

Client Alert
July 2017**Reform of the Brazilian Mining Sector – Key Aspects**

On 7/25/2017, President Michel Temer approved 3 Provisional Measures (PMs) to reform the Brazilian mining sector: (i) PM No. 789, which alters the regime of the Financial Compensation for Exploitation of Mineral Resources (*Compensação Financeira pela Exploração de Recursos Minerais* – CFEM); (ii) PM No. 790, which amends several provisions of Decree-Law No. 227, of 2/28/1967 (the so-called Brazilian Mining Code); and (iii) PM No. 791, which replaces the National Department of Mineral Production (*Departamento Nacional de Produção Mineral* - DNPM), with the newly formed Mining National Agency (*Agência Nacional de Mineração* - ANM) ¹.

The reform has a positive intent of modernizing the Brazilian mining legal framework, by establishing that reports on mineral research and the determination of reserves in mineral deposits shall comply with internationally adopted criteria, and by increasing the independence and supervision prerogatives of the Brazilian mining regulator, including with respect to compliance by the miner of environmental laws. On the other hand, the new PMs have the downside of increasing the tax burden and other costs applicable to mining activities. The key aspects of the Brazilian mining reform are set out below.

Mining Regimes

PM No. 790 has maintained the regimes set forth in the Brazilian Mining Code for the research and exploitation of mineral resources. The mining concession (*concessão de lavra*) is the regime applicable to the exploitation of most minerals in Brazil and is preceded by a research authorization (*autorização de pesquisa*)².

As a general rule, the party interested in exploiting mineral resources in Brazil will first apply to the ANM for a research authorization for a certain area and a given term. The ANM will deny or impose amendments to the application if the relevant area is already covered in whole or in part by existing mining rights. Once the interested party obtains the research authorization, performs the mineral research and obtains ANM approval of a final research report presented within the term of the research authorization demonstrating to ANM that the economic exploitation of the required mineral in the applicable area is viable, a mining concession may be requested to the Minister of Mines and Energy. The minimum term of the research authorization was increased from 1 to 2 years under the reform. Such term is extendable only once, upon demonstration to ANM that reasonable research has been performed in the applicable area³.

Mining concessions and research authorizations may be transferred to third parties upon consent of the Minister of Mines and Energy and the ANM, respectively. No transfer of mining rights can be authorized in case assignor or assignee has debts with the ANM that have been recorded as federal collectible debt (*dívida ativa*, i.e. debt that is not appealable before the administrative tax court and can be foreclosed on).

The relatively low barriers for private parties to commence mineral research is a positive aspect of the Brazilian mining framework, especially taking into account the substantial costs involved in mining research. Furthermore, the possibility of transfer of mining rights stimulates business in the sector.

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1. Such Provisional Measures must be approved, i.e. converted into law, by the two houses of Congress within 120 days of July 25, failing which the PMs will lose effectiveness retroactively to the date of their issuance.
2. The Brazilian Mining Code also sets forth the regimes of: (i) permission for independent mining (*permissão de lavra garimpeira*), applicable to individual independent miners; (ii) monopolization (*monopolização*), applicable to minerals under special regimes and exploitable solely by the Brazilian Federal Government; and (iii) licensing (*licenciamento*), applicable to the exploitation of sand, rocks and clay for immediate use in civil construction.
3. Previous legislation did not specify how many times a research authorization could be renewed. This was left to the interpretation of the former mining regulator..

Client Alert
July 2017

Another positive innovation of the reform is the possibility to extend the research authorization after the delivery to ANM of the final research report, which allows the owner of the mining right to refine knowledge of the mineral deposit in question.

Electronic Public Auctions

The mining reform also introduced a system to allow the continuation of mining activities in areas previously occupied by third party miners that lost their titles. The area considered free (*desonerada*) by a decision of ANM or of the Minister of Mines and Energy, or as a result of any other loss of the mining rights by the previous holder, shall become available for research or exploitation following electronic public auctions, in which the highest amount offered shall determine the winner. Such payment is one of the newly established sources of revenue for ANM. Failure to pay such amount subjects the highest bidder to a fine equivalent to 50% of the minimum price established by ANM, as well as temporary suspension of such party from any process of obtaining mining rights.

Mining Regulator Independence, Supervision Prerogatives and Applicable Penalties

The replacement of the DNPM with the ANM aims primarily to increase the independence and budget of the Brazilian mining regulator. The body will have a collegiate board (*diretoria colegiada*) formed by 5 members with fixed terms. Regulation proposals are to be discussed in public consultations, which shall enhance independence and transparency of the body. PM No. 791 brings an array of sources of funds for ANM, which seeks to resolve the historical underfunding of the regulator which affected its efficiency.

ANM may demand biannual reports on the progress of researches. All research reports shall follow international standards. Failure to report is subject to penalties.

Although such disclosure requirements may increase compliance costs, they will also work as a deterrent against parties who seek authorization and subsequently failing to perform research in the applicable area, thus obstructing the possibility of research by other parties. This has been a frequent issue in the Brazilian mining sector.

ANM is also to have a greater level of supervision over the environmental licensing procedure preceding the granting of the mining concession. The private party having requested a mining concession shall report to ANM every 6 months the status of the environmental licensing and evidence of compliance with requests of the relevant environmental authority, under penalty of denial of the mining concession.

The reform has increased the amounts of previously existing penalties for the breach of mining laws and regulations. Fines now vary from R\$2,000.00 to R\$30,000,000.00. Additional penalties have been included: (i) daily fines of R\$100.00 to R\$50,000.00; (ii) temporary suspension, in whole or in part, of mining activities; and (iii) seizure of minerals, assets and equipment, in addition to the cancellation of mining rights.

Tax Burden, TFAM and Other Costs

The reform seeks to increase the CFEM tax burden. CFEM is calculated based upon net sales (*faturamento líquido*) of mining products⁴, and the taxes levied upon such sale and expenses with insurance and transportation are deductible therefrom. In case PM No. 789 is timely approved by Congress, CFEM shall be due following the sale of mining products, based on the gross revenues (*receita bruta*) of such sales, maintaining the deductibility of the taxes levied thereupon⁵.

4. Pursuant to Law No. 7,990, dated 12/28/1989, and Law No. 8,001, dated 3/13/1990. Amendments to tax burdens set forth in PM No. 789 shall only become effective as from 1/1/2018, if it is timely converted into law.

5. Additionally, CFEM will be levied upon: (i) the consumption of mining products, based on the calculated revenue, considering the price of the product in the local market; (ii) exportation of mining products to legal entities based in tax havens, based on the calculated revenues, considering standards defined by the Brazilian Federal Revenue Secretariat; (iii) public auctions of mining products, as applicable, based on the price paid; and (iv) first acquisition of mining products extracted by independent miners (*garimpeiros*), based on the value of such acquisition.

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based on the gross revenues (*receita bruta*) of such sales; the deductibility of the taxes levied thereupon remains unchanged⁵.

PM No. 791 creates a Surveillance Charge for Mining Activities (*Taxa de Fiscalização de Atividades Minerárias* - TFAM). TFAM is payable for the inspection of mining activities by ANM and shall be charged once a year, until April 30, from the owners of mining rights under the regimes of research authorization, mining concession, licensing and independent mining.

Annual amounts of TFAM applicable to the regimes of research authorization, mining concession and licensing are as follows: (i) R\$2,000.00 per research authorization, between the date of its granting until the delivery of the final report; (ii) R\$1,000.00 per research authorization between the delivery of the final research report to ANM until the granting of the mining concession; (iii) R\$5,000.00 for each effective mining concession; and (iv) R\$3,000.00 for each licensing in force. Late payments of TFAM shall be punished by fines of 50%.

The assignee of a given mining right shall be jointly liable for any prior debts of CFEM and TFAM. This is to be taken into account in due diligence procedures for the acquisition of mining enterprises.

Other costs to which miners are subject will also be increased. Brazilian law sets forth that owners of lands where mining activities take place cannot oppose such activities by the holder of relevant mining rights, but are entitled to a portion of the results of the exploitation, corresponding to 50% of amounts paid as CFEM. With the increase of the CFEM, these amounts will also increase. This is without prejudice to other amounts due by miners to landowners, not revoked by the mining reform: (i) revenues for the occupation of the land – corresponding to the loss of revenues of the landowner due to the occupation of the area by mining activities, in whole or in part; and (ii) indemnification for damages caused by mining activities to the respective land.

Environmental Aspects

According to the new wording of Articles 7 and 47 of the Brazilian Mining Code, the closing of a mine is an integral part of mining activities and executing a mine closing plan adequately is a condition for the extinction of the mining concession. This includes the mitigation, to the furthest extent possible, of environmental impacts stemming from mining activities during and after the useful life of the mine. The performance of mining activities entails the liability of the miner for the environmental recovery of the affected areas.

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