

Considerations in Establishing and Operating a Brazilian Subsidiary

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It is no surprise that foreign investment interest in Brazil has increased recently. The country's booming economy has justified the legal and regulatory hurdles foreign companies and individuals face in order to enjoy the benefits from the world's eighth largest economy.

There are many reasons for overcoming the obstacles to establish a presence in Brazil. First, obtaining a loan in Brazil as a foreign entity is not that attractive: higher interest rates and stringent collateral requirements. But, state-owned BNDES (*Banco Nacional de Desenvolvimento* – National Bank of Development) makes loans more attractive to a Brazilian subsidiary by offering lower borrowing costs. Second, by being physically present in Brazil, the company will be in tune with Brazil's culture in which personal relationships are critical for a successful business relationship. Lastly, Brazil's policies regarding its market are still rather protectionist, limiting certain sectors only to Brazilian companies.

In establishing and operating a subsidiary in Brazil, certain basic procedures and regulations must not be ignored. How to make the foreign investment, which type of business entity the subsidiary should choose, and compliance with labor laws are a few of the aspects to be considered when doing business through a Brazilian subsidiary.

Making a Foreign Investment in Brazil

The *Banco Central do Brasil* (Central Bank of Brazil), or BACEN, oversees foreign capital movements to and from Brazil and sets rules and regulations for registering investments, among other activities related to foreign investment. In order for profits from a Brazilian subsidiary to be remitted back to a foreign investor, the Brazilian subsidiary must purchase the foreign currency by presenting certain documentation such as proof of tax payment and the mandatory registration with the BACEN.

The mandatory registration includes the sum of the original investment, any additional investments made, plus profit reinvestments in the subsidiary. The total amount registered serves as the basis for the calculation of capital gains and any repatriation of capital. Amounts, that exceed what was registered, sought to be remitted abroad are treated as capital gains and subject to a 15% withholding tax (or higher if the foreign investor resides in a tax haven) and approval by the BACEN.

As mentioned above, certain segments of the Brazilian market are restricted, which impacts where foreign investments can be made. These restricted segments include purchase of rural land, telecommunications, banking and insurance, with each having a different type of restriction on foreign capital ranging from percentage ownership limitation to outright prohibition.

Choosing the Right Business Entity for Your Subsidiary

The Brazilian laws recognize more than nine different types of business entities. Companies choosing to open a Brazilian subsidiary must carefully plan its operations in Brazil to choose the most adequate corporate structure for its business.

The two most popular business forms in Brazil are the *Sociedade Anônima* (S.A.) and the *Sociedade Limitada*, or simply *Limitada*. The latter recently dispensed with the two partners minimum requirement and is similar to the American Limited Liability Company. Any amendment to its articles must be approved by a 75% majority, so this form may be desirable for foreign companies choosing to establish a wholly owned subsidiary.

The S.A. is close in structure to the American corporation and therefore optimal for situations in which multiple groups will have a stake in the Brazilian entity. This type of business structure is mandatory if the Brazilian entity intends to be publicly held.

Registration Requirements: Federal, State, and Local

After the foreign capital is properly registered in Brazil and all individuals involved have agreed on the type of business entity, it is time to file with the proper authorities. The process usually begins at the state level by registering with the *Junta Comercial* (Commercial Agency) or through the *Cartório de Registro da Pessoa Jurídica* (Legal Entity Registry Agency). This registration is tantamount to the birth of the company—it begins to officially exist.

The *Contrato Social*, the equivalent to the Articles of Incorporation, is the most important document and is required, among other documents related to the individuals involved in the venture, to validly register the business. Once registered, the company will be issued an identification number, *Número de Identificação do Registro de Empresa* (NIRE), which is affixed to the company's instituting documentation.

With the NIRE in hand, the next step is to register with the *Receita Federal* (Federal Revenue) to receive the CNPJ (*Cadastro Nacional de Pessoa Jurídica* – National Registry of Legal Entities), which is done exclusively online by downloading a software application from its website. The business will be required to disclose its intended activities for taxation purposes as well as for future regulatory inspections of the business. Next, the business will need to obtain its operating permit (*Alvará de funcionamento*) from the local agency. This permit is mandatory for all business types, whether it is a commercial, industrial, agricultural or service provider.

An additional registration at the state level is also required before operations can begin what is necessary for the business to receive its ICMS (*Imposto sobre Circulação de Mercadorias e Serviços* – Assessment on the Circulation of Merchandise and Services). Although most states currently permit that this registration to be done simultaneously with the CNPJ registration, some do not.

Labor Requirements – A Brief Summary

After all of the capitalization and business registration matters have been resolved, the enterprise should be ready to hire and begin operating in Brazil. In hiring and dealing with employees, beware. Labor laws in Brazil are rather complex, guaranteeing employees certain rights, much greater than the ones enjoyed in the United States.

A few examples of different laws include: the imposition of a legal limit of 44 regular working hours per week or 8 hours a day (per the Brazilian Constitution); entitlement to a minimum vacation time and pay upon completion of each 12 months of work; entitlement to an annual gratification, or the 13th salary, as it is popularly known; and entitlement to overtime pay of at least 50% of the hourly rate, among other rights. In labor litigation, employees usually win.

Conclusion

Establishing a Brazilian subsidiary can bring great advantages to foreign companies and investors, and although many would like to grab a slice of the booming Brazilian economy, the regulatory hurdles are many. For a successful registration, establishment and operation of Brazilian subsidiary, do not move forward without consulting with an attorney knowledgeable in the process and the culture to bring you the most benefit in your ventures in Brazil.

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