Trends in Brazilian Regulation of Business

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TRENDS IN BRAZILIAN REGULATION OF BUSINESS*

KEITH S. ROSENN**

I. INTRODUCTION

Brazil is an extraordinarily legalistic country. Enormous efforts are made to try to regulate most aspects of socio-economic relationships. Virtually all economic activity is subject to a substantial amount of governmental regulation. A decade ago I described this Brazilian abhorrence of a legal vacuum in the following terms:

Brazil has reams of laws and decrees regulating with great specificity seemingly every aspect of Brazilian life, as well as some aspects of life not found in Brazil. It often appears that if something is not prohibited by law, it must be obligatory.¹

There was some hyperbole to that statement ten years ago; there is less today. New regulatory laws and decrees are continually being churned from governmental printing presses with mind boggling rapidity.

No one really knows how many laws are in force in Brazil. Instead of specifically repealing superannuated legislation, standard practice is to include in new legislation an article declaring that all laws inconsistent with this law are hereby revoked. The explanation for this legislative modus operandi is simple: No one really knows which laws conflict with the measure being enacted. Aliomar Baleeiro, when still a member of the Supreme Federal Tribunal, estimated the number of laws in force in Brazil at 65,000. The late Pontes de Miranda, Brazil's most prolific jurist, lowered that estimate by about one-third in posing the following rhetorical question to the University of Brasilia Law School in 1980:

If you professors wish to perform a service for the young persons who are preparing here for their juridical life, alert their con-

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science to this absurdity: how can one understand the law of a
country which has 45,000 laws in force?\(^2\)

A recent editorial by one of Brazil's leading newspapers summed up the chaotic state of Brazil's legal system in these terms:

Since it is impossible to know our law, given the excess of legal texts theoretically in circulation, new laws have been made on the supposition that they will affect areas still unregulated. The result is that there are laws which in part repeat themselves, laws which contradict themselves, and laws which result from pure speculation without contact with social reality. Consequently, these laws have only formal validity, remaining, as Miguel Reale has said, "in the limbo of normativity." Problems arise; one makes new laws designed to solve them. But these laws are not applied and the problems continue and worsen. The Brazilian becomes ensnared in this normative mess, therefore, in which he becomes immobilized and loses hope, be he a public servant or merchant, a handyman or industrialist. This is because when he least expects it, a bureaucrat pulls from his desk a legal provision, as if it were a gun, and shoots the citizen who wishes to engage in any kind of productive activity.\(^3\)

The image of bureaucrats firing legal missiles to kill productive activity is most apt. No one really knows how much government regulation reduces Gross National Product, nor how much inflation is attributable to maintaining Brazil's huge bureaucracy and absorbing the costs of bureaucratic bungling, but both figures are surely strikingly high.

It is not simply the huge number of laws in force that generates confusion, but also the poor quality of so many laws and regulations. All too often new Brazilian legislation overlaps with existing legislation and is dreadfully drafted. Rarely can one understand a new measure without simultaneously looking at a number of prior statutes and decrees. Then, one must await clarifying decrees and regulations to find out what a new law really means. Even then one is never sure, for typical practice in drafting regulations is to repeat verbatim or paraphrase the words of the statute. Tax laws, which can be issued by executive decree, tend to suffer more than most legislation from hasty draftsmanship and inadequate conceptualization.

For example, as part of its increasing efforts to contain inflation and to expand its monetary reserves, the government recently decided to raise the rates on the Tax on Financial Transactions (IOF: Imposto

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sobre Operações Financeiras) and to expand its scope. Without any public discussion or even notice, the government simply issued a decree-law tripling the tax rate on most credit transactions.\(^4\) This decree-law also doubled the IOF rate on insurance premiums, imposed a 10% tax on purchase of securities on credit, and effectively produced a partial, unannounced devaluation by imposing a 15% (subsequently increased to 25% by Decree-Law No. 1,844 of December 30, 1980) tax on the purchase of foreign exchange to cover imports. This dramatic boost in tax rates, the expansion of the types of taxable transactions, and the failure to provide for any exemptions produced a huge outcry from affected interests. Great uncertainty also prevailed as to the tax basis. Was the revamped IOF to be calculated solely on the principal amount, or were financing costs and monetary correction to be included in the tax base? The Central Bank, which is charged with administering the IOF, quickly began issuing a series of resolutions and circulars “clarifying” the scope of the IOF and creating exceptions.\(^5\) Some of these measures merely modified a prior clarification. The life of this series of resolutions and circulars was extraordinarily short. All were revoked by Central Bank Resolution No. 619 of May 29, 1980, which contains forty pages of detailed regulations completely reformulating the IOF. These reformulated regulations, which contain a long list of exemptions, are unnecessarily complex and difficult to understand, particularly since many rules require the reader to refer to prior Central Bank rules. In addition to these drafting and conceptualization problems, the reformulation of the IOF has another serious defect. Its application to 1980 transactions violates the constitutional precept against retroactivity, a conclusion recently reached by the Federal Appellate Tribunal (TFR) sitting en banc.\(^6\)

Since 1964 the bulk of all legislation has been initiated by the Executive. A recent study made by José Costa, a federal Congressman, concluded that between March 1964 and November 1979 the Executive promulgated 1,756 decree-laws and 30,370 decrees, while the Congress approved only 3,631 laws. Focusing on the most authori-

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\(^4\) Decree-Law No. 1,783 of Apr. 18, 1980. The tax's name was also changed to the Tax on Credit, Foreign Exchange, Insurance, and Securities Transactions (Imposto sobre Operações de Crédito, Câmbio e Seguro e Normas Relativas a Títulos e Valores Mobiliários), but the abbreviation IOF has been retained.


\(^6\) Agravo em Mandado de Segurança No. 91.332-S.P.
tarian period, the decade between 1965 and 1975, José Costa discovered that 73% of the 1,743 laws passed by Congress were drafted by the Executive. Some of the legislation enacted since 1964 has been highly imaginative and has worked well in resolving perceived problems. On the other hand, much has been poorly drafted, in part because economists and engineers did much of the drafting. However, a more fundamental reason better explains the technical deficiencies of so much of the legislation of the post-1964 period. A serious cost of the 1967 Constitution's allocation of enormous law-making powers to the Executive and its administrative agencies is that laws are placed on the statute books without sufficient empirical research and feedback from those affected to permit elimination of most of the kinks prior to promulgation.

II. Brazil's Regulatory Style

Businessmen accustomed to operating in North America and Western Europe occasionally suffer a severe case of the cultural bends when suddenly submerged in Brazilian regulatory waters. Two basic assumptions, namely that the legal system operates evenhandedly and that those administering it subscribe to the notion that all people are equal before the law, are somewhat attenuated in Brazil. For such assumptions to be tenable, governmental institutions have to operate within reasonably well defined limits. Citizens must be given advance knowledge of their rights and duties and must have meaningful remedies against arbitrary exercise of administrative discretion. Despite considerable improvement in recent years, these preconditions prevail only to a limited extent today in Brazil.

One reason for their absence is that many governmental agencies operate with exceedingly broad delegations of legislative power that invite arbitrary or unprincipled actions. The legal norm is often only the starting point for negotiations that produce ad hoc solutions. Knowing the law is ordinarily not nearly as important as knowing the policy of a given regulatory agency, and, more importantly, knowing how to convince that agency to accord favorable treatment to your case.

A second reason is that it is extraordinarily difficult in Brazil to know which legal rules are in force. A bewildering variety of laws, decree-laws, conventions, complementation agreements, decrees, regulations, ordinances, portarias, normative opinions, circulars, and instructions are regularly published in the Diário Oficial, an official

Brazilian regulatory agencies also occasionally slow down or refuse to process legitimate requests altogether when they deem such a policy to be in the public interest. Institution of such a policy usually has no legislative blessing, nor is it announced to the public. For example, the Foreign Commerce Board of the Bank of Brazil (CA-CEX: Carteira do Comércio Exterior do Banco do Brasil S.A.) from time to time holds up requests for import licenses to aid the country's balance of payments situation. CACEX is also reputed to have a secret list of goods that may not be imported under any circumstances. One concludes that a product is on the list only after repeated requests for an import license are refused or deferred without rational explanation.9

A third reason for this seemingly unlimited regulation is that certain government agencies make themselves parties to contractual negotiations between private parties. The government operates on the paternalistic premise (not always well-founded) that foreign firms have greater bargaining power and that governmental intervention is necessary to redress the balance. Once a foreign lender and Brazilian borrower have agreed upon the terms of a loan, the Central Bank

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reviews the transaction to make sure that the interest rate and commissions are not excessive and that the conditions of repayment are as favorable to the borrower as possible. Brazilian firms signing licensing or technical assistance agreements with foreign firms must have their contracts approved by the National Institute on Industrial Property (INPI: Instituto Nacional da Propriedade Industrial) and registered with the Central Bank in order to remit royalty payments in foreign currency. INPI commonly insists upon renegotiation of contract provisions to make them more favorable to the Brazilian contracting party. Though both INPI and the Central Bank have published some of the criteria they use in deciding whether to approve foreign loans and technology transfer agreements, it is hard to predict in advance what action either agency is likely to take.

A fourth factor is that government agencies feel free to disappoint legitimate expectations by changing the rules of the game in midstream. Important modifications of the rules of the game are regularly sprung on the public with little or no notice and often with retroactive effect. For example, after lulling the business community into the belief that the exchange rate policy of mini-devaluations would be maintained by repeatedly denying the rumor of a maxi-devaluation, on December 7, 1979, the government devalued the cruzeiro by 30%. Some borrowers of foreign currency were badly burned. Others clearly had advance notice, for Resolution 432 deposits, which shifted the exchange risk to the Central Bank, surged sharply shortly before the devaluation. Yet even those who correctly anticipated the devaluation were hurt because the Central Bank also unexpectedly froze the bulk of Resolution 432 deposits for the life of the loan. While deposits made by borrowers under Resolution No. 63 (cruzeiro repass loans from Brazilian banks) may be liberated after 180 days, the bulk of Resolution 432 deposits can be liberated only if converted to equity investment or invested in projects deemed of high priority by the Central Bank. In this fashion the Central Bank produced a de facto confiscation of many borrowers' rights to use the proceeds of their loans.

10. Under the scheme established by Cent. Bank Res. No. 432 and Circ. No. 349 of June 23, 1977, firms with foreign loan obligations can reduce their exchange risk exposure by purchasing and depositing foreign exchange with authorized banks. These deposits bear interest at the rate fixed in the loan agreement. The withholding tax burden is assumed, though not necessarily paid, by the Central Bank. A borrower used to be able to use Res. 432 deposits at any time so long as 30 days had elapsed since the last deposit or withdrawal.

Perhaps an even more blatant recent example of changing the rules on investors and savers in midstream occurred in April 1980, just after the 1979 tax returns were due, when the government retroactively imposed a compulsory loan on 1979 tax-exempt income. As originally enacted, the compulsory loan was set at 10% of the individual's 1979 nontaxable (or taxed exclusively at the source) income in excess of Cr$ 4,000,000 (then about U.S. $77,500). Although this exaction had all the earmarks of a loan (repayable in full starting in July 1982 at 6% annual interest), it was actually a disguised tax on capital gains and unearned income.

The compulsory loan generated vast amounts of criticism. Many objected to its sneaky timing. Others complained that retroactive taxation of exempt monetary correction and stock dividends resulting from mandatory capitalization of a firm's fixed assets amounted to a breach of good faith. The Brazilian Lawyers Institute prepared an extensive study concluding that the statute was unconstitutional. Some lawyers also expressed the opinion that the statute conflicted with the National Taxation Code. Just as the regulations for this statute were to have been issued, the government instead promulgated Decree-Law No. 1,790 of June 9, 1980, which revamped the compulsory loan to make it more palatable. The new law permitted monetary correction of the loan plus 3% annual interest and imposed a maximum limit on the loan of 3% of the lender's net worth. Judicial review of this statute appears to have been blocked by the threat of a thorough tax audit for any taxpayer contesting the law's constitutionality in court.

For a good many years the government has manipulated the computation of monetary correction on its Readjustable Treasury Bonds (ORTN: Obrigações Reajustáveis do Tesouro Nacional). The inflation adjustment was originally based upon the percentage change in the wholesale price index between the present and prior quarters, with a three-month lag. Without bothering to enact new legislation, the government from time to time has purged acts of God and acts of Arabs from the wholesale price index used to derive the adjustment coefficient; it has also altered the formula used to calculate the adjustment several times to lower the rate of return. On January 16, 1980, with no advance warning, the National Monetary Council

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13. With an annual inflation rate running at approximately 100%, repayment of the principal without monetary correction is economically indistinguishable from a tax with an effective rate of about 75% of the face amount of the "loan."
abandoned the concept of *ex post* monetary correction by deciding to readjust ORTNs two months in advance in accordance with a presumed rate of inflation. This rate was fixed by the National Monetary Council at 45% for calendar year 1980 and was subsequently upped to 50% on a June-to-June basis. Nonetheless, the presumed rate of inflation still under-estimated the actual rate of inflation by approximately one-half. Since Brazilian law requires virtually all monetary correction be linked to the ORTN readjustment rate, the interest rate on all indexed obligations and savings deposits turned sharply negative. Brazil thus turned monetary correction into an inflation control device that sharply disappointed the legitimate expectations of bondholders, depositors, and other creditors. Curiously, this flagrant impairment of the obligation of contracts failed to produce much public outcry in Brazil, perhaps because Brazilians are so accustomed to governmental tinkering with the rules of the game. As one would expect, Brazilians did respond, however, by shifting their resources out of indexed deposits and obligations, producing a sharp drop in the savings rate. In November 1980 the government suddenly reversed its policy and resumed *ex post* indexation. ORTNs are now fully indexed to the percentage change in the national consumer price index.16

A fifth factor is Brazil’s huge and astoundingly inefficient bureaucracy. Many departments are open only a few hours each day. Governmental forms often must be purchased at places distant from where they are to be filed. Payment of fees normally must be made at commercial banks and subsequently presented to the processing agency. Businesses are compelled to resort to the services of *despachantes*, official red tape cutters, in order to move all the necessary pieces of paper through the bureaucracy any time they need a license or authorization.17

The volume of paper that must be moved through the labyrinthine bureaucracy in order to secure licenses or authorizations is astronomical. Even though the government has streamlined the process somewhat as part of its energetic campaign to stimulate exports, securing an export license still involves 1,470 separate legal actions with 13 government ministries and 50 agencies.18 Even so simple an act as registering to vote may take weeks to secure the approvals of a dozen different governmental agencies and to prove that one has been

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15. Law No. 6,423 of Je. 17, 1977.
17. The *despachante* is more fully described in Rosenn, *supra* note 1, at 536-37.
registered to vote in every previous place of residence. Moreover, oftentimes an approval from one government agency expires before all of the other necessary documentation is in order, requiring one to begin the process anew.19

There is a decided tendency in Brazil to deal with any new problem by creating a new agency to deal with it. The proliferation of governmental agencies in the past few decades is truly astonishing. Each agency accumulates staff and soon acquires a vested interest in maintaining, if not enlarging, its own area of supervision. It is not uncommon for the jurisdiction of a new agency to overlap with that of an existing agency. Each agency is a law unto itself, and one sometimes vetoes permissions or projects approved by another.

For the past forty years governments have made a series of efforts to reform. In July 1979 the government acknowledged that Brazil's bloated, foot-dragging public administration had become a significant problem. The government decided to deal with this problem in characteristic Brazilian fashion by creating a special Ministry for Debureaucratization. Headed by Helio Beltrão, former Minister of Planning, this new agency has thus far issued a series of sensible decrees simplifying several bureaucratic procedures.20 Unfortunately, the bureaucracy has also dealt with the Ministry of Debureaucratization in typical Brazilian fashion by ignoring many of its debureaucratization measures. Reacting to numerous complaints about the bureaucracy's disregard of debureaucratization measures, Beltrão recently issued a decree requiring the bureaucracy to take the Ministry of Debureaucratization seriously.21

The costs to Brazil of this regulatory style are quite high. The difficulty in knowing the rules of the game, coupled with frequent midstream changes, produce considerable insecurity among investors and businessmen. For private capital to play an important role in Brazil's economic development, investors and businessmen must feel

19. Id.

20. E.g., Decree No. 84,541 of Mar. 11, 1980 (simplifying the process of obtaining a passport and abolishing the exit visa requirement for Brazilians traveling abroad); Decree No. 84,451 of Jan. 31, 1980 (validating photocopies of notarial acts or civil registries performed by Brazilian consuls); Decree No. 83,936 of Sept. 6, 1979 (eliminating five documents from list of prerequisites for federal government permissions).

21. Decree No. 84,585 of Mar. 24, 1980, provides that all requests for information by the Ministry of Debureaucratization must receive priority, that the general public be allowed to complain directly to the noncomplying agency, and that an offending agency modify its procedures to comply with the new debureaucratization measures.
not only that they can understand and work within the system, but they can also rely on the ground rules remaining stable. The vital role of the legal system in providing the security and foreseeability necessary for capitalist development was pointed out many years ago in the economic sociology of Max Weber. "[T]he rationalization and systematization of the law in general and . . . the increasing foreseeability of the functioning of the legal process in particular, constituted one of the most important conditions for the existence of . . . capitalistic enterprise, which cannot do without legal security." All too often the necessary degree of predictability is absent in Brazil. This flexible and cumbersome style of regulation enormously increases the transaction costs of doing business in Brazil. Part of these costs stems from additional fees for lawyers and despachantes. Part results from the income lost while investment projects are delayed as negotiations proceed before government agencies. Indeed, some worthwhile projects are abandoned because of the difficulty in obtaining simultaneously all the necessary governmental permissions. Some funds that would otherwise have been invested in Brazil flee the country or never enter. In addition, this regulatory style impedes legitimate regulatory activities. With good reason Brazilians insist upon using bearer shares, but how can one regulate abuses of "insider trading" with bearer shares?

Excessive governmental regulation also contributes to the growth of state capitalism. The most common reason given for chartering a state company to undertake a given investment is that private capital is not available for the task. Yet private capital is often unavailable because freewheeling governmental regulation has generated unacceptable risks. By this analogue to the self-fulfilling prophecy, bureaucracy begets more bureaucracy.

The costs to Brazil would be even higher were it not for the important paralegal institution of the jeito, a characteristic technique for bending legal rules to expediency. Much constructive and productive economic activity has been accomplished because Brazilian bureaucrats have allowed the jeito to circumvent legal and administrative hangups. Indeed, without this felicitous Brazilian tendency to bend the rules or reinterpret them in the light of good sense, the wheels of the economy would have ground to a halt long ago.

Nevertheless, the Brazilian regulatory style is not conducive to efficient decision making. Nor is it a style compatible with a modern,
developed industrialized society. Though Brazil has made great strides towards becoming a modern, developed nation, it has yet to jettison this *ad hoc* regulatory style and substitute rule for discretion.

The government has recently taken two significant steps towards reducing the high social and economic costs of its regulatory processes: (1) the December 7 *Pacote* (discussed below) and (2) the debureaucratization campaign. Unfortunately, there has been no significant follow-up to the former, and it is doubtful whether the incipient debureaucratization campaign will do much more than scratch the surface in reducing these high costs. Administrative reform has been tried often in Brazil, but the bureaucracy has a formidable track record of successful resistance. Perhaps more importantly, the government continues to pass legislation granting vast amounts of discretion to executive agencies with virtually no guidelines for its exercise.

III. Current Trends in Governmental Regulation of Business

According to Delfim Neto, the present economic czar, Brazil’s long range goal is to return to a free market economy. Similar statements have been strewn all along Brazil’s path towards state capitalism. Nevertheless, a significant step along the path toward a free market economy was taken on December 7, 1979, when the government closed down all foreign exchange operations and enacted a series of reforms designed to deal with the interrelated problems of inflation, burgeoning foreign debt, and the balance of payments deficit. These measures also reflect the spirit of debureaucratization; a number are designed to eliminate governmental controls and subsidies and to restore a greater semblance of the free market. The reform package is summarized below.

24. In a recent speech given in Argentina, Planning Minister Delfim Neto stated: Basically, Brazil wants to reach its development in the frame of a politically open society, with full awareness that this demands the existence of a highly important private sector.

To express this aspiration implies expressing that we have to lean heavily on a market economy. In other words, that within a lapse which cannot be calculated, we shall return fully to a market economy. We really believe that this is the most effective means for the utilization of our resources . . .

Hence, it must be borne in mind that, on the long term, we shall open our economy.

Translated in Ministry of Economy, Coordination and Economic Planning Secretariat, 107 Economic Information on Argentina, 11-12 (1980).
The December 7 Pacote

1. Maxi-devaluation. The cruzeiro was devalued by 30 percent to stimulate exports and discourage imports. Though the government announced that it intended to follow an exchange rate policy of mini-devaluations from time to time to correct the differential between Brazil's internal inflation rate and that experienced by its principal trading partners, during 1980 the rate of devaluation was only about half the inflation rate.

2. Increase in Rebate on Income Tax on Interest Remitted Abroad. In 1975 the Brazilian Central Bank instituted a policy designed to reduce the effective interest cost of foreign loans to certain Brazilian borrowers by rebating to borrowers 85% of the 25% withholding tax imposed on interest payments by the Brazilian Income Tax. On July 26, 1979, the Central Bank sought to discourage foreign borrowing by reducing this rebate from 85% to 50%. The Central Bank later decided to stimulate foreign loans by increasing the tax rebate from 50% to 95%.25 Because of complaints by U.S. banks of unfair competition, stemming from an I.R.S. ruling restricting the foreign tax credit available to U.S. lenders to only that portion of the withholding tax not rebated to the Brazilian borrower,26 the Central Bank in May 1980 decided to reduce the portion of the tax rebated to the borrower from 95% to 40%.27

3. Demise of the Import Deposit. The requirement that importers make a cruzeiro deposit for 360 days of 100% of the FOB value of the imported goods was eliminated as of December 10, 1979.28 The purpose of this reform was to eliminate a bureaucratic labyrinth, especially for those seeking exemptions, and to mitigate the 30% increase in import prices resulting from the maxidevaluation.

4. Demise of the International Travel Deposit. The Cr$22,000 deposit which those traveling abroad had to leave for a year without interest or monetary correction was also eliminated as of December 10, 1979.29

5. Elimination of Freeze on Proceeds of Foreign Loans. Central Bank Resolutions Nos. 532 and 553, which imposed a freeze on 50%
of the value of the proceeds of foreign loans, were revoked. The freeze provisions on the other half of the loan were made less onerous in January 1980. On foreign private sector loans, one-fourth of the cruzeiro equivalent is released to the borrower immediately. The remaining 75% is deposited with the Central Bank, which assumes the exchange risk and service obligations. One-third of this deposited amount is released after 60 days, one-third is released after 90 days, and the balance after 120 days.  

6. Establishment of an Export Tax. Concern that the 30% devaluation may cause detrimental reductions in the prices for exports of primary products has led to the imposition of a 30% export tax on certain products, based upon a table of minimum values. (This tax has already been eliminated or is being phased out on several products.)

7. Restructuring Credit Subsidies. The government decided to reduce the budgetary burden of huge amounts of subsidized credit, as well as to avoid having the amount of subsidy increase directly with the inflation rate. With the exception of special programs under the Superintendency for the Development of the Amazon (SUDAM: Superintendência do Desenvolvimento da Amazônia) and Superintendency for the Development of the Northeast (SUDENE: Superintendência do Desenvolvimento do Nordeste), the minimum rate for subsidized governmental credit has been set at 40% of the monetary correction rate plus a fixed interest charge. Exporters can receive financing at 40% of the monetary correction rate plus 2% annual interest.

8. Elimination of IPI Subsidies for Exports. Exemptions from the Tax on Industrialized Products (IPI: Imposto sobre Produtos Industrializados) for exports have been eliminated. The 30% devaluation was deemed more than ample to replace these exemptions, which were producing dumping charges by other nations and adding another bureaucratic layer.

9. Limitation on Imports by the Public Sector. To try to reduce the balance of payments deficit and contain inflation, a ceiling on public sector imports was imposed for 1980 of 80% of the value of the sector’s 1979 imports. Included within this limitation are domestic

market purchases, leasing, or rental of imported goods or services. This limitation does not apply, however, to three areas: (1) petroleum, (2) the steel industry, and (3) electric energy.35

10. Freezing of Resolution 432 Deposits. As previously discussed, loan deposits shifting the exchange risk to the Central Bank could not be withdrawn.36

11. Demise of the Law on Similars. The President announced that the role of the Law of Similars, which is really more of a policy than a law, in protecting national industry from foreign competition would be sharply diminished. This so-called law prevents tariff reductions on products similar to those currently being produced in Brazil. Determining whether products are really similar has been an administrative nightmare. By abolishing most exemptions from import duties, Decree-Law No. 1,726 of December 7, 1979, eviscerated the policy instrument through which the Law of Similars functioned.

While the December 7th package is a commendable step in the right direction, Brazil has a long way to go to reach the goal of a free market economy. The government still controls most prices and wages and tightly controls licenses for imports and exports. The government still directly attempts to control interest rates and the supply of credit. Although a committee of the Ministers of Finance, Planning, and Debureaucratization has recently been entrusted with a destatization directive to sell off certain state-owned companies to the national private sector, a large segment of the economy is directly controlled by the state through government-owned or controlled companies. Foreign investment and technology transfers are also tightly controlled. While the government does not control inflation, it directly controls the rate of monetary correction. Though it has a free market component, the Brazilian economy in some respects resembles and is treated by the government as a gigantic tinker toy.

Regulation of business is accomplished through myriad forms and methods in Brazil. Rather than attempting to cover them all, the next sections will concentrate on current trends in the following important areas of governmental control: prices, wages, credit and interest rates, foreign trade, technology transfers, environmental protection, and the regulation of foreign investment.

36. See notes 10-11 supra and the text thereto.
Price Controls

Despite decades of proven ineffectiveness in controlling inflation, Brazilian price controls continue in force. This Sisyphean task is principally entrusted to the Interministerial Price Council (CIP: Conselho Interministerial de Preços), which has recently been moved from the Ministry of Finance to the Ministry of Planning. CIP controls the prices of about 75% of industrial products, some of the consumer goods, and utility rates. It regulates, in typical Brazilian fashion, without clearly defined rules.

CIP has three regulatory regimes. Certain products are subject to flat controls; their prices cannot be raised without CIP authorization. Others are subject to a potential rollback regime. On these items prices can be raised if forty-five days have elapsed from the last hike and CIP is notified. CIP can then order a rollback. The third regime is called "accompanied liberty." Firms can raise prices freely on these items, but they must keep CIP informed of each increase.

CIP has made an attempt to reward efficiency and to stimulate local industry. Whenever the Council has determined that a firm's salaries, commissions, or input costs were too high, it has cut back a request for a price increase accordingly. If a firm imported items that CIP believed could have been purchased locally, the Council has pared the increase sought or withheld approval until concessions with regard to greater local content were forthcoming.

Until recently, there was little evidence that CIP intentionally misused its powers by forcing firms to operate at a loss, although foreign pharmaceutical firms were treated particularly poorly. Nevertheless, the lags, paperwork, and uncertainty created by the regulatory process invariably caused substantial economic prejudice to price-controlled firms. Although CIP is supposed to take action within forty-five days of the filing of a request for a price increase, the Council can, and frequently does, extend this for another forty-five days simply by requesting more information to justify the requested

38. BUSINESS INTERNATIONAL CORP., A CORPORATE GUIDE TO SOLVING OPERATING PROBLEMS IN BRAZIL 183-84, 190-94 (1978). One would think the results of this policy would be to force foreign firms to undercut domestic firms. If it were imposed in isolation, that might be true, but it is only part of the total picture. Local laboratories are free to pirate drugs from foreign companies. The process of obtaining permission from the National Service for Regulation of Medicine and Pharmacy (SNFMF: Servicio Nacional de Fiscalizao da Medicina e da Farmacía) to introduce new drugs, usually a source of high profits for the foreign firms, has been recently lengthened from about six months to two years, and very few applications are being approved. CPI has also been underpricing new drugs. Id. at 190-94.
increase. Hence, even if CIP grants the entire amount of a request, with average price levels rising at 6% to 7% per month, a delay of forty-five to ninety days often causes serious shrinkage of profit margins.

CIP is not the only government agency that controls prices. The National Superintendency of Supplies (SUNAB: Superintendência Nacional do Abastecimento) controls the prices of essential foodstuffs. In 1979-80 the number of commodities controlled directly by SUNAB increased, as did the number of spot shortages. Insurance rates are set by the Superintendency of Private Insurance (SUSEP: Superintendência de Seguros Privados), while the prices of gasoline and other petroleum products are set by the National Petroleum Council (CNP: Conselho Nacional do Petróleo). Consequently, the consumer has been deprived of the benefits of price competition in these products.

The government has announced plans to turn its antitrust agency, the Administrative Council on Economic Protection (CADE: Conselho Administrativo de Defesa Econômica), into a price control agency. As an antitrust watchdog, CADE has been a fiasco. Since its creation in 1964 to enforce an antitrust law modeled after the U.S. antitrust laws, CADE has brought only forty-one administrative actions. Only three of these resulted in convictions; twenty-one are still being decided, and seventeen resulted in findings of no violation. Whether this moribund agency will be more effective in prosecuting price raisers for abuse of economic power is questionable. Much more effective, if not precisely ethical, has been the Treasury’s fine-tooth comb investigations of the income tax returns of firms whose prices have risen rapidly.

Toward the end of 1979, a significant change was made in Brazilian price control policy. Instead of permitting price increases whenever justified by rising input costs, Brazil decided to limit firms to just two price increases a year. Moreover, these increases were to correspond with the reported increase in the general price level rather than with increases in a firm’s actual costs. The results of this policy were predictably disastrous. Business profits and investment fell sharply, and many firms were forced to operate at a loss. In November 1980 the government announced both the abandonment of this price control strategy and a general easing of controls.

Brazilian price controls require that firms engage in huge amounts of paper work in their attempts to justify price increases.

40. Id.
They also discourage firms from launching new products, deprive consumers of a broad range of prices and products, create periodic shortages, and badly distort economic efficiency. They obviously do not control inflation in Brazil. Instead, they have become devices for pursuing other socio-economic policies, such as promoting national products and what regulators think is economic efficiency. In an era of rapid inflation, stringent price controls often result in a *de facto* taking of property, a contention which Brazilian courts have thus far refused to recognize.\(^42\)

**Wage Policy**

The Brazilian government has exercised extensive control over the labor movement ever since Getúlio Vargas instituted a syndicalist system modeled upon the experience of Fascist Italy. Under this paternalistic system, employers are grouped into trade associations and employees into government-controlled unions. The Ministry of Labor runs a dues check-off system and turns funds back to officially approved unions. Government-dominated labor courts resolve labor grievances and determine wage levels whenever collective bargaining breaks down (*dissidios*). The government also determines fringe benefits, which in Brazil constitute a large chunk of every employer’s wage bill. The right to strike is subject to a series of procedural constraints, such as the requirement of two strike votes, separated by a minimum of two days, with the first needing a two-thirds majority. Moreover, all strikes are prohibited against public services or essential activities.\(^43\)

In November 1979 a new wage policy was instituted with the expectation of sharply reducing the rash of strikes accompanying political liberalization.\(^44\) The new policy has utilized inflation as a device to redistribute income from higher-paid to lower-paid workers. It has also provided for semi-annual rather than annual wage adjustments, which had been a source of considerable dissatisfaction in the context of galloping inflation. As originally implemented, the new wage law automatically granted workers earning up to three times the minimum wage a semiannual wage adjustment of 110% of the infla-

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42. The Supreme Federal Tribunal has held that price controls do not result in an unconstitutional taking of property even if they require a firm to operate at a loss. *Sociedade de Laticínios Dominio Ltda. v. União Federal*, R.E. 52.010, 33 R.T.J. 720 (Supreme Tribunal Federal *en banc* 1965).

43. Law No. 4,330 of June 1, 1964. Although in theory unions have a right to strike, this right was almost never exercised between 1964 and 1978 because of fear of military repression.

tion rate since the previous wage adjustment. Those earning between four to ten times the minimum wage received an inflation adjustment equal to the inflation rate, and workers earning more than ten times the minimum wage received an 80\% inflation adjustment. The inflation adjustment has been determined by a new national consumer price index, prepared by the Brazilian Institute of Geography and Statistics (IBGE: Fundação Instituto Brasileiro de Geografia e Estatística), by weighting preexisting consumer price indexes for the principal cities and regions. Productivity increases, an undefined concept, have been left to collective bargaining and the labor courts.

This wage policy has been subjected to considerable criticism. Higher paid workers have complained about falling behind inflation. Critics have also claimed that the automatic semiannual wage adjustment of lower paid workers by more than the increase in the cost of living is inflationary. A further complaint has been that the new measure has done little to ensure labor peace. Instead, it has merely shifted the name of the conflict from cost-of-living increases to productivity increases.

The new wage policy is presently in a state of flux. Legislation adopted in December 1980 decidedly modified wage policy for those on the high end of the salary scale. Those earning between 11 and 15 times the minimum wage now receive 80\% of the increase in the consumer price index, while those earning between 16 and 20 times the minimum wage receive only 50\% of that increase. Those earning more than 20 times the minimum wage are now free from the mandatory inflation adjustment system. Modification may well be in store for those at the lower end of the scale as well, for the minimum wage levels which went into force on May 1, 1981, in all but a few states in the Northeast did not contain the additional bonus of 10\% of the inflation rate for those earning between one and three multiples of the minimum wage. Moreover, the rate of inflation reported by the national consumer price index for the twelve-month period ending in April 1981 was only 101\%, well below the 121.3\% figure reported for the same period by the Getúlio Vargas Foundation's general price index, the traditional inflation yardstick in Brazil.

The wage policy adopted in November 1979 has much to commend it in terms of social justice. Nevertheless, both the automatic increases of wages in excess of productivity gains and the compensa-

45. Law No. 6,886 of Dec. 10, 1980.
tion of workers for price increases resulting from declines in the terms of trade were bound to fuel the country's already raging inflation. Moreover, the wisdom of a policy which gives a sizeable percentage of the work force a vested interest in sustaining a continually rising inflation rate is dubious.

**Regulation of Credit and Interest**

The Brazilian government regulates credit markets through a variety of techniques other than traditional monetary and fiscal policy. The government is by far the largest banker, influencing resource allocation directly through its lending policies, which often consist of providing funds at below market interest rates for activities it desires to encourage. Currently, agriculture, exports, and energy have top priority. The Bank of Brazil provides large amounts of credit to the agricultural sector, much of it at heavily negative interest rates. The Bank of Brazil and the National Economic Development Bank (BNDE: Banco Nacional de Desenvolvimento Econômico) maintain a number of special funds to lend money at subsidized rates to Brazilian controlled firms for specific purposes. Restricting access to the coffers of these special funds to Brazilian controlled firms, provides a strong incentive to foreign firms to accept a minority position in joint ventures with Brazilian firms.

Subsidized credits for exports are available through CACEX. Companies wishing to invest in the Amazon or Northeast regions, for example, can receive subsidized financing through SUDENE or SUDAM, which distribute tax incentive funds for investment projects in their respective areas.

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47. A substantial rise in import prices relative to export prices cause a decline in the country's real income. Brazil's trade account ran a deficit of $2.8 billion in 1980, despite an impressive 31% increase in export earnings, primarily because of the sharp increases in the price of oil imports, which accounted for 43% of Brazil's total import bill. Failure to net out this real income decline from a wage indexation scheme contributes to a wage-price spiral. Brazil's experience is confirmed by the sharp rises in inflation rates in 1974 in several Western European countries indexing wages to the consumer price index. Ross-Skinner, *The Failure of Indexation*, *DUN's Review* 76-79 (Sept. 1977). See also, Bernstein, *Indexing Money Payments in a Large and Prolonged Inflation*, *Essays on Inflation and Indexation* 71, 73-75 (H. Giersch et al. 1974)

48. For example, the Fund for the Financing of Industrial Machinery and Equipment (FINAME: Fundo de Financiamento para Aquisição de Máquinas e Equipamento Industriais) provides credit for the production and purchase of domestically produced capital goods; the Fund for the Democratization of Company Capital (FUNDECE: Fundo de Democratização do Capital das Empresas) lends funds for working capital of companies going public.
Government regulatory policy has been to require the private banking system to make an increasing percentage of its loans to Brazilian controlled firms. The latest of the Central Bank pronouncements on this subject raises the percentage of the total value of credit transactions by banks, credit companies and financial institutions that must be extended to Brazilian individuals or locally controlled firms from 60% to 70%. This leaves only 30% to be divided among the multinational and state companies.

Foreign firms unable to tap the domestic credit market through the banking system used to raise funds by tapping the Brazilian capital market. But the Securities Commission (CVM: Comissão de Valores Mobiliários) recently invoked an unwritten rule imposing a toll charge on foreign firms wishing to issue debentures. Such firms must agree to bring into Brazil equity capital in an amount equal to that raised by issuing debentures.

Foreign loans are tightly regulated by the Central Bank. These regulations change fairly rapidly in accordance with the Bank’s appraisal of the country’s balance of payments, market conditions and capital needs. New loans presently can have a spread of 1.5-2.0% over LIBOR (London Inter-Bank Offered Rate). Although they must also have a minimum term of eight years and a thirty month grace period, they may later be repassed to other borrowers for 18 month intervals. Import financing arrangements of up to 180 days need no special authorization; those extending between 181 and 360 days need special authorization from CACEX; and those extending beyond 360 days need both authorization from CACEX and registration with the Central Bank. The Central Bank also influences the length of loans through its policy of rebating to the borrower part of the 25% Brazilian withholding tax on remittances abroad. This rebate is currently set at 40% of the tax. To be eligible for the rebate, foreign currency or import financing loans must extend over a minimum of eight years.

The drying up of cruzeiro financing is causing firms to look to the Eurodollar market again, even though many suffered severe losses in the December 1979 maxi-devaluation. The government’s response to these exchange losses has left much to be desired. To prevent a decline in tax collection levels, it enacted a decree-law which denies companies whose base year includes any month in the second half of 1979 the right to deduct for income tax purposes foreign exchange losses in

excess of the percentage variation in the ORTN. Since the ORTN increased in value by only 47.19% in 1979, firms were prevented from writing off as much as 60.61% of the increase in their indebtedness from the 1979 devaluation. This decree-law was quickly followed by a ruling of the CVM which permitted open capital corporations to defer writing off the portion of exchange loss exceeding the ORTN variation. This accounting alchemy permitted a number of firms to turn large losses into profits on their 1979 balance sheets. One result of these measures was to increase the effective tax rate on the firms most seriously hurt by the maxi-devaluation and to make it more difficult for the public to evaluate the bottom line on corporate balance sheets.

In 1979 and 1980 the Central Bank made a concerted effort to achieve two mutually contradictory goals: a reduction in interest rates and a reduction in the amount of credit. In August 1979 the Central Bank ordered all lending institutions to reduce their average interest rates on loans to the private sector by 10% starting September 3, 1979. In April 1980 the Central Bank ordered Brazilian lending institutions to limit expansion of their credit operations to 45% of their normal financing and discount operations on the last day of 1979. It is not surprising that such measures have been difficult to enforce and have been the source of considerable tension between the Central Bank and the private banks, many of which have been warned and reprimanded for violations. Moreover, these measures have spawned a wide variety of evasionary artifices, such as requiring borrowers to pay for “consulting” fees, insurance policies, compensating balances, and purchase of government paper at special prices. These artifices not only raised the effective interest rate, but also raised the transaction costs for loans. The policy of attempting to hold

52. Decree-Law No. 1,733 of Dec. 20, 1979. Firms have two options with respect to the non-deductible portion of their foreign exchange expenses. They can add these sums to the cost of fixed assets, increasing depreciation deductions. Or they can maintain these sums in a monetarily corrected deferred account to be written off as these foreign currency obligations are repaid. In either case not more than 20% of these deferred sums can be written off in any single fiscal year. But if the holder of a foreign currency debt elects to convert it into equity (i.e., where parent corporations are owed debts by their Brazilian subsidiaries), this 20% limitation does not apply.

53. CVM Deliberation 8, Jan. 8, 1980.

54. Cent. Bank Res. No. 560 of Aug. 30, 1979, ordered the reduction for commercial banks, and Res. No. 561 imposed a corresponding cutback for investment banks, finance, and credit companies. Excluded from this across-the-board interest rollback were rural credit, foreign loans, refinancing operations to official financial institutions, and other credit operations subject to specific regulations. The average lending rate was weighted for each type of loan transaction and was based upon lending rates in effect during the month of August 1979.

interest rates well below the inflation rate worked badly, forcing the government to free interest rates for commercial and investment banks in January 1981.\textsuperscript{56} The government has retained, however, its policy of tightly limiting credit expansion. The rate of bank expansion of credit has been limited to 5\% for the first quarter of 1981 and to 50\% for the entire year.\textsuperscript{57} The combined effect of these policies has been to make it exceedingly difficult for businesses to obtain cruzeiro financing.

\textit{Foreign Trade}

Imports, exports, and the foreign exchange rate have long been subject to tight governmental control in Brazil. Both exports and imports require licenses from CACEX and are subject to substantial taxes or duties. Until December 10, 1979, imports were further discouraged by the requirement of a 100\% prior deposit, while exports were encouraged by exemptions from the Tax on the Circulation of Merchandise (ICM: Imposto sobre Operações Relativas à Circulação de Mercadorias) and the IPI.

The December 7th \textit{pacote} eliminated both the 100\% prior deposit for imports and the IPI tax exemptions for exports, though the effects of these changes were, at least for a time, more than counterbalanced by the 30\% maxi-devaluation. Imports were also discouraged by another requirement: the public sector had to reduce its 1980 imports to 80\% of 1979 levels. Since the domestic inflation rate during 1980 was approximately twice the rate of cruzeiro devaluation, imports became progressively more attractive. To try to reduce imports even further, CACEX instituted an unwritten policy of limiting imports of capital goods for a firm’s own use to the value of the firm’s imports in the previous year. Imports for resale were also limited to 80\% of the previous year’s imports. Foreign controlled firms were told to import capital goods for their own use without exchange cover (in effect characterizing their imports as equity investments) or to arrange external financing for at least five years. Even Brazilian controlled firms were told to arrange a minimum of five years external financing, but if such financing proved to be unobtainable, CACEX considered waiving this requirement. Cash sales were not prohibited, but CACEX considered them “undesirable.” Machinery components, whether imported by foreign or locally controlled firms, were re-

\textsuperscript{57} Id.
required to have a minimum of two years' foreign financing and could be imported only for projects granted export incentives.\textsuperscript{58}

In September 1980 a modified version of CACEX's informal import constraint policy was formally enacted into law in the form of a Central Bank resolution.\textsuperscript{59} This resolution established a sliding scale of minimum external financing terms for imports, ranging from three years for those machines, equipment, instruments, vehicles, ships, and airplanes with an FOB value of U.S. $100,000 to $300,000, up to eight years for goods with values in excess of $5,000,000.\textsuperscript{60} Spare parts had to have a two-year minimum financing period if the import license were issued prior to December 31, 1980, and one year if issued thereafter. Durable consumer goods and raw and intermediate materials for the steel and chemical industries had to have a minimum term of 180 days if the invoice amount exceeded $100,000.

The increase in the IOF tax rate from 15\% to 25\%, imposed at the end of 1980,\textsuperscript{61} has also made imports less attractive. This tax on the purchase of foreign exchange, which applies to a little over half of all imports (only petroleum is exempt), is a more pervasive disincentive to imports than the 100\% prior deposit scheme, which affected only 20\%-30\% of imports and was eliminated as part of the December 1979 pacote.\textsuperscript{62} In addition, during 1981 the government has sharply stepped up the pace of devaluation of the cruzeiro,\textsuperscript{63} thereby making imports even more expensive.

With few exceptions, goods may be freely exported from Brazil. A nontransferable export license must be obtained from CACEX for all products except coffee, whose exportation is subject to special rules issued by the Brazilian Coffee Institute. CACEX controls the prices at which goods are exported by publishing minimum export prices. At the time it issues a license, CACEX must approve the firm's expenses for freight, insurance, and agent's commission. Generally, CACEX will not permit payment of a commission from the exporter to a parent or affiliated companies on exports for which a company has received investment incentives in return for a commitment to export.\textsuperscript{64}

\begin{itemize}
\item \textsuperscript{58} Bus. Lat. Am., Jy. 16, 1980, at 226-27; Gazeta Mercantil, Je. 20, 1980.
\item \textsuperscript{60} Circ. No. 574 defines the FOB value as the corresponding amount set forth in the respective import license.
\item \textsuperscript{61} Decree-Law No. 1,844 of Dec. 30, 1980.
\item \textsuperscript{63} Id.
\item \textsuperscript{64} CACEX Communique No. 79 of Jan. 31, 1979.
\end{itemize}
Exporters still receive substantial tax and financing incentives. Thus exporters can reduce their taxable income for income tax purposes by the same proportion that export sales bear to total sales. The 25% withholding tax on foreign remittances may be reduced or refunded for exporters of manufactured goods. A drawback regime permits reductions of import duties and the value added tax (ICM) on exported goods. A special agency, the Commission for the Concession of Fiscal Benefits and Special Programs for Exportation (BEFIEX: Comissão para Concessão de Benefícios Fiscais e Programas Especiais de Exportação), is empowered: to extend the tax loss carry forward by two additional years, to permit Brazilian companies to use any supplementary tax on dividends in excess of 12% of registered capital paid to foreign shareholders as a credit against its own federal taxes, and to reduce duties on imported components. An Export Incentives Commission (CIEX: Comissão de Incentivos às Exportações) also grants incentives similar to those in the BEFIEX program to companies carrying out a specific export commitment. Special legislation permits the tax-free importation of an entire factory into Brazil so long as its output is essentially designed for export. In addition, export financing is available at interest rates well below the market.

Brazil is presently seeking a dramatic increase in exports. Consequently, some of the bureaucratic red tape accompanying exports is being cut back. In addition, the Industrialized Products Tax (IPI) credit, which had been eliminated as part of the December 1979 reform package, has been reinstated at a level of 15 percent for exporters of manufactured goods. This tax credit is scheduled to drop to 9% for 1982 and to disappear completely in mid-1983. Revival of the IPI credit for exporters is likely to revive complaints of unfair incentives to exporters from Brazil’s major trading partners. Moreover, it restores another layer of bureaucratic complexity. The measure is, however, a logical outgrowth of Brazil’s policy of devaluing the cruzeiro far less than the differential between the domestic inflation rate and the inflation rate of its major trading partners.

Technology Transfers

One of the most frustrating aspects of Brazilian regulation of business is the transfer of foreign technology. Brazilians have long

66. Red tape still abounds, however. See notes 18-19 supra and accompanying text.
harbored a deep-seated conviction that Brazilian licensees are being overcharged for the use of foreign technology. They are also convinced that balance-of-payments, import substitution, domestic technology development, and export promotion goals can best be served by tight regulation of technology transfers.

The basic statutory rules are themselves fairly arbitrary. Trademark royalties are limited to a maximum of 1% of net sales, and patent royalties cannot exceed 1% to 5% of net sales.\(^68\) The precise percentage permitted depends on both how important the National Institute of Intellectual Property (INPI) deems the technology and how the product fits into a table prepared in 1958 for the purpose of limiting income tax deductions for royalties paid by Brazilian subsidiaries to foreign parent companies.\(^69\) This table, which made little sense in 1958, makes even less sense today.

If the recipient of foreign technology is controlled by the transferor, royalty payments may be neither remitted nor deducted for tax purposes. Payments for technical assistance between subsidiary and parent are treated as if they were dividends for the purpose of assessing the supplemental tax on profit remittances above 12% of registered capital.\(^70\)

All technical assistance and patent licensing agreements must be approved by INPI and registered with the Central Bank before any foreign currency payments can be made to the transferor of the technology. Unless the agreement is part of a project which the government considers of high priority, securing INPI approval is very difficult and time consuming. Payments can be made in cruzeiros, but the tax authorities have taken the position that the Brazilian payor may not deduct such payments as business expenses unless the agreement is duly approved by INPI.\(^71\) The Federal Appellate Tribunal (TFR) has, however, recently permitted such deduction, ruling that the tax authorities' position had no basis in law.\(^72\)

INPI has made patent licensing extremely difficult. No royalty payments can be made until the foreign patent has been registered

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\(^70\) Law No. 4,131 of Sept. 3, arts. 13-14.
\(^71\) This position was originally set out in Normative Opinion No. 102/75 of the Coordinator of the Tax System. It is now embodied in art. 176(1)(e) I, 176(2), and 177(3) of the Income Tax Regulations (Decree No. 76,186 of Sept. 2, 1975).
with INPI, which in 1980 had a nine-year backlog.\textsuperscript{73} INPI flatly refuses to register certain types of patents, such as product or process patents on drugs, food, or medicine. Patent licensors are required to grant the licensee ownership of all improvements made by the licensor. No tie-in provisions are permitted, nor can there be limitations on output, price, or export of the product. The licensor cannot prevent free use of data or technical information after expiration of the patent. Moreover, he can charge for the basic engineering package only as an advance against royalties.\textsuperscript{74} Since the term of the Brazilian patent is deemed to run from the date of the application and royalties cannot be remitted beyond the life of the patent in the country of origin,\textsuperscript{75} the potential life of a licensing agreement is relatively short. Some potential licensors rationally conclude that the rewards from Brazilian licensing operations are not worth the hassle.

To register an unpatented technology or know-how agreement, one has to satisfy INPI that the technology meets the following six criteria: (1) domestic unavailability, (2) compatibility with national development priorities, (3) utility in developing the sector, (4) utility in improving the quality of the product, (5) utility in import substitution, and (6) the ability of the transferee to absorb the technology during the life of the agreement.\textsuperscript{76} Secrecy clauses, which are often critical with unpatented technology, are limited to those INPI deems reasonable.\textsuperscript{77} To register a technical assistance agreement, one has to satisfy INPI that the proposed agreement meets the following five criteria: (1) the proposed technicians are not available locally, (2) the proposed compensation and expenses are reasonable, (3) the foreign technicians will not remain in Brazil longer than necessary, (4) the Brazilian company will master the technology quickly, and (5) the investment is consistent with developmental priorities.\textsuperscript{78}

Generally speaking, technical assistance agreements cannot exceed five years even if the parties are unrelated. Once authorities at

\textsuperscript{73} INPI is now examining patent applications submitted between 1972 and 1976. It hopes to cut back its backlog by farming out some of these applications and by determining applications submitted in 1977 in 1981. Gazeta Mercantil, May 17, 1980.


\textsuperscript{75} \textit{Id.} at 443-44.

\textsuperscript{76} Normative Act No. 15 of Sept. 11, 1975, art. 4.1.2 and 4.2(h).

\textsuperscript{77} \textit{Id.} at 4.5.2(d)(vi). With respect to patent licenses, INPI prohibits the licensor from impairing free use of data and information transferred after expiration of the patent. \textit{Id.} at art. 2.5.2(b)(iii).

\textsuperscript{78} \textit{Id.} at art. 4.
INPI are convinced that technological innovations require a greater period, they may grant an extension of up to five more years. In no case, however, may a technical assistance agreement exceed ten years.\(^7\)

INPI has recently decided that certain sectors should be freed from dependence on imported technology. This policy determination is most clearly reflected in Normative Act No. 30 of January 19, 1978, which states that INPI will no longer approve technology transfer agreements for the automobile industry. The only exception is for Specialized Technical Services which are necessary but unavailable in Brazil. Normative Act No. 30 also prohibits foreign auto manufacturers from charging their Brazilian subsidiaries with any expenses for: (1) administrative, financial, and marketing services; (2) salaries and travel or transfer expenses of foreign personnel assigned to activities not specifically linked to specific and temporary technical services; and (3) research and development performed by the parent company. No payments can be made for any projects of new models and manufacturing methods developed abroad, with the exception of projects for engines and mechanical components beyond the technological levels currently attained in Brazil. One can anticipate that INPI will gradually extend this type of treatment to other industries as Brazil strives to stimulate and develop its own sources of technology and to cut the umbilical cord to foreign technology.

INPI has also recently added an additional layer to the time-consuming process of securing its approval by requiring that virtually all technology agreements be submitted to it for prior approval.\(^8\) Parties to technology transfer agreements, with the exception of those of an occasional nature involving less than $20,000 or the inspection or assembly of imported equipment, must submit a draft of the proposed agreement, along with a Portuguese translation in parallel columns on the same page as the language chosen by the foreign party. The draft must be accompanied by a complex special form detailing the stock ownership of the Brazilian company, any relationships between the parties, the need to import the technology, the exact terms of the compensation agreed upon, alternative sources of the technology, either in Brazil or abroad, and why this particular technology supplier has been chosen. In addition, all existing or contemplated technology agreements between the parties must be submitted regardless of whether approval has been already granted or is unnecessary. Although ostensibly designed to expedite the process of securing approval of technology transfers, the compulsory prior consultation has

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\(^7\) Law No. 4,131 of Sept. 3, 1962, art. 12(3).

\(^8\) Normative Act No. 32 of May 5, 1978.
a tendency to slow them down because INPI approval must be secured twice. Prior approval does not prevent INPI from refusing final approval. Moreover, the procedure is designed to permit INPI to take an even more active role in making itself a party to the negotiations by insisting upon changes in the language and terms of the agreement.

Despite the guidelines of Normative Act No. 15 and the prior consultation procedure of Normative Act No. 32, INPI is still both unpredictable and dilatory. In recent years it has been following a fairly restrictive policy because of Brazil’s serious balance-of-payments problems. In 1979 INPI refused to approve about 36% of the applications it considered; however, this figure is misleading because it does not mention the much larger number of agreements that had to be modified substantially to secure INPI approval. INPI has also been encouraging Brazilian firms to pay fixed prices for technology rather than a percentage of receipts.

INPI’s delays are more exasperating than its disapprovals or exigencies. When an agreement is signed, the technology is almost invariably needed yesterday. But just supplying the necessary documentation for INPI’s preliminary consultation is likely to require several months. Receiving a response from INPI typically consumes several more months, not to mention the additional time required to renegotiate the changes that INPI is likely to insist upon. The applicant must wait for final INPI approval, which typically requires several additional months. Even after INPI approval, on occasion, the Central Bank has refused to register an agreement because it deemed the technology marginal.

Two recent court challenges seeking to compel INPI to approve technology agreements without changes were unsuccessful. The fact pattern of the first case illustrates the frustration and delay that INPI all too frequently produces. This suit was brought by Resena S/A Indústrias Químicas, which began negotiations for a patent license with a French company in 1974. In April 1975 the proposed agreement was submitted to INPI for prior approval. In August 1975, after INPI insisted upon certain changes in the agreement, the patent agreement was renegotiated and resubmitted to INPI in April 1976.

81. Jornal do Comércio, May 7, 1980, at 6. Of the agreements approved by INPI, 80% were in the areas of petroleum and petro-chemicals, nuclear and electric energy, capital goods, steel, and nonmetallic materials. The great bulk of the approved agreements were for engineering services. Id.
One of the two patent applications involved in the agreement was issued in Brazil in April 1978. In June 1979 INPI informed the licensee that a number of additional changes would have to be made before approval of the license agreement. These changes were based upon the guidelines of Normative Act No. 15, issued subsequent to the initial request for approval. The petition for a writ of security was rejected on two grounds: (1) the total compensation called for in the agreement had to be reduced because only one of the two patents being licensed had been registered in Brazil (the other had been denied); and (2) one of the clauses now objected to by INPI had not been in the original draft of the agreement. Significantly, the federal judge's opinion indicated that had both patents been issued and had no new clauses been introduced into the agreement, INPI's insistence upon additional requirements for an agreement previously approved would have been an abuse of power.

The second suit was brought by Royal Diamond Dielectricos S.A., which had also negotiated a technology transfer agreement with a French company. The proposed agreement was submitted in June 1978. In April 1979 INPI insisted upon several changes, including a reduction in the term of the agreement to five years, starting from December 1, 1977. In this case the Brazilian licensee directly attacked INPI's actions for exceeding its powers and for having no legal basis. The federal court rejected both challenges as unfounded and sustained INPI's authority to regulate transfers in a manner deemed appropriate to national development needs.

INPI is a classic example of an agency whose bureaucratic meddling either drives up the cost of investment projects or drives them away. No one really knows how much useful technology remains unavailable in Brazil because of the restrictive and unpredictable regulating of INPI. It is highly probable that future research will show that Brazil would have been far better off if INPI had been confined to registering patents and if Brazilian companies had been allowed to purchase whatever technology they wished upon terms dictated by the market.

Brazil's success in obtaining foreign technology despite INPI's unpredictable regulation is quite remarkable. Most firms evidently feel the Brazilian market is too large and has too much potential to ignore and are therefore willing to tolerate the hassle in order to enter it. The danger is that this calculus may be changing, and Brazil may

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be missing the boat in acquiring the latest technology. Nevertheless, Brazilian supporters of INPI feel that Brazilian firms must be pressed to develop their own technology, and that INPI's efforts have helped keep the import bill at a minimum.

Environmental Protection

Until fairly recently Brazil was a polluter's paradise. Indeed, many heavy pollution industries fled to Brazil to escape restrictive legislation in their home countries. The official Brazilian attitude used to be: pollution is a price we must pay for our development. In recent years Brazil has decided to shave that price by enacting three significant measures: (1) creation of a Special Secretariat for the Environment (SEMA: Secretaria Especial do Meio Ambiente) with powers to promulgate pollution control regulations, \(^{85}\) (2) a national environmental zoning law, \(^{86}\) and (3) a national environmental policy. \(^{87}\)

The environmental zoning law creates three types of zones. Zone one is for the heaviest polluters. All firms which emit objectionable noises, smoke, radiation, or hazardous wastes must be located in areas zoned one. Zone two is for normal industry, and zone three is for non-industrial use. Firms causing some environmental damage or discomfort are, however, permitted to locate in zone three, provided that they are not hazardous to the health of the residents of that area. Pollution standards for all three zones are set by the SEMA or local environmental protection agencies. In the past few years state and local agencies have taken the lead in forcing polluters to clean up and to install protective devices. But firms whose operation is considered of high interest to development or national security may not be shut down without an order from the federal government.

A recent statute requires relocation of industries situated in the wrong zone if suitable controls cannot be installed. \(^{88}\) As zones become more saturated, authorities have the power to insist upon greater controls. Licensing from SEMA and state and local authorities is now necessary for installation in critical pollution areas. Zoning is still the responsibility of state governments, as is most of the monitoring, but control over location of petrochemical, chlorochemical, carbochemical, and nuclear industries is reserved to the federal government.

\(^{87}\) Law No. 6,938 of Aug. 31, 1981.
\(^{88}\) Law No. 6,803 of Jy. 2, 1980.
Although Brazilian pollution standards are still less stringent than those of more developed countries, they are tightening up. This trend towards stricter pollution control enforcement is likely to accentuate as governments become more concerned with the quality of life and less concerned with economic growth statistics.

**Foreign Investment**

The basic regulations on foreign investment in Brazil have not changed significantly since 1964. Generally speaking, foreign companies are free to invest money or assets, such as machinery and equipment, in Brazil. Such investments must be registered with the Central Bank in order for the investor to be able to repatriate them and to remit dividends, but the Bank normally acts expeditiously and does not act as a screening agency. The original investment is registered in the currency of the country where the foreign investor is incorporated or domiciled.

Duly registered investments are freely repatriable at any time. Only if there is a serious disequilibrium in the balance-of-payments may such repatriation be suspended, but this provision has never been invoked. To encourage profit reinvestment and to discourage excessive remittances, profit remittances that average more than 12% of registered investments and reinvestments a year over a three-year period are subject to a steep supplemental tax, which starts at 40% and rises quickly to 60%. Because there is a 25% withholding tax (reduced to 10%-15% by treaty for certain countries) on profit remittances, the maximum permissible dividend without incurring the supplemental tax is 16%.  

Brazil has an enviable record for treating the foreign investor fairly. Particularly if one compares the Brazilian experience with neighboring countries, such as Argentina, Chile, Mexico, Peru, and Venezuela, it is plain that Brazilian treatment of the foreign investor has been exceptionally hospitable since 1964, when the basic rules were fixed in their present form. These rules impose comparatively few restraints on the foreign investor and have enjoyed remarkable longevity.

These basic rules are, nevertheless, deficient in several respects. First, they presuppose that the investor’s home currency is stable, an

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89. Law No. 4, 131 of Sept. 3, 1962, as modified by Law No. 4,390 of Aug. 29, 1964, art. 28.
91. Id. at 255-78.
assumption that is obviously not true. Inflation has reduced the real value of investments denominated in U.S. dollars by more than half since 1969. Consequently, the maximum rate of return without incurring the supplemental tax on an investment registered in 1969 dollars is actually less than 6% in real terms (ignoring reinvested profits). Second, these rules encourage firms to make a large percentage of their investments in the form of loans rather than equity capital. In 1964 interest rates were considerably lower than they are today. Rates of return can be much higher than the 12% dividend limitation if the investment is characterized as a loan, and part of the withholding tax can be rebated to the Brazilian borrower. A sizeable chunk of Brazil’s foreign debt results from the economic incentive to invest by means of loans rather than equity. Third, the 12% return to registered capital is unfair to service companies, such as engineering or accounting firms, which have relatively low capital needs. Fourth, the rules generally do not permit firms to make an investment in the form of technology, a policy which makes no economic sense.92 Yet these rules seem to work reasonably well in practice, and few feel they are really unfair. Thus far, most firms have been remitting much less than 12% on their registered capital, preferring to reinvest their earnings in Brazil. Given the deep seated emotions surrounding foreign investment, the present regime has no desire to reopen the issue of the Profit Remittance Law. For a time, at least, Pandora’s box will remain closed.

There is, however, an increasing trend towards imposition of more restrictive conditions upon foreign investment and towards declaring certain areas off limits entirely to foreign investors. Brazilian controlled companies are being preferred in obtaining cruzeiro financing and investment incentives. Bidding on the firms the government is offering to restore to private hands is restricted, at least initially, to Brazilians. Foreigners cannot acquire rural land except under certain conditions, nor can they acquire shares of Brazilian companies directly on the stock market; only purchases of shares of special investment companies are permitted. Foreigners are barred from participation in the communication media, domestic airlines, and coastal shipping. New foreign investment in banks and insurance

92. A few companies have been permitted to capitalize technology. For example, Hydreco was permitted to capitalize its technology by making a five-year sales forecast and calculating the value of the technology by projecting royalties received from European countries at rates higher than INPI would have approved. A 25% withholding tax was assessed upon this valuation. Brazilian authorities, however, are reportedly reluctant to permit other firms to follow the same procedure. Business International Corp., supra note 38, at 19-20.
companies is restricted, though existing companies are permitted to do business normally. There is an unwritten rule that foreign capital cannot control more than one-third of the voting stock of newly established leasing companies and financing companies. It is government policy to insist that Brazilians own a majority of the equity in virtually all large mining projects, ventures for the production of telephone exchange equipment, mini-computers, and semi-conductors. Generally, the government has pushed a three-way split among foreign capital, state capital, and Brazilian private capital in petrochemical ventures. Government agencies usually exert continual pressure on foreign investors to accept local partners and to increase the percentage of national content in their products.

Foreign companies have been effectively excluded from much of the computer industry. Normative Act No. 16, issued by the Secretariat for Data Processing in July 1981, mandates rejection of new data processing projects unless all of the following three conditions are satisfied: (1) control of the proponent's stock is in the hands of Brazilian individuals who are both resident and domiciled in Brazil, (2) the proponent's capital structure is compatible with the size of the project, and (3) the project utilizes technology developed in Brazil.

An ominous portent of the trend of future legislation reserving certain activities to Brazilians is a recent law limiting the business of highway transport to Brazilians. This statute's restrictive provisions make it extremely difficult for foreigners to accept even a minority interest in Brazilian highway transport firms. Such firms must be owned by Brazilian individuals or legal entities in which 80% of the voting stock is owned by Brazilians. In addition, all directors and administrators must be Brazilian. If it has any foreign capital, a highway transport firm's legal structure must be a corporation (sociedade anonima) with registered shares, and no special treatment for the foreign shareholder may be stipulated. While these restrictions do not apply to companies presently engaged in highway transport, even this grandfather clause contains the seeds of foreign capital's divestment. With the exception of shares stemming from monetary correction of the balance sheet, 80% of any future increases in common stock must be in registered form and must be subscribed to by Brazilians.

Finally, securing visas permitting foreign personnel to work in Brazil generally requires an exasperating number of trips around bureaucratic mulberry bushes. A new immigration law, primarily

93. Law No. 6,813 of Jy. 10, 1980.
94. Law No. 6,815 of Aug. 19, 1980.
aimed at controlling missionaries and illegal aliens, has added an extra layer to already tortuous visa procedures. Unless working for the Brazilian government, foreign personnel sent to Brazil must satisfy the requirements of both the newly created National Council on Immigration and the Ministry of Labor. The new statute also permits conditioning issuance of a permanent visa on the immigrant's spending up to five years in a region designated by the Brazilian government.

The welcome mat is still out for foreign investment. Nonetheless, this trend towards greater reservation of certain markets, credit, and incentives for Brazilian capital indicates that the mat is being steadily pulled back, at least around the edges.

IV. TRENDS IN REGULATION OF BUSINESS DURING THE 1980s

Future trends in government regulation of business are obviously going to depend upon the paths of political and economic events. Brazil is presently in the grips of a serious economic crisis. The country must find a way of reducing its annual inflation rate from more than 100% to a more normal 15%-20% rate. It must generate enough foreign currency to service its huge foreign debt and to pay for its essential imports; the two, taken together, far exceed export income. It has to curtail the rash of strikes and buy labor peace. And it has to generate about 1.5 million jobs a year due to population growth.

Delfim Neto, the Planning Minister, unsuccessfully gambled that inflation could be reduced on the supply side. His theory was that economic growth would cause the supply of goods and services to increase more rapidly than demand would be fueled by the 45% increase he had targeted for the money supply in 1980. He also sought to reduce inflationary pressures by curtailing expenditures by state-owned companies, restricting credit while keeping a lid on interest rates, prefixing monetary correction at rates well below the actual inflation rate, forcing manufacturers to absorb cost increases through price controls, and slowing the rate of devaluation to about half the inflation rate. As a result of these policies, Brazil’s GNP grew by 8.5%

95. At the end of 1979 Brazil’s overall foreign debt was $54 billion. During 1980 Brazil's overall foreign debt increased by $7.3 billion to $61.3 billion. The cost of servicing that debt in 1980 came to $6.94 billion in interest and $7 billion in amortization of principal. Despite an impressive 31% increase in export earnings, Brazil ran a trade deficit of $2.83 billion in 1980. Pardo, Brazil's Needs and Sources of External Financing in 1981, paper presented at Brazil: Update for the Foreign Investor in Miami, Fl. on Mar. 11, 1981.
in 1980, but triple-digit inflation persisted. Savings and investment declined, and the overvalued exchange rate encouraged imports and discouraged exports.

In November 1980 Delfim recognized the failure of his gamble and resorted to more traditional belt-tightening economic policies. Price controls are being less rigidly applied, permitting many firms to improve their profit picture. Full ex post monetary correction has been restored, albeit tied to a price index that has been reporting a lower rate of inflation than traditional price indexes. The cruzeiro is being devalued more rapidly in accordance with the differential between Brazilian inflation and that of Brazil's principal trading partners. In addition, interest rates have been allowed to rise to more realistic levels. Nonetheless, triple-digit inflation has persisted.

Other parts of Delfim's economic policies have been more successful or offer greater potentiality for success. The goal of increasing exports by more than 30% was met in 1980, and Brazil was able to borrow $12 billion abroad to cover its balance-of-payments deficit. The large investments in programs to modernize agriculture and to substitute imported oil with alcohol and hydroelectric power show considerable promise for the future.

There are at least three possible scenarios for the future of governmental regulation of business in Brazil. The likelihood of their coming to pass depends upon a complex mix of economic and political developments.

One possible scenario is that Brazil will successfully weather the present economic crisis. With more orthodox fiscal and monetary policies, the inflation rate should gradually decline to more tolerable levels. Increased exports and foreign lending should enable Brazil to resolve its short run balance-of-payments crunch. In the medium run, the investments in Pro-Alcohol and a modernized agricultural sector might cure the balance-of-payments deficit and relieve some of the inflationary pressure. In this event, the transition from 16 years of military rule to full democracy might well proceed as planned. If this occurs, a new constitution is likely to be one of the first items on the agenda. Politicians are becoming increasingly vocal in their demands for a constituent assembly, for the 1967 Constitution bestowed on the country by the military contains a number of provisions inconsistent with traditional Brazilian concepts of democracy. The model for a new constitution is likely to be the 1946 Constitution, widely regarded among jurists as Brazil's only modern and authentic democratic constitution. Modeled after that of the United States, it differs primarily in the greater legislative power of the federal government at the
expense of the states and the greater executive power of the president at the expense of the Congress. Under this constitutional format, a democratically elected Congress would do the bulk of the legislating, while the President would do less legislating and more administering. The nation's highest court, the Supreme Federal Tribunal, which was packed and unpacked like a suitcase during the 1960s, would be restored to its traditional strength and independence.

A return to a 1946-style constitution would provide the business community with the benefit of greater predictability. Less rapid legislative change would occur because bills would have to be aired in committee and then debated. The more open legislative process should also provide businessmen with greater opportunity to make their views heard and to know what kinds of legislative changes to expect. Though likely to retain broad decree-making powers, the executive should lose his power to present legislation to Congress as a fait accompli.

One current trend likely to continue or accelerate with a democratically elected regime is the trend towards nationalistic legislation regulating multinationals and foreign investors. After so many years of overt encouragement of foreign investors and such a substantial multinational presence, a popular reaction is to be expected. A substantial amount of nationalistic legislation has already been proposed, and some of these bills are likely to become law in the near future.

One measure which may be slated for early passage is a Multinational Ethics Code, already passed by the House of Deputies and approved by the Senate's Commission on the Constitution and Justice. 96 A glance at the bill makes it clear that the executive has no monopoly on poor draftsmanship. The bill simply states that the conduct required from any foreign-controlled company operating in Brazil shall be to refrain from the practice of any of the following acts:

1. Interfering in Brazil's internal affairs or those involving Brazil and any other nation.
2. Acting as an instrument of foreign policy of any country.
3. Failure to cooperate in achieving national objectives and priorities for development fixed by the federal government, or doing anything that effectively prejudices such objectives.
4. Offering an obstacle to the federal government's obtaining infor-

96. This bill is reproduced in its entirety in Jornal do Brasil, May 8, 1980, and Je. 1, 1980. It is actually an adaptation of 11 basic rules contained in a draft that Brazil and other Latin American countries submitted to a U.S. Intergovernmental Commission on Corporations and is sponsored by Deputy Herbert Levy.
mation relating to its activities with the intent to make it impossible to determine whether such activities are consistent with the objectives determined by the government.

5. Acts which translate as:
   (a) a negative contribution to the development of the scientific and technological capacity of the country;
   (b) a resort to restrictive practices recognized as disloyal competition or abuse of economic power; and
   (c) a disrespect for the social and cultural identity of the country.

Practice of any of these acts subjects a corporation to the sanctions of loss of fiscal incentives, government intervention, cancellation of its right to operate in Brazil, or expropriation of a controlling block of its shares.

The basic difficulty with the Multinational Ethics bill is its vagueness. If a company seeks to have its government espouse its claim of expropriation, has it violated the first clause? If the corporation promotes good trade relations between Brazil and its home country, has it violated clause 2? If a parent corporation refuses a request from the Brazilian government to convert its Brazilian subsidiary’s debt into equity investment, has it violated clause 3? If a corporation refuses to disclose its marketing strategy or reveal its pricing policies, has it violated clause 4? Does refusal to start a research laboratory in Brazil because it will duplicate research being performed elsewhere for the corporation violate clause 5(a)? Does a corporation have to be convicted of violating Brazil’s antitrust laws in order to violate 5(b)? Would corporate sponsorship of a scholarly article critical of Brazilian policy violate clause 5(c)? Obviously, the answers to such questions depend upon how the regulations are drafted and how the measure is administered. In typical Brazilian fashion, this kind of bill proposes to grant untrammeled discretion to the bureaucracy to do justice to its friends and apply the law punitively to its enemies.

A variety of other bills currently under consideration give some indication of what can be expected in the near future. One drafted under the auspices of the Ministry of Health would bar government entities from making any health services contracts with a foreign controlled firm, and would also prevent any foreign controlled firm from entering the health care services field in Brazil without special permission from the President of the Republic.97 A bill proposed by Olavo Setúbal would require that all foreign investment be in nominative form and that all foreign controlled companies be obliged to

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publish certified balance sheets in the same form that the Securities Commission (CVM) now requires from publicly held corporations.98

The Industry and Commerce Ministry has proposed a bill to create a watchdog agency to screen foreign investment and to police the activities of foreign companies, defined to include all companies in which as little as 25% of the stock is in foreign hands. Although this bill has been killed for the time being, the Ministry is reportedly considering legislation that would spell out the areas in which foreign investment would be either welcome or prohibited.99

It is quite unlikely that Brazil will slam the door on foreign investment. Brazil needs the roughly U.S.$2 billion capital inflow, and even more important, the inputs of foreign technology, and it will continue to need them for the foreseeable future. Nonetheless, Brazil wants to encourage foreign investment on its own terms. Under a democratically elected government, major changes in the Profit Remittance Law are unlikely. On the other hand, creation of a watchdog agency to police and screen out all undesirable new foreign investments is a likely possibility.

INPI and Normative Act No. 15 will probably be retained unless Brazil begins to fail to attract the latest technology. The pattern of reserving an increasing number of markets to Brazilian controlled firms will surely continue. One would expect to see statutes enacted requiring the gradual fade out of companies already doing business in areas that nationalist sentiment deems properly restricted to Brazilian firms. Another likely possibility is legislation giving Brazilian capital a right of first refusal prior to take over of a Brazilian-owned company by a foreigner.100 Access to Brazilian credit and capital markets by foreign controlled companies is likely to be even more restricted. A more nationalist government is also likely to compel multinationals to capitalize all loans to their Brazilian subsidiaries.

A large-scale wave of nationalization or expropriation of foreign investment is most unlikely. Such action would involve confrontations with the international community and would run contrary to Brazil’s historic attitudes toward foreign investment. Moreover, little foreign investment currently remains in highly sensitive areas, such as public utilities. A continuation of the present tendency towards tight regula-

100. In 1975 a decree-law requiring prior approval of the Finance Ministry before a foreign firm could acquire a domestic firm was drafted but never published in the Diário Oficial. The CVM is presently able to block any takeover it deems prejudicial to national interests.
tion, tempered by practicality and ad hoc negotiated solutions, is much more likely.

A democratic regime would be more concerned about income redistribution and the quality of human life. The compulsory loan is apt to be replaced with a progressive income tax on capital gains.\footnote{The Secretary of Federal Revenue has reportedly already prepared several drafts of such a bill, which is expected to be promulgated in 1981. Jornal do Comércio, Apr. 18, 1980, at 1.} Income tax rates on corporate income should rise from the basic 35% rate to about 45%, and the present excess profits surtax of 5% will probably be retained. Progressive income tax rates on individuals may well rise, pushing the top bracket of 55% to about 70%. The inheritance tax is likely to be stiffened to try to break up some of the huge family fortunes. The proceeds of these increased taxes will probably be redistributed to those on the lower end of the economic spectrum through increases in governmental expenditures for health and education and subsidized food and housing. The outdated, paternalistic Consolidated Labor Laws is a prime candidate for the scrapheap. Labor should win a less qualified right to strike, more independent unions, and greater real wage gains. It is doubtful, however, that labor will be able to resuscitate the old tenure system, which worked so badly in practice. More environmental regulation appears certain, which means businesses can expect to allocate more resources for pollution control devices. The pace of land reform will also be stepped up, but little significant agrarian reform will result from the new Tax on Rural Territorial Property (ITR: Imposto sobre a Propriedade Territorial Rural).\footnote{Law No. 6,476 of Dec. 10, 1979, as regulated by Decree No. 84,685 of May 6, 1980. This law imposes 22 different tax rates upon the assessed value of raw land, varying from 0.2% to 3.5% in accordance with size. These rates can be reduced by as much as 90%, depending upon productivity and the percentage of the tract in productive use.}

A second scenario would be for the present regime to lose control of the economy, or that President Figueiredo's health may prevent him from completing his term,\footnote{Figueiredo suffered a heart attack in September 1981. Unlike 1968, when President Costa e Silva suffered a stroke, the Brazilian military permitted Vice President Chaves, a civilian, to stand in for the convalescing president. President Figueiredo resumed his office in November 1981.} setting the stage for a center-right authoritarian regime to restore economic order. Such an authoritarian regime could conceivably adopt the Chilean model and dismantle Brazil's elaborate set of economic controls. A substantial number of government agencies, such as INPI and CIP, would be consigned to the scrapheap. Wages would be reduced in real terms, and labor

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peace would be insured by repressive measures. The welcome mat for foreign investment would be stretched out full length. The exchange rate would be allowed to float freely, and tariff barriers would be sharply reduced. Competition would replace agency rules and discretion as the basic regulatory device.

The chances of Brazil’s adopting the Chilean model seem slight. The bureaucracy is a huge source of employment, and the notion that business requires close regulation is deeply rooted in Brazil. It is more likely that a center-right authoritarian regime would retain the existing controls while instituting a more orthodox stabilization policy.

A third scenario is that a leftist nationalist regime will come to power. The vehicle might be a coup from nationalist leftist elements of the military or from populist-military alliance. An alternative vehicle might be the democratic election of a populist candidate. Such a regime would almost surely change the basic rules governing foreign investment. In such event, an obvious starting point would be to revert to the 1962 version of the Profit Remittance Law, which denied use of reinvested earnings to build up the remittance base. One would also expect to see the percentage of earnings remittable without the supplementary tax fall from 12% to the 8%-10% range. Restrictions upon technology transfer would be tightened further, and the payment of royalties might be prohibited altogether. The few banks presently owned by foreign companies would probably be nationalized, upon payment of at least partial compensation.

A leftist regime might seek to reschedule Brazil’s huge foreign debt or perhaps default on part of it. Given the size of the debt, foreign banks would probably be inclined to be quite flexible with regard to rescheduling. But it is hard to see Brazil, even under a leftist regime, cutting itself off completely from the Eurodollar market.

A leftist regime would probably squeeze the business community between price controls and massive wage increases. One would expect to see a rash of strikes, a decline in labor productivity, and an increase in governmental subsidies. The number of state controlled firms would increase. The risk contracts under which foreign oil firms have been prospecting for oil would, no doubt, be terminated, and foreign controlled firms would probably be forced out of all mining and energy ventures.

The first scenario seems the most likely. Even if Delfim does not pull off another miracle and has to ask to reschedule the foreign debt and institute austerity measures, it is doubtful that either a popular uprising or a coup d'état will occur. The present regime appears to be sufficiently skillful politically to avert either action.
CONCLUSION

There is a kernel of truth in the familiar adage: “Brazil progresses at night when the politicians sleep.” The idea underlying this adage is that it is the politicians who produce the vast amount of laws and regulations that impede productive economic activity; consequently, progress occurs only when this vast regulatory apparatus they have created is asleep. In the past two decades Brazil has obviously made great strides toward becoming a modern, urban, industrialized, developed nation. While some of this progress is undoubtedly attributable to sensible laws and policies adopted by the modernizing military regimes that have governed the country since April 1964, some is also attributable to the skillful circumvention of the excessive government regulation, part of which was inherited by the military and part of which it has created. What Brazil urgently needs is to clarify and simplify a set of ground rules for business activity and to adhere to those rules for a lengthy period of time. Brazil also needs a strong commitment to deregulation and to the dismantling of large parts of its bloated bureaucracy. Helio Beltrão’s debureaucratization program is on the right track. A greater commitment of resources and manpower to support this imaginative but slender program should be a high priority. Were the government truly to remove itself from the backs of the Brazilian people, the dynamism of the economy and the industriousness of the people are likely to produce a dazzling and self-sustaining “miracle.”