sufficient to support himself or herself and family; (d) have no criminal record; and (e) be in good health (which condition shall be waived if the foreigner has lived in the country for more than two years).

Antitrust

Legislation and Scope

Law No. 8,884 of June 11, 1994, as modified, forbids "violation of the economic order." In general terms, this means any act that limits competition, increases profits on a discretionary basis, controls twenty percent (20%) of the market share by means other than competitive efficiency or abuses market control. Liability for violation extends not only to the company itself, but also to managers and officers and to entities within the same group of companies.

Violations of Antitrust Laws

The law cites conduct that is prohibited, including but not limited to the following:

- Limiting or hindering access of new companies to the market;
- Fixing prices in collusion with a competitor;
- Regulating markets by agreement, aiming at controlling technological research and development of the production of goods and services;
- Unjustifiably refusing to sell goods or render services within normal payment terms;
- Obstructing the exploration of industrial, intellectual or technological property rights;
- Abandoning or destroying crops or harvests for the purpose of causing difficulties, hindering competition or obtaining an arbitrary profit;
- Selling goods below cost, aiming at market domination;
- Imposing exclusivity requirements upon broadcast companies in connection with mass media advertisements;

- Imposing resale prices, discounts, sales conditions, minimum and maximum quantities and profitability upon distributors and retailers; and
- Severing business relations where the other party refuses to comply with terms or business conditions that are unreasonable or anti-competitive.

Registration

Any transaction that may limit competition or result in the control of more than twenty percent (20%) of a relevant market, or in which the prior fiscal year's revenues of one of the participants exceeds R$ 400 Million, must be approved by the antitrust authorities. "Relevant market" has been interpreted to mean not just the national market, but also regional and sector markets, effectively rendering any transaction between competitors subject to government review. The R$ 400 million threshold has been interpreted by the antitrust agency as encompassing the whole economic group worldwide.

The notification to the antitrust agencies can be filed in two different ways: in advance or within fifteen working days after the execution of the first binding document between the companies involved, except whenever any change occurs in the competitive relations between them or, at least, between one of them and a third party agent, on another occasion. In some cases, and depending on the scope of the document, a letter of intent, Memorandum of Understanding etc, may be considered by CADE as the first binding document. The antitrust authorities have been strict about the moment of the application, applying several fines against the parties for late submission.

Three government agencies are empowered to analyze merger control filings. The Secretariat of Economic Surveillance (SEAE), an agency of the Ministry of Finance, the Secretariat of Economic Law (SDE), an agency of the Ministry of Justice, and the Administrative Council for Economic Defense (CADE), an independent federal agency, linked to the Ministry of Justice.

SEAE and SDE each have 30 days to issue their opinions, and CADE has 60 days to decide, after it has received the dockets with the opinions issued by the two other agencies (SEAE and SDE). Requests for additional information suspend these deadlines. Currently the Brazilian Antitrust Authorities take six to ten months in average to decide on an Act. It is worth mentioning that the three agencies have divulged, in a press release issued in March 2002, that cases that clearly do not harm competition in any way may be decided in a shorter period of time.

Enforcement

Three government agencies are involved in the review of conduct or transactions covered by the law: SEAE, SDE and CADE.

SDE monitors market practices and carries out investigations. CADE is the enforcement arm. It reviews cases sent by SDE, issues warnings and requests court execution of its decisions. Execution is subject to judicial review, but for decisions requiring the payment of fines, only if the party posts bond to ensure eventual compliance.

Fines against companies range from one to thirty percent (1-30%) of gross pre-tax revenues for the preceding fiscal year (or double if there has been a recurring violation). Fines against individual managers range from ten to fifty percent (10-50%) of that amount. Foreign companies may be notified through its Brazilian subsidiary, agency, representative or local office, regardless of Power of Attorney or statutory dispositions.

In addition, CADE is authorized to impose certain other penalties and remedial measures. These include ineligibility to participate in public financing or bidding; blacklisting on the Brazilian consumer protection list; withholding of patent rights; and mandated company spin-off, transfer of corporate control or sale of certain assets or other measures to eliminate harm to the economy.

Law No. 10.149/00 created the Leniency Program which provides that immunity be granted to companies (and its executives) or individuals which denounce antitrust violations in which such persons are participants, before such violation is known or investigated by authorities. If the violation is already under investigation, the investigated party may still obtain a reduction of between one to two thirds of the amount of the fine, provided such party cooperates with the investigation.

Sales Representatives and Distributors

Sales Representatives or Agents

The Brazilian legal concept of a sales agent is rather broad, including practically any independent agent who works as an intermediary in the sale of products or services. Given the size of the country, many companies employ sales representatives so that they may best take advantage of Brazil's vast potential market. As a result, a number of rules have been established, creating an extremely protective environment for sales representatives in Brazil.

Legislation: General Requirements

Law No. 4886 of December 9, 1965, as amended by Law No. 8420 of May 8, 1992, regulates the activities of independent commercial representatives ("sales agents") in Brazil. The law provides that sales agents are individuals or legal entities that, without the existence of an employment relationship, are responsible for negotiating commercial transactions and soliciting purchase proposals or orders on behalf of one or more persons (the "principals").

Certain minimum protection is provided to these non-employee sales agents, along with the same general principles of labor laws for the protection of employees. The law requires that sales representative agreements in Brazil include general terms and conditions of the representation, a general or specific identification of the products or articles on which representation is based, the term (definite or indefinite) of the representation, the territory, the nature (exclusive or non-exclusive) of the representation and the duties and responsibilities of the contracting parties.

Brazilian law does not prohibit an agency contract for a fixed term. However, a contract in force for a fixed term may be renewed for an indefinite term, only. Likewise, an agency contract executed by the same parties within six (6) months after termination or expiration of another agent contract shall mandatorily be in force for an indefinite term.

On the other hand, the sole difference between an agent and an employee is that the latter works under the command of the employer. The giving of orders by principal to agent, as well as the payment of benefits typically due to employees such as Christmas bonus and vacation, could characterize an employment relationship between principal and the agent.

Indemnification

The law also provides for the indemnification of sales agents upon termination of a contract by the principal without "just cause" or by the agent with "just cause." The conditions calling for indemnification

are clearly favorable to and protective of sales agents, setting the minimum amount at one twelfth (1/12) of the agent's total compensation during the term of representation, in case of indefinite term representation contracts. In case of termination of a fixed-term contract, the indemnification shall be equal to the monthly average of the commissions paid until the date of termination, multiplied by one half (1/2) of the number of contractual months, as set forth in Law No. 8420/92. Apparently there is a **typo** in Law 8420/92 as the indemnification should be the average commission calculated as above, multiplied by one half of the number of the remaining months of the contract. However thus far such typo has not been corrected.

Furthermore, in the case of indefinite term contracts, if the contract is terminated without cause, the terminating party is required to give 30-day advance notice of termination or to pay a compensation equal to one-third (1/3) of the commissions earned by the agent in the past three (3) months.

Exclusivity of Representation

The agent is also guaranteed exclusive right to the zone of activity specified in the contract, unless otherwise stated. This exclusivity means that the agent is guaranteed the whole commission for that region, even if the company itself carries out the sales. The agent is not prohibited from representing other companies with the same or similar products in that zone unless otherwise agreed with the company.

Distributors

Law No. 4886 of 1965 applies only to sales agents. Distributors who purchase products and resell them in their own name and for their own account are not afforded the specific protection outlined in Law No. 4886, nor are they provided with a means of indemnification by law.

There being no specific legislation protecting distributors, distribution agreements are governed by the Brazilian Civil and Commercial Codes. In the event of breach of a definite term contract before the end of the contractual term, the breaching party may be liable for damages. These damages include direct and (sometimes) indirect losses, but not punitive damages.

Due care should be exercised whenever terminating a distribution agreement with a Brazilian party contracted for an indefinite term. It is recommended that the terminating party give as much prior notice as possible (e.g., three to six months), so as to allow the other party sufficient time to reorganize its business and to eliminate any basis for damages for unreasonable termination.

One exception to the absence of specific legislation covering distribution agreements is Law No. 6729 of 1979 (as amended by Law No. 8132 of 1990), which regulates the distribution of automotive vehicles in Brazil and, amongst other matters, provides for specific indemnification due to distributor upon termination of the distribution. This statute is very specific and is only enforceable with respect to Brazilian automotive industry distribution agreements. Nevertheless, there were cases in which Brazilian courts have applied Law No. 6729/79 to ordinary distribution agreements (as a matter of analogy).

Banking

Regulatory Environment

The Brazilian financial system is primarily regulated by our Federal Constitution, Federal Law No. 4,595, enacted in 1964, Federal Law No. 6.385, enacted in 1976, the National Monetary Council rulings ("*Resoluções*"), and the Central Bank of Brazil ("*Banco Central do Brasil*" or "*Central Bank*") rulings and administrative acts ("*Circulares*" and "*Carta-Circulares*"). Federal Law No. 4,595 provides that a legal

entity is deemed a financial institution when its principal or ancillary activity is the collection, intermediation, or investment of financial resources for its own account or for third parties, in national or foreign currency, as well as the custodianship of assets belonging to third parties. In light of this broad definition, certain activities that somehow are related to, but do not in fact constitute strict banking activities (e.g., capital markets transactions) have been deemed as activities of financial institutions in Brazil. The Brazilian financial system thus includes banking and non-banking institutions.

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Normative Institutions

The main normative agencies in Brazil are the National Monetary Council ("CMN") and the Securities Exchange Commissions. The Central Bank of Brazil enforces the CMN's monetary policy and is in charge of inspecting all financial institutions operating in Brazil.

CMN is a policy-setting and regulatory body. It is the highest-level entity of the Brazilian financial system, responsible for establishing the currency and credit policy of the country through its rulings ("*Resoluções*"). The CMN is composed of the Minister of Finance as President, the Minister of State Planning, Budget and Management, and the President of the Central Bank.

The Central Bank is responsible for implementing the currency and credit policy established by the CMN and, within such policy parameters, for (I) overseeing all public and private financial institutions; (ii) conferring their respective licenses; and (iii) approving any merger, acquisition, or change in the corporate control relating to financial institutions. Through its foreign investment department entitled FIRCE, the Central Bank also controls and supervises foreign capital investments in Brazil.

The CVM, created by Federal Law No. 6.385 enacted in 1976, is an autonomous agency with powers to regulate and supervise activities related to the activities of listed companies, issue and trading of securities on the Brazilian stock exchanges and over-the-counter markets, as well as investment funds composed of securities.

Intermediary Institutions

The entities described below, play a key political and financial role in Brazilian credit policy.

Commercial Banks ("*Bancos Comerciais*"). Typical commercial banking transactions include (i) granting loans to the public; (ii) holding checking and investment accounts; (iii) receiving cash deposits; (iv) receiving and processing payments of public utility bills; and (v) collecting drafts and other credit instruments. Commercial banks may also obtain authorization to deal in foreign exchange transactions, provided that they observe certain legal requirements.

Investment Banks ("*Bancos de Investimento*"). The main activities of investment banks are the management of investment funds and the provision of medium to long-term debt or equity financing. Investment banks may also obtain authorization to deal in foreign exchange transactions, provided that they meet certain legal requirements.

Savings Banks ("*Sociedades de Poupança e Empréstimos*"). These are mostly state-owned institutions. They have a role similar to that of commercial banks in that they receive savings deposits from the public.

Caixa Econômica *Federal – CEF* is currently the major savings bank in Brazil and it is one of the largest financial institutions of the country. Most of the loans under the Federal Housing Credit Program are granted by CEF. CEF also manages the funds of the National Unemployment Compensation Fund (FGTS), the Social Integration Program (PIS/PASEP), and the national lotteries.

Credit, Financing and Investment Companies ("Financeiras"). Their main business consists of (i) financing consumer purchases of goods and services; and (ii) trade credit instruments, such as promissory notes, bills of exchange, etc.

Brokerage firms ("Corretoras" or "CCVM"). They have the exclusive right to deal on the Brazilian stock exchanges in authorized securities and other negotiable instruments, pursuant to Laws No. 4.728/65 and No. 6.385/76. These companies may be established corporations or limited liability quota companies. They operate as intermediary in operations between the stock exchange and third parties. As such, they may (i) organize, manage, and participate in consortia for underwriting and managing securities offerings; (ii) purchase and resell securities; and (iii) distribute and place securities on the capital markets. CMN Resolution No. 1.655/89, as amended by Resolution No. 2.099/94, regulates the organization and operation of CCVM's and specifies all activities that such companies may perform.

Dealing firms ("Distribuidoras de Títulos de Valores Mobiliários" or "DTVM"). These companies are also subject to Laws No. 4.728/65 and 6.385/76. Their main business is subscribing to securities issuance for resale or distribution, thus acting as intermediaries in the placement of public offerings. Their business is similar to that of brokerage firms, although they may not directly deal in stock exchanges. The organization and operation of such companies are set forth in CMN Resolutions No. 1.120/86 and No. 1.653/89. They may be organized as corporations or limited liability quota companies.

Currency Exchange Brokerage Companies ("Corretoras de Câmbio"). These institutions, regulated by CMN Resolution No. 1.770/90, perform foreign currency exchange transactions. They may be organized as corporations or limited liability quota companies. Other financial institutions may be permitted by the Central Bank to deal with exchange currency.

National Economic Development Bank (Banco Nacional de Desenvolvimento Econômico e Social "BNDES"). The BNDES is a state-owned financial institution that acts as an auxiliary agency to implement the federal government's credit policy. Its principal activities include financing industrial, agricultural, and commercial projects.

Banks with multiple portfolios ("Bancos Múltiplos"). Bancos Múltiplos arose out of the 1988 reforms of the financial system and are now regulated by CMN Resolution No. 2.099/94. The main purpose of multiple banks is to enable a single financial institution to maintain different types of portfolios (e.g., commercial bank portfolio, investment portfolio), which, in turn, significantly increases the administrative efficiency among banking conglomerates.

The state-owned *Banco do Brasil S.A*. is the largest multiple bank in Brazil despite the fact that most of the banking activities in Brazil are effected though private *Bancos Múltiplos*.

Leasing Companies (*"Sociedades de Arrendamento Mercantil")*. The main role of leasing companies is to enter into leasing transactions.

Incorporation of Financial Institutions

Brazilian financial institutions may only operate with the prior authorization of the Central Bank. To obtain such prior authorization, a company shall prove the following: (i) financial conditions compatible with the proposed undertaking; (ii) good standing of its directors and officers; (iii) the required minimum capital payment; and (iv) acceptance of certain protection mechanisms of creditors. The total assets of the controlling shareholders or quota holders, whether direct or indirect, must be equal to or greater than 220% of the investment in the new institution. The Central Bank grants authorizations for an indefinite, non-negotiable, and non-transferable term.

Corporate Structure

Depending on the type of the subject transaction, a financial institution may be established in Brazil as (i) a representative office or branch of a foreign business entity or (ii) a subsidiary, in the form of a corporation (*Sociedade por ações)* or a limited liability quota company (*Sociedade por Quotas de Responsabilidade Limitada*). Some financial institutions, such as banks and leasing companies may not be organized as limited liability quota companies.

Pursuant to Resolution No. 2.099/94 enacted by CMN and divulged by the Central Bank, financial institutions must obtain prior authorization from the Central Bank to, among other acts: (a) modify their corporate purpose; (b) convert into a multiple bank (please note, however, that Leasing companies may not do so); (c) change their corporate form; or (d) merge with or acquire another financial institution.

Representative Office or Branch of Foreign Entity

Establishing a branch of a foreign financial institution in Brazil is a bureaucratic and time-consuming process, as it requires the Brazilian President's prior authorization by Decree, issued on a reciprocal basis. In addition, a branch is generally not recommended due to tax and immigration requirements and implications.

The establishment and operation of representative offices of foreign financial institutions in Brazil is regulated under CMN Resolution No. 2.592/99, which provides that a representative office of a financial institution headquartered in a foreign country requires the Central Bank's prior authorization. Such authorization is normally granted to individuals. However provided that the institution has headquarters in Brazil, a company may also be authorized by the Central Bank to operate as legal representative of a foreign bank. Please note that representative offices may only have a promotional role and may not carry out any actual banking activity.

Foreign-Owned Bank Subsidiaries

All banks shall be organized as corporations and at least fifty percent of the stated initial capital (conforming with the applicable minimum capital requirements depending on the type of bank) shall be paid-in at the time of incorporation. The remaining balance must be paid in within one year and before any credit or guarantee operations may be commenced.

Article 52 of the Transitory Constitutional Provisions Act (*Ato das Disposições Constitucionais Transitórias*) of the Brazilian Federal Constitution of 1988 prohibits foreign financial institutions from (i) opening of new branches of financial institutions domiciled abroad in Brazil; and (ii) increasing their equity interest in Brazilian financial institutions, unless authorized by international agreements providing for reciprocity or in the event such transactions are in the interest of the Brazilian govern

The Federal Government tends to treat most acquisitions of Brazilian financial institutions by foreign investors as in the best interest of the country. As a result, Brazilian financial institutions interested in receiving foreign equity participation may present a proposal to the Central Bank, which shall review and submit the same for approval by the CMN, the latter forwarding the request to the President for final authorization by Decree. The formalities and timing of approval depend on the structure of the transaction. For instance, if the foreign interest is obtained through the issuance of new shares rather than the purchase of existing shares, the new subscription amount must be deposited with the Central Bank prior to obtaining final approval for the change in control. In addition, the Central Bank may require that the foreign purchase certain assets (i.e., loans receivable) of banks undergoing intervention or liquidation.

Operational Requirements

The Central Bank imposes certain operational rules on financial institutions, including (i) the period during which bank agencies may remain open to the public; (ii) operational limits for certain financial transactions; (iii) formalities for recording financial transactions; and (iv) requirements for opening new branches.

Moreover, Brazilian financial institutions are subject to the Basel Convention rules, incorporated into Brazilian law under CMN Resolution No. 2.099/94, as amended subsequently. This regulation sets forth the minimum capital flow and net worth for a financial institution to be organized in Brazil as well as the formula for the calculation of the Demanded Net Worth ("*Patrimônio Líquido Exigido*" or "PLE"), which a Brazilian financial institution must maintain as to any risks that may be incurred in the transactions frequently entered into.

Bank Secrecy

Financial institutions shall maintain confidentiality as to all information regarding their clients. Client information and data may be disclosed only upon judicial order or as required by law. Various measures have been proposed to lift such secrecy rules for purposes of criminal investigation and enforcement, however, to date; none of these have been adopted.

Money Laundry Regulation

Federal Law No. 9.613 enacted in 1998, lists transactions that are considered money laundry and which are defined as felony. The same law establishes the creation of the Council for the Control of Financial Activities – COAF ("*Conselho de Controle Atividades Financeiras*"), an agency subordinated to the Ministry of Finance that will be responsible for the regulation and investigation of operations suspected of money laundry. COAF also has the power to impose administrative penalties. Some entities such as stock exchanges, commodities exchanges, derivative exchanges, banks, securities brokers and dealers, insurance companies, and factoring companies, shall inform COAF about any transaction that may seem to violate the legislation on money laundry. Moreover, any transaction with those entities, involving assets that can be converted in currency exceeding R$10,000 (ten thousand Brazilian Reals), shall be reported to COAF. The Central Bank has also published rules regarding Money Laundry.

Domestic Branches

The establishment of branches by certain Brazilian authorized financial institutions shall follow the requirements of Circular No. 2.501. Moreover, Exhibit III of Resolution No. 2.099/94 provides that *Bancos Múltiplos,* commercial banks, investment banks, savings banks, securities brokerage firms, dealing firms, and currency exchange brokerage firms may establish up to ten (10) branches within Brazil. The establishment of additional branches is contingent upon the stated capital and net worth of the financial institution.

Bankruptcy and Reorganization

Financial institutions are not subject to the reorganization ("*concordata*") rules that apply to ordinary commercial entities, but rather to a special administrative procedure called "intervention". Intervention may occur in the following circumstances: (i) losses arising out of mismanagement; (ii) violation of rules resulting in significant losses; or (iii) facts constituting bankruptcy, as provided under Articles 1 and 2 of Decree-Law No. 7.661/45. During the intervention proceedings, a trustee appointed by the Central Bank will take over the management of the institutions and will carry out an investigation. Based on such report, the Central Bank then decides to (i) cease the intervention procedure; (ii) maintain the intervention procedure until any irregularities are eliminated; (iii) liquidate the institution; or (iv) authorize the trustee to request the judicial bankruptcy of the institution. Depending on the nature and risk of the acts or facts causing the institution's financial and economic instability, the Central Bank may decide to liquidate the institution without a previous intervention procedure. During the process of liquidation or intervention, all the assets belonging to the directors or officers of the financial institutions are frozen and may not be disposed of until the end of the investigations carried out by Central Bank. During the liquidation procedure, should the financial institution not have sufficient assets to pay all its creditors, the trustee shall request the declaration of its bankruptcy.

Proposed Legislation

The 1988 Federal Constitution provides that a Complementary Law shall regulate Brazilian financial institutions and Central Bank activities, and insurance companies, among other items. A bill for the Complementary Law was proposed in 1988 to a committee of the Brazilian Congress created especially for this purpose. Since then, the bill has been subject to debate among all interested financial and commercial groups,and a revised text continues to be amended since 1991. As such, it is difficult to predict when the regulation of the aforesaid constitutional command will be regulated by the Complimentary Law.

Consumer Protection

Introduction

The Brazilian Consumer Protection Code (Federal Law No. 8078 of September 11, 1990) ("the Code") establishes legal principles and requirements applicable to consumer relations in Brazil. The Code regulates, among other things, product and service liability, contractual clauses, commercial practices, advertising and relevant information about products and services to the consumers. The Code also includes rules on civil procedure for individual and collective claims, including class actions, as well as administrative and criminal sanctions.

Suppliers and Consumers: Definitions

The Code defines a supplier as any private or public, individual or legal entity, Brazilian or foreign, that manufactures, assembles, creates, builds, transforms, imports, distributes or markets products or renders services to consumers. The Code defines a consumer, as a general rule, as any end-user (whether an individual or a legal entity) that acquires or uses products or services.

By this definition of consumer, the Code governs not only retail sales to consumers, but also sales of products and services to manufacturers, who will be treated as consumers when they are end-users of products and services. This is an important and controversial change in business relationships that differentiates the Code from consumer protection laws of other countries.

Basic Rights of Consumers

The Code includes the following among the basic rights of the consumer:

- The protection of life, health and safety against risks related to the supply of hazardous or harmful products and services;
- The right to proper information regarding the adequate use of products and services;
- The right to clear and adequate information regarding quantity, characteristics, composition, quality, price and potential risks of the products and services;
- Protection against misleading and abusive advertising and coercive or unfair business practices;
- Amendment of contractual clauses that are excessively burdensome;
- Effective protection from damage; compensation for property damage; and
- Access to courts of law and administrative agencies to protect consumers' rights.

Information and Advertisements

Pursuant to the Code, suppliers are held liable for any and all information and advertisement regarding their products or services. The Code also contains specific provisions prohibiting misleading or abusive advertising. There is also a Federal Decree on labeling of products that contain more than 4 % of genetically modified organisms.

Potentially hazardous or dangerous products and services are required by law to bear clearly visible and adequate information, in Portuguese, about any risks of usage.

The manufacturer, producer, builder, supplier of services or importer, regardless of nationality, is strictly and jointly liable for any damages caused by insufficient or inadequate information on the utilization and risk factors associated with the product, as well as if damage is a direct result of services rendered or of the product's defective design, manufacturing, construction, assembly, formula, manipulation, presentation or packaging.

Contractual Rights and Protection

Specific provisions under the Code ensure the contractual rights and protection of consumers. The Code provides that certain clauses will automatically be deemed invalid if included in a contract:

- Limitation of suppliers' liability;
- Restriction on the consumers' right to return products or services and to reimbursement;
- Transference of suppliers' liabilities to third parties;
- Shifting the burden of proof to the consumer in the event of litigation;
- Creation of excessive disadvantages to the consumer; and
- Requiring the consumer to bear costs of collection.

Administrative Rulings 04/98, 14/98, 03/99 and 03/01 of the Economic Law Department of the Ministry of Justice, published on March 13, 1998, June 22, 1998, March 19, 1999 and March 15, 2001 respectively,

included new clauses that will be deemed automatically invalid. They include, among others, the following: preventing consumers from taking advantage of a more favorable event, pursuant to a contractual guarantee term; imposing sanctions in case of delay in complying with an obligation or default by a consumer; electing a Court to resolve any dispute arising from consumer relations, other than courts of jurisdiction where the consumer lives; hindering, reducing or impairing the application of Consumer Protection Code rules to disputes arose from air-transportation, agreements which impose time limits for hospitalization other than those prescribed by a physician; establishing restriction on the consumer's right to question any possible damages arising from executed agreement within the judicial and administrative level.

Products Liability

The Brazilian Consumer Defense Code establishes two types of products liability: (i) liability resulting from damages caused by the product (Art. 12); and (ii) liability resulting from qualitative or quantitative defects of the product (Art. 18).

Liabilities resulting from damages caused by the product

The Code contains specific rules providing that the manufacturer, producer, builder, or importer, regardless of nationality, will be held both strictly and jointly and severally liable if the damage incurred by the consumer is a direct result of the product's defective design, manufacture, construction, assembly, formula, manipulation, presentation, or packaging. These parties will be held liable if the damage is a direct result of the services rendered or of insufficient or inadequate information regarding the product's use and risks. In addition, if the damage is caused by a component or device that was incorporated to a product or service, the manufacturer, builder or importer and the third party responsible for such incorporation will be held both strictly and jointly and severally liable. These parties will be held strictly and jointly and severally liable unless they are able to prove that (i) they did not put the product into the market; or (ii) the defect deemed as cause of the damage does not exist; or (iii) the damage resulted from the consumer or a third party's exclusive fault.

Liabilities resulting from qualitative or quantitative defects of the product

According to the Code, the suppliers (physical or legal entity, regardless of nationality, that perform activities of production, assembling, creation, construction, transformation, importing, exporting, distribution, or commercialization of products or services) are jointly and severally liable, regardless of fault, for qualitative or quantitative defects of products. For the purpose of this provision, a product is considered defective when it presents qualitative or quantitative changes that: (i) make the product inadequate or unfit for its ordinary purpose; or (ii) diminish the product value; or (iii) result from differences between the product and the related data of packages, recipients, labels or publicity messages, unless these differences are inherent to the product's nature.

The Code also dictates administrative and criminal penalties that may be applied against suppliers (e.g., seizure and destruction of products, fines and imprisonment).

Warranty

The Code establishes two different kinds of warranty, which are the legal warranty and the contractual warranty. The legal warranty is comprised of a series of provisions of the Code, which establishes a minimum set of consumer protection requirements, including the imposition of a strict civil liability regime for damages caused by the product or service or for the product's imperfections, that may not be disclaimed as a matter of non-waivable public policy.

When a product is covered by the legal warranty, the consumer is able to demand replacement of the defective parts. If the supplier does not correct the imperfection within thirty days from the consumer claim, the consumer may alternatively demand, at his option: (i) replacement of the product by another of the same kind, in a perfect state of use; (ii) immediate reimbursement of the amount paid, with monetary updating, notwithstanding his right to recover any losses and damages; (iii) proportionate price reduction.

The contractual warranties are those offered by the suppliers under their own discretion. The contractual warranties are deemed complementary to the legal warranties and must be expressly stated in documentation written in Portuguese, accompanying the products. This documentation (the "warranty instrument") shall also be standardized, and adequately clarify what the warranty consists of, including the form, term and place where it may be exercised and the charge to the consumer.

Statute of Limitations

The Code also sets time limits and prescriptive periods during which consumers may exercise their legal warranty rights to raise product liability claims against suppliers:

- 30 days for non-durable and 90 days for durable products and services from the date of delivery of the product or termination of the rendering of service for immediately and easily verifiable defects;
- The same periods above mentioned from the date that concealed defects are discovered; and
- Five years for claiming damages caused by a defective product or service to third parties.

Limitation of liability

The Code expressly prohibits contractual provisions that limit or exonerate a supplier's responsibility for adequacy of products and/or services or for damages caused by products or services. The only exception is that, in consumer agreements between two legal entities, the parties may limit the value of the supplier's indemnification in justifiable situations.

The Power Industry

Introduction

Unlike other infrastructure industries in Brazil, the power industry began in the late 1800s as a private investment. It was not until the early 1950s, due to a post-war nationalization wave, that the sector became predominantly state owned. Almost fifty years later, the Brazilian federal and state governments are carrying out one of the world's largest privatization programs in the power sector, and all restrictions to foreign investment have been lifted. Together with the privatization program, Brazil is remodeling its regulatory framework to accommodate such privatization. Public utilities must comply with new rules of concession; independent power producers are expected to compete for customers; an independent regulatory agency was created to monitor the industry; and a spot market is expected to be fully operative by 2006.

Industry Overview

Historically, the power industry in Brazil has enjoyed outstanding growth. According to Eletrobrás, Brazil's installed capacity increased from 8.7 GW in 1970 to 63.2 GW in 2000. In June 2000, the installed capacity was 63.2 GW (of which 57.4 GW correspond to hydroelectric power and 5.8 GW correspond to

thermoelectric power). Different from most countries, the Brazilian industry is primarily based on hydropower generation, which in 2000 accounted for 90.82% of Brazil's installed capacity. Nevertheless, the 1997-2006 expansion plan also relies on thermoelectric generation to meet future demand. On February 25, 2000, the Ministry of Mines and Energy enacted the Thermoelectricity Priority Program, aiming at implementing a thermoelectric generation system so as to achieve by the year 2009 a hydro/thermo ration of eight/twenty percent, respectively, increasing the participation of the natural gas in the national energetic matrix from 3% to 10%. New sources of gas supply (mostly from Argentina and Bolivia) and the recent abolition of the state monopoly on upstream prospecting will certainly foster thermal expansion. In 2000, in order to encourage co-generation projects were also included in the Ministry of Mines and Energy Thermoelectricity Priority Program through Ordinance 551.

During the years of 2001/2002 the National Electric Energy Agency ("ANEEL") is planning to promote the invitation to bid for the grant of concessions of 27 hydroelectric plants, which jointly will add the capacity of 8,898MW to the Brazilian electric system. These hydroelectric projects are directly supported by ANEEL, since they may not be subject to several restrictions regarding commercialization to final consumers and may also be released from the payment of transmission connection and usage fees.

Of Brazil's 163,000 km of transmission lines, 62,000 km (38%) are high voltage (230 kV or more). Federal-owned Eletrobrás controls more than 51% of such high voltage lines, the remainder of which are owned by public utilities, state and municipal governments. Given the unique features of hydropower, most plants in Brazil are interconnected to regional systems and are subject to control of their respective dispatch by the National System Operator ("ONS"), which is responsible for the dispatch, schedule and planning of generation, as well as for coordination and management of the transmission grid. Such interconnection/coordination allows power plants to participate in power pools through which they can trade excess capacity, thus reducing waste. The country is divided in two interconnected systems - the South/Southeast/Center/West system and the North/Northeast system. In addition, several "isolated", non-interconnected systems exist, mostly in the far north. In 1999, with the implementation of the North/South Transmission Lines, the former systems were connected, creating a National Interconnected System, which handles approximately 98% of the Brazilian power market. The Interconnected System is now operated by the ONS.

For the use and interconnection to the Brazilian Interconnected Basic Grid agents must execute two agreements: (i) one for the interconnection to the grid (*Contrato de Conexão à Transmissão - CCT*) - paying the correspondent fees and (ii) another for the use of the transmission lines of the grid (*Contrato de Uso do Sistema de Transmissão - CUST*) - also paying the use fees established by ANEEL.

The exploration of the transmission line system is also opened to the private sector by means of the grant of authorizations for the operation and maintenance. The purpose of the authorization is two-fold: to expand the national market' supply capacity and to allow all industry agents free access to the Brazilian Interconnected Basic Grid. In July 1999, the federal government unleashed the first bid contest for the purpose of granting authorization to private companies to render transmission services of a 323 km, 500kV transmission line in the North Region of Brazil. For the construction, operation and maintenance of important and large transmission lines of 3,693 km, the federal government scheduled a bid contest for the grant of concessions to private investors, which shall be held by mid-2001.

The first large generating company was privatized in 1998. Important generating companies were privatized in 1998 and 1999. Other generation companies such as Manaus Energia S.A. and Cia. de Geração do Paraná shall be privatized in 2001.

Utilities supplied more than 241,909 GW/hr to 47 million customers in 1999 and 253,487 GW/hr to 49 million customers in 2000. On average the demand increases at a rate of 5% per annum. As the state-

owned utilities are rapidly losing investment ability, brownouts and blackouts are threatening customers. Approximately 50% of the utilities have already been privatized. Two distribution companies are expected to be privatized in 2001: FURNAS and CHESF.

Regulatory Overview

The Brazilian Constitution grants to the federal government the power to legislate over energy matters. It also grants to the federal government ownership rights over hydropower resources. Conversely, the Constitution requires that the federal, state and municipal governments render to the public certain services, including the supply of electricity. The power to explore energy resources and the responsibility for supplying electricity to the public may be delegated by the government to private entities. Such delegation is generally granted and regulated by concession/permission contracts and authorization deeds (see chapter on Concessions).

Brazil has been undergoing a comprehensive regulatory reform since it started the current privatization program in 1995. To date, the major sources of law are: (i) the Federal Constitution of 1988 as altered by the Sixth Amendment of 1995, which eliminated certain restrictions to foreign investment in the industry; (ii) the Water Code (Decree 24,643 of 1934), (iii) the Antitrust Statute (Law 8884 of 1994), whose regulations are being currently adapted to the electricity market; (iv) Law 8631 of 1993, which altered the ratemaking rules; (v) the Statute of Concessions (Law 8,987 of 1995); (vi) Law 9074 of 1995 which, among other innovations, allowed for the formation of independent power producers; (vii) Law 9427 of 1996, which created ANEEL (see below) and (viii) Law 9648 of 1998, which created the Wholesale Energy Market (see below). Some of the above statutes are being amended or expanded at the time of this writing.

As part of the regulatory reform, in 1996 Law 9427 created an independent agency to regulate and monitor the electric industry called ANEEL. Along with other objectives, ANEEL shall carry out the federal government's electric energy policies and directives; promote public bidding for hydropower projects; executes concession/permission agreements and issue authorization deeds; mediates disputes among the agents and between agents and customers; and provide and enforce industry regulations in connection with antitrust restrictions, tariffs, quality standards, transmission fees, and others. By means of cooperation agreements, ANEEL may delegate monitoring power to local agencies.

Moreover, the new regulations provide for the future creation of a spot market (the Wholesale Energy Market or WEM) and the ONS, to be composed of the agents of the industry and of "free" customers. "Free" customers are usually large customers with an electric-energy demand equal to or higher than 10 MW; in the year 2000 this number will decrease as low as to 3 MW. The ONS shall be responsible for the dispatch, scheduling and planning of generation, as well as for the coordination and management of the transmission grid.

Law 9648 provides for a 8-year transition period, starting in 1998 and ending in 2005, during which the energy currently negotiated under bilateral, supply contracts shall be gradually diverted to and be negotiated by means of bilateral agreements and at the WEM.

In 2000, ANEEL approved the rules of the WEM ("Regras do MAE") through Resolution No. 290. ANEEL established a schedule for the adaptation of the agents to the rules of the WEM.

Environmental Controls

Any business activity, which may cause harm to life and the environment, is subject to environmental controls (discussed generally at Chapter XIII). Under existing regulations, the construction of any electrical energy generation plants with a capacity greater than 10 MW requires the submission and

approval of an environmental impact report ("RIMA"). RIMAs must discuss alternative technologies and locations; identify and evaluate the environmental impact during construction and operation; define the impacted areas; and evaluate whether governmental plans, proposed or in process, within the construction area are compatible with the project.

Forms of Doing Business

The industry businesses are generally done in two main forms: public utilities and independent power producers/self-generators. Each form is subject to distinct guidelines, which are briefly described below. One may also form *consortia* or special purpose companies for particular purposes (joint bidding, tax or financing requirements).

Public Utilities

Public utilities (*concessionárias de serviço público*) are those entities that are granted a concession or permit to serve the public with electricity. The rights and obligations arising from the concession/permit are set forth in a concession/permission contract (see chapter on Concessions).

Generally, concession contracts are for a term of up to 35 years for generation or for a term of up to 30 years for transmission and distribution. Extensions are permitted for one additional term. The rationale for the length of the terms and extensions is that the investor must be allowed a concession term sufficient to amortize its investment.

Several utilities have already been privatized and are currently run by private investors, foreign and domestic. Privatized utilities usually have their prior concession contracts replaced by new ones that already incorporate the current requirements of the law. The concession terms are renewed accordingly.

The major advantage of a public utility is the right of exclusivity over a service area (such exclusivity does not apply to large customers, areas supplied by cooperatives, or other exceptional cases provided by law. In consideration for such monopoly right, the utilities must observe certain obligations, mostly focused on public interest, such as to render services on a regular, continuous, efficient and safe basis and to observe quality standards.

Public utilities are also subject to price controls enforced by the concession authority. The law requires that the tariffs be reasonable moderate amounts and nondiscriminatory among customers. Current tariff formulas allow pass through of costs subject to certain caps. Tariffs are adjusted yearly for inflation and further revised up or down according to performance targets within periods generally varying from three to seven years (depending on each specific contract). Public utilities may also seek sources of revenue that are alternative, complementary or accessory to the public service being rendered. The additional revenue resulting there from shall be subject to the tariff revisions mentioned above.

Independent Power Producers (IPPs) and Self-Generators

IPPs and self-generators do not receive concessions or permits to render *public services*. Rather, they receive authorizations (or specific concessions to explore water resources) that merely allow them to produce, use or sell electric energy. The IPP may sell part or all of its output to customers on its own account and risk. The self-generator may sell or trade any exceeding energy it is unable to consume.

IPPs and self-generators are not granted monopoly rights. With the exception of specific cases, they are also not subject to price controls. The IPPs, in particular, compete with public utilities and among themselves for large customers, other public utilities, pools of customers or any customer that is

unattended by a public utility. The law provides for a gradual enlargement of the range of "free" customers that may purchase from IPPs.

The existing generating companies that are being privatized will be converted from the public utility to the IPP regime. Nevertheless, most of their existing output (the so-called "old energy") shall be subject to the regulated regime of the Initial Contracts for the transition period ending in 2005.

Project sponsors and lenders are well advised to pay particular attention to the intricacies of current law when negotiating or reviewing project documentation. In addition to the above-mentioned authorization deed, the rights and obligations of IPPs are stated in the power purchase agreements ("PPAs") they execute with customers. To date, no model draft of a PPA exists, and the regulatory framework is not as organized and thorough as it is in other countries with project financing history. Nevertheless, certain important terms may be secured through the proper use of our codified contract law and the construction of existing industry principles.

Consortia

The investors may form *consortia* to generate electric energy under the regime of public utilities, IPPs or self-generators, being subject to, in each case, each applicable specific regulation. The *consortia* are also allowed to take over the completion of unfinished projects and may eventually elect to run such projects under one of the regimes above.

Environmental Protection

Introduction

The Brazilian Constitution regulates Brazil's environmental protection by federal, state and municipal legislation, by international treaties and by the provisions of MERCOSUR. The scope of liability for polluters and the standards for environmental protection for pollution emission are, in some cases, at a level comparable to those of developed nations. Some Brazilian states, including the State of São Paulo, have established supplemental rules and standards that exceed federal minimums.

There is pending in Congress a proposal for an Environmental Protection Code which would consolidate all federal legislation regarding environmental issues. Besides maintaining strict liability for polluters, this code would define the scope of liability for financial institutions and others. In the State of São Paulo, a code for the consolidation of state environmental law is also being discussed, and the State of Rio de Janeiro has recently enacted its own environmental code. Although Brazil now possesses the necessary legal tools for monitoring the environment, what is still lacking is a community awareness to match the demands of the law. However, recent judicial decisions have applied "moral damages" as a tool for punishing the violator.

Federal and state District Attorneys as well as Brazilian non-governmental organizations (NGOs) registered with Brazilian public record offices have standing to sue polluters for money-damages and specific performance (e.g., clean up or recovery of damaged areas) in public civil actions (similar to U.S. class actions) regulated by Federal Laws No. 7,347/85 and No. 8,078/90. Although individuals are not entitled to sue under Federal Law No. 7,347/85, they may sue to recover personal damages under Brazilian nuisance and tort laws.

Environmental protection agencies at the state and federal levels have concurrent jurisdiction to control the quality of waters destined for public water supplies and certain other uses; to establish environmental

standards and discharge limitations; to issue construction and operating licenses for new and existing sources of pollution; to monitor polluting activities; and to shut down serious violators, temporarily or permanently.

Administrative penalties against industrial polluters at both federal and state levels include fines, denial of public subsidies and financing, and suspension of plant operations until adoption of necessary control measures. Judicial courts may suspend polluting activities even though the activity is properly licensed.

Federal Law No. 9,605/98, establishes criminal and administrative liability for damage to the environment. The law imposes severe criminal punishment on individuals and legal entities that contribute to environmental damage, including officers, controllers, boards of directors, managers and employees of legal entities.

The law provides for crimes against fauna and flora, pollution crimes, crimes against urban order and historical sites, and crimes against environmental administration. Pollution crimes impose more severe penalties - imprisonment from one to five years and fine - whenever environmental or human health damage results from the emission of liquid, gas or solid residues outside of the legal parameters.

The law also provides for piercing the corporate veil in any situation where the existence of a legal entity is a barrier to the recovery of damages caused to the environment.

The penalties for such crimes are severe and may include restrictions on freedom (imprisonment and confinement), rights (rendering services to a community, temporary limitation of rights, temporary loss of authorization or license, interruption of activities, etc.) and fines (such fines will range from the minimum amount of R$ 50,00 - fifty Reais - approximately US$ 18,00 to the maximum amount of R$ 50 million - fifty million Reais - approximately US$ 18 million). The penalties restricting freedom imposed on individuals may be replaced by those restrictive to rights in some situations.

Federal Decree No. 3,179/99 which regulates Federal Law No. 9605/98 establishes administrative penalties for any action or omission that violates legal rules of use, enjoyment, promotion, protection or recovery of the environment. Administrative sanctions include warnings, simple fines, daily fines, seizing, destroying or making products useless, hindering an activity or work, demolishing a construction work, total or partially interrupting the activities, intervening in establishments and restricting rights such as tax benefits and financial credits offered by governmental financial entities.

Scope

Existing federal legislation addresses these aspects of the environment:

Water. Water quality standards applicable to specific bodies of water depend upon officially designated uses for which the waters are intended to be suitable. Brazil's water quality standards cover a broad range of pollutants and substances, from oil and solids to fecal coliform, dissolved oxygen and various toxins (currently 29). The use of specific segments of streams and water bodies is designated by governmental agencies with jurisdiction over bodies of water. São Paulo was the first state of Brazil to develop and implement for an experience period of four years from October 2001 its own reference values for underground water and soil pollution. Therefore during the period mentioned above, instead of using international standards, the State environmental agency will use those recently established.

National Policy for Hydro Resources (Federal Law No. 9,433/97). This law, enacted on January 8, 1997, establishes the National Policy for Water Resources based on the idea that the water is a public good and a limited natural resource with economic value. Under this law, the Federal Union will grant the right

to use the water for some cases (art. 12). Companies will be charged for both extraction and discharge of water. In addition, this law creates regional river-basin committees comprised of public and private parties to manage the water resources and implement its policies and regulations on a regional basis. Besides, the National Water Agency ("ANA"), governmental agency responsible for implementing the national water policy, was created by Federal Law No. 9.984/00, regulated by Federal Decree No. 3.692/00.

Hazardous waste. According to the Brazilian legislation, the waste generator is responsible for the proper final disposal of hazardous and non-hazardous waste. Federal and State regulations require that transport, treatment and disposal of solid wastes, hazardous and non-hazardous, including medical wastes, be subject to prior approval and/or licensing by the environmental authorities. In some cases, Companies may temporarily store waste at their facilities under state approval and supervision. In the State of São Paulo, the approval for waste disposal is made by CETESB through a Certificate of Approval - Disposal of Industry Wastes - "*Certificado de Aprovação - Destinação de Resíduos Industriais* - CADRI", which contains the qualifications of the waste generator, transporter, and site of disposal.

There are also specific requirements for hazardous waste classification, waste inventory and disposal reporting requirements, waste import and export, waste transportation and waste storage and final disposal.

Landfills and hazardous wastes processing and disposal sites are listed as activities that require compulsory Environmental Impact Study ("EIS") for licensing purposes. (Resolution CONAMA 01/86, Art. 2, X). Usually, such activities are also subject to prior approval by the municipality.

Open burning or storage of wastes and disposal of solid wastes in water collection systems are also forbidden. In addition, some States establish construction, hydro geological characterization, and groundwater monitoring requirements for waste storage and/or disposal sites. There are also specific requirements for transportation and disposal of used lube oil (Resolution Conama 09/93), transportation and disposal of wastes generated by transportation facilities such as airports and ports, and for materials containing PCB (Interministerial Regulation 019/81; Instruction Standard/SEMA/STC/CRS 001/83).

Some Bills of Law on Waste Management Policies are under discussion at the Federal and State levels.

Air pollution. Federal and State legislation establish standards of air quality and composition according to the concentration of atmospheric pollutants - suspended particles, sulfur dioxide, carbon monoxide and photochemical oxidizers. The manufacturing, marketing and import of combustion engines and vehicles require proper licensing. Regulations set the maximum allowed levels of pollutants generated by vehicles, which levels are currently being progressively lowered.

Industrial hygiene and safety. Employers may be held liable for damage to the health of their employees caused by an unhealthy work environment. State District Attorneys are increasingly requiring companies to adopt effective health and safety policies for their employees, which go beyond merely supplying safety equipment. Labor laws define the maximum period to which employees may be in contact with hazardous products and unhealthy and dangerous conditions at work. Industrial facilities must periodically submit to inspection and registration by the Ministry of Labor. Non-compliance may subject a company to fines and possible temporary suspension of activities.

Toxic fertilizers. Brazil has enacted laws dealing with all aspects of the research, production, packaging and labeling, destination, registration, transportation, storage, commercial advertising, use, control and inspection of toxic fertilizers, their components and similar products. Criminal liability is imposed on those who fail to follow the legal requirements applied to toxic fertilizers.

Contaminated land. Owners of contaminated land may be held liable under Brazilian property law, which determines that owners must eliminate any problems on their property, which may endanger the community.

International Treaties

The United Nations Environment and Development Conference held in Rio de Janeiro, Brazil, in June 1992 established targets for "sustainable development" — the integration of environmental concern with social-economical development — through programs set forth in its "Agenda 21." Brazil has recently ratified such Convention by Federal Decree No. 2,519/98.

Brazil is also party to the following international agreements:

- 1985 Vienna Convention for the Protection of the Ozone Layer, effective in Brazil as of June 17, 1990.
- Montreal Protocol on Substances that deplete the Ozone Layer, effective in Brazil as of June 17, 1990. Federal Decree No. 2,699, of July 30, 1998 and Federal Decree No. 2,679, of July 17, 1998 promulgated the amendments of the Montreal Protocol.
- Convention on Biological Diversity, approved in Brazil by Legislative Decree No. 2 of February 3, 1994.
- The United Nations Framework Convention on Climate Change, adopted in New York City on May 09, 1992, took effect in Brazil on July 01, 1998, by the Legislative Decree No. 2,652.
- Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal, approved in Brazil by Legislative Decree No. 34 of June 17, 1992.
- Brazil signed on 15 October 1994 the International Convention to Fight Desertification, adopted in Paris on June 17, 1994. This convention became effective on August 20, 1998, by the Legislative Decree No. 2,741.
- The International Convention on Preparation and Cooperation in case of Oil Pollution, signed in London on November 30, 1990 took effect in Brazil on December 10, 1998, by the Legislative Decree No. 2,870.
- Brazil is also a party to the International Convention for the Prevention of Pollution caused by Ships, adopted in London on November 02, 1973 (Protocol of 1978). The Convention was promulgated by Legislative Decree No. 2,508, of March 04, 1998. The Convention deals, not only with oil, but also with all forms of marine pollution caused by ships.
- There is also the International Convention on Tropical Wood, which took effect on August 05, 1998, by the Legislative Decree No. 2,707 and the International Convention ratifying the Agreement on River Transportation through the Paraguay-Paraná Waterway, which took effect on August 11, 1998, by the Legislative Decree No. 2,716.

MERCOSUR

Brazil is a member of the Southern Common Market, or MERCOSUR, established in Paraguay in 1991. The concern of MERCOSUR's Environmental Protection Commission is to resolve transborder pollution issues such as the contamination of rivers by mercury used in gold mining; erosion due to deforestation; problems in monitoring national parks; construction of dams for generation of electric power without previous environmental impact analysis; air pollution caused by industries and thermoelectric centers;

unlawful settlement of the land; contamination of rivers by toxic fertilizers and oil from river boats; illegal transportation by river of toxic waste; and sewage.

Since the directives proposed by the commissions of MERCOSUR are not self-implementing, member states must enact domestic legislation to put the directives into action. Although change is slow, MERCOSUR is heading towards internationally accepted standards and a more integrated regional environmental protection policy.

Recent Actions

Environmental licenses. Under the new Environmental Crimes Law (Law No. 9,605/98) the environmental licenses are playing a much more important role. Lack of such licenses (installation or operating licenses) is listed as an aggravating circumstance and may result in the interdiction of the activities, as well as confinement and/or fine for those who, somehow, cooperate, or fail to act, in the commission of the crime. The issuance of such licenses may also be more severe, since the environmental authority is also subject to punishment for issuance of licenses for companies that do not comply with legal requirements.

Recycling and take back requirements. CONAMA Federal Resolution No. 257/99, establishes that the producers or importers of cell phones and batteries must adopt environmentally adequate procedures for recycling, re-use and treatment of final disposal of cells and batteries that contain lead, cadmium or mercury in their composition, which are necessary for the functioning of all types of device, vehicles or systems, mobile or fixed phones, as well as the electronic products that contain non-replaceable cells and batteries, after they have been depleted. CONAMA Federal Resolution No. 258/99, obliges the producers and importers of tires to collect and give environmentally adequate destination to non-useful tires existing in Brazil. In addition, Federal Decree No. 3,550/00, enacted on July 28, 2000 establishes take back requirements for packages containing toxic fertilizers.

Bio-Safety. Brazil has few rules on Genetically Modified Organisms (GMOs), mostly issued by the National Technical Bio-Safety Commission (CTN-Bio). According to CTN-Bio rules, all national, foreign or international legal entities, which develop activities and projects related to GMOs, must secure a Bio-Safety Quality Certificate from the National Bio-Safety Commission Normative (Instruction No. 01/96). The procedure to release such organisms on the environment is regulated by Normative Instruction No. 03. This Instruction also establishes that an Environmental Impact Study (EIS) may be required in some cases for release purposes. There are also CTN-Bio rules on GMO transportation; prohibiting the genetic manipulation of germinal human cells and experiments on any kind of cloning technique and defining specific procedures for planned introduction of genetic modified plants and importation of Genetically Modified Organisms (animals and plants/vegetables).

The production of Genetically Modified Organisms (such as soy and corn) is under strong debate in Brazil. Several Brazilian States have proposed Bill of Laws forbidding the production of such products. In the State of Rio Grande do Sul, the State Court ordered the burning of a genetically modified soy crop. In the City of Belo Horizonte, State of Minas Gerais, a municipal law was issued in order to prohibit commercialization of any GMO. There are also some pending regulations on labeling of GMO (see item "Consumer Protection"). In 1998, a Class Action was filed against the Federal Government challenging approval of production and commercialization of GMOs on the grounds of lack of Environmental Impact Study, labeling regulations and safety information that should support such approval. In June, 2000 the final decision condemned the Federal Government to oblige the elaboration of an Environmental Impact Study, prior to the release of GMOs. The Federal Government appealed from this decision. The Government's appeal is still under judgment.

Environmental Audits. The practice of environmental auditing in Brazil is relatively recent. Given the growth of potential liability for polluting activities and the impact of activities of subsidiaries on their parent companies, environmental audits are becoming increasingly important as a means to determine compliance with Brazilian environmental law.

Parallel to voluntary initiatives, some legislation has been developed by some States, (including provisions in some State Constitutions), and the Federal Government in order to mandate environmental auditing to some industry sectors. The State of Rio De Janeiro initiated these legislative approaches in 1991, followed by Minas Gerais and Espírito Santo. Other States are also adopting similar legislation. Major cities have also included environmental auditing mandates as part of the local environmental requirements (e.g., Santos-SP and Vitória-ES). A Bill of Law regarding environmental audits at the Federal level is pending in the Federal House of Representatives.

Environmental Control and Inspection Tax. Federal Law No. 10.165 of December 27, 2000 altered Federal Law No. 6,938/81 by creating and implementing the Environmental Control and Inspection Tax (TCFA). The TCFA was created in order to generate funds to allow the appropriate control and inspection of potentially polluting activities. The creation of such tax was severally criticized by those who were obliged to pay the tax. A number of law suits were filed in order to refrain the companies from the payment of the tax, a few of these individual law suits were granted in first degree of jurisdiction and are now, due to the appeal of the government, under appreciation of the Court of Justice. Even a constitutional challenge was filed in order to revoke the tax, but due to formal issues, the challenge was not received by the Supreme Court of Justice.

Cities Statute. The basic policy on the use of urban land was introduced by Article 182 of the Federal Constitution, and was recently supplemented by the "Estatuto da Cidade" ("Cities Statute") (Federal Law No. 10,257/2001). Through the mentioned Federal Law many legal possibilities for the regulation of the use of urban land and real estates were implemented or appropriately regulated. Therefore, further to defining a policy for use of the urban land based on the social function of the land, the mentioned Federal Law implemented the charge of Tax for Urban Land (IPTU) progressive in time, the expropriation with payment of government debt instrument; the special adverse possession in urban real estate; the surface right; the pre-emption right; onerous granting of the right to build; transfer of the right to build; and neighborhood impact study, among others.

Telecommunications

Introduction

The Brazilian telecommunications sector began to be privatized in 1995 once the Federal Government realized that it would not be able to make the investments needed to keep up with emerging technology. The privatization was made possible thanks to an amendment in the Brazilian Constitution, which allowed private entities to invest in telecommunications services under licenses granted by the Federal Government. The amendment also called for a new law to establish the general rules of the telecommunications sector and the creation of a specific regulatory agency ("ANATEL"). This law was enacted in July of 1997 (Law No. 9.472/97). However, the scope of ANATEL's powers does not include jurisdiction over broadcasting (Radio and open TV) services.

Licensing

Companies need licenses to engage in any form of telecommunications services. Licenses are granted through a concession, permission, or authorization. Concessions, contractual in nature, are generally used

for complex services considered to be of public interest (where the obligation of universal service is present). Fixed telephony services rendered by the now privatized companies that formed the Telebrás system is one example. Authorizations are granted for services where the obligation of universal service is not present. Almost all services fall today under the latter classification, including mobile services, private networks etc. Permissions are used only in exceptional circumstances, and for a temporary period of time.

Telecommunications-related licenses are most often non-exclusive in nature. Concession terms vary from ten (10) to twenty (20) years, depending upon the nature of the service and level of investment, and are generally renewable for one or more additional periods. For authorizations, term is undefined. In principle, public bidding is required for the granting of a concession, while it is only required for the granting of an authorization when demand exceeds availability or when the use of spectrum is involved. The particular licensing procedures for each type of service need to be reviewed on a case-by-case basis.

According to the applicable legislation, 2002 is the year when the opening of the fixed switched telephone service market begins. This means that the incumbent operators that have complied with their obligations of quality and universal service will be able to render the service in other areas besides the ones defined in their existing licenses. In addition to that, new players (and not only the incumbents) may request authorization to render this service in different areas of the Country.

Competition

Nowadays, all telecommunications services are carried out by private companies, including fixed and mobile telephony services. The government aims at the establishment of an environment of free and fair competition among telecommunications services providers. In the fixed telephony service there has a duopoly in place, with two operators in each of the four regions in which the country was divided. One is the incumbent company originated from the privatized state-owned company, and the other is the newcomer, also called “mirror” company. The market was further liberalized in January 2002, since other companies are now allowed to seek fixed telephony licenses to compete with the established duopoly.. With regards to the mobile telephony service, there are already two companies operating in each state of the Country (operating in two different frequencies, the “so-called” bands A and B). In 2001, there was a public auction for further frequencies (bands C, D and E) and new competitors are expected to enter in the mobile telephony market this year, in several states. The auction was not a complete success, and some licenses that were offered were not acquired.

Consolidation of mobile operators through mergers and acquisition is already underway, and it is expected that, in the near future, there will remain a 4 or 5 large operators providing mobile services in the whole country.

With respect to most of the remaining services, there is a fair degree of competition, with many operators exploring the main regions of the country. For private network services, a new regulation has been published, establishing the Multimedia Communication Service (SCM). There is currently a judicial dispute aiming at a precise definition over the services that may be provided under the SCM license, which, however, does not prevent Anatel from granting licenses.

Restrictions on Foreign Investment

Decree No. 2.617/98, issued June 6, 1998, established that the only requirement for the rendering of telecommunications services is that the company and its immediate shareholders be located in Brazil and organized under the laws of Brazil. However, a few restrictions still apply for specific services.

The following chart evidences current restrictions (aside from those stated on Decree 26/7/98) on foreign investment in connection with licensing:

No restrictions General Rule:	Fixed Telephony, Cellular Telephony, other services
Foreign investment limited to 49% of voting capital	Cable TV
Only Brazilian ownership	Radio and television broadcasting. A proposition of constitutional amendment (PEC) has recently been approved by the Brazilian House of Representatives, to allow foreign investment in radio and television broadcasting of up to 30% of the voting and total capital of operators. The amendment has yet to be approved by the Senate and calls for further regulation.

Restriction to cross ownership

In order to guarantee a competitive environment, the Brazilian regulations are very strict on cross ownership in the telecommunications sector. As a general rule, licensees that operate a service in a given region are prohibited from obtaining additional licenses or acquiring companies that operate the same service in the same region. The same restriction applies to any shareholder that has actual control power on a given licensee.

Licensees are subject to several penalties if they fail to comply with this cross ownership requirements, being the cancellation of the license the most severe.

To guarantee the compliance with the cross ownership rules, the Law establishes that any merger or acquisition involving a telecommunications services licensee must be submitted to prior approval by ANATEL, and must also be approved by the competition authorities.

Fees and Taxation

All telecommunications services are subject to fees collected by ANATEL for licensing and inspection based on a number of factors, such as the specific type of service, the number of stations, space used in the radio frequency spectrum, among others. Moreover, all companies that render telecommunication services shall contribute 1% of the gross operational revenues earned from the provision of the services to the Universal Service Fund for Telecommunications (Fundo de Universalização dos Serviços de Telecomunicações - FUST). The Fund resources are to be channeled to far-reaching social projects associated with fixed telephony. The main tax for telecommunications services if the sales tax ("ICMS"), collected at the state level, is due at a rate varying from 25% up to 33% of the total price charged for the telecommunications service, depending on the state. The taxable event is broadly defined to include the generation, transmission, retransmission, repetition, amplification or reception of communications of any nature. As a practical matter, taxes are not imposed on call originating outside of Brazil unless they are collect calls.

Internet Providers

The provision on Internet service is classified as value added service, which means an activity that adds value to a telecommunications service. Since Internet is not considered a telecommunications service, Internet Service Providers (ISP) are not subject to licensing before ANATEL.

Public Bids and Concession of Public Services in Brazil

This chapter provides an overview on the applicable regulations regarding public bidding procedures in Brazil, and the rules on concession of public utility services for a number of industries, such as Oil & Gas, Power, Roads, Mining, Water Sewage, Waste Treatment, and Telecommunications, among others.

Public Bidding and Administrative Contracts

In Brazil, the Government must contract or purchase by means of public bidding. According to the 1988 Federal Constitution, Article 37, XXI, "except for cases specified in law, public works, services, purchases and sales shall be contracted by means of public bidding, that ensures equal conditions to all bidders, with clauses that establish payment obligations, maintaining the effective conditions for the proposal, according to the law, which shall only allow requirement of technical and economic qualifications essential to secure performance of the obligations."

In compliance with the constitutional requirement, the general rules on **public bidding** and **administrative contracts** for works, services (including advertising), purchases, sales and leases within the jurisdiction of the Federal Government, States, the Federal District and Municipalities, including their direct administrative bodies, autonomous government entities, public foundations, state-owned companies, mixed-capital companies and other entities (the "Public Administration"), are set forth under Law No. 8.666 of June 21, 1993, as amended by Law No. 8.883 of June 8, 1994 and subsequent statutes ("the Bid Law"). Without prejudice of the aforementioned, according to Brazilian Constitutional Amendment No. 19, of 1998, state-owned companies and mixed-capital companies that are engaged on the exploration of economic activity of manufacturing or commercialization of goods or rendering of services are allowed to have simplified bidding process provided that said process is created by law and it is conform the main principles set forth in Law 8883/94.

Public Bidding

The Bid Law does not define "public bidding". Nevertheless, case law is quite unanimous in understanding that public bidding is a procedure by which the Public Administration is bound to evaluate – pursuant to objective and previously established guidelines and criteria — the largest number of alternatives possible for any given contract to be entered into with a private enterprise or individual.

Administrative Contracts

According to the Bid Law, administrative contracts are "any and all contracts between the Public Administration and private entities in which there is a binding arrangement — stipulating reciprocal obligations — regardless of the name given thereto" (Article 2, Sole Paragraph). These contracts are governed by the Bid Law, the principles of administrative law, and, as a supplement, by the general theory of contracts and private law. However, due to the legal status of such contracts, the Public Administration has certain prerogatives on which we shall elaborate later.

Administrative Contracts for the Concession/Permission of Public Services - Legal Background and Concept

Not only the "routine" administrative contracts, however, are subject to the Bid Law. Concession and Permission contracts, "which involve both the Public Administration and third parties, shall necessarily be preceded by bidding", pursuant to Article 2 thereof. Article 124 of the Bid Law further establishes that provisions, which do not conflict with specific legislation on the matter, shall also apply to contracts for the permission or concession of public services.

The Bid Law is, therefore, in line with the provisions of Article 175 of the 1988 Federal Constitution, which states that the Public Administration is responsible for providing public utility services, either directly or through concession or permission, which will always be preceded by public bidding. The Constitution further establishes that the law shall provide for:

- the regime for public utility service concessionaires and permission holders, the special nature of their contract and of extensions thereof, as well as the conditions of forfeiture, control and termination of the concession or permission;
- the rights of users;
- tariff policy;
- the obligation of maintaining adequate services.

On February 13, 1995, specific legislation on this matter was enacted under No. 8.987 (the "Concession Law"). For purposes of the Concession Law, the following definitions apply (Article 2):

Public Service Concession. The delegation for the rendering of services, made by the granting authority (the Federal Government, the States, the Federal District or the Municipality in which the service is located), by means of a competitive bidding process, to the legal entity or consortium of companies that demonstrates capacity for performance there under, on its own account and for a definite period of time;

Public Service Concession Preceded by Execution. The total or partial construction, maintenance, remodeling, extension or improvement of any works of public interest, delegated by the granting authority, by means of a competitive bidding process, to the legal entity or consortium of companies that demonstrates the capacity for execution thereof, on its own account, in such a way that the investment of the concessionaire is remunerated and amortized by means of the exploration of the service or work for a definite period of time;

Public Service Permission. The delegation (on a temporary and revocable basis) by means of a competitive bidding process, of the rendering of public service, made by the granting authority to the individual or legal entity that demonstrates the capacity for performance thereof on its own account.

General Rules of the Bid Law — An Overview

The lawful accomplishment of any administrative contract (including concession and permission contracts) is subject to prior bidding in most of the cases. Pursuant to the Bid Law, the general **rules on the matter are:**

the bidding is classified into different categories [competitive bidding *("concorrência")*, "price request" (*"tomada de preço"*), invitation to bid (*"convite"*), contest (*"concurso"*) and auction (*"leilão"*)], and adopted depending on the estimated value of the contract. For concession contracts, the competitive bidding is the suitable category;

At the end of 2000, the Federal Government issued the Provisional Measure No. 2108-10, with a new category of bidding, for the acquisition of common goods and services: the *"Pregão"*. This new category provides for a simpler procedure than the standard public bid procedure, with the presentation of the proposal before the eligibility stage, without the need to present a guarantee of the proposal etc. Decree No. 3697/00, which regulates such Provisional Measure, in its definition of "common goods and services", lists the products and services, which may be acquired by the *Pregão* category of public bid. It includes, among others, services of equipment maintenance, general utensils (except computer goods), and office supplies etc.

the bidding process may be *waived* in a number of specific situations (which are described in Article 24). The process may also be *deemed inapplicable*, if competition is unfeasible, for instance: (i) in the event of a single existing supplier; or (ii) in case of hiring technical services from professionals or companies of known expertise (Article 25).

any interested party meeting the minimum qualification requirements (Articles 27 to 33) of legal capacity, technical and economic/financial qualification, as well as tax or fiscal standing, may take part in a competitive bidding (see below);

the request for proposals or *"Edital"* is the instrument by which the conditions of the transaction to be entered into with the Public Administration are made public. Pursuant to Article 40 of the Bid Law (as confirmed in different wording by Article 18 of the Concession Law), the *Edital* must, among other details, indicate: (i) the object of the bidding; (ii) deadlines and conditions for execution and performance of the contract, as well as for delivery of the contracted object; (iii) penalties for non-compliance; (iv) the executive project, if any; (v) conditions for taking part in the bidding and form of presentation of proposals; and (vi) criteria for the judgment of proposals.

Other important rules contained in the *Edital* may include: (i) judgment procedures; (ii) contractual principles, rules on contract execution, amendment, performance, non-performance and termination; (iii) administrative sanctions; (vi) definition of crimes and relevant penalties; and (v) procedures for administrative appeals.

Eligibility to Bid - Fundamental Principles

In principle, any entity able to meet the preliminary qualification requirements may submit a proposal. The Bid Law provides, in Article 3, that "the bidding is designed to guarantee the observance of the constitutional principle of equality, as well as to select the proposal that is most advantageous for the Administration. The bidding shall be processed and analyzed strictly in accordance with the basic principles of legality, impersonality, morality, equality, publicity, administrative probity, abidance by the public invitation notice, objective judgment, and other related items." (emphasis added)

The Law expressly forbids public agents from allowing the *Edital* to contain any conditions that may restrict or hinder in any way the competitive nature of the bidding. In this sense, preferences or distinctions between bidders based on **nationality**, domicile, or other conditions irrelevant to the object of the bidding are forbidden. Establishing differentiated treatment between **domestic and foreign** companies is not allowed either (Article 3, Paragraph 1). However, the Bid Law does set a preference criterion for *Brazilian companies of national capital*, where there is a tie between proposals (Article 3, Par. 2). The Concession Law, in turn, gives preference to proposals presented by *Brazilian companies* (Article 15, Paragraph 3).

The Concession Law, also maintains the above-mentioned guidelines by reiterating that concessions shall be necessarily preceded by a bidding procedure, in accordance with **the terms of the applicable legislation**. The previously mentioned principles of legality, morality, publicity, judgment in accordance with objective criteria, and compliance with the invitation notice are also to be observed in the case of concessions. (Article 14)

The Bid Law and the Concession Law convey one of the most important principles in Brazilian Public Law, i.e., the "equality among bidders". Nevertheless, this does not prevent the Public Administration from establishing *minimum participation requirements*, provided that they are necessary to guarantee the performance of the contract, the security and perfection of the work or service, the regularity of the supply, or the meeting of any other public interest, in accordance with the provisions of the Bid Law.

Concession Contracts - Stability and Preservation of Financial - Economic Equilibrium

In any contract entered into with the Public Administration, one of the major concerns of the contracting party is the stability of the contract. Certainly, this is the case of concession contracts, which require a considerable amount of investments. In this respect, it is advisable that some of these issues be analyzed.

A contract is a typical Private Law arrangement, based on the parties' free will to contract. Nevertheless, when used by the Public Administration, a few adaptations are required. This is the reason why, as previously mentioned above, administrative contracts are governed not only by Public Law principles but also (supplementary), by Private Law rules.

A number of characteristics can determine a contract to be of an administrative nature. However, the essential feature that typifies an administrative contract is the presence of the Public Administration as one of the parties with supremacy of power over the private contracting party. Another crucial element of administrative contracts is the underlying **public interest**, on which we shall comment further.

Due to the legal status of this type of contract, the Public Administration has the prerogatives of:

- modifying the contract unilaterally to adjust it in accordance with public interest;
- terminating the contract unilaterally, should the public interest make it inconvenient, as well as in those material cases established by the law;
- monitoring performance under the contract;
- applying penalties for total or partial non-performance; and
- as a precaution, in case of essential services, taking temporary possession of personal property, real estate and services comprised by the object of the contract.

The private contracting party's rights are also clearly assured by the Bid Law. In case of termination for causes attributable to the Public Administration (as listed in items XII to XVII of Article 78 of the Bid Law), for which the contracted party has not contributed, the latter shall be reimbursed for the losses actually incurred, without prejudice to devolution of guaranties, payment for works executed up to the termination date and payment of stoppage costs. (Article 79, Paragraph 2 of the Bid Law). The private party has also assured under the Brazilian Federal Constitution and under the Bid and Concession Laws the right to revise the prices or tariffs contracted whenever necessary to restore or preserve the original conditions of its proposal or the so-called "financial and economic equilibrium" between the obligations and respective compensation.

Concession Contracts - Termination

The events of termination of a concession are regulated by Articles 35 to 39 of the Concession Law. To this effect, the concession shall be terminated if one of the following events occurs:

- expiration of the contractual term;
- expropriation
- forfeiture (by the Public Administration, by means of administrative process, for failure by the concessionaire);

- rescission (by the concessionaire, by means of a lawsuit, for contractual breach by the Public Administration);
- annulment (for any illegality in the bidding which precedes the concession); and
- bankruptcy or termination of the concessionaire.

Termination of the concession entails reversion to the granting power of all "revertible assets, rights and privileges", as established in the contract and in the original public invitation notice. In this event, the Public Administration is also entitled to take over the service and relevant premises in order to allow its continuity (Article 35, Paragraphs 1 to 3).

Pursuant to Article 35, Paragraph 4, however, termination for completion of the contractual term or expropriation obliges the granting power to proceed with prior surveys and appraisals in order to determine the indemnification due the concessionaire for the investments made.

Upon completion of the contractual term, the ownership of the concession assets must be reverted to the Government, along with reimbursement, by the Public Administration, of the non-amortized or non-depreciated amount of the investment made in assets subject to reversion. (Article 36)

The concessionaire is also entitled to indemnification in case of expropriation. For purposes of the Concession Law (Article 37), expropriation is considered to be the take-over during the term of the concession, for **public interest** reasons, upon enactment of an authorizing law to that effect. The indemnification due the concessionaire in this case is also to be calculated in accordance with the criteria mentioned in Article 36 of the Concession Law.

In case of forfeiture, the concessionaire is also entitled to indemnification, from which any penalties or contractual damages due the Public Administration are to be deducted. In this event however, termination is only effective after the applicable administrative procedure, in which full defense is allowed. Pursuant to the Concession Law, forfeiture of the concession may be declared by the granting power in the following events:

- services rendered in an inadequate or deficient manner;
- failure by the concessionaire to comply with contractual, legal or regulatory rules regarding the concession;
- if the concessionaire halts or contributes in the halting of the services, except for acts of God or force majeure;
- loss of concessionaire's economic, technical or operation conditions to maintain the concession;
- failure by the concessionaire to comply with penalties imposed by the granting power, or with notice to rectify the rendering of the services; or
- if the concessionaire is convicted for tax evasion. (Article 38)

The Concessionaire's Rights and Duties

In addition to the rights and obligations described in previous topics, the Concession Law dedicates Article 31 to the description of the concessionaire's duties:

- rendering adequate services;

- keeping up-to-date inventory and registration of the concession assets;
- keeping the Public Administration and users informed of the management of services;
- allowing free access to inspection;
- carrying out expropriations and establishing rights-of-way, pursuant to the contract and relevant bid invitation;
- taking care of and insuring the concession assets; and
- collecting, investing and managing the financial resources necessary for the rendering of the services.

For purposes of the Concession Law, adequate services are those which meet conditions of regularity, continuity, efficiency, security, modernity (in technology, equipment, premises and relevant maintenance, as well as enhancement and enlargement of the service), generality, courtesy in providing, and at a moderate rate of tariff. (Article 6)

In regards to the concessionaire's rights, however, the Concession Law does not show the same level of systematization. Nevertheless, we list below some of the most important rights assured a public service concessionaire in Brazil:

Article 9: maintenance of the service tariff in accordance with the criteria established in the Concession Law, the contract and the relevant bid invitation;

Article 13: establishment of differentiated tariff levels, given the technical characteristics and specific costs of each segment of users;

Article 14: abidance on the part of the Granting Power, by the previously mentioned principles of the bidding (which precedes the granting of the concession);

Article 25, Par. 1: outsourcing activities that are complementary, accessory or inherent to the concession (keeping, however, its original responsibility for losses and damages caused to the Public Administration or to any third parties);

Article 26: granting sub-concessions within the limits of the contract and if authorized by the Public Administration;

Article 28: offering the rights emerging from the concession in guarantee to financing agreements (provided that the operation and continuity of the service is not hindered);

Article 39: terminating the contract in case of breach by the Public Administration;

being indemnified for the investments made, as previously described, as well as being granted full opportunity of defense in administrative procedures brought against the concessionaire.

Insurance

Introduction

The insurance business in Brazil is regulated mainly by laws passed in 1966 and 1967 which delegated regulatory authority to (i) the National Council of Private Insurance (*Conselho Nacional de Seguros Privados*), also known as "CNSP", which is composed of government authorities and is responsible for establishing the principal rules for the organization and operation of insurance companies in Brazil; (ii) the Superintendence of the Private Insurance (*Superintendência de Seguros Privados*) also known as "SUSEP", which is the CNSP regulatory and implementing agency subordinated to the Ministry of Finance, responsible for implementing operational standards, monitoring compliance and imposing penalties for insurance companies in Brazil; and (iii) the Brazilian Institute of Reinsurance (*IRB Brasil Resseguros S.A.*), formerly *Instituto de Resseguros do Brasil*, also known as "IRB – Brasil Re." or simply "IRB", a mixed-capital entity responsible, to date, for all reinsurance, coinsurance and retrocession in Brazil. IRB is currently undergoing severe transformation due to privatization.

The insurance rules and regulations are divided into two categories, one for life insurance and the other for non-life insurance, consisting all property and casualty insurance. Health insurance and retirement funds are regulated separately.

In 1992 the Ministry of Finance and SUSEP implemented an Insurance Guideline Plan liberalizing certain legal restrictions. Such guidelines were adopted to deregulate insurance operations while maintaining strict control on financial solvency, to promote competition in the insurance market, to end the monopoly over reinsurance activities and open the sector to foreign investment. For instance, SUSEP has lifted restrictions on insurance premium charges and eliminated pre-approval requirements for adopting new insurance products. In September 1996, SUSEP also eliminated the requirement that insurance premiums be indexed. As such, premium increases may now be realized pursuant to freely established price indexes. On the contrary, the mechanisms for verifying the solvency and reserves of insurance companies were strengthened.

Incorporating an Insurance Company

An insurance company in Brazil must be organized in the form of a stock corporation (*sociedade anônima*) and may not conduct any business other than insurance. Pursuant to CNSP Resolution No. 65 of September, 2001, the insurance licensing rules specifically require that insurance companies be managed by individuals with proven professional experience and a university degree. Moreover, the managers must not have been charged with a criminal offense. Finally, insurance companies are not subject to the Brazilian general bankruptcy and reorganization legislation, but rather to specific liquidation rules.

Licensing Requirements

The original CNSP restrictions on foreign equity and voting interests in Brazilian insurance companies are no longer upheld. To obtain a license authorization for operation, the company must submit to SUSEP a license application spelling out the information required by SUSEP Circular No. 122 of 2000, along with an operational plan indicating its location and types of insurance activity to be held. SUSEP will review the application and forward it to the Minister of Finance, which, in its capacity as President of the CNSP, grants authorizations by ordinance. Subsequently, the Minister of Finance will grant final authorization subject to the company presenting evidence of compliance with certain measures.

Minimum capital

Upon incorporation and prior to submission of the license application, the founding shareholders must pay in cash or cash equivalent (Brazilian federal bonds) at least fifty percent (50%) of the company's stock capital. That cash contribution must be deposited in a special bank account and pledged to SUSEP until such time as the granting of the license. The remaining 50% of the stock capital must be paid-in within one year from the issuance of the operating license and its publication in the official newspaper.

CNSP Resolution 73/2002 revoked CNSP Resolutions 23, 24 and 25 of 1992, refreshing the minimum capital requirements for insurance, pension and capitalization companies.

To operate either property and casualty insurance or life insurance, the company must have a minimum capital, divided into a fixed portion and a variable portion. For either life or non-life, the company's (i) fixed portion of the capital is R$1,200,000, and (ii) the variable portion of the capital, depending on the area of operation (i.e., a city or group of cities, as the case may be), varies from R$120,000 to R$2,400,000. For instance, the variable portion for Rio de Janeiro is R$1,800,000 and for São Paulo is R$2,400,000. The variable portion required for all Brazilian regions is R$6,000,000. To operate exclusively property and casualty insurance, or exclusively life insurance, in all Brazilian regions, the insurer must have a capital of R$7,200,000. For a composite license (life and non-life) to operate in all regions, the insurer's required minimum capital is R$14,400,000.

CNSP established a transition period of 24 months for insurance companies existing in Brazil on May 2002 to comply with the new capital requirement. As of May of 2004, all Brazilian insurance, pension and capitalization companies must have adapted to the required minimum capital. Companies incorporated or licensed after May 2002 must comply with such minimum capital right away.

Operational Requirements

Every six months, insurance companies must prove compliance with the mandatory solvency ratios imposed by CNSP Resolution No. 8 of 1989, as amended by CNSP Resolution No. 55 of 2001, which requires an adjusted net worth sufficient to cover the greater of (i) twenty percent (20%) of the annual average adjusted insurance premiums collected in the last year, or (ii) thirty-three percent (33%) of the annual average adjusted claimed losses in the last three years, taking into account all premiums collected except for individual life and retirement insurance. In addition, the following two types of technical reserves are required: (i) "non-committed technical reserves" for risks of potential future losses (i.e., reserves consisting of unexpired risks and "mathematical reserves" (i.e., reserves for guarantee of payments on all unexpired life insurance policies, subject to an update every ninety days), and (ii) "committed technical reserves" (reserves for losses IBNR and those which have occurred but have not yet been settled, as well as maturing term individual life insurance).

Operational and technical limits exist according to the level and type of insurance coverage provided.

The insurer's premiums collected for the past 12 months must be equal to or higher than a pre-established portion that varies from 0.3% to 3% of the insurance company's net assets depending of various factors. In some circumstances, the retention limit may be as low as 0.075% of the insurer's net assets so as to enable start-up companies to reinvest funds.

The retention limit precludes insurance companies from undertaking a single risk in excess of three percent (3%) of the company's net assets. The company's net assets is the company's net worth plus gains accrued on stock investments not realized and all revenue received related to future accounts; less the value of any direct or indirect participation (net worth value) in other companies with similar activity and/or pension funds, all expenses due in the future and paid in advance and all accelerated expenses.

Offices (headquarters and branch offices) of the insurance companies, as well as those of its brokers, are subject to periodic inspections by SUSEP officials for the review and audit of financial statements. Insurance companies are subject to further review by an official council of actuaries, irrespective of whether an actuary has previously approved the company's financial statements contracted by the company itself.

Brokers

Insurance brokerage provisions of Law 4,595 and Decree-law 73 define "insurance broker" as the intermediary legally authorized to solicit and market insurance contracts putting together insurance companies and prospective customers.

Normative rules of the CNSP and SUSEP set forth that, save for authorized agents and direct marketing sales, the attraction of potential customers for new insurance coverage may only be performed by brokers licensed and registered with SUSEP, or by a *preposto* (delegate) of the broker duly empowered by him and also registered with SUSEP.

Only licensed and registered brokers may receive insurance applications, certify the corresponding policy and collect commissions through physical receipt of cash or bank account deposits. A broker may pay his *preposto* a portion of the commission received. The *preposto* is required to receive insurance training at an official insurance academy and obtain a registration with SUSEP.

Direct Sales

Also, Law 4,595/1964 permits insurance companies to sell insurance policies without intermediation of brokers. In such case, the commission that otherwise would have been paid to a broker must be paid to FUNENSEG, an insurance research and training foundation. Because insurance commissions are not indexed, nominal commission are paid to FUNENSEG pursuant to direct sales. Another practice that has been adopted by insurance companies as direct sale refers to the use of a registered individual insurer to officially certify policies sold directly by the insurance company and therefore legitimates the sale as if it was intervened by a broker.

The direct sales are usually made through a toll-free telephone line advertised through the media and destined to receive calls from prospective applicants. By telephone, quotes may be obtained for insurance coverage, application forms may be ordered and, in certain cases, insurance contracts may be concluded.

Reinsurance

Pursuant to Decree-law No. 73/66, the Brazilian Constitution initially reserved reinsurance activities for the exclusive domain of the Government, namely, the government-controlled entity IRB-Brasil Re. The 13th Constitutional Amendment passed on August 21, 1996, provides that reinsurance activities may also be carried out by non-governmental entities pursuant to regulation in the form of a normative law (*lei complementar*) governing the authorization of private companies to enter this field.

On December 1999, Law No. 9.932 was published in the official newspaper. It transferred IRB-Brasil Re.'s regulatory and enforcement attributions and duties over reinsurance to SUSEP and delegated the authority to regulate reinsurance to CNSP – which enacted several rulings in connection therewith – but an equitable injunction granted by the Brazilian Constitutional Supreme Court in connection with a lawsuit for unconstitutionality declaration suspended the effectiveness of Law 9.932/99. On October 2002, the Supreme Court finally confirmed the injunction and declared Law 9,932 unconstitutional.

The foreign reinsurance companies that have opened a Representative Office in Brazil and executed an accord with IRB have preference to receive, in reinsurance, portions of the risks retroceded by the IRB.

IRB has issued Circular PRESI-018/2002, containing the General Rules of Reinsurance and Retrocession ("NGRR") whose provisions are applicable to all participants of reinsurance transactions in Brazil. Its clauses (clauses 101-597) provide for matters pertaining to reinsurance transactions, such as those regarding retention capacity, reserves and recovery advancements; adjustment and settlement of claims; and provides for other matters not directly related to the reinsurance agreement, such as the duties to communicate court proceedings of interest to the IRB.

While establishing those General Rules of Reinsurance and Retrocession, the Directorate of IRB revisited dozens of procedures affecting the commercial relation with insurance companies in the process of acceptance and cession of risks. One of the novelties refers to the interest rate embedded in the premium's fractioning. Previously, the IRB used to follow the interest rate for premium installments set forth in the underlying insurance agreement. The fractioning is limited to seven installments of equal value. See also IRB Circular PRESI 6/2003 for the terms and conditions of reinsurance premium installments and applicable rates.

According to the NGRR, the reinsurer must give its prior approval for the acceptance of insurance products requiring reinsurance. The IRB has 15 days from the receipt of the proposal to accept or deny the facultative reinsurance.

Insurance companies with risks reinsured by the IRB must give notice to the IRB, within 72 hours, of the existence of any court proceedings related to a claim, and must report to IRB, within 60 days, of any settlement of claims made in pursuance to a court decision.

The NGRR requires that any disputes between the reinsurer and the reinsured be submitted to an arbitration proceeding under the rules of the Rio de Janeiro Arbitration Court (*Câmara de Mediação e Arbitragem do Rio de Janeiro*).

Privatization

Introduction

To date, the Brazilian privatization program has included transfers by the Government to private investors of public services and/or shares of state-owned companies.

The privatization may be carried forward under one of the following structures:

- sale of controlling shares;
- initial public offer;
- capital increase, with total or partial waiver or transfer of government's subscription rights;
- sale, transfer or lease of assets and real estate;
- dissolution of companies or partial suspension of activities;
- grant of concession, permit, or authorization for public services.

emphyteusis (*"aforamento"*), purchase of full property (*"remissão de foro"*), assets exchange (*"permuta"*), concession of right of use and purchase of real estate of the federal government.

Alternatively to the traditional privatization structure, the government may in certain cases choose to seek so-called "strategic [private] partners" with whom it executes joint venture agreements or shareholders agreements. Although such a partnership does not follow the same rules as the privatization, some principles and concerns are valid for both. This chapter will not analyze such partnerships.

Foreign and domestic investors are equally entitled to participate in privatizations.

Sources of Law

The privatization rules vary according to the government that ultimately sponsors the project. Companies controlled by the federal government follow federal privatization rules; companies controlled by the state or municipal governments are subject to state or municipal rules respectively. This chapter will focus on current federal rules consolidated in Law 9491 of September 9, 1997, as amended. Investors should also pay attention to the documentation specifically drafted for the relevant company being privatized such as the executive summaries, due diligence reports, requests for proposal, share purchase agreements, concession agreements, stock exchange regulations, and other documents.

Eligible Companies

A state-owned company is eligible for privatization only upon its inclusion in the privatization list ("PND"). A company is included in the PND by a Presidential decree after recommendation of the National Council for Privatization ("CND"). If a company needs to be restructured prior to or in preparation for its privatization (e.g., merger, spin-off, amalgamation) it may also need congressional approval for such restructuring.

Relevant Entities

The major federal governmental entities for privatizations are the CND and the Economic and Social Development Bank ("BNDES"). CND is the deliberative body of the federal privatization program. The coordination and control of the privatization fall under the guidance of the Secretary of the Ministry of Planning. The main attributes of the CND are (a) to coordinate and supervise the execution of the National Privatization Program, (b) to recommend to the Brazilian President the inclusion or exclusion of public companies in the National Privatization Program; (c) to approve the sale structure of each privatization and making the necessary corporate and financial adjustments; (d) to determine the destination of funds collected in each privatization, and (e) to approve the reports and studies in connection with the privatization.

BNDES acts as the manager of the privatization fund. It is also the executive body of the National Privatization Program and its duties range from the selection of the financial advisors to the preparation of the bidding documentation.

The relevant stock exchange and its respective clearing house usually play an important role in the process to the extent they receive and analyze the qualification packages, regulate and monitor the presentation of bid bonds, coordinate the auction, and generally manage the take over and closing proceedings. The major Brazilian stock exchanges are located in São Paulo ("BOVESPA") and Rio de Janeiro ("BVRJ").

Typical Procedure

Although the privatization processes vary, a typical case normally involves the following stages:

The state-owned company is listed in the PND by recommendation of CND;

BNDES selects the consortium of advisors that will prepare the privatization documents. The consortium presents the documents (executive summaries, due diligence reports, requests for proposal, share purchase agreements, etc.), which, upon CND's ratification, are then published;

Public hearings are usually held to clarify the privatization procedure and documents;

Site visits and data rooms are generally available to interested investors who are conducting their own due diligence investigations;

Investors present their qualification packages and bid bonds for the bidding;

The bidding takes place, usually as a public auction at a stock exchange; and

Closing takes place a few days after the bidding.

Employment Relations

Introduction

The basic rules governing the legal relationships between employers and employees in Brazil are set forth in the Brazilian Labor Code (*Consolidação das Leis do Trabalho*, or CLT) and in the Federal Constitution. The CLT includes rules for the formation and termination of employment relationships, employer/employee relations, severance indemnity, fringe benefits, among others. The CLT is supplemented by labor and social security legislation, case law and collective bargaining agreements. All legal claims involving labor matters are decided in labor courts.

Brazilian Labor Code regulates all aspects of a labor relationship.

Employment Relationships

The Brazilian Labor Code defines employee as an individual rendering services to a company, entity or another individual on a non-occasional (i.e. continuous) basis, under the direction of such company, entity or other individual, for compensation. Brazilian courts consistently recognize the existence of an employment relation whenever those three elements are evidenced, whether or not a written agreement exists.

If a worker is not under the direction of the employer (for example, an independent sales representative), the relationship between such person and the company would be subject to general Brazilian civil and commercial contract rules, and not to the CLT or other labor regulations. Nevertheless, Brazilian labor courts are generally sympathetic towards individuals who claim an employment relationship, essentially shifting the burden of proof to the presumed employer.

Economic Group Concept

According to Article 2 of the Brazilian Labor Code (the "CLT"), when one or more companies are under the same direction or control of another company, they are jointly liable for labor liabilities. Therefore, the registration of the employee in only one company and the fact that the employee renders services only to this company does not exclude the joint liability of the company's economic group.

Salary and Remuneration

The CLT distinguishes between salary (*salário*) and remuneration (*remuneração*). Salary is the fixed and/or variable amount paid by the employer to the employee generally on amonthly basis. Commission is deemed as a variable salary. Remuneration includes salary and all benefits the employee receives by reason of the employment such as housing, car allowance and other in-kind benefits.

The distinction between salary and remuneration is relevant for the calculation of certain labor obligations such as social security contributions, FGTS deposits (see below), withholding tax and severance indemnity, which are based on the employee's remuneration. If an employee receives remuneration from both a non-Brazilian parent (or a related non-resident company) and its Brazilian subsidiary, the basis for calculating the employee's severance indemnity will in most cases be the sum of the remuneration received from both sources.

Other Rights

Under Brazilian law an employee is entitled to the following mandatory benefits in addition to what may have been agreed to in a written employment agreement, such as: an annual 30-day paid vacation after each 12-month period of work, coupled with a vacation bonus in an amount equal to one-third of the regular monthly remuneration; a Christmas bonus (the so called "thirteenth salary") of one full additional monthly remuneration normally at the end of the year; a normal work day not exceeding 8 hours daily and 44 hours weekly, with reductions allowed through collective bargaining agreements; overtime work pay of at least fifty percent (50%) above the normal rate; the first 15 days paid for sick leave by the employer, maternity leave of 120 days; paternity leave as established by law (currently set at 5 days); and prior notice of dismissal proportional to the period of service, of at least 30 days.

Profit Sharing

The Federal Constitution enacted in 1988 provides that Brazilian employees have the right to participate in the profits or results of their employer, without this participation being treated as remuneration. Law No.10.101, of December 19, 2000, regulates the procedures and requirements that must be met by Brazilian companies to implement a plan for the employees' participation in the profits or results of the company. Provided that the requirements set forth by the law are met, the amounts paid to the employees under the plan will not be treated as compensation.

Pursuant to the law in force there are no minimum pre-established amounts payable to the employees. All that is required is that employer and employees (represented by the employees' committee or Employee's Union) enter into an agreement setting forth (i) clear rules in connection with the right of employees to receive a share of the company's profits or a certain payment upon achieving certain results; (ii) objective conditions for the employees to achieve such a right; (iii) the dates of profit sharing or result achievement payments, the maximum being on a semi-annual basis; and (iv) the term of the agreement and the dates for revision thereof. The participation of the labor union - or of one of its representatives - is clearly required.

Probation Period

Under Brazilian labor laws the Employer may hire an employee for a probation period that corresponds to a maximum of 90 days or for the period provided in the respective Collective Bargaining Agreement, provided that such term is agreed to in writing, in order to observe if this employee has the appropriate skills. The probation period is supposed to give the Employer enough time to evaluate its employee.

During such period the employer is able to terminate the agreement without paying the severance fund penalty (FGTS) as well as the 30-day previous notice. However, if the employment continues after the above-mentioned period, it will be understood as an indefinite term of duration.

Term of Employment

Employment agreements are executed for a definite or indefinite term of duration (Article 443 of the Consolidated Labor Laws - CLT). In the first case, the parties previously come into an agreement in connection therewith, whereas in the second case, there is no term provided for its termination. In practice, the second type of agreement prevails. Exceptionally an employee may be hired under a temporary agreement in the following cases: (i) for a maximum of ninety days (or as provided in the Collective Bargaining Agreement), on a probation basis or as a temporary replacement for a regular and permanent employee; (ii) to perform services of a temporary nature, in which case the term of employment shall be that necessary to complete the services, limited to two years; (iii) as additional work force, for a term of up to two years.

Part-Time Employment

Part-time work can be contracted up to a maximum of 25 hours per week. The compensation of the part-time employee must be proportional to that of another employee working full time (i.e. 44 hours per week) in the same function.

Severance Indemnity

Until 1988, Brazil had two severance indemnity systems: the FGTS or "new" system, created by Law No. 5107 of September 13, 1966; and the CLT or "old" system, which was contained in the CLT itself. Employees were required to opt for either system within 365 days after commencing an employment relationship. Since enactment of the 1988 Federal Constitution, only the FGTS system applies, but the rights of employees who are already under the CLT system must be observed.

The CLT System

Under the "old" CLT system an employee dismissed by the employer without cause was entitled to an indemnification equal to one-month salary per year of service. Employees with ten or more years of service could not be terminated without just cause duly proven in court.

FGTS Severance Indemnity System

Under the FGTS system, the employer makes monthly deposits (in addition to the monthly compensation), equivalent to eight and a half percent of the employee's monthly remuneration, into a blocked bank account opened in the name and on behalf of the employee. The FGTS account is part of a specific fund managed by a Brazilian government agency. The account is subject to monetary correction.

Any employee dismissed without cause is entitled to withdrawal the amounts, which were deposited into his/her blocked account (FGTS) during the employment relationship, plus accrued interest and monetary correction related to the period of employment. In such cases, the employer must make an additional deposit in an amount equivalent to fifty percent of the total amount deposited in the FGTS account.

In cases of employee's resignation or dismissal by the employer with just cause, the employee will not be entitled to unblock the FGTS account and the fifty percent supplement shall not be due. The employee will have access to the FGTS account only in limited circumstances (i.e., retirement).

After the enactment of the 1988 Federal Constitution there is no longer the difference between tenured *(estável)* and non-tenured employees, although employees holding positions at the Employees Union and in other specific cases may not be terminated without cause. Terminations for cause must meet certain requirements and the Brazilian Labor Code provide legal cause for termination of a labor contract on the part of an employer.

Other Severance Payments

Other severance-related indemnities must also be paid to the employee upon termination of the employment relationship. For example, the employee may be entitled to receive accrued and proportional vacation pay, vacation bonus, Christmas bonus, payment of salary to cover the notice of dismissal period (if dismissed without having received prior notice) and other benefits. The total severance-related payments to an employee vary, depending on the circumstances of each specific case and also from particular conditions of the employment agreement and /or the Collective Bargaining Agreement in force.

Termination Formalities

Both the employee and the company may terminate the employment relationship at any time for any reason, with or without cause. The concept of at-will employment is recognized inBrazil. Brazilian labor legislation provides for three different situations (termination with cause, without cause and resignation) have different legal and economic impact. Termination of an employment relationship in Brazil is a rather formal matter, as Brazilian law requires the filing of a Termination Form with the relevant labor authority, even in case of resignation. The payment of severance indemnities and the execution of the Termination Form must take place in the presence of a representative of the employee's union or the Labor Department save if the employment relation lasted less than one year. It is important to rephrase that under Brazilian labor laws the termination of an employee without cause, requires a prior notice corresponding to a minimum of thirty (30) days or the payment of a monthly salary.

Social Security

The employer must pay the contribution to Social Security Department, on a monthly basis, the equivalent of approximately twenty percent (20%) of the gross salary of each employee plus other social costs in relation to which percentage may vary according to the company's activities from 5,4% to 8,8%. The employee must individually make the payment of social security contribution of between eight and eleven percent (8-11%) over gross monthly salary, which amount is withheld by the employer from the employee's earnings, up to a limit established by the government annually.

Outsourcing

Outsourcing or independent contracting by the company of a service or activity to a third party must be carefully carved out of the typical employment relationship. Although there are no specific laws in this regard, the outsourcing has been well accepted by the labor Courts when the outsourced activity is not linked to the core business of the contracting company.

Outsourcing of services related to the main activity of the company is always some what problematic because labor Courts may construe the existence of an employment relationship between the company and those individuals performing the services, even if they are employed by and registered in the payroll of another company – the service provider company.

Mediation Committee

A company can create a mediation committee to mediate claims from its employees. The committee has no power to decide a case presented to it, but rather tries to lead the parties to an out-of-court settlement. Mediation is available for only individual, as opposed to collective disputes. The employees' union can also create a Mediation Committee for same purposes.

Unions

The creation and activities of unions for both employers and employees are dealt with in the Federal Constitution. In Brazil you have Unions representing the employees and Unions representing the employers. The employees, regardless of their affiliation to the Union, are entitled to the labor benefits that are granted in the Collective Bargaining Agreement that was previously negotiated with the employers and employees Union for the specific economic category. Employers and employees are necessarily represented by their respective unions on certain matters of collective employment relations.

Unions are organized following business activities, such as commerce, metallurgist, chemical etc. The union representing a given company shall be that of the main activity of the company. Employers and employees must pay annual contributions to their respective unions. The employer's contribution is generally paid in January of each year based on the number of employees and on the capital of the company; the employee's contribution is equivalent to one-day salary generally paid in March. Annually the employers' and employees' unions representing a given business activity negotiate the terms of a collective agreement dealing with salary raise and several other issues to be in force for a term of one year. If no agreement is possible, the parties can avail of the mediation by the Labor Department or the Labor Courts.

Mandatory Salary Adjustment

One of the mandatory benefits to which the employees are entitled is the annual salary increase at the percent rate set forth in the collective bargaining agreement executed between the employee's union and the employer's association. The Inter-Union Collective Bargaining Agreement is legally binding as much as any law enacted by the government.

This memo provides employers with general information about employment relationship. It should neither be taken as an advice of any particular matter. No client should act or refrain from acting on the basis of any matter contained in this report without taking specific professional advice on the particular facts and circumstances at issue.

Upon request we will be glad to provide you with any additional information on this matter.

Real Estate

Overview

In Brazil, Law 3.071, dated January 1, 1916 (the "Brazilian Civil Code") generally governs the rights associated to immovable properties.

The Brazilian Civil Code divides assets into two different categories: movables (i.e. personal) and immovable assets. The immovable assets category encompasses the land together with its surface and all accessions, constructions and improvements attached to or forming part of the land, the air space above the land and the subsoil. However, waterfalls and also mines and products from the subsoil are considered

separate assets from the land. The exploitation of mineral resources and hydroelectric power are subject to authorization from the federal government, according to the Brazilian Federal Constitution.

In furtherance, although certain assets are physically moveable (i.e. machinery and equipment used at industrial manufacturing and ships) they are construed under the Brazilian Civil Code as immovable assets, by means of a legal fiction.

The rights related to immovable assets (including real estate properties) are divided into the right of possession and the right of ownership.

The right of possession is the personal right arising from the ownership or dominion over the property.

The right of ownership is the right of an individual to use, enjoy and dispose the property. Some restrictions may apply to such right, such as in cases of creation of easements, expropriation of the property by government authorities or in case of creditors composition, insolvency or bankruptcy. Also, restrictions may apply in case of national interests. In addition, the use of the property may be subject to zoning and construction limitations as provided under the relevant laws.

Several individuals or entities may be jointly entitled to the right of ownership in relation to the same property. In this case, a co-ownership (or *condominium*) will be deemed construed among the different owners, and each of them will be entitled to all rights associated to a specific ideal portion (*fração ideal*) of the property. The costs associated to the maintenance of the property (i.e. housekeeping and security) are shared among the members of the *condominium*.

In case of a *condominium*, any of its members may exercise all rights of ownership, except those that are not consistent with the indivisibility of the property. Therefore, the entire property cannot be transferred without the agreement of all the *condominium* members. Brazilian Law 4.591, dated December 16, 1964, generally governs the rights and obligations attributed to the *condominium* members.

Brazilian laws restrict the acquisition by a foreign individual or entity of a property within any rural area larger than 3 *módulos rurais*. The size of a *módulo rural* varies depending upon the region and the state in which it is located. Other restrictions may apply in case of properties located in areas considered as of national security.

Restrictions to foreigners are not applicable in case of collateral of rural properties, provided that in this case actual title to the property is not transferred, but only a security interest is created for the benefit of the foreigner creditor.

Acquisition of properties

In Brazil the transfer of title to a property only occurs upon registration of the act that transferred it, or the rights thereto, with the relevant Real Estate Registry. For registration purposes, every property must be registered at the specific Real Estate Registry having jurisdiction over the area in which the property is located. Such registration is made under a specific enrollment (*matricula*), which lists all data in respect of the property, including details of its current and former ownership, the existence of liens and mortgages and easements.

Typically, a property is transferred upon the registration of the purchase and sale agreement executed by buyer and seller at the *matrícula* of the property at the Real Estate Registry. As a general rule, for purposes of transferring title, the purchase and sale agreement must be executed in a public format, by means of a public deed executed before a notary public.

A property may also be acquired by inheritance, *usucapio* or accession (the enlargement of the land arising from the conveyance of parcel of the soil through natural causes). In these cases, the court order granting the rights over the property is the instrument to be registered at the Real Estate Registry.

Provided the *matrícula* of the property is the relevant document which details the relevant data of the property, any document, act or instrument which may modify, extinguish, transmit or create rights related to the property, must also be registered. Hence, to be perfected and valid before third parties, a mortgage or a lien over a property shall be registered.

The transfer of a property is subject to the payment of the Real Estate Transfer Tax (*ITBI*). The *ITBI* rates vary in accordance to the city in which the property is located, and is calculated upon the actual value of the transaction or the appraised value of the property, whichever is higher. According to the Brazilian Federal Constitution of Brazil, the *ITBI* does not apply to real estate transfers pursuant to corporate mergers or contributions to paid-in capital.

Real estate lease

Law 8.425, dated October 18, 1991, and, supplementary, the Brazilian Civil Code, govern urban real estate lease agreements for both residential and commercial purposes (including the lease of premises located in shopping centers).

According to the law, among other obligations, upon execution of a lease agreement landlord must deliver the leased property to tenant in condition of use for the purposes set forth under the agreement. Moreover, landlord is liable for any damage or defects in the leased property prior to the lease and also, if that is the case, for the payment of the extraordinary *condominium* fees charged during the lease term (in other words, for the expenses necessary to maintain the structure and safety of the real estate).

Tenant shall be responsible, amongst other obligations, for (i) the correct and timely payment of the rent, charges, duties and ordinary *condominium* fees, if that is the case; (ii) the use of the real estate according to the purpose set forth at agreement; and (iv) returning the real estate at the term of the lease in the same condition tenant received it, except for the regular wear and tear. Further, tenant shall give landlord notice of any damage or defect, which falls into landlord's obligations to repair.

The parties are free to negotiate contractual conditions with respect to the term of the lease, rent amounts and improvements. Notwithstanding, in Brazil it is typical to provide that tenant shall be responsible for the payment of the property tax levied on the leased property during the term of the agreement.

According to price adjustment rules today in force, the rent may be monetarily adjusted for inflation every 12 months as of its effective date. Rent should be adjusted in accordance to one of the various Brazilian inflation indexes (i.e. the *IGP* - General Prices Index - published by the *Fundação Getúlio Vargas*). Regardless the annual adjustment for inflation, according to article 19 of the Law 8245/91, after three years of the lease term, any of the parties may request in court a revision of the rent, in order to adjust it to the market price.

When a lease exceeds five years, tenant has the right to apply for an automatic renewal of the lease (if some conditions are met, i.e. maintain the purposed use of the leased premise) and cannot be removed from the leased property unless for specific defaults. The rent for the lease extension is negotiable and if the parties cannot agree on the amount, the rental amount will be determined in court.

In case of sale of the real estate, tenant has the legal right of first refusal (if not such right was not waived under the agreement). If tenant does not exercise such right, and only (i) if the agreement establishes that it

shall continue in force in case of sale to third parties; (ii) the agreement was entered for a fixed term; and (iii) if it is registered before the relevant Real Estate Registry; then the new owner of the real estate must comply with the agreement.

The law also provides for different types of collateral, landlord may request as a security for tenant's compliance with the agreement (unless the rent is paid in advance): (i) a deposit equivalent to the maximum of three rents to be deposited into a savings account during the term of the lease; (ii) a personal guarantee extended by an individual or an entity (it may be replaced by a bank guarantee); or (iii) an insurance policy covering compliance of tenant's obligations. The law does not permit more than one type of collateral for the same lease agreement.

During the term of the lease, landlord may not demand repossession of the property except (i) if by mutual agreement with tenant; (ii) in case tenant breaches any contractual or legal obligation; (iii) if tenant does not pay the rent and other duties or, lastly, (iv) if urgent repairs in the leased property have been ordered by the a public agent. Tenant, however, has the right to terminate the lease before its term, subject to the payment of the contractual penalty established by the parties on a pro rata basis, taking into account the elapsed term of the agreement. In the event of an expropriation of the property by public authorities, landlord and tenant may both seek indemnification from the expropriating authority, unless otherwise provided under the lease agreement.

Lease in shopping centers

In Brazil, shopping centers are incorporated under a condominium arrangement ruling (i) the use of private areas (or the leased premises); and (ii) the access to every shopkeeper or tenant to its common areas. Thus, subject to the comments above with respect to the obligations regarding ordinary and extra ordinary condominium fees, both landlord and tenant shall bear the costs for the maintenance of the common areas of the center in good safety, order and cleanliness condition, including public rest-rooms, parking areas, entrances, exits, sidewalks, ways, alleys and trash collection.

In furtherance, typically there are four documents associated with the landlord-tenant relationship with regard to the ruling of the use of private and common areas in a shopping center: (i) the Declaratory Deed of General Norms Regulating the Functioning, Utilization and Lease of the Shopping Center; (ii) the Internal Rules of a Shopping Center; (iii) the Shopkeepers Association rules; and (iv) the specific lease between the landlord and the individual tenant.

The Declaratory Deed sets forth the development, construction and basic operating rules for the center, and is a registered document with the incumbent Real Estate Registry. Provided the Declaratory Deed is registered it has priority over all subsequent documents such as individual leases, whether such leases are registered or not. If there is a conflicting clause between the Declaratory Deed and the individual lease, the clause in the Declaratory Deed takes preference, unless the lease specifically references the conflicting clause and specifies the difference. It is not sufficient to state in the lease a general clause, that in case of conflict between the two documents, the lease clause applies. Each conflicting clause must be specifically enumerated and referenced in the lease for the clause to apply.

Oil & Gas

Introduction

On October 5, 1988, the Brazilian Congress enacted a new Federal Constitution which states that the research and exploration of crude oil, natural gas and other fluid hydrocarbon materials, as well as the

refining, importation, exportation and transportation of these products through pipelines or by sea constitutes a monopoly of the Federal Government (Article 177). The Brazilian Constitution, Article 177, 1st paragraph, at that time, determined that the Federal Government would be prohibited to assign or grant any type of participation, in kind or in money, in the exploration of crude oil and natural gas. Only the concessions already granted remained in force.

However, on November 10, 1995, Constitutional Amendment No. 9 was approved by the Brazilian Congress, which modified the original text of Article 177, 1st paragraph, in order to allow the Federal Government to contract private or public companies to perform the activities described in the above paragraph, in accordance with a law to be enacted.

On August 6, 1997, the Brazilian Congress enacted Law No. 9,478 (the "Petroleum Law"), which established the Brazilian energy policy, regulated activities related to the oil monopoly and created the National Council on Energy Policy and the National Oil Agency.

The Petroleum Law confirms the Federal Government monopoly over crude oil, natural gas and other fluid hydrocarbon materials existing in Brazil. It also states that the activities listed in Article 177 of the Brazilian Constitution may be exercised by companies constituted under Brazilian law, with head office and administration in Brazil through concessions or authorizations.

In order to conduct the crude oil and natural gas policies, the Petroleum Law created the National Oil Agency (*Agência Nacional do Petróleo* or *ANP*) linked to the Brazilian Ministry of Mining and Energy.

The concessions for oil companies imply the obligation to explore oil and gas, at its own account and risk, and in the event of success, to produce oil or natural gas in the respective blocks. The ownership of these products will be conferred to such companies, after their extraction, together with all charges relative to the payment of due taxes and the corresponding legal or contractual participation shall also be borne by the concessionaire company.

According to the Petroleum Law, the Brazilian state controlled oil company (*Petróleo*

Brasileiro S.A.- Petrobras), would have the right over each of the fields that were in effective production on the initial date of the Petroleum Law. Further, the blocks where Petrobras has achieved commercial discoveries or advanced expressive investments in exploration, should be kept by Petrobras to proceed with the exploration and development work for a period of 3 years, provided that Petrobras should demonstrate its financial capacity to the ANP. The ANP may grant blocks not kept by Petrobras or where exploration was unsuccessful to interested parties by concession contracts, after the accomplishment of the public bid procedure briefly described below.

The Brazilian government will be compensated for the concessions granted under the Petroleum Law by means of the following governmental takes:

- signature bonus;
- royalties;
- special participation; and
- payment for occupation or retention of area.

The Petroleum Law revoked Law No. 2,004, of October 3, 1953, which created Petrobras. Petrobras is now regulated by the Petroleum Law, which authorizes Petrobras to be associated with other companies for the purposes of conducting the activities listed in the Petroleum Law. The performance of these

activities may also be implemented through consortiums between Petrobras, either as the lead company or not, and domestic or foreign companies, provided the latter has incorporated a Brazilian subsidiary with head office and administration in Brazil.

The exploration and production of gas fields are also regulated by the ANP and must follow the same regime applied to oil corresponding activities. Gas processing and transportation of natural gas are activities that also require a prior authorization from the ANP. However, as oppose to oil by-product distribution, pipeline gas distribution is governed by state monopoly.

Public bids

According to the aforementioned new legislation, it is now possible for any Brazilian company to bid for a concession to explore crude oil or natural gas.

The public bids must comply with the following procedures: *(i)* pre-qualification of the biding companies; *(ii)* qualification of such companies; *(iii)* the ANP's publication of the bid notice, which must contain all bidding rules; *(v)* examination of the bids; *(vi)* registration of the tender; and *(vii)* signature of the concession contract.

In December 1998, ANP announced Brazil's first oil and gas exploration and production licensing round. This round was brought to a successful conclusion on September 30, 1999, when 11 domestic and international companies - the latter trough their local subsidiaries - signed Concession Agreements with the ANP for 12 exploration blocks.

In December 1999, ANP announced Brazil's second licensing round, which was concluded on September 20, 2000, the deadline for the winners to sign the Concession Agreement. On June 7, 2000, during the Second Bid Round, 23 blocks were offered by the ANP, 21 of which have been successfully awarded during the referred public bid, being 12 offshore and 9 onshore.

In October 2000, ANP announced Brazil's third oil and gas exploration and production licensing round. On 20 June 2001, during the Third Bid Round, 53 blocks were offered by the ANP, 34 of which have been successfully awarded during the referred public bid, being 27 offshore and 7 onshore.

In December 2001, ANP announced Brazil´s fourth oil and gas exploration and production licensing round. On June 2002, during the Fourth Bid Round, 54 blocks were offered by the ANP, being 39 offshore and 15 onshore.

In November 2002, ANP announced Brazil´s fifth oil and gas exploration and production licensing round. During the Fifth Bid Round, which shall occur in August 2003, 1,075 blocks were offered by the ANP, being 262 onshore and 813 offshore. The reason why the number of blocks offered by the ANP have substantially increase is the fact that the Agency has decided to reduce the areas of the block offered, in addition to implementing several other new rules to be observed by the applicant companies interested in participating in the Fifth Bid Round.

Governmental Takes

The Governmental takes are regulated by Decree No. 2,705, of August 3, 1998 ("Decree"). According to such Decree, there are four types of governmental takes, to wit: (i) signature bonus; (ii) royalties; (iii) special participation; and (iv) payment for occupation or retention of area.

The signature bonus, which represents the actual amount offered by the interested company in the proposal for obtaining the concession, has its minimum value established in the bid notice, and shall be necessarily paid prior to the signature of the Concession Contract.

The royalties will be paid monthly in Brazilian currency and in the amount varying from 5% to 10% of the oil and natural gas production.

The special participation will depend on the volume of production or earnings under the Concession Contract.

The President of Brazil shall also issue a Decree in order to regulate the annual payment for occupation or retention of the area, which shall be fixed by square kilometer or fraction thereof of the block's surface.

At the criteria of ANP, a part of the payments listed above, and a variable percentage between 0.5% and 1.0% of the oil or natural gas production shall be paid to the surface holder.

Environmental aspects

Brazilian environmental policy is implemented at federal, state and municipal levels. The Brazilian Institute of the Environment (*Instituto Brasileiro do Meio Ambiente* - IBAMA) is an agency of the Brazilian Environmental Ministry and is responsible for implementing environmental policy at the federal level. States and municipalities have their own environmental agencies.

The environmental policy is regulated by Law No. 6,938, of August 31, 1981, which also defines the jurisdiction of each environmental agency, and the correct procedure to receive an environmental license. CONAMA (National Council of Environment) Resolutions No. 23/94 and No. 237/97 regulate and establish special procedures for environmental licenses for the exploration, drilling and production of petroleum and natural gas and provide general licensing procedures, requirements as well as list operations and facilities that must obtain environmental licenses, including drilling wells, petroleum and natural production operations. These licenses are the following:

- Operating License for Seismic Activities;
- Pre-Drilling License;
- Pre-Research Production License;
- Installation License; and
- Operating License.

In order to better regulate petroleum activities, IBAMA created an office responsible just for petroleum activities in early 1999; the Office for Licensing of Petroleum and Nuclear Activities is located in the capital city of the State of Rio de Janeiro, where 80% of Brazilian oil production takes place. The office is responsible for the review and issuance of license applications (which must include environmental studies, if requested by IBAMA) related to the oil industry.

The Brazilian Institute of the Environment – IBAMA understands, based on Article 10º of Law No. 6,938, of 8/31/81, regulated by Decree No. 99,274, of 6/6/90, and Article 1º of CONAMA (National Council of Environment) Resolution No. 06/86 that any offshore seismic activity requires prior approval.

The applicant for a seismic permit must demonstrate to IBAMA that the seismic activity will not cause any damage to the environment, and to any local economic activity. Federal and State Laws provide for

administrative, civil and criminal liability and sanctions for violation of environmental licensing requirements. These laws also provide penalties and sanctions for non-compliance with environmental licensing requirements. Important statutes are Law No. 9,605, of February 13, 1999 and Decree No. 3,179, of September 21, 1999, which define environmental crimes and establish the applicable sanctions. The Federal Environmental Crimes Law (Law No. 9.605/98) regulates criminal and administrative liability for environmental damages. It imposes severe administrative and criminal punishment on individuals and legal entities that participate in environmental damage, including officers, controllers, board of directors, managers and employees of legal entities (Article 2). Under the Environmental Crimes Law, enterprises and companies that operate without the necessary licenses or in disagreement with environmental legal requirements may be subject to grave penalties such as suspension of the activities as well as fines and imprisonment of the responsible individuals (Article 60). Fines may range from R$ 50,00 to R$ 50.000.000,00.

In addition to these statutes, there are several other supplementary regulations in connection with the registration of companies dealing with environmental inspections, publication of environmental licenses in the Official Gazette, implementation of Environmental Impact evaluation, etc (CONAMA Resolution No. 06/86).

CONAMA Resolution No. 265 of January 27, 2000, considering the need to establish safe strategies for prevention and management of environmental impacts generated by establishments, activities and oil installations and derivatives in the country, CONAMA decided, among other things, to make Petrobras and other companies, in the area of oil and derivatives, present for analysis and deliberation in the maximum period of 180 days, a work program and respective timetable for independent environmental audits in its oil and derivative plant facilities located in the national territory.

ANP Ordinance No. 3 of January 10, 2003, establishes procedures for the communication of the incidents listed therein, which include any intentional or accidental damages to environment or individuals, to be adopted by Concessionaires and companies authorized by ANP to exercise activities of exploration, production, refining, processing, storage, transportation and distribution of oil, its by-products and natural gas.

Normative Ruling No. 1, of July 14, 2000, published on the Official Gazette on July 17, 2000, which establishes criteria to be adopted by IBAMA (Brazilian Institute of the Environment), for the concession of the registry of chemical dispersants in leakage of oil and their derivatives in the sea.

Law No. 9,985, of July 18, 2000, published on the Official Gazette on July 19, 2000, whish regulates article 225, first paragraph, items 1, 2, 3 and 7 of the Brazilian Constitution and create the National Conservation Unit System, among other provisions.

Law No. 10.165, of December, 2000, published in the Official Gazette on December 28, 2000, institutes the new Environmental Inspection and Control Fee, to be paid to the Brazilian Institute of the Environment and Renewable Natural Resources (IBAMA) by all individual and legal entities which exercise potentially polluting activities and are users of natural resources. Fines may range from R$ 50,00 to R$ 2.250,00, based on pollution potential, grade of use of natural resources and size of company and its payment shall be quarterly.

CONAMA Resolution No. 273, of November, 2000, published in the Official Gazette on January 8, 2001, established that the location, construction, installation, modification, enlargement and operation of distributors, gas station, retail system installation, and floating gas stations shall depend on the prior licensing of the authorized environmental agency without detriment to other licenses legally required.

CONAMA Resolution No. 269, of September 14, 2000, published in the Official Gazette on January 12, 2001, established that the production, importation, selling and use of chemical dispersants for operations to deal with spills of oil and its derivatives at sea, may only be done after obtaining registration of the product with the Brazilian Institute of the Environment and Renewable Natural Resources – IBAMA. The use of chemical dispersants on leaks, spills and discharges of oil and its derivatives at sea shall obey the criteria provided in the regulation annexed to this Resolution.(Article 2).

Ordinance No. 38 of March 8, 2001, published in the Official Gazette on march 9, 2001.This Ordinance together with the Brazilian Institute of the Environment and Renewable Natural Resources – IBAMA and the Secretariat of the Environment and Hydro Resources of the Federal District – SEMARH, with the purpose of establishing a Environmental Technical Chamber, resolve to install the Environment Technical Chamber – CTA, to analyze the environmental licensing process of undertakings considered as effective or potential polluters, as well as those capable, under any circumstance, of causing environmental degradation within a radius of 10 kilometers around existing Federal Conservation Units in the Federal District, aiming to comply with the provisions of CONAMA Resolutions Nos. 13/90 and 237/97. The respective Environment Technical Chamber will analyze, among others, undertakings such as: land parceling, mineral exploration, gas pipelines/multi-pipelines, industrial operations among others.

CONAMA Resolution No. 281 of August 12, 2001, relating to model environmental licensing application forms, was published in the Official Gazette of the Union on August 15, 2001. This Resolution establishes that publication models forms for a license application, its renewal and concession are required only for undertakings and operations pursuant to Article 2, of CONAMA Resolution No. 06/1986, including among others: ports and terminals for minerals, oil and chemical products, oil, gas and mineral pipelines; power transmission lines above 230 kV; extraction fossil fuels (oil, shale and coal); electric power plants above 10 Mw, whatever their source of primary energy; industrial and agro-industrial complexes and units (petrochemical, steel mills, chlorine-chemicals ...), or for those undertakings or operations which are identified as having a significant environmental impact according to the criteria of the authorized

For other cases where environmental licensing is required, authorized environmental agencies may establish simplified publication models forms for licensing, renewal and concession. However, on the omission of the environmental agency, the norms established in CONAMA Resolution No. 06/1986 shall prevail.

Brazilian Institute of the Environment (IBAMA) published in the Official Gazette, on August 29, 2001, Normative Ruling No. 10, which establishes the Federal Technical Registry of Potentially Pollutant Activities or Users of Environmental Resources. The referred Normative Ruling establishes that those who are subject to the Environment Control and Inspection Tax - TCFA are required to deliver the Annual Report to IBAMA by March 31 of each year in regard to the preceding year's activities. The current Annual Report should be sent via the Internet to the IBAMA site at http://www.ibama.gov.br, E-mail or by mail. Noncompliance shall subject the violator to a fine as provided for in paragraph 2 of Article 17-c of Law No. 6938/91.

However, for those who have not as yet delivered the Annual Report on Activities for the year 2000 shall have their date of delivery extended to October 31, 2001, according to IBAMA Normative Ruling No. 16, published on October 1, 2001.

The complexity of the environmental studies performed and the timing for the issuance of licenses may vary depending on where the exploration activities are to be performed. Activities performed close to an environmental reserve, for example, may require a more complex investigation and therefore a longer time period for IBAMA to review the application.

Environmental licenses always are issued with certain conditions that the applicant must comply with or the license will lose its validity.

Finally, since petroleum activities have only recently resumed in Brazil, the regulation of these activities from an environmental standpoint has just begun, based on existing licensing procedures, the Petroleum Law and the interpretation of IBAMA. However, the new legislation illustrates the Brazilian authorities' concern regarding the increase in petroleum activities.

Downstream

Any company may submit a proposal to ANP to operate or to construct refineries or operate natural gas processing units, as well as to construct installations and use any means of transportation for the oil, its derivatives and natural gas, either for domestic supply or for import and export, provided they company with the provisions set forth under Article 5 of the Petroleum Law as well as the applicable regulations.

The opening-up of a distributor in Brazil is a simple procedure, which requires a prior authorization and registration by ANP. The Agency issued several specific ordinances regulating and explaining in detail all necessary documentation and information to be provided so as to obtain said authorization.

In order to obtain both the registration and the authorization, the prospective distributor must meet several conditions, among which is the minimum stated capital, and it must have the necessary infrastructure for storing the by-products.

Exportation and importation

In order to receive the authorization to export or import crude oil and its by-products, the exporter or importer must provide ANP with all necessary information and documentation related to the business to be rendered, in observation of the ANP's applicable regulation. Such information must be updated by the companies every 18 (eighteen) months, subject to the cancellation of said authorization.

Both the importation and exportation of crude oil, its by-products and condensed gas, according to specific ordinances issued by the ANP which regulate this business, shall be performed in strict compliance with certain objectives and principles set forth by the Petroleum Law, such as protection of the consumer's and the Brazilian Treasury, foreign trade rules, national energy policy, principles of transparency and legality, rules for protection of the economic order and environmental regulation.

Taxes

Companies engaged in the oil industry are obliged to pay all the mandatory Brazilian taxes and contributions that apply to any other industry. In addition, they are also subject to a specific contribution, the so-called CIDE, to be levied on local sales and import transactions involving oil, natural gas, ethyl alcohol fuel and their by-products. The CIDE is levied at fixed rates depending on the nature of the product and can be deducted from the PIS and COFINS (federal welfare contributions) levied on revenues resulting from the products commercialization.

Special tax payment treatments may apply for companies in the oil industry, such as: the up-front payment as a substitute taxpayer of certain taxes and contributions for the activities performed from the refinery to the consumer.

The Brazilian IRS Regulation also provides special benefits to companies engaged in oil & gas activities, as well as the possibility of amortizing costs and expenses incurred in the exploitation of oil & gas deposits for the number of fiscal years in which the benefits arising from these expenses and costs shall be enjoyed.

In order to develop the oil & gas industry in Brazil, the Federal Government also created a special customs regime called "REPETRO". This regime intends to provide E&P companies access to research and exploitation equipment with a reduced tax burden. It also aimed to grant local suppliers favorable conditions *vis-à-vis* foreign equipment.

The REPETRO regime allows that:

goods imported under the temporary admission regime remain in Brazi with complete suspension of federal taxes levied on importation (Import tax and Federal Excise Tax) for the duration of the contracts entered into to carry out operations;

raw materials, finished or semi-finished products and parts to be used in the manufacture of goods used in research and exploitation of oil & gas to be imported under the drawback regime, that is to say, with suspension of federal taxes levied on importation;

domestic sales of goods to be equated to that of exportation for fiscal and exchange purposes, provided that the purchaser is a company domiciled abroad and that the payment is made through convertible currency. This benefit is called "fictitious export".

Note that the temporary admission regime, mentioned in item (i) above, might be granted for foreign goods and equipment as well as for goods and equipment manufactured in Brazil, under the drawback regime, or not, and symbolically exported.

The Federal Revenue Office enacted Normative Ruling No. 04/01 clarifying the REPETRO procedures. This Normative Ruling provides a list of goods and equipment which might be subject to REPETRO regime. Vessels and wet Christmas trees, among others, are included in this list. Notwithstanding the above, REPETRO regime is also applicable to equipment and spare parts to guarantee the operation of the goods listed in Normative Ruling No. 04/01.

International Trade Regulation

The international trade system, established under the WTO, has a direct impact on virtually all trade in goods, the international provision of services, including distribution, telecommunications, financial and professional services, and the protection of intellectual property rights. These rules provide businesses with access to new markets, improved competitive conditions in existing ones, a predictable framework in which to plan investment and within which to rely upon meaningful enforcement of international obligations.

Brazil is a founding member of the WTO and, as such, the Brazilian Government is responsible for ensuring compliance with the WTO Agreements at a national level, for safeguarding the Brazilian industry against unfair trade practices implemented abroad, as well as for affording commercial predictability to foreign companies.

The WTO Agreements were incorporated into national law in December 1994, following the ratification of Presidential Decree No. 1.355 of December 30th, 1994. In order to comply with its obligations under the WTO, Brazil has adopted supplementary regulations in several fields, including subsidies and countervailing measures, antidumping measures and safeguards. Law No. 9.019/95 provides for the application of antidumping duties and countervailing measures, and Decrees Nos. 1.602/95 and 1.751/95 discipline the administrative proceedings carried out for determination and elimination of the practices of dumping and subsidies, respectively.

An Overview of the Brazilian Trade Remedy Regime

Other than import restraints, a number of policies of firms or governments are designed to influence international trade flows. In particular, both governments and enterprises may wish to promote exports through the use of discriminatory pricing or subsidies. For decades, many versions of these practices have been considered by the international system and many national systems to be "unfair". To such practices the international rules have permitted certain responses from the importing nations, such as antidumping duties or countervailing duties.

In brief, the administrative procedure for the investigation of alleged dumping or subsidy can be divided into three phases. The first entails a scrutiny of the petition, filed by the petitioner(s) representing a domestic industry. This petition should include, *inter alia*, positive information so as to demonstrate the practice of dumping/subsidy, the harm to the domestic industry and the causation link between the dumping/subsidy measure and the injury to the domestic industry. The Brazilian authorities (SECEX/DECOM) will carry out an examination of the petition, and they may ask for additional information during the second phase of the procedure, which will be concluded after a final hearing to be attended by the petitioner and interested parties. At this hearing a technical note will be circulated, summarizing the main data that will be considered by SECEX/DECOM when evaluating the case.

The last stage encompasses the submission of the final opinion drafted by SECEX/DECOM for the review of the Trade Protection Technical Group (GTDC), which is a task force created under the authority of the Brazilian Chamber of Foreign Commerce (CAMEX). CAMEX, which is in charge of formulating policies and coordinating activities related to foreign trade, will then issue a final decision as to whether or not impose a provisional or definitive antidumping duty or countervailing measure.

Trade remedies are efficient tools that may be used by the private sector in Brazil as a competitive advantage to impede that the increase on imports jeopardizes its market share in the national market. Among the **benefits** of trade remedies stand out guaranteeing market presence at a national level and protecting investments related to the entry into this market.

Given the frequent recourse to the above-mentioned remedies by WTO Members, such mechanisms have actually been applied as non-tariff barriers against imports. Therefore, participating and intervening in dumping investigations undertaken abroad is of great importance to Brazilian exporters. Likewise, foreign companies exporting to Brazil must be aware of possible investigations initiated at a national level that may affect their commercial interests.

WTO Law in Brazilian Courts

The Presidential Decree No. 1.355 of December 30th, 1994, incorporated the WTO Agreements into national law, thereby conferring jurisdiction to domestic courts to overview claims of violations to such rules.

The WTO offers importers and exporters a set of tools with which to open markets that would otherwise remain closed. To take advantage of WTO opportunities a business must learn how to use the rules, understanding and incorporating them into its strategies and monitoring a country's compliance with its obligations under the WTO.

When should a business use domestic courts in Brazil to enforce WTO rules? The following are examples of situations in which a government may be in violation of its WTO undertakings, and a remedy may be available:

Internal laws and regulations are applied in a manner so as to protect domestic production *vis-à-vis* imports;

A government discriminates against imported or exported products, or services and service suppliers based on the country of origin, i.e. goods or services from distinct origins are granted with different treatments;

Antidumping or countervailing duty investigations are conducted by governments in a manner that is not consistent with international law, to the detriment of imports;

Environmental protection rules, sanitary measures or technical requirements are applied so as to block imports;

Import licensing regime inconsistent with WTO rules;

A government imposes export restrictions to joint ventures that have foreign investment.

Private companies are increasingly presenting claims before domestic courts questioning WTO-inconsistent measures, especially in the fields of tax regulation, rules of origin and environmental law.

Corporate Criminal Law

Some of the main issues related to corporate criminal law in Brazil involve:

- crimes against the National Financial System;
- crimes against the economic order;
- unfair competition crimes;
- antitrust crimes;
- tax evasion crimes;
- copyright crimes;
- industrial property crimes;
- crimes against consumers;
- environmental crimes;
- money laundering crimes;
- corruption crimes;
- crimes against the Social Security;
- press act crimes; and,
- crimes against the honor.

Brazilian System of Evidence

The criminal procedure and the criminal probationary system in Brazil are governed by principles and rights provided in the Brazilian Federal Constitution ("Federal Constitution").

The Federal Constitution, in its Article 5, sets forth that no individual will be deprived of his/her own freedom or assets without the right of defense by the due legal procedure, further securing the right to the so-called adversary proceeding and legal defense.

In addition to the legal defense, as well as the adversary proceeding and due legal procedure, the Federal Constitution also establishes, among other guarantees, the following:

- "no one will be submitted to torture nor to inhumane or degrading treatment",
- "inviolability of intimacy, private life, honor, home, and mail, telegraphic communication, data and telephone communication and personal image",
- "there will be no judgment or court of exception",
- "there is no crime without a previous law that defines it nor penalty without a previous legal sanction",
- "the criminal law will not retroact unless for the benefit of the defendant,
- "no penalty will go beyond the person of the defendant",
- "penalty individualization",
- "no one will be prosecuted nor sentenced if not by the competent authority",
- "inadmissibility in the proceedings of evidence obtained by illicit means",
- "culpability until the criminal sentence becomes final and unappealable",
- "publicity of the procedural acts", and
- "the right to remain in silence".

The due legal procedure presupposes the adversary proceeding (guaranteeing equal procedural defense opportunities) and the guarantee of full defense (technical defense and self-defense).

The due legal procedure provides for the possibility to reverse the judgment rendered – it could be appealed at the higher courts, as provided in the Federal Constitution in the already referred to Article 5, item LV, and Article 93, item III ("access to the higher courts").

Illicit evidence is prohibited by the Federal Constitution because evidence must be provided by law – *nulla coatio sine lege* – and by legal means – Federal Constitution, Art. 5, item LVI).

Accordingly, we highlight the principle of presumption of innocence, i.e. every defendant is presumed to be innocent until the award of the final condemnation sentence (Federal Constitution, Art. 5, item LVII) – negligence should be legally and judicially proved and evidence should fully regard the due legal procedure.

In the Brazilian Criminal Procedural System, the one who makes any allegation has the burden to prove it (Criminal Procedure Code, Art. 156). However, the defendant has no obligation to prove his innocence because it is presumed. During the course of the criminal action the prosecution is in charge of proving all the allegations contained in the accusation complaint (denunciation).

The Brazilian Criminal System grants the defendant the right to remain in silence, which cannot be interpreted against him/her. This is the constitutional guarantee of no self-incrimination (Federal Constitution, Art. 5, item LXIII), the right not to produce evidence against the defendant. Thus, the

defendant cannot be prosecuted for lying or omitting facts in his/her own defense nor be prosecuted for crime of false testimony.

In case of doubt, the defendant should always be acquitted because of another constitutional guarantee, i.e. *in dubio pro reo*.

Therefore, the evidence is the spinal column of the criminal procedure, thus identifying the effects of the crime, its results and reasons. There is no crime without a result, and criminal conviction for simple presumption or formal evidence is not admissible.

Summary of the Legal Procedures

Please see below summary of the criminal law procedures in Brazil.[1]

According to the Brazilian law, the Criminal Prosecutor is allowed to denounce the offender when there are elements proving that one or more crimes were committed and also that there are enough elements to indicate who committed the crime. Usually, the Criminal Prosecutor grounds the formal accusation on the outcome of the investigations conducted during the police enquiry.

Additionally, a police enquiry may be launched at the request of the Prosecutor or Judge, as well as upon the pressing of a charge or preliminary investigation.

Once the police enquiry starts, the Police Chief in charge will indicate what kind of investigation should be conducted and will make other provisions, such as the conduction of hearings.

In spite of the fact that it is difficult to accurately estimate, a police investigation is expected to last from at least six months to a few years, sometimes getting close to the term set forth in the the statute of limitations.

According to the Brazilian applicable laws, every thirty days or so the police enquiry has to be sent to the Criminal Court, to request additional time for further investigation, until the Police Chief writes a final report. It takes a few days for the proceedings to be submitted to Court, where the Criminal Prosecutor has to agree with the time requested, and then the proceedings return to the Police Station.

In Brazil the police enquiry is in writing, and includes deposition (but excludes cross-examination).

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1 The following underlined terms are defined as provided below:

Criminal lawsuit [*Ação Penal*]: a formal proceeding instituted against the defendant, which is commenced at the Criminal Court;

Criminal Judge [*Juiz Criminal*]: the judge who is responsible for the Lower Criminal Court;

Formal accusation or "Denunciation" [*denúncia*]: the charge pressed against one or more persons by the Public Prosecutor at the Criminal Court; denunciation;

Indictment [*indiciamento*]: the formal act by which the Police Chief identifies the presumed suspect of the crime;

Criminal Prosecutor [*promotor criminal*]: the public prosecutor (district attorney) who works at the Lower Criminal Court and is responsible for overseeing the investigations and filing a formal accusation or shelving the records of the police enquiry;

Shelving of the records [*arquivamento*]: the act by which the Criminal Prosecutor requests the Judge to close the case when there is no crime or there is no suspect at all;

Police enquiry [*inquérito policial*]: a formal proceeding in course at the Police Station and headed by the Chief of Police, which aims to gather evidence to support the formal accusation;

Police precinct clerk [*escrivão de polícia*]: the assistant to the Police Chief, who will launch the police enquiry;

Police Chief [*delegado*]: the precinct chief who heads the police enquiry;

Criminal Expert *[perito*]: the technical professional who assists in the investigations whenever requested by the Police Chief and Criminal Prosecutor and who usually works at the Criminal Institute [*Instituto de Criminalística*];

Police inspector [*investigador*]: the assistant to the Police Chief, who will conduct the necessary investigations.

In fact, the Police Chief is supposed to gather all evidence that will enable the Criminal Prosecutor to opt for one of the following alternatives:

- File a formal accusation - there is evidence of crime - in which case the Criminal Prosecutor will ask the Judge to commence a criminal lawsuit against the individuals responsible for the crime;
- Shelve of the records - there is no crime, there is lack of evidence or there is no one responsible for the crime – in which case the Criminal Prosecutor asks the Judge to close the case;
- Ask the police to make further investigations.

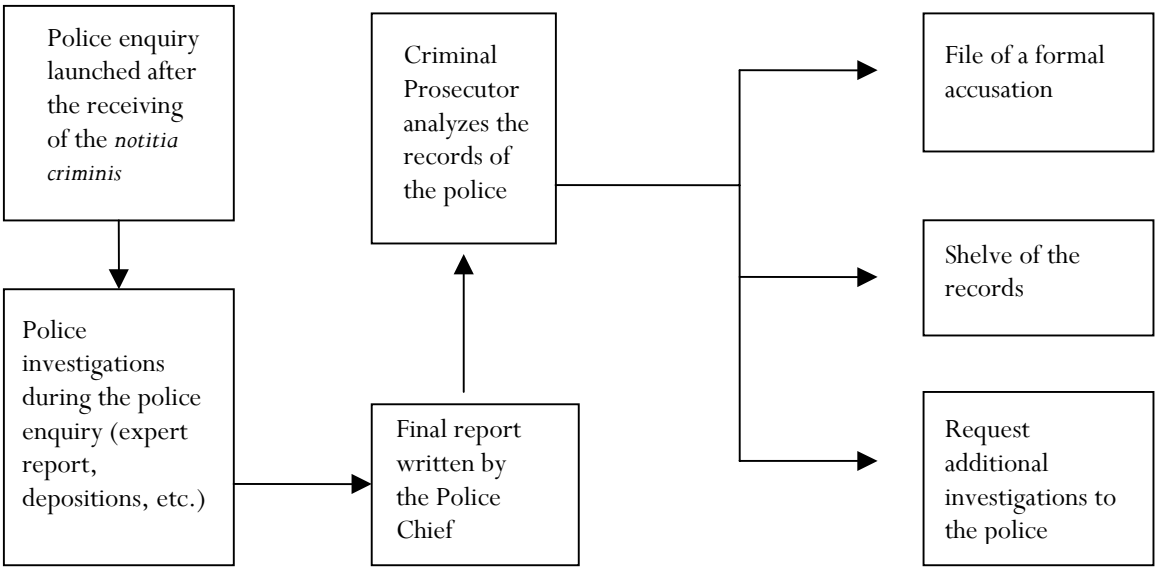
During the police investigation, when the Police Chief decides he has enough elements to identify an individual as a suspect, he/she will be indicted (indictment).

Moreover, the Police Chief can request the production of a criminal expert report if there is any sign that a crime was committed.

Notwithstanding the fact that the request for production of a criminal expert report is made by the Police Chief or Criminal Prosecutor, the Criminal Institute [*Instituto de Criminalística*] is deemed an independent public body.

A criminal lawsuit only starts when the Criminal Judge receives a formal accusation or "denunciation" (technical term). After receiving the document presented by the Criminal Prosecutor, whereby he/she states that one or more crimes were committed and also that there are enough elements to identify who committed the crime, the Judge will set a date for interrogatory (the hearing of the defendants). The formal accusation/denunciation presented by the Criminal Prosecutor lists the witnesses he wants the Judge to hear.

Below follows a chart summarizing the flow of the Police Enquiry until the start or discontinuance of a Criminal Lawsuit:



Criminal liability of corporate managers

On the one hand, the criminal liability results from the committing of a crime, which is an unlawful fact provided by law, imputable to someone due to willful misconduct or negligence. This fact must be set forth in the criminal legislation, considering that there is no punishment or crime without a previous law (*nulla poena nullo crime sine lege*).

On the other hand, the criminal offense does not exclusively lead to the State's intention to punish. It also leads to the individual's intention to seek indemnification for the damage caused to the victim. The civil liability, therefore, can also arise from an offense, which resulted in damage, pecuniary or not, to the victim.

Thus, the system adopted in Brazil is that of the Separation or the Independence of Instances, in which it is recognized the independence between the civil and the criminal courts, excepting, however, that the criminal decision regarding the authorship and the existence of the offense prevails over the civil decision. Therefore, the Judge of any civil lawsuit is allowed to suspend the course of the respective proceedings until the judgment of the criminal lawsuit.

This means that an unappealable criminal decision is valid at the civil courts, where the party may directly file for a collection lawsuit, without the need to commence a new discovery phase (with hearings, experts etc).

Differently from what occurs in the civil sphere, the Brazilian Criminal Law does not accept the so-called strict liability, once all crimes must be evidenced and, necessarily, result from willful misconduct or negligence. The chain of causation has to be present as a condition to establish the criminal liability. The Brazilian Criminal Law, therefore, operates under the name of culpability or subjective responsibility Criminal Law.

The criminal liability is personal. It has always been personal, which means that only the person who is directly related to the crime may be held liable for the illicit act. Such principle, under Article 29 of the Criminal Code, sets forth that the corporate entity, exception to the offenses committed against the environment, is not to be criminally held liable for its actions. Nevertheless, all of its employees, managers, officers and legal representatives, who committed any criminal act, will be held liable for the offense, even if acting on behalf of the company, to the extent of their culpability.

Resulting from the explanation above, we may conclude that only the individual who participated in the offense can be criminally sued. Officers, managers, legal representatives or employees of the company, who have not taken part in the offense, whether due to lack of authority or interference in the matter, or because they were not in the company upon occurrence thereof, cannot be held criminally liable for the offense.

The purpose of the criminal liability is to punish the company's manager for the acts performed by him/her previously identified as a crime under the provisions of the current criminal laws in force.

Finally, it is important to mention that the Public Prosecutor, upon preparing the charge (technically called "denunciation"), must describe the facts, as required by law, informing the conduct of each defendant, further clarifying how each defendant effectively participated in the criminal act.

However, our case laws and jurisprudence have different opinions about the validity of the generic denunciation, which does not specify and separate the defendant's conduct, in the so-called corporate crimes.

According to our understanding, however, even in corporate crimes, the description of the participation of each defendant in the criminal act is a requirement essential to denunciation (formal charge pressed by the Public Prosecutor) because of the imposition of the constitutional guarantees of the criminal proceedings. In crimes committed "through a corporate entity", the criminal liability of the ones that took part in the offense is subject to the degree of culpability of each one of them.

We also agree with the understanding that the acceptance of the generic denunciation confirms the criminal strict liability, what is inadmissible in view of the specific constitutional guarantee of presumption of innocence.

In summary:

- criminal liability is personal;
- legal entities do not commit crimes and do not have criminal liability, except in crimes against the environment;
- the criminal liability of officers or managers cannot be determined due to the fact that they are representatives of the corporate entity;
- the criminal liability of the representatives of the corporate entity must be verified separately by evidencing their participation in the illicit act, and strict liability cannot be accepted in relation thereto.

Corporate crimes

In the beginning of the eighties, the first laws concerning corporate crimes, also known worldwide as white-collar crimes, started to appear in Brazil.

The appearance of corporate crimes, distinguished by a more intelligent and sophisticated *modus operandi* of the one who practices the crime, led to development and adjustment of the criminal legislation in order to provide and effective response to this special kind of criminality.

Below follows a summary of the criminal liability of corporate managers in accordance with the current laws in force, mainly under the provisions of (i) tax, (ii) labor, (iii) bankruptcy, (iv) environmental, (v) consumer, and (vi) economic laws:

Criminal Liability of the managers under tax laws (Brazilian Tax Code and Law No. 8.137/90)

The manager would be held criminally liable for tax evasion crimes and crimes against the economic order provided in Law 8.137/90[2], if the company's manager, for example, neglects information or provides false information to the tax authorities or deceives the tax inspection authorities, providing incorrect or untrue data or neglecting operations of any kind in a document or book required by the tax laws.

2 It defines the crimes against the tax and economic order and against consumer relationship, and makes other provisions.

Criminal Liability of managers under labor laws

In the criminal sphere, the manager would be held liable if, for example, he/she fails to comply, through fraud or violation, with a labor right assured by the labor laws currently in force.[3]

Criminal Liability of managers under bankruptcy laws (Decree No. 7.661/45)

Decree-Law No. 7.661/45 further provides for criminal liability in the event certain typified acts are performed upon the company's bankruptcy. In addition, the managers will be held equivalent to the debtor or the bankrupt party for all criminal purposes provided in the aforementioned Decree-law.[4]

Criminal Liability of managers under environmental laws

The manager could be held liable for environmental crimes, if he/she contributes to the performance of a criminal act or if, being aware of such illegal conduct of a third party, the manager fails to prevent its performance, as the case may be.[5]

The Environmental Code has introduced a new provision, which foresees the possibility to hold the company's manager liable for the environmental crimes committed.

Criminal Liability of managers under consumer laws (Law No. 8.078/90)

The company's manager could be held liable for the crimes provided in the Consumer Protection Code, if the manager contributes to such crimes or causes, allows or in any other manner approves the supply, offer, display for sale or maintenance in warehouse of products, or the rendering of services under the conditions not provided by the Consumer Protection Code.[6]

Criminal Liability of managers under economic laws (Laws No. 8.884/94 and No. 8.137/90)

Law No. 8.137/90 defines the acts deemed crimes against the economic order, which may be attributed to the manager, provided that performed by the company's manager.

Other considerations regarding the liability of managers within the criminal sphere

The Brazilian Criminal Code does not provide for the criminal liability of the managers in any special chapter, but typifies certain conducts, i.e. the manager who makes a false statement about the economic situation of the company or willfully neglects, fully or partially, facts related to the company or distributes fictitious profits or dividends.[7]

It should be noted that, in connection with the liability of managers within the criminal sphere, the deprivation of freedom and alternative sanctions are to be applied to the company's legal representatives, once proved that they have contributed to the practice of the crime through negligence, imprudence or malpractice.

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3 Article 203 of the Criminal Code.
4 Article 191 of Decree-Law No. 7.661/45.
5 Article 2 of Law 9.605/98
6 Article 75 of Law No. 8.078/90
7 Article 177 of the Criminal Code

Notwithstanding the crimes provided in the Brazilian Criminal Code and the abovementioned laws, the criminal liability of managers is also provided in case of crimes against welfare (Law No. 1.521/51) and crimes against intellectual property and unfair competition (Law No. 9.279/96).

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