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BRAZIL

I. LEGISLATIVE AND ADMINISTRATIVE RULINGS

Tax Exemption for Cinema Equipment

On July 5, 1984, the Brazilian President granted a tax exemption for imported cinema equipment (Decree-law No. 2.151). Equipment and material not produced in Brazil and intended for use in cinema studios, exhibition rooms, laboratories, and facilities for the transcription of cinema films onto video tapes and for the duplication of cinema films onto video cassettes will be exempt from import duties and taxes until June 30, 1985 (DOU-I, July 6, 1984).

Trading Companies

In Ordinance No. 120/84, the Minister of Finance reinstated the special registration requirement for those trading companies that have already reached at least 10% of the aggregate ceiling established in Ordinance No. 112/81. Registration must be made at either the Foreign Trade Department of Banco do Brasil S.A. (CALEX) or the Federal Revenue Office (SRF). The 10% ceiling applies to exports over three years that amount to an average of at least \$10,000,000. The Minister of Finance also cancelled the registration of those trading companies which did not attain the above-mentioned ceiling during the three year period of 1981 to 1983 (DOU-I, July 2, 1984).

Foreign Trade

The Minister of Finance also issued Ordinance No. 127/84 which created the Commission for the Coordination of Foreign Trade Regulation Activities (CONEX). CONEX was created to harmonize all of the efforts that are made within the Ministry of Finance to regulate foreign trade. CONEX will be made up of one representative from the Foreign Trade Department (CACEX), the Federal Revenue Office and the Central Bank of Brazil. Each representative will have two deputies to assist him in his work (DOU-I, July 6, 1984).

Creation of Federal Revenue Work Groups

The Secretary of Federal Revenue issued Ordinance No. 362/84 which organizes work groups within the Federal Revenue Office of Rio de Janeiro: These groups are subordinate to the Tax System Coordination Office: special work groups to promote and coordinate contacts among the Foreign Trade Department (CACEX), the Office of the Special Secretary for Informatics (SEI) and the Customs Policy Commission (CPA) by organizing work meetings at the Federal Revenue Office's main tax departments. These meetings are aimed at developing solutions for problems and gathering information to improve the regulations on foreign trade and the domestic market. Other special work groups were set up to: (i) study and prepare drafts for government acts regarding the Statements of the Coefficient for the Reduction of Import Duties (DCR) which are submitted by companies established in the Manaus Free Zone; (ii) study and prepare drafts for the review, updating and simplification of the nomenclature of the Brazilian Customs Tariff (TAB) and of the IPI Tax Table (TIPI) so that they will conform with the goals of the tax departments of the Federal Revenue Office; (iii) maintain relations with the Brazilian Nomenclature Committee with the aim of making the Brazilian nomenclature of goods conform to the Federal Revenue Office's departmental goals; (iv) make quarterly and successive updatings of the classification of goods manual (alphabetical index of goods) for classification in the IPI Tax Table and Brazilian Customs Tariff. Finally, nomenclature work groups were set up to study inquiries regarding the classification of goods and to set up the respective cases (DOU-I, June 29, 1984).

New Penal Code and Penal Enforcement Law

Law No. 7.209 of July 11, 1984, was sanctioned to amend certain provisions of the Penal Code (Decree-Law No. 2.848 of December 7, 1940). The new law is to become effective six months after its publication and deals with the applications of penal law, crime, penal imputability, personal cooperation, penalties, kinds of penalty, fines, combination of penalties, conditional suspension of penalties, conditional liberty sentence effects, rehabilitation, security measures, penal action, and extinction of punishability (DOU-I, July 13, 1984).

In addition, the President also approved Law No. 7.210 of July

11, 1984 which instituted the Penal Enforcement Law. The purpose of this law is to ensure enforcement of the criminal sentences and verdict provisions and to permit smooth social integration between those who are sentenced and those who are held in prison. The judges and courts of ordinary justice shall exercise their penal jurisdiction throughout the entire Brazilian territory by means of enforcement proceedings according to the new law and the Code of Penal Procedure (DOU-I, July 13, 1984).

Purchase of State Company Shares

Article 1 of Decree-Law No. 2.132/84 provides that the Federative Republic of Brazil cannot acquire (by purchase and sale; purchase and sale commitment; or exchange) capital shares of mixed-capital companies and companies owned or controlled by the Federal Government without authorization from the Minister of Finance. In Decree No. 89.955 of July 11, 1984 the President established that such authorization shall be conditioned upon the prior statement of (a) the Secretary General of the Ministry of Finance as to the advisability of the transaction and its price and payment conditions; (b) the Planning Office of the Presidency of the Republic concerning the funds to be used for payment; and (c) the Office of the Attorney General of the National Treasury as to the lawfulness of the transaction (DOU-I, July 12, 1984).

Taxation of Sales of Real Property and Corporate Interests

The Secretary of Federal Revenue issued Normative Instruction No. 67/84 which states that the provisions of article 1, paragraph 2, of Decree-Law No. 1.892/81 (which encourage the capitalization of companies by granting an income tax exemption for the profits resulting from the sale of real estate and corporate interests) shall not apply to sales or assignments entitled to such exemption if the relevant price is subject to monetary correction according to the indices for the correction of Readjuste National Treasury Bonds (ORTNs) from the date of the sale to the date of actual receipt of the price (DOU-I, July 13, 1984).

Tax Exemption for the Carajás Program

The President of the Republic signed Decree-Law No. 2.152 of July 18, 1984 which extends the period established in article 1 of Decree-Law No. 1.825/80 for the exemption from income tax for undertakings within the Great Carajás program until December 31,

1990 (DOU-I, July 19, 1984).

Standard Articles of Incorporation

The President of the Republic submitted a bill of law to the National Congress for the National Trade Registration Department (the central entity of the National Trade Registration System). The bill is intended to provide a normative act containing standard forms and articles for the articles of incorporation of commercial companies.

Taxation of Brazilians Working Abroad

The Coordinator of the Tax System issued Declaratory (normative) Act No. 14/84 with the following instructions: (a) only those sums that correspond to income from salaried work paid or credited abroad to Brazilian nationals who are working in another country, but have maintained their Brazilian residence, shall be considered as non taxable income in the person's income tax return as of the date of receipt of such income; (b) any sums paid or credited in Brazil to an employee or his dependents under an employment contract providing for work in another country shall be subject to the tax treatment that applies to income from salaried work received by individuals who reside or are domiciled in Brazil; and (c) the above-mentioned exemption is not available if the person works abroad for a period of less than twelve months (DOU-I, July 23, 1984).

Brazilian Informatics Policy

The Secretary of Informatics issued Ordinance No. 169/84 which creates Special Commission No. 019 (Commercial Practice for Computers and Systems). The purpose of the new commission is to examine and analyze relevant issues referring to the basic transactions of sales of computers, peripheral equipment and software and to thereby assist the Special Secretary of Informatics in his duties (DOU-I, July 23, 1984).

National Housing Bank

The Board of Directors of the National Housing Bank (BNH) issued Resolution No. 14/84 which determines that the Fund for the Payment of Installments in the Event of Loss of Income on Account of Unemployment or Temporary Invalidity (FIEL) may

grant loans while financing contracts are in effect to those borrowers who are unemployed or temporarily disabled but who have paid all their contractual obligations up to the date of the event, thereby giving the right to resort to the FIEL Fund (DOU-I, July 19, 1984).

Tourism Service Companies

The acting President of the Republic signed Decree No. 89.707 of May 25, 1984, which recognizes that remunerated services of organization of congresses, conventions, seminars and similar events are of interest to tourism. This recognition is based on article 2, item 7, of Law No. 6.505/77, which deals with tourism activities and services. According to article 1, the new decree will not apply to the organization and holding of commercial or industrial fairs and exhibitions, which are subject to Decree No. 86.761/81. Remunerated services of organization of congresses, conventions, seminars and similar events may only be contracted with companies that are registered for such services at the Brazilian Tourism Company - EMBRATUR (DOU-I, May 28, 1984).

Transport under Brazilian Flag

In Declaratory (normative) Act No. 12/84, the Coordinator of the Tax System ruled that the obligation to transport goods on a Brazilian flag vehicle in order to qualify for a tax exemption or reduction does not apply to imported goods that are donated to Brazilian entities and whose freight is paid by the foreign donor. (DOU-I, June 1, 1984).

Women's Labor Rights

The President of the Republic sanctioned Law No. 7.189 of June 4, 1984, which amends the wording of Article 379 of the Consolidated Labor Laws which were approved by Decree-Law No. 5.452 of May 1, 1943. According to the new wording, women who are more than 18 years old may work at night, except in industrial companies or activities. This prohibition of night work in industrial companies or activities does not apply: (a) to women that hold a managerial position or a technical position involving substantial responsibility; and (b) to women engaged in services of hygiene and well-being, provided that they do not habitually do manual work. In any case, night work for women is only allowed if the medical examination referred to in Article 380 of the Consolidated

Labor Laws is satisfied and if this fact is noted on the employee register book or card (DOU-I, June 5, 1984).

Courtesy Enrollment for Foreign Students

The President of the Republic signed Decree No. 89.758 of June 6, 1984, which provides that foreign employees of diplomatic missions, consulates and international organizations and their legal dependents may obtain courtesy enrollment in graduate courses offered by Brazilian universities (DOU-I, June 7, 1984).

Export Credit Insurance

The Ministers of Finance and of Industry and Commerce issued Interministerial Ordinance No. 90/84 which establishes a work group responsible for examining and proposing the development of an operational system involving the Foreign Trade Department of Banco de Brazil (CACEX) and the Brazilian Reinsurance Institute (IRB) which would provide automatic credit insurance for Brazilian exports. The ordinance establishes that the work group shall be made up of representatives from the Ministry of Finance, the Ministry of Industry and Commerce, the Brazilian Reinsurance Institute and Banco de Brazil-CACEX-CARIN (DOU-I, June 4, 1984).

Withholding Tax on ORTNs

The Secretary of Federal Revenue Issued Normative Instruction No. 59/84, which establishes that the tax which is generated by the exchange fluctuation of Readjustable National Treasury Bonds (subject to exchange correction) (Decree-Law No. 2.014/83, Article 1) must be withheld even if the beneficiary of the income is an entity enjoying immunity from the tax. After redemption of the bonds, the immune entity may file for a refund of the tax withheld by informing the tax authority of the date that the bond was purchased (opinion in case No. 10168.005590/84-54, DOU-I, June 7, 1984).

Deposit of Foreign Loans

The Central Bank of Brazil issued Resolution No. 926/84 which amends item VI of Resolution No. 923/84. The compulsory deposit at the Central Bank of the proceeds of renewals of Resolution 63 loans taken by state entities will no longer accrue at a 6

percent rate of interest, but will earn interest at the rate established with the foreign lender (besides exchange correction) (DOU-I, June 8, 1984).

In Circular Letter No. 1.036/84, the Department of Control and Registration of Foreign Capital, of the Central Bank of Brazil, announced that, pursuant to the arrangements made with the agent bank for Project I (phase 1) of the Brazilian Financial Plan, the proceeds of deposits made under Resolution No. 813/83, item I, for which the period of application in foreign loan transactions was established by Circular Letter No. 1.016 of April 25, 1984, may now be withdrawn until September 30, 1984, provided that the respective parties have informed the Central Bank of their commitment before June 30, 1984 (DOU-I, June 12, 1984).

No Tax Immunity for Private Pension Funds

The Attorney General of the National Treasury issued an opinion establishing that the tax immunity provided by Article 19, item 3 (c), of the Federal Constitution, does not apply to closely-held or publicly held private pension entities since these entities are not social assistance institutions. The opinion holds that: (a) private law entities under the Brazilian system are civil companies, foundations and commercial companies (the latter being governed by commercial law); (b) civil companies are either organized for profitable purposes or organized for charitable purposes; (c) civil companies organized for charitable purposes include charitable and philanthropic companies that provide social assistance; (d) charitable companies should seek solidarity with mankind and should not provide any monetary advantage for their participants or principals; (e) private pension entities, even when organized as closely-held companies, are not associations or close assistance institutions or companies, as they have no charitable or philanthropic nature; and (f) private pension entities are organized to provide monetary advantages, to supplement retirement and pension payments, to provide income for life, and other benefits to their members and also to provide monetary advantages for their principals, thereby depriving these entities of any charitable character (opinion in case No. 10168.005590/84-54, DOU-I, June 7, 1984).

Changes in Income Tax

The President of the Republic signed Decree-Law No. 2.124 of June 13, 1984, which amends certain income tax legislation. The

changes affect the method of calculating the prepayments of income tax due during fiscal year 1984 by financial institutions and the wording of Article 2 of Decree-Law No. 1.968 of November 23, 1982. The income tax of individuals that is withheld or prepaid will henceforth be corrected every three months on the basis of the variation between the average value of the Readjustable National Treasury Bond (ORTN) over the four quarters of 1984, and the value of the ORTN in January, 1985. The Minister of Finance is also authorized to eliminate or institute accessory liabilities regarding federal taxes administered by the Secretary of Federal Revenue, with the clarification that the document formalizing the fulfillment of any such accessory obligation and attesting to the existence of a tax credit shall constitute an acknowledgement of indebtedness and evidence sufficient to claim the credit with the legal surcharges (DOU-I, June 14, 1984).

Conversion of Foreign Loans into Risk Capital

By means of an official note, the Central Bank of Brazil decided to adopt new internal criteria for approving conversions of the principal or interest from foreign loans and financing into foreign investments in Brazil in the form of risk capital. These new criteria are temporary and will take effect on June 14, 1984. This legal letter includes a translation of the official note of the Central Bank (see part III below).

Tax Exemption for Savings Accounts

The President of the Republic signed Decree-Law No. 2.127 of June 20, 1984, which provides an income tax exemption on interest and dividends paid or credited on the savings accounts maintained by individuals under the Financing Housing System. This exemption now also applies to accounts with an average credit balance of more than the equivalent of 3,500 Standard Capital Units (UPCs) (approximately Cr\$ 35.822.000,00/US\$ 20,785.00) and refers to income tax withheld at source up to December 31, 1985 and income tax due under the income tax return up to and including fiscal year 1986 (DOU-I, June 22, 1984).

Crimes against the Financial Market

The Minister of Finance sent the Minister of Justice a proposal for a bill of law that is designed to define crimes against the financial, capital and securities markets, to establish the respective

criminal penalties and to provide for the appropriate criminal sanctions. The draft of the bill was prepared by the Central Bank of Brazil. The proposal consolidates the current individual legislation that specifies many offenses, including: irregular trading of bonds and securities; appropriation and deviation of bonds held in custody; inspector and investor fraud; fraudulent or reckless management; suppressing information or providing false information; loans to officers or board members of the accused institution; secrecy violations; unauthorized fabrication of documents; irregular bills of exchange; trading of bonds without being legally qualified to do so; acting as a financial institution; abusive or irregular remuneration; and fraud in obtaining foreign currency.

Taxation of Debentures

According to Decree-Law No. 2.133 of June 26, 1984, signed by the President of the Republic, income and capital gains that are made on non-endorseable book and registered debentures shall be taxed at the rate of 25 percent (DOU-I, June 27, 1984).

Extension of Tax Incentives

The President of the Republic issued Decree-Law No. 2.134 of June 26, 1984, which extended the effectiveness of tax incentives afforded under income tax legislation. The following incentives were thus extended to 1986: (a) the additional tax representing 10 percent and 15 percent of the income tax due by companies and financial institutions, respectively, above the normal tax rate of 35 percent and as regards those taxable or arbitrated profits that exceed the equivalent of 40,000 Readjustable National Treasury Bonds (ORTNs) (approximately Cr\$ 48.552,000,00/US\$ 28,170.00); (b) the tax incentives for the development of the SUDENE and SUDAM areas, the SUDEPE and MOBRAF programs, the purchase of EMBRAER shares, and the Fund for the Recovery of the State of Espirito Santo; and (c) the income tax exemption on gains made on the liquidation of contracts on commodity exchanges. The tax incentives for exports of Brazilian manufactured goods, even when exported by commercial companies, were extended to 1988 (DOU-I, June 27, 1984).

II JUDICIAL AND ADMINISTRATIVE DECISIONS

Bad Debts

The mere protest of a bill, even if the debtor makes no effort to lift it, is not sufficient for the respective credit to be considered uncollectable. Except in the case of minor amounts, the loss resulting from the failure to collect a credit can only be charged to the provision for bad debts after all means of collection, including judicial means, have been exhausted (Decision No. 105-0.242 of the Fifth Chamber of the First Taxpayers Council).

Offset of Losses

The right of offset losses does not depend exclusively on having exercised such option on preparing the relevant income tax return. Once a tax issue superior to the data of the income tax return has been determined in tax proceedings, a loss can be deemed to be still pending and can thus be offset according to the law (Decision No. 103-05.713 of the Third Chamber of the First Taxpayers Council).

Profit Distribution

The stockholders of a company that made a profit which was submitted to taxation are liable for the tax on distributed profits. There is no proof that a stockholder would not be so liable at the time when the tax liability arose (Decision No. 102-20.410 of the Second Chamber of the First Taxpayers Council).

Taxation as a Corporate Entity

An individual who sells real property to a company with which he has a connection, even if only by capital subscription, will be held equivalent to a corporate entity for purposes of income tax, if the purchaser company engages or intends to engage in the construction and sale of real property (Decision No. 102-19.638 of the Second Chamber of the First Taxpayers Council).

Loans to Quotaholders

Loans granted to quotaholders which are credited to their current accounts are not to be considered as a disguised profit distribution if such loans are not granted at a time when the company has accrued profits or reserves not required by law, and are formalized by signed written documentation before the loans are granted

(Decision No. 105-0.193 of the Fifth Chamber of the First Taxpayers Council).

Donations and Contributions

Donations and contributions are only deductible if they are limited to 5 percent of a company's operating profit. Any excess over this limit must be added to the net profit for the year (Decision No. 105-0.127 of the Fifth Chamber of the First Taxpayers Council).

Company Succession as to FGTS

When one company succeeds another, the employees of the succeeded company do not acquire the right to withdraw the deposits made in their Employment Guarantee Fund (FGTS) accounts, even if they have not opted for the FGTS system (Decision of the Second Panel of the Federal Court of Appeals on Appeal No. 39.574).

Foreign Tax Credits

The right to offset the income tax paid on income derived from sources situated outside Brazil depends on an agreement signed between Brazil and the country where the income was produced, or on reciprocal treatment afforded income produced in Brazil. In the absence of an agreement, reciprocity may not be assumed; it must be proved by means of concrete examples or shown to satisfy specific legal provisions recognizing the respective tax exemption or credit in a similar situation (Decision No. 102-19.480 of the Second Chamber of the First Taxpayers Council).

Supplementary Salary

When conditions exist which make it necessary for employees to temporarily relocate, the monthly supplementary salary that is paid to the employee cannot be classified as a cost allowance which may be deducted under article 47, item 7, of the Income Tax Regulations as long as those conditions persist (Decision No. 102-20.307 of the Second Chamber of the First Taxpayers Council).

Remittances Abroad

Remittances of money to another country for the maintenance of the offices or facilities of a Brazilian company are not subject to

withholding, especially if the financial plan for such expenses has been approved by the Central Bank of Brazil (Decision No. 102-20.318 of the Second Chamber of the First Taxpayers Council).

Homologation of Foreign Court Decision

An arbitration award rendered abroad and granted "exequatur" by the judge of the country of origin, if not appealed, acquires the authority of "res judicata" (Homologation of Foreign Court Decision No. 3.236-8 by the Brazilian Federal Supreme Court).

III. CENTRAL BANK DECISION ON CAPITALIZATION OF FOREIGN CURRENCY LOANS

As of June 14, 1984, the Central Bank decided to temporarily adopt new internal criteria for the approval of conversions of credits derived from foreign financing and loans (whether of principal or of interest) into foreign investments in risk capital.

The establishment of these new criteria follow the policies which support conversions of credit into investment. The goals are an immediate reduction in the level of foreign indebtedness and the respective charges, and the retention of funds invested in productive activities in Brazil.

The trading of Brazilian bonds on the foreign secondary market by purchasing credits at a discount, however, discourages spontaneous investments. This frustrates attempts to raise funds by obtaining entries of risk capital and to reduce the exposure level of the financial institutions toward Brazil. In light of these problems, those cases that are eligible for examination and approval by the Central Bank were defined as follows:

(a) inter-company credits which include transactions originally contracted between foreign nonfinancial companies and Brazilian companies, (normally with share participation) and between financial institutions (parent company-branch, parent company-subsiary), provided that they were not preceded by assignments of credit rights;

(b) credits of international financial institutions, whose funds are or are not linked to projects for raising new funds and to repayments of the principal of debts, in 1983 and 1984, respectively, when the financial institution is the actual investor (without assignment of credits abroad); and

(c) credits of international financial institutions, the funds of which are or are not linked to the above-mentioned projects, when the transactions are guaranteed by companies abroad and such companies assume title to the investment (applications for conversion of such credits shall only be eligible for approval if the existence of an irrevocable and unconditional guarantee has been communicated to the Central Bank at the time of registration of the loan transaction or against evidence which, at the discretion of the Central Bank, has the same effect).

Anyone seeking such authorizations must apply to the Central Bank. Except for those specified in (a), authorization shall be conditioned upon the future investor submitting a liability commitment in which it undertakes the following: to keep such funds in Brazil for a period at least equal to the term of the loan that is to be converted; not to repatriate any other previous investment within the same period; and in the case of an international financial institution, not to transfer title to the investment within the same period.

In view of the above-mentioned problems, which justified the introduction of these new criteria, loan conversion or financing of international financial institutions that are preceded by credit assignments where the funds are linked to the projects mentioned above (items (b) and (c), where the transactions are not guaranteed by companies abroad or are derived from credits of international financial institutions granted prior to phase I of the Brazilian financial program and entered into directly (Law No. 4.131) with companies in Brazil, will not be permitted unless guaranteed by companies abroad and preceded by credit assignments.

This decision, which is eminently circumstantial, is fully supported by current legislation for foreign investments in Brazil and does not involve any changes in the existing rules. The other rules for the conversion of credits not derived from loans and financing as already made by the Central Bank remain unaltered.

Finally, it must be stressed that the adoption of these circumstantial criteria does not permit any unfounded assumptions that the Brazilian authorities are considering any changes in the laws on foreign capital. On the contrary, the authorities believe that Law No. 4.131 of September 3, 1962, as amended by Law No. 4.390 of August 29, 1964, and pertinent regulations, represents and will

continue to represent a factor of trust for the foreign investor due to its stability over an effective period of twenty years.

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