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J.M. Pinheiro Neto

Irene Dias da Silva false

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Incentives for Investment in Brazil

by *J.M. Pinheiro Neto**
and
*Irene Dias da Silva***

IT IS INTERESTING to observe the development of a country slightly larger than the continental United States,¹ which until a few decades ago, was solely interested in a peaceable life in which economics did not play a large part. Until the Second World War, private initiative was the principal purveyor of goods and services, and foreign investments were largely made in public services - railroads, power, telephones, gas, banks, etc. The needs of those engaged in the war, and the supply of foodstuffs and manufactured articles demanded by them, gave rise to an awakening to basic economics. The Brazilian Constitution, considerably changed in 1946 after the fall of Getulio Vargas, established that a National Council for Economy should concern itself with the study of the economic life of the country, suggesting to the executive branch of the Government the steps that should be taken to foster the development of the country.²

It was some years before this Council was actually created. This occurred only in 1949,³ but little was done to implement the grandiose objectives incorporated in its organizational paper.⁴ It took the far sighted views of a much criticized President, Juscelino Kubitschek, to give life to the desire of Brazil's population to see the country arise from the platitude of four centuries of slow progress. In 1956, the Development Council was created as part of the executive branch of the Federal Government, subject directly to the President.⁵ Its terms of reference were to study the

* Senior partner, Pineiro Neto - Advogados with offices in São Paulo, Rio de Janeiro, Brasilia, Campinas and London. L.L.B., University of São Paulo School of Law (1938). Member of Brazil Bar. The author would like to express his gratitude to those members of his firm who aided in the preparation of this article.

** Senior Associate, Pinheiro Neto - Advogados, L.L.B., University of São Paulo Law School, (1972). Member, Brazil Bar.

¹ Brazil has a total area of 8,511,965 km. 122 NAT'L GEOGRAPHIC 351 (Sept. 1962).

² See CONSTITUÇÃO of Sept. 18, 1946, art. 205 (Braz.).

³ See Law No. 970 of Dec. 16, 1949, [1949] 13 Coletanea de Legislação Lex 376 (Braz.) [hereinafter cited as Coletanea].

⁴ This law regulated the attributions and organizations of the National Council for Economy.

⁵ See Decree No. 38.744 of Feb. 1, 1956, [1956] 20 Coletanea 40 (Braz.), as regulated by Decree No. 38.906 of Mar. 15, 1956, [1956] 20 Coletanea 77 (Braz.).

steps required for the advancement of the economic policy of the country, and the organization of plans to obtain greater efficiency of the public sector while also fostering private initiative.⁶ It was shortly afterwards that in line with these ideas a first incentive was created for the establishment in Brazil of an automotive industry.⁷ Up to that time, with imports reasonably free, the main automotive concerns imported their vehicles into Brazil, although some vehicles were locally assembled. The new provisions allowed these concerns, and any others interested in the country and in this activity, to bring used equipment into the country which could be registered as foreign investment after proper appraisal, forming the basis for future remittances of profits.⁸ This created an excellent opportunity for many concerns to send their obsolete machinery to Brazil and thereby take part in the creation of a new industrial activity in the country. Further incentives granted included a reduction of import duty⁹ and the creation of special conditions for foreign financing.¹⁰ To obtain these incentives, plans had to be submitted and approved by a newly created department within the Development Council; the Executive Group of the Automotive Industries (GEIA).¹¹ GEIA could also allow the importation of parts required for the manufacture of the vehicles with reduced duty or even free of duty.¹² This last incentive would be granted only for a limited period,¹³ as it was the stated policy of that department to see an independent industry created in the country for supply to the automotive concerns of all that they might require. GEIA could also propose to the proper department the allowance of immigration of technicians and specialized workers required by the newly created activity.¹⁴

The first plans approved by GEIA had to do with trucks.¹⁵ In 1957, plans for passenger cars were also approved with the stated intent of having cars with 95 percent locally made parts by the year 1960.¹⁶ The proposals to be submitted to GEIA had to indicate quite clearly the manner in which this percentage was to be attained.¹⁷ By 1959, the engine would have to be locally manufactured and contain at least 60 percent by weight

⁶ Decree No. 38.744 of Feb. 1, 1956, art. 2, [1956] 20 *Coletanea* 40 (Braz.).

⁷ See Decree No. 39.412 of June 16, 1956, [1956] 20 *Coletanea* 262 (Braz.).

⁸ *Id.* art. 2, §1.

⁹ *Id.* art. 5, §1(b).

¹⁰ *Id.* art. 2, §2.

¹¹ *Id.* art. 14.

¹² *Id.* art. 5, §1.

¹³ *Id.* art. 5.

¹⁴ *Id.* art. 13.

¹⁵ See Decree No. 39.568 of July 12, 1956, [1956] 20 *Coletanea* 299 (Braz.).

¹⁶ See Decree No. 41.018 of Feb. 26, 1957, [1957] 21 *Coletanea* 121 (Braz.).

¹⁷ *Id.* art. 6.

Brazilian parts.¹⁸ Following in quick succession were plans concerning four-wheel vehicles,¹⁹ light trucks²⁰ and tractors.²¹ At the same time a law was passed granting exemption from import duty and consumers tax for plant equipment required for the local manufacture of automotive parts and engines.²² Realizing that a new industrial activity could not be created without some experience, the Federal Government also allowed companies with approved plans to import disassembled vehicles with some parts omitted that could already be locally obtained.²³ These imports were allowed to be made with reduction of import duties in proportion to the content of the parts to be obtained locally.²⁴ As another incentive, the government also allowed these companies to have access to government financing, which was already then at a lower interest rate than that normally prevailing.²⁵

During the subsequent period (from approximately 1958 to early 1964), the Federal Government used this system of incentives to foster the creation or the development of other industries. In this way it was possible to indicate the directions in which the country should proceed: machines for surface transport and agriculture,²⁶ heavy machinery,²⁷ metallurgy,²⁸ pharmaceuticals,²⁹ fertilizers,³⁰ textiles³¹ and shoes.³² Various Executive Groups were then organized under the umbrella of the Development Council; all independent but subject directly to the President. In 1964, the Development Council was extinguished, and a new Commis-

¹⁸ *Id.* art. 7, §2.

¹⁹ Decree No. 39.569 of July 12, 1956, [1956] 20 *Coletanea* 299 (Braz.).

²⁰ Decree No. 39.676-A of July 30, 1956, [1956] 20 *Coletanea* 334 (Braz.).

²¹ Decree No. 47.473 of Dec. 22, 1959, [1959] 23 *Coletanea* 585 (Braz.).

²² Law No. 2.993 of Dec. 6, 1959, [1959] 20 *Coletanea* 615 (Braz.).

²³ See Decree No. 42.820 of Dec. 16, 1957, art. 91, [1957] 21 *Coletanea* 755 (Braz.).

²⁴ *Id.* art. 91, §3.

²⁵ See Decree No. 39.412 of June 16, 1956, art. 11, [1956] 20 *Coletanea* 262 (Braz.).

²⁶ See Decree No. 50.519 of May 2, 1961, [1961] 25 *Coletanea* 449 (Braz.), which created the Executive Group of the Agricultural and Highway Machinery Industry (GEIMAR).

²⁷ See Decree No. 50.522 of May 3, 1961, [1961] 25 *Coletanea* 451 (Braz.), which created the Executive Group of the Heavy Mechanics Industry (GEIMAPE).

²⁸ See Decree No. 50.521 of May 3, 1961, [1961] 25 *Coletanea* 451 (Braz.), which created the Executive Group of the Metallurgic Industry (GEIMET).

²⁹ See Decree No. 52.471 of Sept. 13, 1963, [1963] 27 *Coletanea* 1.095 (Braz.), which created the Executive Group of the Pharmaceutical Industry (GEIFAR).

³⁰ See Decree No. 52.732 of Oct. 23, 1963, [1963] 27 *Coletanea* 1.296 (Braz.), which created the Executive Group of the Fertilizer Industry (GEIFERC).

³¹ See Decree No. 53.585 of Feb. 21, 1964, [1964] 1 & 2 *Coleção das Leis, Atos do Poder Executivo* 171 (Braz.) [hereinafter cited as *Coleção*], which created the Executive Group of the Textile Industry (GETEC).

³² See Decree No. 53.586 of Feb. 21, 1964, [1964] 1 & 2 *Coleção* 172 (Braz.), which created the Executive Group of the Shoe Industry (GECAL).

sion for Industrial Development (CDI) organized.³³ The purpose of this new commission was to coordinate all activities of the various groups and be the arbiter of the incentives to be granted. In 1969, the CDI became the Council for Industrial Development³⁴ and the Executive Groups were extinguished and substituted by sectorial groups, with basically the same duties. There are presently seven sectorial groups: capital goods industries; basic metallurgic and intermediary metal products industries; chemical, petro-chemical and pharmaceutical industries; intermediary non-metal products, and cement, paper, and cellulose industries, automotive and automotive components industries; and war material industries.³⁵

In line with these measures, the Federal Government also created special incentives for areas in which development has been slow or which lack the resources for major advancement. The better known agencies are those for the North-East (SUDENE)³⁶ and the Amazon basin (SUDAM).³⁷ There are, however, a number of others: for the Southern part of the country (SUDESUL),³⁸ for the Mid-West region (SUDECO),³⁹ for the San Francisco Valley (CODEVASF),⁴⁰ and for the Free Zone of Manaus (SUFRAMA).⁴¹ One State of Brazil merited a special program, and the Fund for the Economic Recovery of the State of Espirito Santo (FUNRES)⁴² was created. These agencies granted two incentives: a tax

³³ See Decree No. 53.898 of Apr. 29, 1964, [1964] 3 & 3a Coleção 19 (Braz.).

³⁴ See Decree No. 65.016 of Aug. 18, 1969, [1969] 5 Coleção 247 (Braz.).

³⁵ See Decree No. 81.651 of May 11, 1978, [1978] 42 Coletanea 368 (Braz.).

³⁶ The Superintendency of the Development of the North-East (SUDENE), was created by Law No. 3.692 of Dec. 15, 1959, [1959] 23 Coletanea 567 (Braz.).

³⁷ The Superintendency of the Development of the Amazon (SUDAM), was created by Law No. 5.173 of Oct. 27, 1966, [1966] 7 Coleção 322 (Braz.).

³⁸ The Superintendency of the Development of the South Region (SUDESUL), was created by Decree-Law No. 301 of Feb. 28, 1967, [1967] 1 Coleção 530 (Braz.). SUDESUL is responsible for providing the development of municipalities situated in the South Region of Brazil.

³⁹ The Superintendency of the Development of the Mid-West Region (SUDECO), was created by Law No. 5.365 of Dec. 1, 1967, [1967] 31 Coletanea 2250 (Braz.). Sudeco is responsible for directing federal action in the Mid-West Region of Brazil. Both SUDESUL and SUDECO do not count on funds derived from tax incentive schemes to carry out their programs and their duty is to make studies for the investment of federal funds in programs benefitting projects in the area.

⁴⁰ The Company for the Development of the São Francisco Valley (CODEVASF), was created by Law No. 6.088 of July, 1974, [1974] 5 Coleção 64 (Braz.), to replace the Superintendency of the São Francisco Valley (SUVALE) Decree-Law No. 292 of Feb. 28, 1967, [1967] 1 Coleção 506 (Braz.). CODEVASF has the purpose of utilizing the water and soil of the São Francisco Valley.

⁴¹ The Superintendency of the Development of the Free Zone of Manaus (SUFRAMA), was created by Decree-Law No. 288 of Feb. 28, 1967, art. 10, [1967] 1 Coleção 492 (Braz.).

⁴² See Decree-Law No. 880 of Sept. 18, 1969, [1969] 5 Coleção 218 (Braz.). FUNRES provides for the investment of funds in fishing, tourism, agricultural or industrial projects in the State of Espirito Santo.

reduction or exemption for the new industries established in the area, and a contribution of equity non-voting funds. A caveat should be added in regard to the last form of incentive. All income tax payers, whether individuals or companies, were and still are authorized to deduct a certain percentage of their tax for investment in one of these areas.⁴³ The possibility existed to determine in which company the funds should be invested, but this is presently modified, and all these allocations of funds are controlled by government created banks to deal exclusively with these investments.⁴⁴ For the taxpayer, the advantage was in obtaining its return through a sale of the shares five years after the investment. For the company, the benefit was the availability of funds at a very low rate of interest, as the dividends to be paid on the non-voting shares were very low. This system has not been modified and the advantages remain the same.

The Federal Government was also concerned with certain activities which it wanted to foster or promote, irrespective of the region where they might be developed. And so, a number of sectorial organizations were created. They are the Superintendency of Fishing Development (SUDEPE),⁴⁵ the Brazilian Institute of Forest Development (IBDF),⁴⁶ the Brazilian Tourism Company (EMBRATUR),⁴⁷ the Brazilian Aviation Company (EMBRAER),⁴⁸ the Executive Group of the Mining Industry (GEIMI),⁴⁹ and the Commission for the Concession of Tax Benefit's to Special Export Programs (BEFIEX).⁵⁰

All the incentives previously mentioned may be given to companies established in Brazil regardless of who their shareholders are and in whom control is vested. Financial incentives also exist and become very important in a country with high inflation. These incentives are given only to companies with a majority voting shareholding and control in the hands of Brazilians or Brazilian residents under certain conditions. The incentives are long term financing at rates of interest lower than those normally charged by private and official financial institutions. The agents that provide these incentives are, first, the National Bank of Economic Development (BNDE),⁵¹ and then the State Development Banks. Besides

⁴³ See Income Tax Regulation as approved by Decree No. 85.450 of Dec. 4, 1980, Book I, Title IV, Chap. II and Book II, Title III, Chap. XVIII.

⁴⁴ See Decree-Law No. 1.376 of Dec. 12, 1974, [1974] 38 *Coletanea* 1153 (Braz.).

⁴⁵ Created by Delegate-Law No. 10 of Oct. 11, 1962, [1962] 26 *Coletanea* 288 (Braz.).

⁴⁶ Created by Decree-Law No. 289 of Feb. 28, 1967, [1967] 1 *Coleção* 498 (Braz.).

⁴⁷ Created by Decree-Law No. 55 of Nov. 18, 1966, [1966] 7 *Coleção* 101 (Braz.).

⁴⁸ Created by Decree-Law No. 770 of Aug. 19, 1969, [1969] 5 *Coleção* 130 (Braz.).

⁴⁹ Created by Decree No. 62.352 of Mar. 5, 1968, [1968] 1 & 2 *Coleção* 461 (Braz.).

⁵⁰ Created by Decree-Law No. 1.219 of May 15, 1972, [1972] 36 *Coletanea* 798 (Braz.).

⁵¹ This Bank was created by Law No. 1.628 of June 20, 1952, art. 2, [1952] 16 *Coletanea* 165 (Braz.), to act as the agent of the Federal Government in its financial operations for the re-equipment and furtherance of the national economy. BNDE was later allowed to operate

the granting of financing, BNDE also has four subsidiaries, three of which are allowed to take an equity non-voting participation in Brazilian companies in need of working capital and desirous of expansion. One of them, the first one to be created, the Financing Fund for the Acquisition of Industrial Machinery and Equipment (FINAME),⁵² provides financing to Brazilian-controlled manufacturers or to the purchasers of their products. The others, Mecânica Brasileira S.A. (EMBRAMEC), Insumos Básicos S.A. - Financiamento e Participações (FIBASE), and Investimentos Brasileiros S.A. (IBRASA) are allowed to subscribe to non-voting preferred shares in Brazilian companies engaged in the manufacture of heavy machinery, in basic inputs industries, and in selected activities.⁵³

The definition of a Brazilian company used to be a clear and easy one, and it was initially given by a law passed in 1962 regulating foreign investment in Brazil.⁵⁴ A company in which Brazilians or Brazilian residents had the majority of the voting shares, was Brazilian. This is still so, but not to BNDE and its subsidiaries and state development banks, which inquire as to the shareholder with effective control of the business. If for different reasons it is established that the control of the concern lies with the foreign shareholder, then the company cannot avail itself of this subsidized financing. This type of financing is subject to a three to nine percent annual interest, with monetary correction (indexing)⁵⁵ and enjoys a grace period of up to three years in loans for nine or fifteen years for payment. The reasoning behind this system is that the Brazilian company, especially the small or medium sized one, does not have access to other sources of financing normally available to foreign controlled companies established in the country, or to the subsidiaries of foreign concerns.

Since additional tax credits, exemptions, and reductions are granted to locally controlled companies, the tax usually assessed and the tax incentives granted should be examined. The corporate income tax is charged at the rate of 35 percent on the taxable profit of each year, and at an additional rate of 5 percent for profits exceeding Cr\$ 30,000,000 (roughly US\$ 500,000), such additional tax being applicable in the fiscal year 1980, 1981 and 1982, corresponding to the base periods 1979, 1980, and 1981, respectively.⁵⁶

as a public company by Law No. 5.662 of June 21, 1971, [1971] 35 Coletanea 877 (Braz.).

⁵² Created by Decree No. 55.275 Dec. 22, 1964, [1964] 28 Coletanea 1441 (Braz.).

⁵³ These BNDE subsidiaries were incorporated in 1974.

⁵⁴ See Law No. 4.131 of Sept. 3, 1962, as amended by Law No. 4.390 of Aug. 20, 1964, and Decree No. 55.762 of Feb. 17, 1965, [1965] 29 Coletanea 1500 (Braz.), reprinted in Banco Central do Brazil, *Foreign Investment in Brazil*, LEGISLATION, Jan., 1977, at 19.

⁵⁵ The Federal Government established the maximum rate of indexing at 45 percent for the year 1980. The rates of indexing for the year 1981, however, will correspond to the rates of inflation verified monthly by the Federal Government.

⁵⁶ See Decree-Law No. 1.704 of Oct. 23, 1979, [1979] 43 Coletanea 823 (Braz.).

The Tax Manufactured Products (IPI) is a federal tax, payable on the domestic manufacture of products and on the importation of foreign products.⁵⁷ The domestically produced or imported products subject to IPI are listed in the IPI Table,⁵⁸ which is identical to the Brazilian Customs Tariff. Both are based on the Brazilian Nomenclature of Merchandise which, in turn, corresponds to the Brussels Customs Nomenclature. The rates of IPI contained in the table vary according to the nature of the products, in general, from 10 to 15 percent, although higher rates apply to cigarettes, beverages, cosmetics, etc. The Tax on the Distribution of Goods (ICM) is a State tax, payable at all stages of distribution, or rather at all stages of sale, from the manufacturer until the final customer.⁵⁹ ICM rates at the present time are: 13 percent on export operations (when applicable), for interstate and intrastate operations in the South-East and South of Brazil, 15 percent in 1980, 15.5 percent in 1981, and 16 percent from 1982 onwards; and for intra-State and inter-State operations in the North, North-East and Mid-West of Brazil, 16 percent in 1980 and following years.

Import duty⁶⁰ is payable on the entry of foreign goods into the country for internal consumption.⁶¹ The foreign goods subject to the duty are listed in the Brazilian Customs Tariff,⁶² which is identical to the IPI table. The rates of import duty are, as a general rule, *ad valorem*, and vary according to the nature of the products and their degree of indispensability, from zero to 205 percent.

The main policy maker in the area of incentives is the Council for Economic Development (CDE),⁶³ which is comprised of all the secretaries

⁵⁷ See Law No. 4.502 of Nov. 30, 1964, [1964] Consolidação (Braz.); Decree No. 83.263 of Mar. 9, 1979 (IPI Regulations), *as amended* by Decree No. 84.113 of Oct. 23, 1979, [1979] 43 Coletanea 827 (Braz.).

⁵⁸ The IPI Table currently in force was approved by Decree No. 84.338 of Dec. 26, 1979, [1979] 7 & 8 Coleção 228 (Braz.).

⁵⁹ Although the principles and rules for ICM are established in Decree-Law No. 406, of Dec. 31, 1968, *as amended* by Decree-Law No. 834 of Sept. 8, 1969, [1969] 5 Coleção 183 (Braz.) (which is federal legislation), ICM is a state tax and is collected under State legislation.

⁶⁰ The current legislation on import duty is sparse and in need of consolidation, which is likely to occur within the near future. Basically, the legislation comprises Law No. 3.244 of Aug. 14, 1957, [1957] Legislação Alfandegária e de Imposto de Importação 1573 (Braz.); and Decree-Law No. 37 of Nov. 18, 1966.

⁶¹ The internal consumption of the imported goods is a prerequisite to the charge of import duty. In certain circumstances, however, where there is no element of consumption, there is no prerequisite to pay import duty or payment need only be made when the goods are dispatched to the customer.

⁶² The Brazilian Customs Tariff currently in force was established by Resolution No. 1.959 of Dec. 16, 1973, [1973] Diário Oficial da União I (CPA)(Braz.) [hereinafter cited as D.O.U.].

⁶³ See Law No. 6.036 of May 1, 1974, [1974] 38 Coletanea 708 (Braz.).

involved in fields having to do with the economy of the country and directly responsible to the President. Its functions are to set priorities for the national economic development process, and to establish guidelines for the implementation of the development plans of the country.⁶⁴ CDE is also responsible for proposing the Brazilian policies of regional and sectorial resources derived from the incentive funds.⁶⁵ The sectorial or regional agencies receiving the resources of these funds thus implement their respective programs according to the guidelines established by CDE. This permits the establishment of enterprises in those areas considered as unfavorable for that purpose due to lack of production factors, skilled employees, commercial infrastructure and markets. SUDAM and SUDENE are the most important regional agencies.

SUDAM is a federal autonomous body in charge of direct federal action in the Amazon area. The incentives available are intended for agricultural, livestock, industrial and basic service projects.⁶⁶ They are: equity investment of FINAM and FIDAM funds;⁶⁷ exemption from income tax and non-refundable additional charges for a period of 10 years, for industrial and agricultural undertakings in the SUDAM area, which are set up, modernized, expanded or diversified up to and including the fiscal year 1982;⁶⁸ and exemption or reduction of import duty, of IPI tax and of other federal duties for the importation of machinery and equipment not produced in Brazil, when intended to implement undertakings approved by SUDAM.⁶⁹ SUDENE is the body in charge of supervising, coordinating and controlling the implementation of investment projects for the de-

⁶⁴ The Third National Development Plan, covering the period 1980-1985 has already been approved by the National Housing through Resolution No. 21 of May 21, 1980, [1980] D.O.U. (III PND)(Braz.) and its main objectives are: increasing the internal income and number of jobs; improving the distribution of income, reducing the levels of poverty and increasing the standards of living of the lower classes; reducing the regional unevenness; reducing inflation; equalizing the balance of payments and control of the external indebtedness; developing the energy sector; and ameliorating the political system.

⁶⁵ See Decree-Law No. 1.376 of Dec. 12, 1974, arts. 2 & 10, [1974] 38 *Coletanea* 1152 (Braz.). The investment funds are operated by banks: the Northeast Investment Fund (FINOR) by Banco do Nordeste do Brazil S.A.; the Amazon Investment Fund (FINAM) by Banco da Amazônia S.A. (BASA); and the Sectorial Investment Fund (FISSET) by Banco do Brazil S.A., which must keep three separate accounts for the fishing, forest and tourism programs.

⁶⁶ See Decree-Law No. 756 of Aug. 11, 1969, art. 1, [1969] 5 *Coleção* 105 (Braz.). The basic services for the purposes concerned are those related to energy, transportation, communication, colonization, education, sanitation and public health.

⁶⁷ See SUDAM, Law No. 5.173 of Oct. 27, 1966, Chap. 3, art. 45, [1966] 7 *Coleção* 322 (Braz.).

⁶⁸ See Decree-Law No. 756 of Aug. 11, 1969, art. 22, [1969] 5 *Coleção* 105 (Braz.); and Decree-Law No. 1.328 of May 20, 1974, [1974] 38 *Coletanea* 757 (Braz.).

⁶⁹ See Decree-Law No. 756 of Aug. 11, 1969, art. 26, [1969] 5 *Coleção* 105 (Braz.).

velopment of the North-East region of Brazil.⁷⁰ The incentives available are similar to those offered by SUDAM.⁷¹

As regards the sectorial incentives: SUDEPE is the body in charge of orienting and implementing the fishing development policy,⁷² IBDF is responsible for the forestation and reforestation policy; EMBRATUR is in charge of formulating, coordinating and directing the Brazilian tourism policy,⁷³ EMBRAER has the objective to further and develop the aviation industry by investing the funds at its disposal for designing and building its own aircrafts;⁷⁴ and GEIMI is a body created to further the exploitation of the country's mineral resources, to provide for the substitution of mineral imports, and to encourage the exportation of mineral products.⁷⁵ The incentives available consist basically of tax reduction or exemption, as well as contribution of the corresponding sections of the incentive funds as non-voting equity capital.

The concession of any sectorial or regional incentives depends on the presentation and approval of projects by the appropriate authorities. It should be mentioned that it may occur that a given project is included in an area or sector which could enjoy the benefits granted through more than one of the sectorial or regional bodies and, in this case, all the tax incentives granted for the applicable programs would be available to that given project.

The policies on industrial development and related matters are CDI's duties. This body is responsible for conducting the industrial development policy of the country under the guidance and direction of the Minister of Industry and Commerce. For such purpose, CDI establishes the programs and conditions for the implementation of its policy and provides for the regional plans to be compatible with the national policies of industrial development.⁷⁶

The industrial projects submitted to CDI are analyzed and appraised by the Sectorial Groups, which prepare a technical opinion on each project to be examined by the Executive Secretary of CDI and, subsequently,

⁷⁰ See SUDENE, Law No. 3.692 of Dec. 15, 1959, arts. 3, 4 & 6, [1959] 23 *Coletanea* 567 (Braz.). See also Decree 52,346 of Aug. 12, 1963, [1963] 27 *Coletanea* 923 (Braz.).

⁷¹ This is generally so, except for the equity funds, which are: North-East Research and Natural Resources Fund (FURENE) as created by Law No. 5.508 of Oct. 11, 1968, art. 8, [1968] 7 & 8 *Coleção* 104 (Braz.), and the North-East Investment Fund (FINOR), as created by Decree No. 64,214 of Mar. 18, 1969, arts. 1 & 3, [1969] 33 *Coletanea* 315 (Braz.).

⁷² See Decree-Law No. 221 of Feb. 28, 1967, [1967] 1 *Coleção* 310 (Braz.), as amended by Decree-Law No. 1.217 of May 9, 1972, [1972] 36 *Coletanea* 780 (Braz.), and Decree-Law No. 1.594 Dec. 22, 1977, [1977] 41 *Coletanea* 1029 (Braz.).

⁷³ See Decree-Law No. 55 of Nov. 18, 1966, [1966] 7 *Coleção* 101 (Braz.).

⁷⁴ See Decree-Law No. 770 of Aug. 19, 1969, [1969] 5 *Coleção* 130 (Braz.).

⁷⁵ See Decree No. 62,352 of Mar. 5, 1968, [1968] 1 & 2 *Coleção* 461 (Braz.).

⁷⁶ See Decree No. 81.651 of May 11, 1978, arts. 1 & 3, [1978] 42 *Coletanea* 368 (Braz.).

to be submitted for final decision to the Minister of Industry and Commerce. The Sectorial Groups are also responsible for following up and controlling the implementation of the industrial projects approved by the Minister of Industry and Commerce and for analysing the fields of business affected by the project's activities, suggesting, where appropriate, changes in the economic policy instruments.⁷⁷

The incentives in favor of industrial development projects are: (1) exemption from import duties for equipment, machinery, devices and instruments, accessories and tools, not produced in the country, and for parts which supplement national production; (2) exemption from the Tax on Industrialized Products (IPI) for the goods mentioned above; (3) credit of the IPI tax amount for the purchaser of domestically manufactured equipment; (4) accelerated depreciation on nationally-produced goods, for purposes of assessing income tax; and (5) preferred financial support from official credit entities.

The incentives referred to in items (1) and (2) are reserved for projects of relevant national interest approved by the President of the Republic. For other projects CDI is authorized to grant only reductions of import duties and the IPI tax, at rates varying from 50 to 80 percent.⁷⁸

Products imported with import duty exemption are also entitled to exemption from the Tax on the Circulation of Goods (ICM). This exemption represents an additional incentive. It is important to note, however, that in the case of a mere import duty reduction, ICM tax will be fully due.⁷⁹

As regards the importation of supplementary parts, benefits may be granted in consideration of the respective nationalization programs (in the sense that it is the Brazilian Government's intention to have as many products locally produced as possible). The enjoyment of the incentive benefits is thus subject to compliance with pre-established nationalization indices.⁸⁰

There are other requirements to be met by companies interested in obtaining incentives. The industrial projects must: be destined to replace imports; be committed to export objectives in the appropriate sectors which have an existing availability; contribute to industrial decentralization or reduction of regional imbalances; be supported by an adequate

⁷⁷ *Id.* art. 8.

⁷⁸ See Decree No. 77.065 of Jan. 20, 1976, [1976] 40 *Coletanea* 82 (Braz.).

⁷⁹ See Decree-Law No. 406 of Dec. 31, 1968, art. 1, §4, para. VI, [1968] 32 *Coletanea* 1550 (Braz.).

⁸⁰ See, e.g., Resolution No. 5-71 of July 7, 1971, [1971] D.O.U. (CDI) (Braz.) which requires a 75 percent national content for teleprinting machines. See also Portaria No. 28-71 of July 19, 1971, [1971] D.O.U. (MCI) (Braz.), which requires 75 percent national content for motor excavator carriers. There are several D.O.U. Portarias setting national content percentages for different products.

financial structure as regards its own capital in relation to third party capital; have sufficient fixed and working capital to meet the specific conditions of the undertaking; provide for a more intense use of national resources; provide for the adoption of technological processes suitable for sectorial and regional development; be compatible with the maintenance of competitive costs; and, satisfy anti-pollution criteria.⁸¹

Industrial incentive legislation makes no distinction between national industries and foreign-controlled industries as regards the enjoyment of incentive benefits. A multitude of projects controlled by foreign groups have been approved. CDI has established a further condition for the granting of tax incentives to Brazilian companies, namely, that they commit themselves not to make any changes in their share control without first obtaining the consent of CDI. Any breach of this commitment would result in the loss of the benefits received. This rule is intended to avoid the transfer of national companies which have received CDI incentives to foreign groups. This condition has also been applied in the case of official financing, particularly when granted by the National Bank of Economic Development (BNDE).

Independent of CDI's incentives, the Minister of Finance is authorized to grant to industrial establishments the right to an IPI tax credit on nationally produced machinery, devices and equipment intended for installation, modernization and expansion and for incorporation into the fixed assets of the favored companies.⁸² The machinery, devices and equipment enjoying this benefit also enjoy exemption from ICM tax.⁸³ The enjoyment of these benefits does not require approval of the projects but is automatically granted if the products acquired are eligible for such benefits.

The Commission for the Concession of Tax Benefits to Special Export Programs (BEFIEEX) is responsible for the granting of incentives for the exportation of manufactured products.⁸⁴ The incentives for export consist of the following: (1) a 70 to 90 percent reduction of import duties and IPI tax on the importation of the machinery, equipment, devices, instruments, accessories and tools required to implement the program;⁸⁵ (2) a 50 percent reduction of import duties and IPI tax on the importation of the raw materials, components and intermediary products relating to the

⁸¹ See Resolution No. 35 of Dec. 12, 1974, [1974] D.O.U. (MIC) (Braz.).

⁸² See Decree-Law No. 1.136 of Dec. 7, 1970, [1970] 7 & 8 Coleção 16 (Braz.).

⁸³ See Convention AE-08/74, entered into by the Secretaries of Finance of all the Brazilian States, including the Federal District, on Dec. 11, 1974, [1974] Convênio AE-8/74 (Braz.).

⁸⁴ See Decree-Law No. 1.219 of May 15, 1972, [1972] 36 Coletanea 798 (Braz.).

⁸⁵ *Id.* at art. 1, §2, para. 1. See also Decree No. 77.065 of Jan. 20, 1976, art. 5, [1976] 40 Coletanea 82 (Braz.).

Program,⁸⁶ and (3) the deduction from the taxable profit of the portion of profit represented by exports of manufactured products.⁸⁷ These benefits may not be enjoyed cumulatively with other tax incentives provided for in current law.⁸⁸ Full import duty and IPI tax exemption may be granted for programs which have also been approved by the President of the Republic upon being deemed to be of relevant economic interest to the country.

Obtaining these benefits requires the interested company to sign an export program with BEFIEX, where the export commitment assumed by the company and the benefits to be received in exchange will be established.⁸⁹ The exports are determined on the basis of the net amount of average yearly exports. This is the FOB value of the total exports of manufactured products, less the value of any components exported by the exporter under any special ruling and incorporated into the exported manufactured products, divided by the years of duration of the programs. The value of the goods imported in each year with these exemptions may not exceed one-third of the net value of the average yearly exports of manufactured products.⁹⁰ Export programs have been signed for 10 year periods and their total value is normally around US\$ 400,000,000, although one of the latest approved programs provides for an export commitment in an amount exceeding US\$ 1,500,000,000. There are also programs for small and medium industries, establishing export commitments for substantially lesser amounts. Experience has shown that only major companies, nearly always large international companies, have assumed the risk involved in signing a Special Export Commitment. As a result, the news has spread that the ruling may be broadened to permit export commitments for only five years, allowing smaller national companies to have access to these incentives.

The benefits granted by the Commission of Export Incentives (CIEIX)⁹¹ are destined for medium-sized companies and consist basically of reductions of up to 90 percent of the IPI tax and import duty of the

⁸⁶ See Decree-Law No. 1.219 of May 15, 1972, art. 10, [1972] 36 Coletanea 798 (Braz.).

⁸⁷ *Id.* at art. 15.

⁸⁸ See Decree-Law No. 1.328 of May 20, 1974, art. 1, §2, [1974] 38 Coletanea 757 (Braz.).

⁸⁹ Failure to carry out the export commitment subjects the participant companies to the payment of the taxes from which they were exempted, or which would otherwise be due, with monetary correction and a fine of up to 50 percent. See Decree-Law No. 1.219 of May 15, 1972, art. 4, [1972] 36 Coletanea 798 (Braz.).

⁹⁰ *Id.* art. 3.

⁹¹ This Commission was created by Portaria No. 100, of Mar. 26, 1976, [1976] D.O.U. (MF) (Braz.). Its main objectives are to establish the rules for concession of tax incentives to exports and the examination of Export Programs, submitting its opinion to the decision of the Ministry of Finance.

machinery and equipment destined for installation, expansion or modernization of the companies which have export programs approved by CIEX,⁹³ and also reduction of or exemption from the income tax due on given operations practiced by said companies.⁹³ Since March 31, 1980, CIEX's duties have been performed by BEFIEIX.⁹⁴ The draw-back system consists of the exemption, restitution or suspension, as the case may be, of import duties, IPI, ICM and other taxes assessed at the time of importation of an item that is to be subsequently industrialized and incorporated in any equipment, machinery or product to be then exported. Draw-back benefits do not require any prior export program to be approved by governmental bodies.⁹⁵

The Export Financing Fund (FINEX) was created to supply funds for Banco do Brasil S.A. to carry out, through its Foreign Trade Department (CACEX), the financing of the export and of the export production of industrial companies that want to begin or increase foreign sales of their products.⁹⁶ According to current regulations, CACEX can use FINEX funds to extend financing to Brazilian exporters; to foreign importers (directly or through foreign financing institutions), but limited to the amount of the payments made to the Brazilian exporter; to companies or institutions abroad that order or carry out jobs and services, with regard to local expenses; or to refinance financing extended by authorized banks. In addition, the Central Bank of Brazil authorized the use of FINEX funds to equalize the rates of export financing extended by accredited Brazilian banks with their own funds or with foreign lines of credit. The purpose of this equalization is to adjust Brazilian rates to the rates for equivalent operations in the international market.⁹⁷

The National Bank of Economic Development (BNDE) is a public company with the basic objective of covering the financing requirements of private and public companies so as to further the economic development of the country.⁹⁸ BNDE financing is granted either directly or

⁹³ See Decree-Law No. 491, of Mar. 5, 1969, art. 13, [1969] 33 Coletanea 252 (Braz.), as amended by Decree-Law No. 1.428 of Dec. 2, 1975, art. 9, [1975] 39 Coletanea 740 (Braz.).

⁹⁴ Decree-Law No. 1.658 of Jan. 24, 1979, [1979] 43 Coletanea 35 (Braz.), extinguished the incentives granted by Decree-Law No. 491 of Mar. 5, 1969, art. 1, [1969] 33 Coletanea 252 (Braz.), which consisted of the credit on taxes paid in connection with products exported by Brazilian companies. This extinction will be gradually made (30 percent in 1979, 20 percent in 1980, 20 percent in 1981, 20 percent in 1982 and 10 percent in June 30, 1983).

⁹⁵ See Portaria No. 016 of Jan. 10, 1980, [1980] D.O.U. (MF) (Braz.).

⁹⁶ See Decree-Law No. 37 of Nov. 18, 1966, as amended by Decree No. 68.904 of July 12, 1971, [1971] 66 Coleção 71 (Braz.).

⁹⁷ See Law No. 5.025 of June 10, 1966, art. 60, [1966] 30 Coletanea 846 (Braz.).

⁹⁸ See Resolution No. 509 of Jan. 24, 1979, [1979] D.O.U. (MF) (Braz.).

⁹⁹ See BNDE, Law No. 1.628 of June 20, 1952, [1952] 16 Coletanea 165 (Braz.); as amended by Law No. 5.662 of June 21, 1971, [1971] 35 Coletanea 877 (Braz.). BNDE is subordinate to the Secretariat of Planning of the Presidency of the Republic.

through previously accredited Financial Agents. BNDE also engages in operations for the rendering of guarantees, corporate participation, underwriting operations and the rendering of guarantees to winners of international bids.⁹⁹

The priority programs of BNDE are: basic inputs (raw material and basic products); basic equipment; operations with agents; modernization of companies; infra-structure; and, technological development. The Basic Input Program is intended to meet the domestic demand for raw materials and basic industrial inputs in order to diminish the importation of these products. The Program is available to mining, steel, non-ferrous metals, chemical and petrochemical, fertilizer, cellulose and paper and cement industries. The Basic Equipment Program has the objective of expediting the development of this sector in order to improve the balance of payments of the country and permit the development of heavy equipment technology, thus consolidating the infra-structure of the national production industry.

The Joint Operations Program (POC) is an incentive for the economic development of the country by strengthening private national enterprises, particularly small and medium-sized companies. The Industry Modernization and Recovery Fund is a sub-program organized to re-equip private national companies with funds derived from the Industry Modernization and Recovery Fund (FMRI).¹⁰⁰ Through the Infra-structure Program BNDE gives governmental assistance in infra-structure projects for the improvement of the economy. The two priority sectors are railways and highways. Under the Technological Development Program BNDE offers highly subsidized financing (without monetary correction) to induce companies to invest in research and development projects. This financing is available to universities and research institutions for joint projects with private companies. Among the non-priority programs of BNDE are two programs organized to encourage the capitalization of private national enterprises: PROCAP and FINAC. The Special Program of Support for the Capitalization of National Private Enterprises (PRO-CAP) favors the capitalization of mainly small and medium-sized companies through the capital market. The Program is implemented through investment banks. PROCAP funds are intended to permit a Brazilian shareholder to pay only part of share issues under a guarantee given by the investment bank that carried out the operation. The financing limit is 50 percent of the value of the securities which have to be registered with

⁹⁹ BNDE prepared several pamphlets which present a summary of each of its operational methods. The pamphlets are available at BNDE and were used in composing this study.

¹⁰⁰ The FMRI is an accounting fund, created within BNDE by Decree No. 67.323 of Oct. 2, 1970, [1970] 34 *Coletanea* 901 (Braz.).

the Central Bank of Brazil.

The Program of Shareholder Operations and Financing (FINAC) is intended to support the capitalization of mainly small and medium-sized companies by extending financing to the shareholders for investment in their own companies. This Program is to be implemented through development banks which, in the opinion of BNDE, have a closer relationship with small and medium-sized companies. All these financings are subsidized, i.e.: charged at lower rates, which vary in accordance with the program adopted, plus indexation. They are not available to foreign controlled companies.

The Financing Fund for the Acquisition of Industrial Machinery and Equipment (FINAME) is a public company in charge of financing operations for purchase and sale, including exportation, of nationally produced machinery and equipment and of importation of supplementary parts and components. Its funds are held by BNDE. The FINAME fund is managed by the Special Industrial Financing Agency (FINAME), this Agency and the Fund having the same name.¹⁰¹ The operations of the FINAME Agency are carried out through previously authorized public and private financial agents, namely: regional and state development banks, commercial banks, investment banks and financing companies. The FINAME Agency establishes the criteria to be adopted in the operations it supports, including criteria with regard to the cost of the operations. This cost is represented by interest charged at more favorable rates, monetary correction and the remuneration of the agent.

There are four kinds of operations: (1) a Small and Medium-Sized Company Program; (2) a Long Term Program; (3) a Special Program; and (4) a Component Importation Financing Program.¹⁰² The Small and Medium-Sized Company Program favors machine and equipment purchases made by small and medium-sized Brazilian companies which are controlled by national capital and which engage in predominantly industrial activities. This program is available only for machinery and equipment manufactured in Brazil with a national content of more than 80 percent or with a progressive nationalization program approved by CDI. The Long Term Program benefits Brazilian companies controlled by national capital which use, lease, or manufacture the machinery and equipment to be financed. This program may favor machinery and equipment produced

¹⁰¹ The FINAME Agency was created to serve as the financing fund of BNDE, by Decree No. 55.275 of Dec. 22, 1964. FINAME was later transformed into an autonomous body, see Decree No. 59.170 of Sept. 2, 1966, [1966] 30 Coletanea 1241 (Braz.). Under Decree-Law No. 45 of Nov. 18, 1966, [1966] 7 Coleção 92 (Braz.) FINAME was allowed to transform into a mixed-economy company. The transformation into a public company soon followed, see Law No. 5.662 of June 21, 1971, art. 10, [1971] 35 Coletanea 877 (Braz.).

¹⁰² The Programs are regulated by Circulars issued by the FINAME Agency; copies can be obtained at BNDE.

in Brazil with a national content of at least 80 percent or a progressive national plan approved by CDI, when basically intended for the activities which FINAME deems to have priority.

The operational system of the Special Program was established to benefit Brazilian companies controlled by national capital, which use or manufacture the machinery and equipment to be financed. This program is available for machinery and equipment produced in Brazil which meet one of the following conditions: they are produced to order and represent a relevant technological innovation or greater national content of value and weight, compared to those already manufactured in the country; they compete with similar imported products in the international market; they are produced to order and require special drawings for their design; or, they are intended for projects of relevant interest to the national economy. Under this Program the FINAME Agency finances the total value of the machinery and equipment having a national content of 80 percent or finances 80 percent when the national content is 60 to 80 percent.

The Component Importation Financing Program benefits companies which manufacture capital goods. This program is available for supplementary parts and components which are: covered by financing already contracted between the FINAME Agency and the credit institutions of the country of origin; which are not produced in the country; which are intended for incorporation into machinery and equipment to be produced by the capital good manufacturers; and the importation of which is given priority by the FINAME Agency. Under this program the FINAME Agency finances 85 percent of the FOB import value.

EMBramec, FIBASE and IBRASA are BNDE subsidiaries and were incorporated in 1974 in order to support national industries in their expansion plans. These subsidiaries provide risk capital to companies by means of a minority participation in the subscription of shares or convertible debentures. Their participation is added to that of national entrepreneurs for determining the nationality of the control of a company. It is thus possible for a Brazilian group to improve the proportion of its own capital to third party capital under actual national control. The equity investments are made after an examination of a project submitted by the interested company. The examination is based on internal criteria. Foreign groups may participate in the companies receiving such equity investments, although only in a minority position.

It becomes obvious, at this stage, that tax and other incentives have become paramount for the organized development of Brazil's economic life. But the imbalances caused by incentives are making themselves felt: incentive is another name for subsidy, and any subsidy given by a country has to be paid for by its inhabitants through more taxes. And the tax burden in Brazil is becoming so high, even if compared to other more advanced industrialized nations, that it will somehow have to be relieved.

A public airing of this concern has been evident in the Brazilian press which indicates that some changes in this area are likely to occur.

