



ICLG

The International Comparative Legal Guide to:

Lending and Secured Finance 2013

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A practical cross-border insight into lending and secured finance

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in Brazil?

Long-term financings in Brazil are funded almost exclusively by State-owned financial institutions (BNDES, Banco do Brasil and Caixa Econômica Federal). Brazilian financial institutions of the private sector, in turn, concentrate their lending activities typically on short and mid-term loans and financings to individuals or corporate entities, or to the on-lending of governmental lines of credit.

Foreign loans tend to benefit from lower interest rates if compared to the domestic rates; however, the overvaluation of the Brazilian currency and a financial tax of 6% on the principal of short-term loans (currently up to 360 days) remitted to Brazil make international financings less attractive.

1.2 What are some significant lending transactions that have taken place in Brazil in recent years?

Some significant transaction are:

The financing of the large hydropower projects Belo Monte, Jirau and Santo Antonio.

The financing of civil works and infrastructure in connection with the 2014 World Cup and the 2016 Olympic Games.

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Yes, it can.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

Yes. Directors may be held liable if they cause the company to engage in transactions that do not benefit the company.

The disregard of legal entity doctrine can be applied, thus causing the shareholders and/or managers to be liable for the company's obligation, if they cause the company to engage in transactions that do not fall within the company's purposes.

If the guarantor is declared bankrupt, guarantees or security granted within a two-year period before the bankruptcy for no consideration to the guaranteeing/securing company are deemed as void in the bankruptcy proceeding.

2.3 Is lack of corporate power an issue?

Yes. Agreements are not binding on the company if executed by individuals that are not duly empowered to act on behalf of the company.

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

No governmental consent is required, except in the case of companies that operate in certain regulated sectors.

Shareholder and/or board approvals may be required depending on the terms of the guarantor's organisational documents.

If the guarantee is issued outside Brazil, (i) the guarantee must have its signatures authenticated by a public notary in the place of signing, (ii) the notary's signature must be authenticated at the nearest Brazilian Consulate, and (iii) the guarantee must be filed (along with a sworn translation, if the guarantee is not in Portuguese) with a Registrar of Deeds and Documents in order to be enforceable in Brazil.

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

There is no net worth limitation. As for solvency, please refer to the last part of question 2.2.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

The Central Bank of Brazil may impose restrictions on the remittance of funds outside Brazil, but currently no restrictions exist for remittance of proceeds from enforcement of a guarantee.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

The types of collateral are a pledge (*penhor*), mortgage (*hipoteca*) and fiduciary transfer (*alienação fiduciária em garantia*). A fiduciary transfer may not be suitable to secure obligations in favour of non-Brazilian entities in certain cases.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

A single agreement can cover several kinds of assets, but the assets over which security is to be created must be specified in the agreement. It is not possible to create security over assets in general without specifying them.

The procedures for the different kinds of assets are described below.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes, it can.

Security over real property and plant can be taken either by mortgage or by fiduciary transfer. Security over machinery and equipment can be taken either by pledge or by fiduciary transfer.

Mortgage over property with an individual value of approximately US\$10,000 or higher must be taken by a public deed made by a notary. Fiduciary transfer and pledge can be taken by a private instrument.

Basically, the public or private security instrument must describe the parties thereto, the secured obligation and the assets over which security is created. If the instrument is executed outside Brazil, it must comply with the requirements described in question 2.4 above.

The public deed and the private instrument must be filed with the Real Estate Public Registry of the places in which the assets are located as a condition for perfection of the lien.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. Security can be taken by a private instrument of pledge or fiduciary transfer. Basically, such instrument must describe the parties, the secured obligation and the assets over which security is created. If executed outside Brazil, it must comply with the requirements described in question 2.4 above. Whether executed in Brazil or abroad, the instrument must be filed with a Registry of Deeds and Documents in the places in which the Brazilian parties are located as a perfection condition of the lien.

The debtors must be notified in order for the security to be enforceable against them.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. The procedure is the same as described in question 3.4, including the need for a notice to the depository bank.

3.6 Can collateral security be taken over shares in companies incorporated in Brazil? Are the shares in certificated form? Can such security validly be granted under a New York or English law governed document? Briefly, what is the procedure?

Yes. In practice there are no shares in certificated form. Brazilian conflict of law rules require a Brazilian law governed document.

The procedure is the same as described in question 3.4 above. Additionally, in the case of Brazilian corporations, the lien must be recorded in the company's books or in the books of the financial institution in which the shares are recorded in book-entry form, as applicable.

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. The procedure is the same as described in question 3.3 for security over machinery and equipment.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes, it can.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

There are fees for notarisation of signatures, consularisation, sworn translation (if the security document is not in Portuguese) and registration. For public deeds, there are notary fees. The amount of fees is determined by the relevant Brazilian State, except fees for (i) notarisation outside Brazil, which are determined by the relevant jurisdiction, and (ii) consularisation, which are determined by the Brazilian Foreign Affairs Ministry.

Registration fees are related to the amount of the secured obligation, subject to a cap.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Registration of security with the Registry of Real Estate can be significantly expensive and time-consuming. In the State of São Paulo, for example, fees for a single registration can be as high as *ca.* US\$56,000.

Registration with the Registry of Deeds and Documents is less bureaucratic and less expensive. In the State of São Paulo, for example, the cap for a single registration is *ca.* US\$6,000.

The fees are multiplied by the number of places in which the document must be filed.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Generally speaking, no. There may be exceptions depending on the

particular case, e.g. security over shares of companies in regulated sectors may be subject to authorisation of the relevant authority.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

No, there are not.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

The legalisation requirements have been described above.

As a general rule, contracts executed in Brazil must be witnessed by two witnesses in order to be entitled to a more expedite foreclosure proceeding.

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; (c) or shares in a sister subsidiary?

(a) Shares of the company

No, there are not.

(b) Shares of any company which directly or indirectly owns shares in the company

No, there are not.

(c) Shares in a sister subsidiary

No, there are not.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will Brazil recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. However, please note that whilst an agent or trustee can act on behalf of the lenders to enforce the loan, the guarantees and security (provided that the supporting documentation grants the agent or trustee sufficient powers to so act), the guarantee and security must be created in favour of the lenders themselves, not in favour of the agent or trustee.

5.2 If an agent or trustee is not recognised in Brazil, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

This is not applicable in Brazil.

5.3 Assume a loan is made to a company organised under the laws of Brazil and guaranteed by a guarantor organised under the laws of Brazil. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

The assignment or transfer agreement must comply with applicable requirements for its enforceability in Brazil, which in the case of foreign documents are notarisation, consularisation, translation and registration.

If Lender A and/or Lender B are outside Brazil, the transfer must comply with applicable foreign exchange regulation, including registration with the Central Bank of Brazil.

6 Withholding, Stamp and other Taxes; Notarial and other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Yes, these transactions may be subject to withholding income tax.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders? What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Foreign lenders may be entitled to reductions on the withholding income tax rate (such as the exemption on interest paid to non-resident investors according to Law No. 12,431, of June 24, 2011). Taxes are not levied in Brazil for the purposes of effectiveness or registration of transactions. Taxes are mostly levied on income. Certain taxes are also levied on financial transactions (e.g., on foreign exchange transactions, or on transactions related to the holding of securities).

6.3 Will any income of a foreign lender become taxable in Brazil solely because of a loan to or guarantee and/or grant of security from a company in Brazil?

Yes. Payment of interest, fees and other charges made by a Brazilian payor (either as principal obligor or as guarantor) to a foreign lender may be subject to Brazilian withholding income tax.

6.4 Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

Yes. Registration costs can be significant – please refer to question 3.10 above.

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

Brazilian companies borrowing funds from abroad may be subject in certain circumstances to thin capitalisation and transfer pricing

rules – for instance, when funds are borrowed from a foreign related party or from a company located in a tax haven jurisdiction.

7 Judicial Enforcement

7.1 Will the courts in Brazil recognise a governing law in a contract that is the law of another jurisdiction (a “foreign governing law”)? Will courts in Brazil enforce a contract that has a foreign governing law?

A foreign governing law shall be recognised by Brazilian courts, and Brazilian courts shall enforce a contract that has a foreign governing law, provided that (i) such law is the applicable law pursuant to Brazilian conflict of law rules, and (ii) the foreign governing law is not against Brazilian national sovereignty, public policy or morality.

Regarding (i), pursuant to Brazilian conflict of law rules, the governing law of obligations is the law of the jurisdiction in which the obligation has been created. In the case of contractual obligation, this is typically the law of the place of signing.

7.2 Will the courts in Brazil recognise and enforce a judgment given against a company in New York courts or English courts (a “foreign judgment”) without re-examination of the merits of the case?

The foreign judgment will be enforceable in Brazil without re-examination of the merits if previously recognised by the Brazilian Superior Court of Justice, such recognition only occurring if: (a) the judgment fulfills all formalities required for its enforceability under the laws of the country where the same was issued; (b) the service of process instituted against a Brazilian resident party is effected in accordance with Brazilian law; (c) the judgment was issued by a competent court after due service of process upon the parties to the action; (d) the judgment is not subject to appeal; (e) the judgment was authenticated by a Brazilian consulate in the country where the same was issued and is accompanied by a sworn translation of the same into Portuguese; and (f) the judgment is not against Brazilian national sovereignty, public policy or morality.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in Brazil, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in Brazil against the assets of the company?

(a) An ordinary proceeding in a Brazilian State court, including obtaining and enforcing a judgment, takes typically from three (3) to six (6) years on average. This period may vary drastically depending on various factors, including the State in which the proceeding is conducted (the estimate made herein considers a proceeding in the courts of the State of São Paulo) and the applicable proceeding.

If, however, the credit is based on a contract or other instrument that fulfils the requirements for a fast-tracking proceeding (*processo de execução*), the creditor does not need to obtain a judgment before enforcing its rights. If this is the case, the enforcement can take between one (1) and six (6) months on average. Again, this period varies according to the Brazilian State and other factors.

(b) The recognition of a foreign judgment before the Brazilian Superior Court of Justice (question 7.2 above) takes typically from one (1) to two (2) years on average. After that, the creditor is entitled to a fast-tracking enforcement proceeding (*processo de execução*) as described in the second part of question 7.3(a) above.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction or (b) regulatory consents?

Generally speaking, certain Brazilian judges tend to construe the law in a manner that is more favourable to the borrower, particularly if the lender is a financial institution or a foreign entity. This state of mind, in addition to the various remedies available to the parties under Brazilian process laws, can turn the enforcement proceeding into a long journey.

A public auction is required for foreclosure of real estate, but a private auction is possible in relation to movable assets if so agreed in the security instrument. The seizure of assets that are not in the physical possession of the lender or its representative, however, is permitted only through a judicial proceeding. Regulatory consents may be required in certain regulated activities.

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in Brazil or (b) foreclosure on collateral security?

A plaintiff who is incorporated or resides outside Brazil and who does not own real property in Brazil must present guarantees (such as a deposit in a judicial escrow account or a performance bond) to the satisfaction of the court to guarantee the payment of the defendant’s legal fees and court expenses, with a few exceptions, which include the fast track procedure mentioned in question 7.3(a) above.

7.6 Do the bankruptcy, reorganisation or similar laws in Brazil provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes. Bankruptcy of the borrower or third party security provider stays the enforcement of individual claims, including individual enforcement of collateral security. The enforcement of claims against an entity under bankruptcy proceeding is conducted exclusively by the bankruptcy court, and creditors are paid according to their statutory ranking and the cash availability. Exception is made to certain types of collateral which are not subject to the stay order and can be enforced by the creditor even during the bankruptcy procedure.

7.7 Will the courts in Brazil recognise and enforce an arbitral award given against the company without re-examination of the merits?

Yes. In case of a foreign arbitral award, enforcement is subject to previous recognition by the Brazilian Superior Court of Justice, such recognition only occurring if the conditions described in question 7.2 are fulfilled. A foreign arbitral award is defined as an arbitral award issued outside Brazil, regardless of the seat of arbitration and applicable law.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

Please refer to question 7.6 above.

8.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g., tax debts, employees' claims) with respect to the security?

Yes. Secured credits are subordinated in a bankruptcy proceeding to: (i) certain so-called "out-of-bankruptcy credits", such as costs and expenses incurred during the bankruptcy proceeding and advances made by creditors to the bankruptcy estate; and (ii) labour credits limited to 150 minimum wages or approximately US\$50,000 per employee, and credits arising out of on-the-job accidents.

In addition, in limited cases, creditors have clawback rights in relation to monies or assets delivered to the debtor before the bankruptcy proceeding. These include creditors under export foreign exchange advances.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

As a general rule, the following entities are not subject to bankruptcy: (i) companies controlled by the Brazilian Federal government, by State governments or by Municipalities; (ii) financial institutions and other institutions subject to regulation by the Central Bank of Brazil (e.g. brokerage and dealership houses); (iii) private pension entities; (iv) insurance companies; (v) entities that operate private health plans; and (vi) special purpose companies dedicated to securitisation of real estate credits.

These entities are subject to non-judicial liquidation according to specific statutes, and some of them are subject to bankruptcy under certain circumstances only.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

No. The taking of physical possession of assets from the borrower or third party security provider in an enforcement is permitted only in a court proceeding.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of Brazil?

Yes, except if the proceeding relates to (i) real estate located in Brazil, or (ii) succession *causa mortis* with regard to assets of the deceased's estate located in Brazil, in which cases Brazilian courts shall have exclusive jurisdiction.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of Brazil?

Yes, it is.

10 Other Matters

10.1 Are there any eligibility requirements in Brazil for lenders to a company, e.g. that the lender must be a bank, or for the agent or security agent? Do lenders to a company in Brazil need to be licensed or authorised in Brazil or in their jurisdiction of incorporation?

Lenders do not need to be a bank or other licensed or authorised entity.

However, a lender must be a licensed Brazilian financial institution in order to grant loans on a financial basis, i.e. (i) with funds raised from third parties, (ii) regularly, and (iii) with profit purposes.

Additionally, loans granted by lenders that are not financial institutions are subject to interest limitation imposed by Brazilian anti-usury laws.

The need for a financial licence and the interest limitation referred to in the preceding paragraphs do not apply to foreign-law governed loans granted by lenders outside Brazil.

There are no requirements in Brazil for the agent or security agent. Please refer to question 5.1 regarding the agents' role.

10.2 Are there any other material considerations which should be taken into account by lenders when participating in financings in Brazil?

Loans granted by foreign lenders must be registered with the Central Bank of Brazil, such registration being a condition precedent for any remittance of principal, interest or other charges abroad. The Central Bank may refuse registration if the loan costs exceed then prevailing international market standards for loans of a similar nature.

Note

The information above is a general overview and not an exhaustive explanation on the matters discussed therein. Brazilian courts often decide based on non-statutory equity principles or extensive construction of rules and case-law, so actual court decisions different from the answers above cannot be excluded. The information above or any part thereof shall NOT be construed as legal advice with regard to any subject matter. Legal advice may be obtained from our firm's attorneys only in the context of an attorney-client relationship.

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Luiz Assis' practice is focused upon the structuring and negotiation of international lending and financial transactions. He has participated in innumerable foreign financing transactions involving capital markets financing (bonds, notes, commercial paper), syndicated loans, and structured finance. He has also negotiated many international aircraft leases and export finance contracts.

Further to his work in international lending and finance, Mr. Assis is also involved in banking and foreign exchange regulation and foreign investment matters. He also represents clients in administrative proceedings before the Central Bank of Brazil and the Appeals Council of the National Financial System.

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Our lawyers are known for their strong analytical skills, their creativity in devising legal solutions, and their team-based approach to serving clients. Levy & Salomão attorneys combine solid academic backgrounds with substantial experience not only in the practice of law, but also in finance, capital markets, international business and accounting, and in government.

The firm's banking and finance practice expertise includes structuring domestic and international lending agreements, including: syndicated loans and trade finance facilities; participating in debt renegotiations; advising on financial system and foreign exchange regulation; providing legal advice on foreign investment in Brazil and Brazilian investment abroad; aircraft leasing; and representing clients before the Brazilian Central Bank and the National Financial System Appeals Council.