

Dear Reader,

We are proud to announce that Dr. Sidney Apocalypse has joined the partnership of **FRAGA, BEKIERMAN AND PACHECO NETO – ATTORNEYS AT LAW**. Dr. Apocalypse was recently listed in the Latin Lawyer Magazine as a “highly recommended” advisor both in banking and in tax law. Dr. Apocalypse also brings to the firm his huge experience in general business law, having participated in some of the most important national and international deals closed in Brazil over the last three decades.

For some time now we have been publishing a bulletin named “Export and Export News”. Since we started publishing this International Report less than one year ago we have been receiving such a great response from our readers that we decided to consolidate the two publications in this one, which is open for your suggestions and comments as usual.

FRAGA, BEKIERMAN E PACHECO NETO – ATTORNEYS AT LAW

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(organised by Atila Passos **OCANHA** -< aocanha@fblaw.com.br >
Rogerio **TUCHERMAN** < rtucherman@fblaw.com.br >)

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Articles

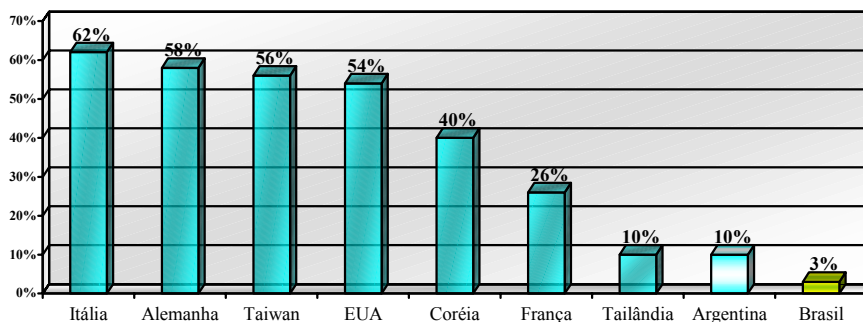
The joint venture as a tool to increasing exports of small and medium-sized enterprises (SME)

Carlos Maria GAMBARO

There is a general consensus that the *small and medium sized enterprises* ("SME") perform a fundamental role in the development and maintenance of a country's micro and macro economy, mainly because of their high operational flexibility, production versatility and job creation capacity, employing a great part of low-qualified employees.

In Brazil, 2.7 million among the 4.9 million companies incorporated in the 1990's were SME. Until August 2001 approximately 3,5 million SME were registered in the country, representing 98.5% of the business community, employing 65% of the whole Brazilian labour force, and accounting for 42% of the total national payroll.

In addition, one of the advantages of the SME is the possibility of expansion into the global markets, exporting genuine national products and therefore contributing to better results in the trade balance. However, in the Mercosur we observe that SME do not perform expressively in exports.



Sources: "A problemática das exportações das Pequenas e Médias Empresas na Argentina"; O Estado de São Paulo¹.

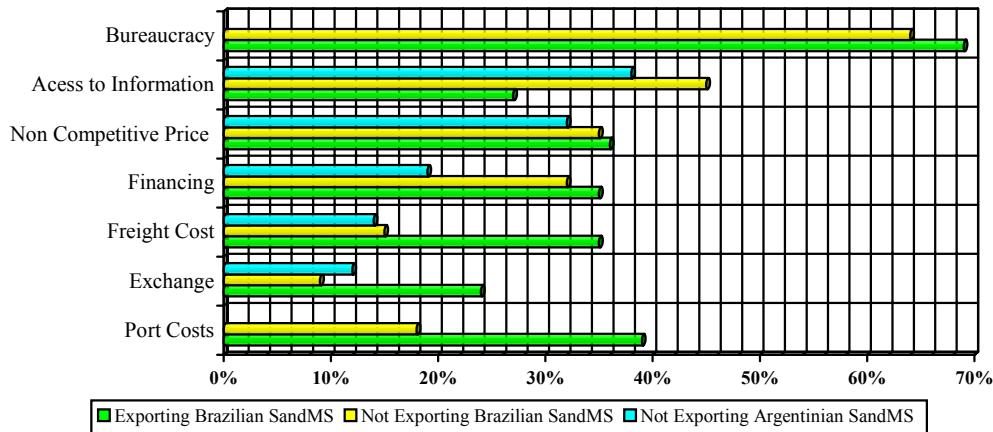
Currently, contribution of the small and medium enterprises in total exports is tiny at best in Brazil and Argentina countries. Moreover, the two countries account for less than 1% and 0.46% of the total of global trade, respectively.

Even though international trade scene has been through successive crises; we do not believe that these are the decisive causes of SME's minuscule revenue and participation in grand total figures. Recent studies point out to internal factors as the main barriers to the export performance of such companies; they also demonstrate that a great part of the exports has been concentrated in very few larger companies,

¹. A LIÇÃO DOS DESENVOLVIDOS. O Estado de São Paulo. Editoriais, 9/12/1999.

meaning that a substantial portion of the small and medium sized enterprises, do not even risk a venture towards the foreign markets.

MAIN HINDRANCES TO THE SME'S EXTERNAL PERFORMANCE.



Sources: *A micro e pequena empresa no comércio exterior*; *La problemática de las exportaciones PyME en Argentina*.

On the other hand, small and medium sized Argentinean and Brazilian entrepreneurs mention the lack of official support (23%) and access difficulty to fairs and international exhibitions (19%) as being important factors that prevent their companies from going global. However, after reviewing the above data, international scenarios have had little impact on SME's decisions not to doing business abroad. The main problems and barriers are, therefore, endogenous.

The joint venture as tool to the SME

Data released by the Brazilian Foreign Relations Ministry estimates that programmes of economical liberalisation, as, for instance, the Mercosur, has promoted a spectacular growth of 300% in intra-block trade between 1990 and 1998, amounting to the sum of US\$ 21 billion. Brazilian trade with other members of the block increased 20% per year, in the last five years.

Part of this success is due to the establishment of approximately 400 joint ventures between Brazil and Argentina, whose companies invested about US\$ 4 billion in the bilateral trade. Still, only 2,1% of the Brazilian small exporting companies made use of any sort of JV structure.

We note that these JV produced quite exciting results for several Mercosur's companies, which have been nonetheless little explored by the SME. Facing such a trend, the Argentinean *Secretaría de la Pequeña y Mediana Empresa* ("Secretariat of Small and Medium Sized Enterprises") has put out programmes aimed at "promoting associative strategies among companies, as an answer to the challenge of competitiveness and the greater Argentinean integration in the world economy." In order to achieve these goals, the Secretariat proposes the "support of programs

guided towards the joint ventures or strategic alliances with foreign SME (AI Invest, Spanish and Italian Regional Nets, UNIDO, etc.)”.

In summary, SME have great potential for development in the global marketplace. However, internal barriers in their own countries hinder such activities. It is necessary that a united performance of all economic players takes place, including political-driven actions to harmonise and coordinate their efforts, facilitating the expansion of small and medium entrepreneurs to areas far beyond their respective territories.

Injunction Relief: No CSLL contribution on exports

Mathias Michael OEFELIN

Mighty Brazilian airplane manufacturer Embraer was granted an injunction relief allowing it not to pay the CSLL contribution on its exports. CSLL taxes 9 percent of the earned profit of a company.

This is a decision from the 2nd Federal Court in the City of São José dos Campos, in the State of São Paulo and there are several other lawsuits pending on this issue.

This lawsuit is based on the controversial interpretation of Constitutional Amendment number 33, enacted in December 2001, by which article 149 of the Brazilian Constitution was changed to the effect that neither social security contributions nor the CIDE contribution can be levied on exports.

This amendment has stirred arguments about the interpretation of the expression “social contribution”. The tax authorities defend that only contributions levied on the revenues - PIS and COFINS - are covered by the amendment. In any case ordinary law already grants the tax exemption on exports for PIS and COFINS.

There is no doubt that CSLL is a duty classified as “social contribution” and under Brazilian jurisprudence and court decisions tax law must have strict interpretation. As a result of that, the original aims and goals of the Legislative Branch and the discussions prior to enactment of the amendment are of no importance in interpreting it. Construction by interpreters can only take into consideration the actual published text. In this case, final wording actually grants tax immunity to profit arising from exports.

The court in São José dos Campos, São Paulo, reinforced this understanding. It is likely that favourable decisions shall follow.

Shall the case be decided by the Supreme Court in favour of the taxpayers it will certainly be a strong relief and incentive for the exporters based in Brazil.

Mandatory Tax Registration for Foreign Investors in Brazil

Karina VIESTI

As noted in the previous issues of our International Report, the Brazilian Internal Revenue Service (Secretaria da Receita Federal - SRF) issued the Normative Ruling (NR) n. 200, dated September 13, 2002 regulating the enrolment of legal entities into the *Cadastro Nacional da Pessoa Jurídica (CNPJ)* - Legal Entities' Taxpayer Registry - and established a mandatory CNPJ enrolment for foreign legal entities which hold certain assets or rights in Brazil. This rule directly affected all foreign investors in Brazil.

In order to proceed with the enrolment, the foreign investor must appoint an individual, resident in Brazil and duly enrolled before the Individual Taxpayers Register (CPF), as its attorney-in-fact with full powers to represent it and handle any issues before the Brazilian Internal Revenue Service (SRF). These comprise the reception of service of process, and manage the assets or rights that have given cause to the CNPJ enrolment.

In spite of all the new bureaucratic procedures brought about by the Normative Ruling 200/2002, the remittances to foreign countries have also been suffering delays due to the hindrance on the closing of the exchange contracts and money transfer by Brazilian banks. Nevertheless, the issuance of the new Normative Ruling 312, on March 28, 2003 softened some of the bureaucratic hindrances of Normative Ruling 200/2002.

As of June 16, 2003, when the new Normative Ruling was implemented, the foreign companies that intend to invest in the country will not face problems with the exchange contracts and money transfer anymore.

In the case of investment funds abroad and foreign entities, which hold in Brazil exclusive investments in the financial and in the capital market, the enrolment will be realised when the Registry of Foreign Investor is granted after being requested from the *Comissão de Valores Mobiliários (CVM)* – Brazilian Securities Commission.

According to Normative Ruling 312/2003, the enrolment in CNPJ will also be necessary when the foreign entity realises the following operations in Brazil: a) acquisition of intangibles with a term longer than 360 days; b) financing; c) financed import; d) leasing; e) lease, equipment rent and ship freightage; e) asset imports without exchange cover intended for payment of subscribed capital of Brazilian companies; f) loans given to individuals resident in Brazil and g) foreign investments in the country.

Thus, according to the new rule, the Brazilian Internal Revenue Service will additionally extend its supervision on foreign loans that before the Normative Ruling 312/2003 did not exist.

The enrolment of the foreign entity that carry-on these operations will be formalised when its Entity Registry (CADEMP) from the Brazilian Central Bank is granted. The new rule allows that the foreign company regularises its enrolment before the CNPJ in the term of 180 days after the operation in Brazil. In the meanwhile the enrolment will be considered "suspended".

Legislation

Decree 4.765 / 2003

It changes Decree 4.543/2002, which regulates the administration of customs activity, the supervision, the control and the taxation on the operations of foreign trade.

IN SRF 335 / 2003

It changes IN SRF 121/2002, which disposes of the transference of goods imported and received in a special customs system to a different one.

Decree 4.702 / 2003

It promulgates the Agreement between the Brazilian Government and the Government of the United States of America regarding cooperation of their Competition Defense Authorities for the appliance of their Competition Laws, aiming to promote a real appliance for them, through such cooperation of their authorities.

News

Inflation adjustment of phone bills: Enforcement of established contracts confirms independence of regulatory agencies from the Executive Branch

After a fierce political battle within the Federal Government, the Lula administration recognised last week that the National Agency of Telecommunications (ANATEL) must enforce the concession agreements signed with the private telecom companies privatised in the tenure of President Fernando Henrique Cardoso. Critics of the average 28.5% increase applied starting in July 2003 phone bills exceeded by far the actual inflation calculated according to several other indexes. Although ANATEL claimed it had no choice but to apply the index established in the concession agreements, several consumer protection agencies filed lawsuits requesting the use of rates as low as 17.14%, regardless of what is established in contracts. The dispute is still to be settled in courts, but the early political decision in favour of ANATEL sends a strong signal to investors that the Lula Administration has made the decision to enforce agreements risking political approval instead of going the populist way.

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National Petroleum Agency (ANP) publishes Fifth Round Rules and Model Granting Instruments

On July 3, 2003, ANP released the rules of the Notice to Bid and the Model Granting Instrument to be signed by winning bidders of the Fifth Round of Concession of Oil & Natural Gas Blocks. The tender offers of the 1.070 onshore and offshore blocks shall take place on August 19 and 20, 2003. The execution of the Granting Instruments is slated for November 30, 2003. The Notice to Bid and the Instrument come with some changes due to the smaller size and scale of the offered blocks and in view of the change in criteria of evaluation of offers, which now strongly stresses minimum local content commitments. ANP reduced from R\$ 1 billion to R\$ 500 million the net equity value required from banks issuing guarantees and letter of credits to the bidders. According to ANP, 10 foreign companies out of the 14 confirmed bidders expressed interest in blocks located in the Potiguar, Recôncavo, Espírito Santo, Barreirinhas, Campos, Foz do Amazonas, Jequitinhinha, Pelotas and Santos basin.

South Africa and Mercosur will enter into a tax preference agreement

By the end of this year, South Africa might sign an agreement of tax preference with the Mercosur, as their first step to the creation of a free trade zone between them, predicted for 2004. Alec Erwine, Pretoria minister of trade, mentioned that by the end of the year, Brazilian mining enterprises will enter into a joint venture agreement with South African enterprises in order to exploit ore fields on the African continent.

Decree makes distinction between rum and “cachaça” and benefits exports.

President Luiz Inácio Lula da Silva is about to sign the alteration of the decree n. 4.072/02, which will institute the difference between rum and “cachaça”. It is believed that this will encourage the export of “cachaça” which is a typical Brazilian alcohol and has not yet been exported as such. Foreigners know it as if it were rum. In order to change such a habit, and modify its denomination abroad, the Internal Revenue Service will notify the World Customs Organisation (WCO) to include “aguardente de cana” in the International Harmonised System until June 30th.

Courts Accept Electronic Petitions

The Second Special Jurisdiction Court for Civil Appeals of the state of São Paulo has enacted an administrative rule permitting the submission of petitions via email. On April 30 2003 the Federal Senate approved Bill 228/00, amending the text of Law 9,800/99 accordingly, and in line with these measures, lawyers who use this method are responsible for delivering the original petitions to the court.

Brazilian government ready to auction off AES's shares in Eletropaulo, hoping to recover part of the US\$ 1.2 billion debt

After exhausting several months of negotiation with senior AES and U.S. Government officials, Brazilian national development bank BNDES rejected their debt restructuring plan and decided to auction off the first block of AES 70% voting shares in Eletropaulo. AES has defaulted on around \$420 million in debt payments to the bank so far this year. The first auction of AES's shares in Eletropaulo, the mammoth power distribution company serving 14% of Brazilian consumers, is expected to take place still in July. The shares were given by AES as guarantees in a loan contract between AES and the bank in a 1998 privatisation auction. AES Elpa, a holding company of the U.S. power group defaulted in January on \$85 million of \$1.2 billion owed to BNDES, which triggered a contractual clause allowing the BNDES to foreclose on the control of Eletropaulo. BNDES has said the sale process would take at least 107 days, including a tender to choose investment banks to evaluate Eletropaulo's market value and set a minimum price for the auction.

In the meantime, AES continues to manage Eletropaulo, an arrangement that is expected to continue until a restructuring deal is worked out or BNDES finds another buyer for the distributor.