

The background of the slide is a dark blue surface with several US one-dollar bills and one Brazilian Real bill scattered across it. The bills are slightly crumpled and overlapping. The text 'THE NEW FOREIGN EXCHANGE AND FOREIGN CAPITAL LAW' is centered in white, serif font. To the left of the text, there is a small decorative element consisting of three stacked blue squares of increasing size.

THE NEW FOREIGN EXCHANGE AND FOREIGN CAPITAL LAW



THE NEW FOREIGN EXCHANGE AND FOREIGN CAPITAL LAW

After more than two years running in the Brazilian Congress, at the end of last year Law No. 14,286 of December 29, 2021 was enacted to revamp, simplify, and consolidate the existing legislation regarding the Brazilian foreign exchange market, and the regulations applicable both to Brazilian capital investments abroad and to foreign capital investments in Brazil (the New Foreign Exchange Law).

This article provides a summary of the main aspects of said new legal framework, as well as provides some insights about the regulations to be implemented during 2022 by the National Monetary Council (CMN) and the Brazilian Central Bank (BCB).



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STATEMENT OF REASONS



Most of the Brazilian laws applicable to the foreign capital investments and the foreign exchange market were developed over periods of foreign currency shortages and restrictions on the country's balance of payments. Such laws were rigid and often provided for obsolete rules that intended to establish foreign exchange controls and price fixing; measures that are currently incompatible with the globalized economy focused on productive investment and free flow of capital .

Undeniable progress has been made in the last 20 years towards more flexibility in the flow of international funds, such as the consolidation of the free foreign exchange market in 2005, and the deletion in 2008 of the obligation for all the Brazilian exporters to transfer back to Brazil the foreign currency received from exportations (cobertura cambial). However, the more progressive new laws and regulations that were issued did not repealed completely the former laws. Accordingly, the foreign exchange legislation was disperse in dozens of legal instruments, some of them enacted more than 100 years ago, with repetitive provisions and, sometimes, conflicting with each other.

Such “patchwork” brought legal uncertainty and high regulatory costs to private players in the Brazilian foreign exchange market, resulting in expensive, bureaucratic products and bad experience for users. Moreover, as CMN and BCB cannot regulate beyond or against what is provided in federal laws, all such outdated legal framework operates as true legal ties, impeding the adoption of structural changes for the sector.

STRUCTURE OF THE NEW LEGAL FRAMEWORK

The New Foreign Exchange Law provides for a deep restructure because it definitely wipes out the ties that impeded the adoption of modern concepts compatible with the global guidelines recommended by the Organization for Economic Cooperation and Development (OECD) and by the Financial Action Task Force (FATF) against Money Laundering and Terrorism Financing, simultaneously providing simplicity and greater legal certainty.

The New Foreign Exchange Law achieves such goal by means of the following:

- The New Foreign Exchange Law revokes several dispersed, old and outdated laws, decrees and normative rules on the matter, such as Law No. 4,182 of 1920, which considered the “forex gambling” [jogo sobre câmbio] a crime. In other words, many of the expected benefits do not come from what the new legal framework brings but from what it excludes from the prior legal framework.



- The New Foreign Exchange Law consolidates the rules applicable to the Brazilian foreign exchange market and the regulations applicable to foreign capital investments into a single concise, simple, and principal normative instrument. The details will be set in the regulations to be enacted mainly by BCB, allowing that new changes, when necessary, are made quickly, technically and safely.

Therefore, the overall amendment will depend on the statutory changes to be made by monetary authorities. The agenda is in favor of free competition, and is modern, progressive and innovative. It is focused on flexibility and improvements but the changes will be implemented gradually and in a prudent form.



EFFECTIVENESS



The New Foreign Exchange Law will enter into force only at the end of 2022. During the period of time between the enactment and the entry into force of the law, BCB will review and enact the regulatory rules to adjust the current ones to the new legal framework. A number of public consultations and dialogues are expected between the regulator and the market. This matter should prevail over this year's agenda and it is important to be attentive to its developments.

GENERAL PRINCIPLES APPLICABLE TO THE FOREIGN EXCHANGE MARKET



The new legal framework consolidates, at the level of federal laws, several principles prevailing in the Brazilian foreign exchange market, in particular:

- Foreign exchange transactions may be held freely, without value limitation;
- Exchange rates are freely agreed upon;

- Foreign exchange transactions must be carried out through institutions authorized to operate in such market by BCB; and
- Such authorized institutions are responsible for identifying the customers and adopting controls to prevent wrongdoings, especially money laundering.



OPENING AND COMPETITION: NEW LICENSES AND NEW BUSINESS MODELS



The New Foreign Exchange Law increases the number of possible new institutions authorized to operate in the foreign exchange market, as well as it fosters new business models, enabling greater competition and efficiency in the sector. This is done in different forms.

On one hand, BCB received powers to establish different and proportional

requirements for the creation and operation of authorized institutions, or even to waive such authorization, considering the volume, nature, innovation capacity, risks and scope of the intended business model.

On the other hand, the new law provides that its legal framework will not apply to transactions involving the purchase and

sale of foreign currency in cash, in the amount of up to US\$ 500, carried out between individuals, on an occasional and non-professional basis. This means that transactions within this scope will not be deemed foreign exchange transactions and may be performed freely, paving the way for peer-to-peer currency exchange models, for example.

STREAMLINING AND BUREAUCRACY REDUCTION: FOREIGN EXCHANGE CONTRACTS AND REGISTRATION CODES



The benefits for companies and citizens is given, initially, with the reduction of bureaucracy, improvement of processes and reduction of costs involving foreign exchange or international transfers of capital.

The New Foreign Exchange Law repealed completely the rules that currently serve as basis for the entire foreign capital registration system (RDE-IED, RDE-ROF and RDE-Portfolio), as well as for the requirement of exchange contracts and

registration codes. At the same time, BCB received broad powers to regulate and monitor the flow of Brazilian capital abroad and foreign capital in Brazil, including availability and remittance procedures. This law also enables BCB to request, in a more flexible, selective and efficient manner, the information necessary for compilation of official macroeconomic statistics.

All such changes will contribute to simplification and rationalization of

exchange contracts, registrations, codes and reports, taking into account reasonable compliance costs, resulting in better and cheaper services.

Also concerning bureaucracy reduction, the new legal framework establishes that institutions engaged in the foreign exchange market will not be allowed to require from customers data or certificates that are available in their own public or private databases of broad access.

MEASURES TO STRENGTHEN THE CONVERTIBILITY OF THE BRAZILIAN REAL



Another import cornerstone of the New Foreign Exchange Law is the strengthening of the grounds for the conversion process of the Brazilian reais. Several measures were taken to foster and simplify the use of the Brazilian currency abroad, including by international players in Brazil. Such measures are:

- Adoption of all international bank correspondents in Brazilian Reais: A foreign bank may open an account in Brazilian reais with a bank in Brazil and use it to make payments of interest to Brazilians abroad. Currently, only the inverse flow is allowed which only permits foreigners to use these accounts for payment orders in Brazil.

- Maintenance of accounts in Brazilian reais by foreign entities: Foreign central banks and non-resident institutions that provide clearance, settlement and custody services in the foreign market may open and maintain deposit and/or custody accounts in Brazilian reais with BCB. Accordingly, the Brazilian real may integrate the assets of those institutions, expanding the use of such currency abroad. It will also facilitate participation of foreign investors in government bonds denominated in Brazilian reais directly abroad.

- Similarity between residents' current accounts with non-residents' current accounts: The new law expressly provides that accounts in Brazilian reais held by non-residents should receive the same treatment as accounts in Brazilian reais held by Brazilian residents. This repeals the current regime for accounts in Brazilian reais opened by non-residents (former CC5), which is highly complex and bureaucratic due to the required reports and the regime applicable to international transfer in Brazilian reais (TIR), among other factors. The investment regime in the financial and capital markets through the so-called accounts 4.373 is also expected to be simplified, so that investments may be made with funds from non-residents' local current account.



OFFER OF FINANCIAL PRODUCTS AND SERVICES ABROAD: END OF CIRCULAR 24 OF 1966

One of the most symbolic changes brought by the New Foreign Exchange Law is that Brazilian institutions and other entities authorized by BCB will be expressly authorized, within the limits of their respective licenses, to allocate the funds they raise in Brazil to credit and financing transactions abroad. This means the revocation of Circular 24 of 1966, an old and anachronistic rule that prohibited Brazilian institutions to carry out this type of offshore operations directly.

This will certainly open new alternatives for Brazilian banks that are now authorized to offer its services to clients within Brazil and abroad, deleting a competitive disadvantage that such entities face in comparison to international banks with presence in Brazil and abroad.

MANDATORY USE OF CURRENCY

The mandatory use of Brazilian currency continues to be the general rule. The new legal framework only consolidates the exceptions in which payments in foreign currency are permitted in Brazil, which include: foreign trade transactions; transactions with a counterparty abroad; foreign exchange contracts; indirect export; and assignment/delegation of these obligations.

However, it introduced some specific innovations. One of them is the possibility of agreements denominated in foreign currency to be entered into between, on the one hand, exporters and, on the other hand, concessionaires, licensees, authorized entities or lessees in infrastructure sectors.

Another novelty, and maybe the greatest one, is the granting of powers to CMN to define new scenarios in which a payment in foreign currency is permitted, as long as it aims to mitigate foreign exchange risks or boosting business efficiency.

CURRENCY INFLOW AND OUTFLOW IN BRAZIL

Regarding the processing of inflows and outflows of Brazilian and foreign currencies in Brazil, the requirement about the obligation to perform foreign exchange transaction through an institution authorized to operate in the foreign exchange market is maintained. Historically, statutory rules have restricted this activity to banks, but, recently, there has been a relaxation so that, in fact, any institution authorized to operate in foreign exchange (such as brokerage companies) can have its own foreign exchange account abroad to make these inflows and outflows.

An exception to this general rule is the cash that international travelers can take in or out of Brazil. This limit was raised to USD10,000 or its equivalent (and no longer the current ten thousand Brazilian reais).



USE OF EXPORT FUNDS HELD ABROAD IN LOAN TRANSACTIONS



Brazilian companies holding export earnings may freely use these funds, including to grant loans. Currently, despite the deletion of the cobertura cambial, there is still a restriction on this type of use, which will be deleted when the New Foreign Exchange Law becomes effective.

PRIVATE OFFSETTING

The private offsetting of credits or values between residents and non-residents, which is currently prohibited, will become expressly authorized in the events to be established by BCB. Therefore, changes in this regard are still subject to regulation.

FINANCIAL CHARGE IN CASE OF CANCELLATION OR WRITE-OFF OF ACC

The financial charge resulting from the write-off or cancellation of advances on foreign exchange agreements (ACC) becomes limited to the total amount of the advance.

FOREIGN CURRENCY ACCOUNTS



Despite the press rumor about foreign currency accounts as one of the major innovations of the legal framework, this matter is already currently regulated by the monetary authorities – since companies from several industries can open a foreign currency account, such as insurance companies and travel agencies, among others. The New Foreign Exchange Law only established that from now on it is incumbent on BCB, and no longer on CMN, to define who can hold a foreign

currency account and which will be applicable requirements.

In the future, BCB can widen the scope to open foreign currency accounts in Brazil, but such entity has already issued an opinion about the fact that this will take place in the long term, in a gradual and prudent manner, based on Brazilian macroeconomic fundamentals. Therefore, the possibility of individuals holding dollar accounts is not a possibility for now.



TAX ASPECTS



Tax matters have not been expressly contemplated in the new legal foreign exchange framework on purpose and as a strategy to secure its approval.

In addition, legal provisions assigning the responsibility for checking the payment of taxes on foreign exchange transactions to the institutions that operate in the foreign exchange market (article 9 of Law 4,131 of 1962 and article 125, sole paragraph(c) of Decree-Law 5,844 of 1943) remain valid, resulting in a high compliance cost and impacting the price and quality of the service.

REMITTANCE OF ROYALTIES AND DEDUCTIBILITY



The New Foreign Exchange Law amended some provisions regarding remittance of royalties and deductibility, aiming at less bureaucracy and further relaxation:

- Amendment to article 50 of Law 8,383 of 1991: It deletes the obligation to register the agreements with BCB in order to allow the tax deductibility of remittances as payment for royalties, being only necessary to register these agreements with the National Industrial Property Institute (INPI).
- Exclusion of article 14 of Law 4,131 of 1962: It repeals the prohibition of remittances of royalties between Brazilian subsidiaries/branches and foreign parent companies.

EXCHANGE CONTROLS IN EXCEPTIONAL AND EMERGENCYV CASES



For the most alarmist ones, it is important to make clear that in this last round of foreign exchange liberalization, the government maintained, through CMN, the ever-prudent prerogative to impose foreign exchange controls again in case of emergency (Law 4,595 of 1964, article 4, XVIII). This is a sovereign right, which, evidently, should be implemented only in extremely exceptional cases.



FINAL COMMENTS

Despite the unquestionable advances within the last years, there are still many aspects to be enhanced in the foreign exchange market and in the international capital regime. It is necessary to improve the business environment, including fostering foreign trade and deleting its limitations; to make foreign exchange and financial transactions more expeditious, reducing cost in Brazil and offering a more favorable scenario to do business; and to open up more possibilities for clients to have access to financial products abroad through local banks.

The New Foreign Exchange Law is the first step towards a thorough and structural reform in the Brazilian foreign exchange market, since several legal ties existing in former and outdated laws and decrees will be definitely broken. It makes room for adopting modern and disruptive concepts, bringing Brazilian foreign exchange regulations in line with the guidelines and practices internationally used. The extent of such reform, however, will be also contingent upon the statutory changes to be made by BCB.

In addition, future initiatives such as the Central Bank Digital Currency (CBDC) and international instant payment (PIX) have already started appearing on the horizon. It becomes clear that CMN and BCB aim at streamlining the foreign exchange rules and creating an environment that enables the Brazilian real to be a convertible currency available on international markets. The first steps have been certainly taken.

Our firm has advised our clients and contributed to all major developments of the foreign exchange market and of the streamlining initiatives. We have been also directly involved in dialogues about the new foreign exchange framework since 2016 and believe that it will be essential to ensure Brazilian economic upturn and boost the inflow of foreign investment, besides contributing to greater competition in the industry and to the offer of best services to consumers. In 2022, BCB will deal with a number of statutory rule proposals. We will continue to closely monitor the development of statutory rules, and keep our clients posted of all details and main opportunities.



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