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# BRAZIL

*The following is a review of legal and economic developments in Brazil.*

## I. LEGISLATIVE AND ADMINISTRATIVE RULINGS

### *The New Brazilian Constitution*

On Friday, September 2, 1988, the National Constituent Assembly finished voting on the new Brazilian Constitution, approximately 19 months after the 569-man Assembly first convened. The result of all these months of work was a 250-article text which introduced substantial changes in the political and economic scenario of the country.

Promulgation of the new Constitution took place on October 5, 1988, when the Assembly met for the last time as a Constituent Assembly.

Breaking away from the Brazilian tradition of having constituent assemblies working on an initial draft, the new Constitution was the result of three dozen subcommittees, whose drafts were put together by committees and finally joined in a first draft taken to the floor of the assembly earlier in the year; it then was submitted to two rounds of votes. In addition to the work of the representatives, about 12,000 proposals generated by unions, organized groups, lobbies and various kinds of organizations received thousands of signatures from voters and were finally voted on the floor of the Assembly.

Reactions to the new constitutional order were diverse. While the number of articles may be a surprise to foreigners, it must be said that, at least in this regard, the new constitution was consistent with the Brazilian legal traditions. So far, the country has had seven constitutions, including the one promulgated just after independence, in 1823, when Brazil was still an empire and had a former Portuguese king as Emperor. All the texts had similar lengths.

In other respects, however, the Constitution was an all-new document. First of all, its bill of rights, with which the Constitution began, was unanimously acclaimed as the most liberal the

country has ever had or could have wished for. A full range of civil rights and liberties was included in the text, from absolute freedom of speech to the right to demand from a court of law that it rule on constitutional provisions that have been left unregulated by legislators, so as not to deny a citizen any of his constitutional rights.

In the more specific field of government, the Constitution provided for the direct election of the President of the Republic, a right denied to Brazilians since 1960, when the last presidential election took place.

However, much of the criticism received by the new Constitution was targeted at its economic provisions. In a world where even Eastern European countries have decided to open up their economies and markets to foreign investment and some sort of free enterprise, the new Brazilian Constitution laid down principles that guaranteed companies controlled by Brazilian citizens preferences over other companies located in Brazil. The possibility of closing certain sectors of the domestic market for only domestic investment and a 12% limitation on "real interest" (a term yet to be defined by law) were some of the provisions that led the business community to manifest strong criticism of parts of the text.

### *Special Export Zones*

For the last two years, heated debates occurred in Brazil about the new economic model the country would adopt. Behind the debates lay the fact that the import-substitution model, adopted from the late 1940s until the early 1980s, was exhausted and a new model had to be found. Notwithstanding the differences in size and diversification of the economy between Brazil and the Pacific Basin countries, the Asian countries were elected by some as the model for observation. The idea of creating special export zones, such as those existing in Taiwan and Korea, where certain facilities are granted to new foreign enterprises established themselves in such areas, was at the center of the debate. While the opening up of the Brazilian economy to foreign competition was defended by most of the groups interested in influencing the federal administration, the degree varied substantially. The competition between companies located in these free trade zones and other companies in the country were considered by most of the business community as unfair.

On July 29, 1988, the President of the Republic put an end to the discussion on the export zones by signing Decree-law No. 2452, creating the so-called Export Processing Zones (ZPE). The ZPE's are free-trade areas, isolated from the rest of the country by trade and exchange barriers. It was expected that foreign industries would be attracted to such areas by the tax incentives and foreign exchange facilities offered. In accordance with article 1, the purpose of the ZPE's was to enhance the Brazilian balance of payments, reduce regional economic imbalances and promote the diffusion of technology and economic growth.

The location of each ZPE would depend on the interest of the Municipalities and the States. Either of these submitted a proposal to the National Council of ZPE's, which would review it based on certain criteria such as access to ports and airports and the availability of infra-structure. In such proposal, the State or the Municipality would assume all of the costs of the works and expropriations required as well as prove the existence of funds to bear such expenses. Decree-law No. 2452 expressly prohibited the federal administration from assuming either directly or indirectly the burden of any such costs.

A company interested in establishing itself in a ZPE would also present a proposal which, in accordance with Decree-law No. 2452, would prove to be incremental to Brazilian exports. If approved, the company would be required to execute a commitment to open a foreign currency denominated account in Brazil, spend in Brazil a minimum amount of the funds necessary for its installation costs, and agree not to produce goods subject to the export quota system on the date of the commitment.

In return, a company installed in a ZPE would be exempt from the following taxes and duties:

- (i) import duty;
- (ii) tax on manufactured products;
- (iii) contribution to the Social Development Fund (FINSOCIAL);
- (iv) additional charge to the Freight for the Renovation of the Merchant Navy;
- (v) tax on credit, exchange and insurance transactions;
- (vi) tax on transactions with securities; and
- (vii) income tax on any remittances and payments abroad.

Such companies would be subject to income tax on the profits earned in their ZPE operations. However, they would be able to import any goods, equipment, raw materials and parts necessary to their manufacturing activities. No license would be required for any such imports, as well as for any export from the ZPE's, except for those required under sanitary, environmental protection and national security regulations. There would be no control on foreign exchange transactions to and from a company located in a ZPE.

In order to protect companies located elsewhere in the country, sales from companies located in a ZPE to the rest of the country would be subject to a 10% tax denominated "interning tax." Any sale from a ZPE to the rest of the country would be treated as an import: conversely, any sale to a ZPE would be treated as an export transaction (DOU-I, July 30, 1988).

### *Warrants*

Acting under its authority to regulate transactions by financial institutions, the National Monetary Council established the rules governing the acceptance by commercial banks of bills of exchange arising from credit transactions guaranteed by the pledge of warrants. These new rules were issued by the Central Bank of Brazil by means of Resolution No. 1502, dated July 28, 1988.

Under Brazilian law a warrant is a registered credit document, transferable by endorsement, issued by warehouse companies together with a deposit receipt, by means of a subordinated guarantee of the deposited merchandise.

Resolution No. 1502 expressly authorized commercial banks to accept bills of exchange arising from credit transactions guaranteed by the pledge of such warrants. These bills of exchange and the credit transactions would have a minimum period of 60 days and a maximum term of 180 days. The warrants would be accompanied by the deposit receipts and would remain with the bank until liquidation of the transaction and may not be issued by warehouse companies connected, directly or indirectly, with the borrower. Moreover, the warrants eligible for transactions under Resolution No. 1502 were only those arising from the deposit of agricultural products. The credit based on such transactions could not exceed 80% of the value of the products represented by pledged warrants, such value to be calculated based on the minimum or guaranteed prices practiced by the federal government for

the respective agricultural product. Subsequent to Resolution No. 1502, the Central Bank also issued Resolution No. 1503, authorizing private and public pension plan companies, insurance companies and capitalization companies to invest in bills of exchange accepted by commercial banks and arising from credit transactions based on the pledge of warrants regulated by Resolution No. 1502.

#### *Sale of Fuel to Foreign Ships*

On August 3, 1988, the Department of Foreign Exchange of the Central Bank of Brazil, based on the Central Bank's powers to regulate foreign exchange transactions in Brazil, issued DECAM Communiqué No. 1110, providing that the supply of fuel to foreign ships was subject to the export license system and the sale to a bank authorized to deal in foreign exchange of the foreign currency received in payment for the fuel supplied. DECAM Communiqué No. 1110 also set forth the rules for the settlement of the sale of the foreign currency by fuel suppliers.

#### *Tax Collection Period*

Struggling with a federal public deficit of 4% of the gross national product, the federal administration searched for new ideas to help reduce the deficit. On July 29, 1988 the President of the Republic signed Decree-law No. 2450, determining that, as of August 1st, the period for the determination and collection of the tax on industrialized products would be 15 days. Until that date, the period for the determination and collection of IPI tax was 30 days; this gave the companies a great advantage as the amounts of this tax could be invested in the market during that period.

#### *Banco Holandês Unido S.A.*

On August 2, 1988, the President of the Republic signed Executive Decree No. 96454, authorizing Banco Holandês Unido S.A., a subsidiary of a financial institution located in the City of Amsterdam, The Netherlands, to open two more branches in Brazil. BHU was one of the few foreign banks operating in Brazil through branches.

*Morgan Guaranty Trust Company of New York*

On August 4, 1988, the President of the Republic signed Executive Decree No. 96471, authorizing Morgan Guaranty Trust Company of New York, a financial institution located in the City of New York, State of New York, United States of America, to operate in Brazil for an indeterminate period of time, as successor of Banca Commerciale Italiana (BCI), to conduct banking activities, including foreign exchange transactions. Morgan Bank agreed to acquire from BCI its two branches in Brazil prior to the issuance of Executive Decree No. 96471.

*The First National Bank of Boston*

On July 22, 1988 the President of the Republic signed Executive Decree No. 96399, authorizing The First National Bank of Boston, a financial institution located in the City of Boston, State of Massachusetts, United States of America, to open seven more branches in various cities of Brazil. The Bank of Boston was one of the few foreign banks operating in Brazil with branches, and was not a subsidiary.

*Intermodal Transportation*

By means of Resolution No. 4, dated August 12, 1988, the Coordinating Committee for the Implementation and Development of Intermodal Transportation (CIDETI), acting under its authority to develop studies on national and foreign legislation governing the international transportation of unitized cargo, released for public comment a project of a bill of law regulating intermodal cargo transportation in Brazil. Suggestions and comments from interested persons and entities were remitted to the Ministry of Transportation, to the attention of the CIDETI.

Divided into six chapters, this project of a bill of law defined intermodal transportation as the transportation of cargo which utilized more than one modality of transportation from the origin until the final destination of the cargo. Companies interested in rendering such services would be registered and accredited with the public agency responsible for regulating each type of transportation as well as the Ministry of Transportation.

The project expressly determined that services of domestic in-

termodal transportation could only be rendered by Brazilian companies duly registered and accredited in accordance with the proposed bill of law. For this purpose, a Brazilian company was one in which two-thirds of the voting capital was held by Brazilians. The proposed bill of law regulated the transportation contracts, the civil liability of the transporter, the penalties for breach of rules set forth therein as well as the rules applicable to the transportation of unitized cargo.

## II. JUDICIAL AND ADMINISTRATIVE DECISIONS

### *The Right to Judicial Review*

In administrative proceedings submitted to the Chief of Staff of the Presidency of the Republic, the Counsellor General of the Republic issued an opinion holding that public companies, as well as other decentralized units of the federal administration, had the constitutional right to sue the Union, i.e., the Federal Government. In the cases on point, it seemed that the federal-owned oil company, *Petróleos Brasileiros S.A. - Petrobrás*, and the federal-owned shipping company, *Companhia de Navegação Lloyd Brasileiro*, had filed suits against the Federal Government and were subsequently ordered to stop the cases since they were suing their own controlling entity, the Federal Government.

In accordance with the opinion of the Counsellor General, it was not possible under Brazilian law to bar the access of anyone to a court of law. This principle was stated in Article 153, paragraph 4 of the Federal Constitution, which provided that "the law shall not exclude from the review of the Judiciary Branch any breach of individual rights." According to the opinion, this provision constituted the very basis for the right to sue and was an absolute commandment to the legislative branch barring it from issuing any rule whatsoever which may be hostile to such principle. In fact, said the Counsellor General, the legislature was the primary target of the constitutional provision. As a consequence of this principle, only the Judiciary could exercise judicial review; otherwise, the legislature would be able to create other courts not provided in the Constitution. This very basic principle of Brazilian law was reflected in Executive Decree No. 93237, of September 8, 1986 which established in article 6 that "disputes between the Federal Government and its autonomous government entities, public companies and mixed-capital companies, or between one and the others,

would be resolved by the administrative authority, as provided for hereunder, without prejudice to access to the Judiciary and subject to the provisions of the law that would regulate Article 205 of the Constitution." In the words of the Counsellor General, this article "stimulated the resolution of the disputes by administrative methods and authorities." To demand that the decentralized entities of the federal administration not sue the federal government or, still, gave up the suits already filed, was unacceptable and fully unconstitutional.

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