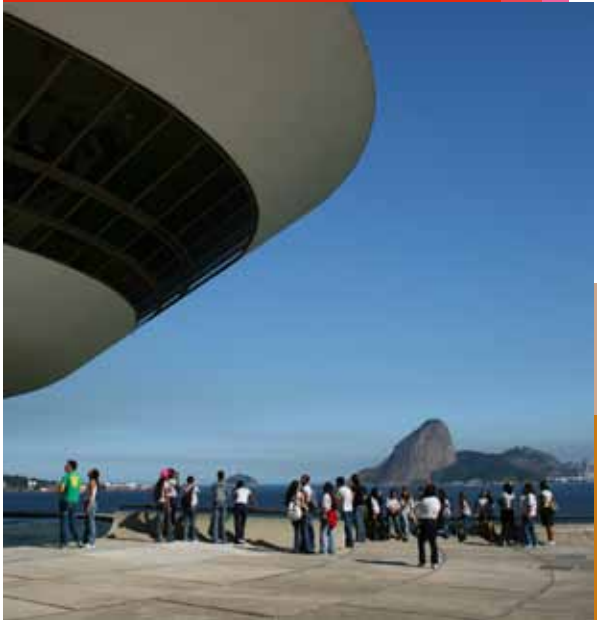


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Doing Deals in Brazil

2011



pwc

Foreword

Brazil is now recognized a mature country - both politically and economically and as one of the most attractive markets in the world for foreign investment.

The country rapidly overcame the turbulence of the recent international economic crisis and has returned a stronger, more attractive global player. The high level of diversification in Brazil's economy and its broad range of trading partners, coupled with a tightly regulated financial system, were central to mitigating the worst effects of the recent crisis. Brazil has nearly two decades of political and currency stability, tight fiscal discipline, increasing international reserves, solid macroeconomic indicators and a fast expanding internal consumer market, all of which make the country one of the most promising emerging markets in the world.

Brazil's success in a generally difficult economic climate, its government's aggressive infrastructure plans and an increasing awareness of the investment opportunities that the country offers, along with the discovery of the pre-salt oil fields – a rare event on the global oil scene – have attracted the attention of the world. And as the global appetite for commodities continues to grow and agribusiness gains international momentum, especially in terms of biofuels, Brazil is becoming an ever more important business destination. Not to mention Brazil's success bids to host the 2014 FIFA World Cup and the 2016 Olympic Games.

(cont...)



Foreword

Despite their increasing interest and confidence in Brazil, prospective investors still find it difficult to overcome complex regulatory and legal matters as well as out-dated perceptions of the country's strengths and weaknesses. To help you improve your understanding of these perceived barriers and the ways to clear the path to a successful investment, we are pleased to publish the 2011 edition of this Doing Deals in Brazil guide, now in a convenient pocket book format. This publication contains summarized information about Brazil's economic environment, financial and tax regulation and M&A activities, as well as information on politics and culture, among other subjects. A team of PricewaterhouseCoopers Brazil specialists has identified some of the critical concerns and risks that you, as a prospective investor, may face.

We believe that this guide will help you to pursue successful and profitable business ventures in Brazil. PwC professionals are available to provide further information on the matters covered in this publication. Note that professional accounting and legal advice should be taken on relevant Brazilian laws and regulations as necessary.

Fernando Alves
Territory Senior Partner
PwC - Brazil

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1 *Investment Drivers and Challenges in Brazil*

Why invest in Brazil?

All four of the BRICs (Brazil, Russia, India and China) are globally perceived as offering huge opportunities and potential for growth. However, the challenges for investors in Brazil are smaller than for those in other emerging economies.

Brazil is rich in natural resources, it has a young workforce and a largely unexploited domestic market: this is a country with great potential. Having constructed over the last decades a durable platform for growth on the pillars of economic and political stability, Brazil is as well placed as ever to capitalize on its potential.

Some of Brazil's attractions and challenges are shared with its fellow BRIC countries:

BRICs: Opportunities

- Rapid economic growth
- High growth rate of GDP per capita
- Increasing market size across all sectors
- An expanding middle class
- Large and growing urban populations
- Burgeoning energy consumption

BRICs: Challenges

- Poor infrastructure
- Inefficient governance
- Ineffective law and order
- Widespread corruption
- High levels of inequality and poverty

Brazil's Key Advantages

Brazil however has a number of qualities that sets it apart from other destinations for investment:

Governance and finance:

- Brazil is a settled democracy with well established governmental and administrative institutions
- Following the adjustment of macroeconomic fundamentals and the improved stability of political institutions, its economic climate is no longer volatile
- There is increasing international trade and globalization and the Government promotes policies favoring exports
- There are new regulations in place favoring minority shareholders, and promoting corporate governance and better accounting practices
- It has strict, modern environmental legislation
- It has a sophisticated, resilient financial and banking system
- Inflation has been under control for almost a decade and a half

The business environment:

- Brazil is currently the world's seventh largest economy (eighth if the Purchasing Power Parity criterion is adopted, as by the International Monetary Fund) and the largest in South America; it is expanding its presence in world markets
- The country has large, well-developed agricultural, mining, manufacturing, and service sectors, with a broad industrial base: in short, it is a diversified economy
- Brazil has been given an Investment-Grade rating by all the major risk agencies

- Foreign investors are eligible for most available fiscal incentives, including tax deductibility of goodwill under certain conditions
- There has been significant improvement in local capital and debt markets, with an increasing number of IPOs in recent years
- There has been a significant reduction in the country risk perception over the last few years
- Brazilian business is facing a transformational period with the introduction of better corporate governance and accounting procedures followed by the convergence of local accounting and auditing standard with International Financial Reporting Standards (IFRS)
- Whilst corruption remains widespread, problems of physical security have greatly improved in recent years

Geography:

- Brazil offers a business-friendly environment for US and European investors (there are no major cultural differences affecting business)
- It is highly urbanized when compared to other emerging market countries
- The whole country speaks one language
- The country has a creative, flexible labor force
- It does not suffer from natural disasters such as earthquakes and hurricanes
- It maintains peaceful relations with neighbor countries
- From Brazil, investors have tariff-free access to the other members of the Mercosur free trade zone (Brazil, Argentina, Chile, Venezuela, Paraguay and Uruguay)

Resources:

- Brazil has immense resources in energy, minerals and raw materials
- It is self-sufficient in oil and is a world leader in the development and production of low emission fuels and biofuels, especially ethanol

The future:

- According to *The Economist*, Brazil will be world's fifth largest economy in a decade
- Many local companies are undervalued and in need of restructuring, capital and technology
- There is a fast-growing consumer market with high growth potential, especially among the middle-classes




The main investment drivers

Brazil was the first Latin American country to emerge from the international recession: it has overcome the recent turbulence in the world economy and has emerged stronger and more attractive to investors. From around a year after the bankruptcy of Lehman Brothers, there was an increased awareness around the world that the actions Brazil took were effective in fighting the recession.

The economic impact of the recent global financial crisis and demand downturn was less severe for Brazil than for the USA, Europe and Asia. This was a consequence of successful public-private long term commitment to growth, involving a combination of factors such as decades of political stability, fiscal discipline, strong international reserves, solid macroeconomic indicators (based on a strong focus on inflation control) and the strengthening of the middle class consumption power.

The government reacted promptly with the implementation of anticyclical measures to sustain the credit flow, especially to the automotive industry and households, and the level of consumption of durable goods. These measures contributed to a lower unemployment rate and economy recovery. A high degree of diversification in Brazil's economy and trading partners, as well as a sound financial system – leveraged by active regulators and the Central Bank – have also helped to mitigate the effect of the crisis in the country.



Although the global environment remains difficult and the Brazilian export sector continues to struggle as a result - compounded by a strongly appreciated real - the size of Brazil (with 2010 GDP of approximately US\$2.0 trillion) and the strength of its domestic demand has propelled its economy into recovery.

However, long term strategies and investments (including pre-salt oil exploration opportunities) are now top of the government's agenda. This effort is expected to bring results in the medium to long term. Some regions, in particular the northeast, now have the challenge to reach out to opportunities that are already available for the rest of the country. The country's social inequalities are also being addressed. The government has made significant progress in attacking poverty (including the "Bolsa Família" program).

Financial and strategic investors are seeing these opportunities and Brazil is a highly attractive investment destination. Cross-border merger and acquisitions and strong capital markets will play an important role.

Brazil deserves close attention while it prepares itself for the future. The country has huge infrastructure demands and a need for further public and private investment in education and healthcare. Top priorities on the government's agenda include structural tax reforms and tight control on government expenses to spur the country's economic growth.

The main investment challenges

Despite significant progress, investors still face numerous challenges. There is a complex tax and labor regulatory environment, with high taxes and social charges on payroll, sales and income. Multiple taxes and fast changing legislation can affect business plans and increase risks for contingent liabilities, potentially blocking the success of both asset and stock acquisitions. There are also complex transfer pricing and foreign capital registration rules.

Brazilian companies may not comply with corruption or anti-bribery laws, including the Foreign Corrupt Practices Act and the UK Bribery Act 2010. They may also have undisclosed off-balance sheet transactions and commitments, which can result in the loose application of accounting rules. There is a generally low quality of historical financial information of businesses and it may not fully adhere to generally accepted accounting practices. A significant number of small and/or family-owned businesses may require investment in post-deal issues such as corporate governance, internal controls, integration of IT platforms, HR related matters etc.

Brazilian companies may not be organized optimally. There may be difficulties in reorganizing companies quickly, since there are high costs for employee terminations. There is also a considerable amount of bureaucracy and regulation for certain businesses and industries. In certain regions and even in some industries, there may be nepotism: “knowing who” is often more important than “knowing how”.

In some, less industrialized, areas of the country, there is a need for further investment in distribution channels and infrastructure. Weaknesses in the education system may also impair the supply of sufficiently skilled labor. This goes hand in hand with Brazil's social inequality and uneven distribution of wealth.

More generally, Brazil still lags behind in investment in innovation and research and development, and Brazilian firm still suffer from poor brand recognition outside the country, although this is improving.

Presented below are examples of more usual difficulties faced by investors when contemplating doing deals in Brazil (pre investment) and post investment (in no particular order).

The main issues usually identified in due diligence processes involving Brazilian target companies

- Material tax, environmental and labor risks and contingencies
- A certain level of informality in the operations (eg unrecorded transactions, two sets of books)
- Significant related party transactions with inadequate documentation (eg family costs)
- A lack of or an inadequate internal controls environment (resulting in poor quality of financial information)
- Inadequate accounting practices, triggering significant accounting adjustments (to EBITDA, net income and net asset) and tax risks
- A lack of regular control account reconciliations
- Inadequate cash management

The main reasons for unsuccessful business deals in Brazil

- Unexpected tax and labor problems
- Excessive legal formalities/bureaucracy
- Low quality of available information
- Market volatility
- Insufficient due diligence prior to investment
- Underestimation of deal execution time
- Overestimated synergy/restructuring gains
- Low quality of acquired management
- Inefficient post-acquisition monitoring



2 *The Economic Environment*

2.1 An Overview of Brazil

Key Figures

- Population: estimated at 192 million
- 26 states and one federal district (Brasília)
- 2010GDP: US\$2.0 trillion
- Currency: Real (rate of US\$1 to approximately R\$1.63 as of March 2011)
- Language: Portuguese

Political Organisation

- Federative Republic of Brazil
- Presidential and state elections held in October 2010
- Former president Mr Luiz Inácio Lula da Silva democratically elected his successor Mrs Dilma Rousseff (Workers Party)

Economic Overview

Facts and Figures

- Brazil is the largest economy in Latin America and the seventh largest in the world
- The GDP per capita is approximately US\$10,000 in 2010
- Primary economic sectors are: agriculture, automotive, utilities, transport, industrial products, mining and energy
- Some main natural resources include bauxite, gold, iron ore, manganese, nickel, phosphates, platinum, tin, uranium, petroleum, hydropower and timber, among others

- Main agricultural products include coffee, soybeans, wheat, rice, corn, sugarcane, cocoa and citrus, among others
- Export items include iron, soybean, automobiles, soybean oil and derivatives and aircraft, among others
- Import items include petroleum, vehicle parts, electronic micro parts, medicines, etc, among others
- The main ports and harbors are Tubarão (ES), Itaqui (MA), Santos (SP), Itaguaí (RJ), São Sebastião (SP), Paranaguá (PR), Aratu (BA), Rio Grande (RS), Belém (PA), Angra dos Reis (RJ)

Population

- Brazil has the largest population in Latin America and the fifth largest in the world
- Approximately 70% of the people are concentrated in the Southeast and Northeast
- Life expectancy is approximately 72 years
- Some 27% of the population is under 14 years of age and only 6% is over 65 years
- The country is highly urbanized: only 14% of the population lives in rural areas

Geography

- São Paulo is one of the fastest-growing cities in the world
- Twenty other metropolitan areas of Brazil have populations of more than 1 million
- The population of the São Paulo and Rio de Janeiro states are approximately 42 million and 16 million, respectively

- The main economic regions are: São Paulo, Rio de Janeiro, Minas Gerais, Paraná and Rio Grande do Sul
- The GDP per capita in the Southeast, South and Midwest regions is much higher than in North and Northeast


Region	Population		Land Mass	
	In millions	%	%	%
Southeast	80.9	42.1		11.0
South	28.4	14.8		7.0
Midwest	13.8	7.2		22.0
North	15.4	8.0		42.0
Northeast	53.6	27.9		18.0
	192.1	100.0		100.0

Source: IBGE – Instituto Brasileiro de Geografia e Estatística

2.2 A Summary of Recent Economic Activity

The Brazilian economy has grown some 7.5% in 2010, contrasting with the much more modest growth rates observed in advanced and other developing economies, which are still struggling to overcome the 2008/2009 international financial crisis. Brazil's growth has been wholly based on the expansion of the domestic market and far exceeded the 4.5-5.0 percent range estimated by the government to be the long-run potential rate of growth in Brazil. Domestic demand has increased steadily at a similarly high rate throughout the year, with consumption increasing 6.5% and private investment 23%. Booming current government expenditure and investments – especially under the Growth Acceleration Programs 1 and 2 (*Programa de Aceleração do Crescimento 1 e 2* – PAC 1 and 2) – and spending on social programs and the social security system, which dominated Lula's administration, have helped increase the disposable income of the lower strata of the population.

The effect of loose fiscal policy on demand has been complemented by a huge expansion of domestic credit by both private and government-owned banks (BNDES, Banco do Brasil and Caixa Econômica Federal). Special credit is due to BNDES, which has supported the investments of middle and large companies during the past three years, when credit has been scarce. Given the narrow limits of domestic supply, the excess demand has been accommodated, to some extent, by the sharp reduction in the trade balance. Goods imports have increased 44% and exports 31% this year, while the services and income account are negative by US\$ 68 billion. The result is a current account deficit of US\$ 52 billion, or 2.6% of GDP, up from 1.5% last year.



Brazil's exuberant growth has been made possible by an abundant supply of foreign capital, both before and – especially – after the 2008/2009 international financial crisis. This credit has financed the current-account deficit and forced the Central Bank to accumulate an additional US\$ 46 billion of reserves (February 2011 reserves reached record US\$ 300 billions) to avoid further appreciation of the exchange rate.

The capital inflow has been diversified, but arbitrage funds have been prominent and directed to the fixed income market to exploit the large interest rate differential between Brazil and advanced countries. While interest rates in the USA, Europe and Japan have been close to zero, Brazilian rates have remained at a worldwide high of around 11% per year (the Central Bank rate). The consequence has been further appreciation of the real relative to the dollar, despite the reserve acquisitions of the Central Bank. In turn, the strong Real has further stimulated the demand for tradable goods and services and enlarged the current account deficit. During the last months of the year, the government increased the tax on foreign portfolio capital (fixed income instruments) from 2% to 6%, but with little effect so far. As in many other countries today, the appreciation of Brazilian currency, and the tradable sector's consequent loss of competitiveness in world markets, poses an important and difficult problem for the coming years.


A consequence of the buoyant domestic demand, largely influenced by consumer credit, which in Brazil still has room for expansion, has been the return of inflationary pressures, especially stemming from the labor market. The rate of unemployment has fallen below 7%, the lowest in two decades, and unit labor costs for firms have been rising steadily. The consumer price index (IPCA) has increased 5.9% this year, well above



the target rate of 4.5% set by the government under the inflation target framework, although the government has successfully maintained actual inflation within a pre-determined inflation range over the past years. Toward the end of the year 2010, the Central Bank abandoned its passive policy and increased the reserve requirements on the demand and time deposits of commercial banks, and raised their capital requirements for consumer loans, in an attempt to curb consumption demand.

Although very high by international standards, Brazilian real interest rates have never been lower. For instance, the Central Bank rate, in real terms, is presently at 5% per year, against the average of nearly 10% for most of the first decade of this century. This helps explain the expansion of domestic credit from 35% to 65% of GDP over the past few years. It also explains the resumption of private investment, which now stands at 20% of GDP. Brazil is currently experiencing a boom in residential and commercial construction, triggered by lower mortgage costs, longer maturities and easier financing requirements.

The stock market, which saw 25 new issues (11 IPOs and 14 follow-ons) in 2010, has recovered from the financial crisis – with stock prices remaining relatively stable during the year – and leveled with international markets. As expected, foreign direct investment fell after the 2008/2009 crisis, but has shown some recovery this year. The bulk of foreign investments have been directed at exploring the opportunities offered by the growing domestic market and there have been record levels of M&A activity in 2010 (see Section 3 below). Little investment has been made in the tradable sector, in view of the strong appreciation of Brazilian currency.




The general elections held in October-November were very favorable to President Lula and his party (PT). He has not only succeeded in electing his chosen successor (Dilma Rousseff), but also won a comfortable majority in both houses of the Brazilian Congress. The coalition parties supporting the government, led by PT and PMDB, took 73% of the seats in the Chamber of Representatives and 75% in the Senate. This theoretical majority, however, should not be overstated, due to the fragmentation and lack of unity among the nine parties composing it. In Brazilian politics, the Federal Administration has to bargain each issue of interest on a case-by-case basis in Congress, as each party votes according to its own interests, and demands political benefits in exchange for its allegiance to the government. Moreover, despite Lula's enormous popular prestige, the opposition candidate, Jose Serra, won a substantial 44% of votes in the second round of the presidential elections, and the opposition parties elected many state governors, which will clearly limit the scope for arbitrary actions by the new federal government. In general though, Rousseff's government will be a continuation of Lula's. The officials appointed to the most important economic positions in the new administration, for instance, all occupied similar positions during the Lula administration, evidence that little will change in matters of economic policy. The other ministries have been distributed among the coalition parties according to their parties' political importance.

2.3 The Outlook for 2011

Brazil is currently enjoying a very favorable cycle after decades struggling with hyperinflation, balance of payments crises and low growth. The outlook for the next few years is one of continuing growth at reasonable rates (4 to 5 percent per year) in a context of stable inflation and balance of payments equilibrium. There are, however, certain unbalances in the economy that have to be resolved if this positive outlook is to remain. Though from a positive angle Brazil is today more foreseeable and stable than it has been in the past, a number of challenges still linger, some economic and fiscal, others concerned with labor skills and infrastructure.


The new government will face three major economic challenges in 2011. The first is to reverse the extraordinary fiscal expansion produced by Lula's government during his second term. Over the past four years, the growth of current federal expenditure, in real terms, has been almost double the growth of GDP. Considering that the tax burden in Brazil is already approaching 40% of GDP and can hardly be raised further, the new administration will be forced to adopt an austere fiscal stance. In 2010, as the general elections approached, several new expenditure proposals were presented in Congress, largely focusing on social security benefits, income guarantees, redistribution programs, and a host of new entitlements. These initiatives would undermine any effort at fiscal stability in the future. The immediate task of Rousseff's administration is to abort these proposals and establish a clear and sustained line of fiscal austerity. In other words, it is time to promote the coordination between monetary and fiscal policies that the Lula administration



lacked, and alleviate the independent Central Bank's task of maintaining the rate of inflation under control. A certain degree of slowdown in domestic demand is necessary to bring the rate of growth in line with the economy's capacity: if fiscal policy remains loose, real interest rates will have to return to the high levels of the past.

The second issue concerns the appreciation of Brazilian currency, a phenomenon that has been in evidence since 2006 and worsened after the international financial crisis of 2008/2009. The continuing appreciation of the Real threatens Brazil's industrial structure, both in terms of manufacturing exports and the capacity to compete with imports, especially from those countries, like China, that keep their exchange rate undervalued. Even recognizing the global nature of the problem – the so-called “currency war” – and that the defensive policies taken by individual countries may prove ineffective, the new government can be expected react and eventually introduce new restrictions on portfolio capital or on imports. The growing current account deficit has been a matter of concern and, if unchecked, may threaten the good performance of the economy.

Finally, in order to sustain growth rates of around 5% per year, Brazil needs to increase its rate of investment by several GDP percentage points, up from the 18-20% range of recent years. Plenty of investment opportunities exist in the economy, especially in the area of infrastructure. A recent example is oil exploration in deep sea waters, which is estimated to require hundreds of billions of dollars over the next years. The same can be said of other areas, like renewable energy, transportation, ports, and telecommunications. For that to happen, however, two things are necessary. The first is to generate positive saving



rates in the public sector (these are currently negative), since many infrastructure segments depend on government investment. Hence there is need for fiscal austerity. The second is to create a friendlier and more predictable environment for private saving and investment. At the end of last year, the government created tax incentives for long term financial instruments, with the goal of promoting the private capital market. This is already a recognition of the resource constraints on the state-owned banks, particularly BNDES (fixed capital formation) and CEF (residential construction), in supplying the funds necessary for financing the investment effort. Brazil's successful bid to host the 2014 FIFA World Cup in and the 2016 Olympic Games has provided an opportunity to mobilize resources to increase the rate of investment.

By the same token, as the present scarcity of labor reveals, there is an urgent need for Brazil to rethink its entire educational system and its labor training programs, which rank poorly in international evaluations of educational performance. During the two past decades, a successful effort has been made to universalize primary and secondary education. But quality has failed to improve – and has even worsened. Lula's government did little in this regard, as it privileged higher education and spent a larger share of the federal budget expanding the network of federal universities across the country. A shift of priority back to primary and secondary education is in order, aiming now at improving the quality and efficacy of the system.

Summary of historical economic indicators.

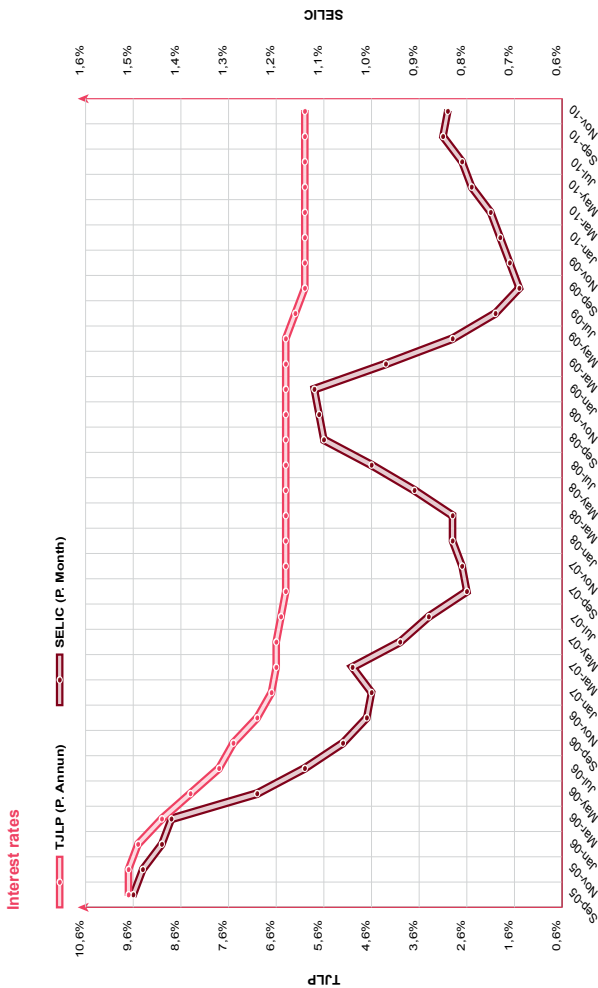
In US\$ billion	2002	2003	2004	2005	2006	2007	2008	2009	2010
GDP (US\$ billion) (1)	506	554	664	882	1,089	1,336	1,636	1,577	2,027
Real GDP growth (% per year)	2.7	1.1	5.7	3.2	4.0	5.7	5.1	-0.6	7.5
Unemployment rate (% of labor force)	10.5	12.4	11.5	9.9	10.0	7.5	6.8	6.8	5.3
General price index - IGP-DI (% per year)	26.4	7.7	12.1	1.2	3.8	7.9	9.1	(1.4)	11.3
Consumer price index - IPCA (% per year)	12.5	9.3	7.6	5.7	3.1	4.5	5.9	4.3	5.9
Exchange rate at year's end (R\$/US\$)	3.63	3.08	2.93	2.44	2.18	1.78	2.39	1.75	1.70
Exchange rate change (% per year)	53.8	(19.3)	(7.1)	(15.8)	(5.9)	(16.9)	34.1	(25.3)	(3.96)
Public sector deficit (% of GDP)	4.2	4.6	2.3	6.6	5.2	2.6	2.0	3.3	2.5
Public sector debt (% of GDP)	50.5	53.5	48.2	48.0	45.9	43.9	38.4	42.8	40.4
Goods exported	60.4	73.1	96.5	118.3	137.5	160.6	197.9	153	201.9
Goods imported	47.2	48.3	62.8	73.6	91.4	120.6	173.0	127.7	181.9
Trade balance	13.2	24.8	33.7	44.7	46.1	40.0	25.0	25.2	20.3
Current-account balance	-7.6	4.1	11.7	14.0	13.6	1.5	(28.3)	(24.3)	(47.5)
International reserves	37.8	49.3	52.9	53.8	85.8	180.3	206.8	239	288.6
Foreign direct investment (2)	14.1	10.1	18.1	15.1	18.8	34.6	45.0	25.9	48.5
Total foreign debt (3)	227.7	235.4	220.2	188.0	199.4	240.5	262.9	277.6	350.4

(1) At the year-average exchange rate.

(2) Including intercompany loans.

(3) Information from web site <http://www.redegoverno.gov.br>

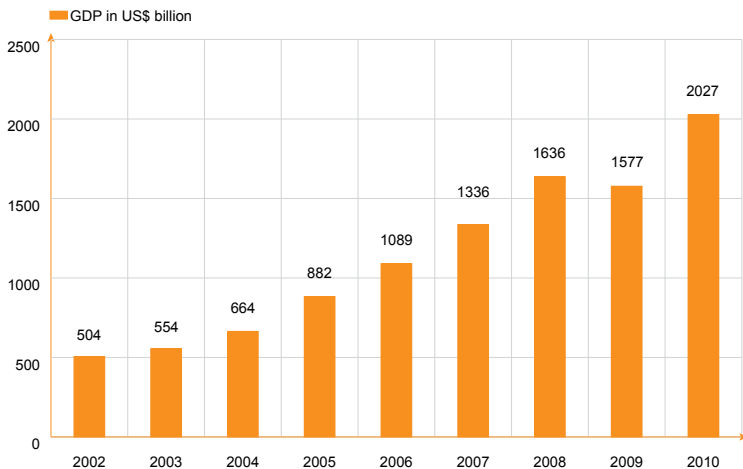
Brazil's interest rates have historically ranked amongst the highest in the world.



Source: Diário oficial da União

Brazil's GDP is the highest of Latin America, driven by its large and developed agricultural, mining, manufacturing and service sectors.

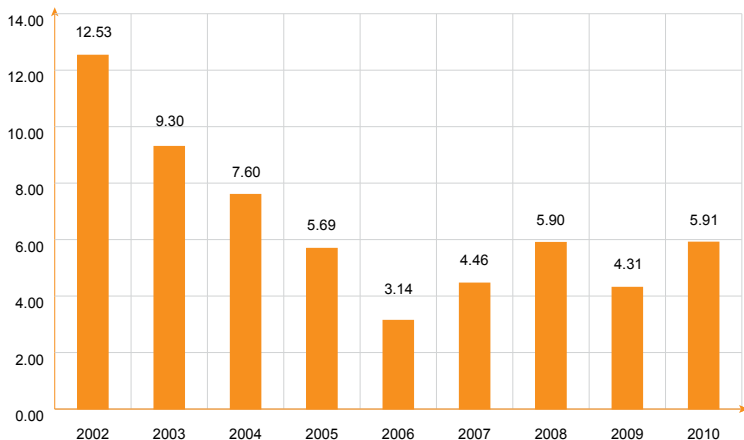
GDP Evolution



Source: IBGE – Instituto de Geografia e Estatística

Brazil has kept inflation under control in the last decade.

Brazilian Inflation Index (IPCA) evolution



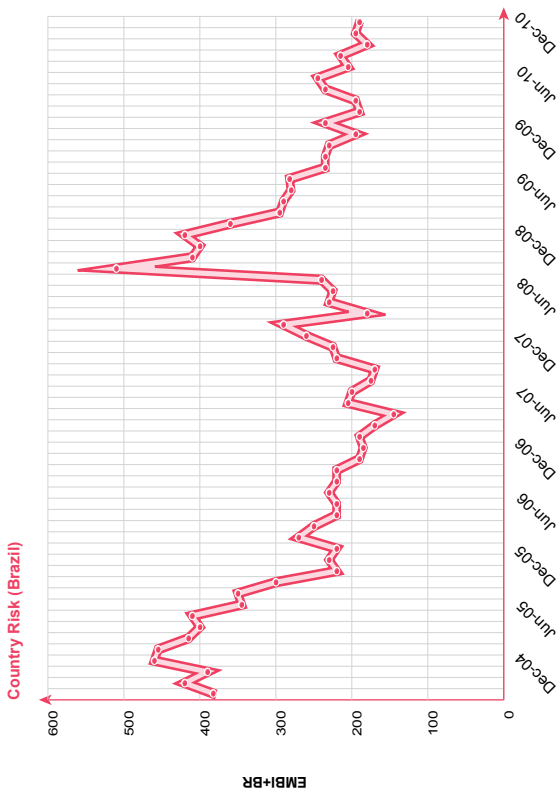
Source: ipeadata (Presidência da República - Secretaria de Assuntos Estratégicos)

Robust economic performance coupled with favorable international conditions have conveyed great capital inflow to Brazil impacting the value of the local currency (Brazilian Real).



Source: Gazeta mercantil

There has been a significant reduction in the country risk perception over the last few years.



Source: Bloomberg

Total exports showed a significant increase in 2010 (32% from the prior year), despite the overappreciation of the Real caused by among other reasons record-breaking foreign direct investments and great inflow of funds attracted by the high interest rates. Note that since 2009 China has become the most significant destination of Brazil's exports, overtaking the United States.

Main exports / imports - by country

Country exports (US\$ Millions)	2006	2007	2008	2009	2010(*)
China	8,399	10,749	16,403	20,191	23,192
United States	24,679	25,314	27,648	15,740	14,155
Argentina	11,714	14,417	17,606	12,785	13,033
Netherlands	5,744	8,841	10,483	8,150	7,335
Germany	5,675	7,211	8,851	6,175	5,926
Japan	3,884	4,321	6,115	4,270	4,594
Russia	3,443	3,741	4,653	2,869	3,081
Italy	3,829	4,464	4,765	3,016	2,988
Chile	3,896	4,264	4,792	-	2,931
Venezuela	3,555	4,724	5,150	3,610	2,848
Mexico	4,440	4,260	4,281	2,676	2,747
Others	58,213	68,343	87,195	73,513	33,339
Total	137,471	160,649	197,942	152,995	116,169

Source: Secretaria do Comércio Exterior (Brazilian Trade Balance Consolidated Data Report)

(*) From January to September. Total exports in 2010 reached US\$201.9 billion

China has also become the main provider of Brazil's imports. Total imports in 2010 reached US\$25 billion, an increase of approximately 60% compared to 2009.

Country imports (US\$ Millions)	2006	2007	2008	2009	2010(*)
United States	14,850	18,887	25,810	20,183	19,948
China	7,989	12,618	20,040	15,911	18,210
Argentina	8,057	10,410	13,258	11,281	10,596
Germany	6,503	8,675	12,025	9,866	9,084
South Korea	3,106	3,391	5,412	4,818	6,377
Japan	3,839	4,610	6,807	5,368	5,038
Nigeria	3,885	5,273	6,706	4,760	4,595
France	2,837	3,525	4,678	3,615	3,545
Italy	2,570	3,347	4,612	3,664	3,530
Chile	2,908	3,483	4,162	2,616	2,881
Others	34,850	46,402	69,687	45,565	48,352
Total	91,394	120,621	173,197	127,647	132,156

Source: Secretaria do Comércio Exterior (Brazilian Trade Balance Consolidated Data Report)

(*) From January to September. Total imports in 2010 reached US\$181.9 billion

Despite exporting a diversified range of products, commodity based items have historically played an important role in Brazil's foreign sales.

Main exports / imports - by product

Exports (in US\$ million)	2007	2008	2009	2010(*)
Minerals (ores)	12,026	18,727	14,453	20,627
Oil and fuel	16,042	19,427	14,497	16,387
Transport material	23,865	27,026	16,160	15,115
Soybeans	11,386	17,986	17,251	14,854
Meats & meats products	11,095	14,283	11,471	9,915
Sugar & Ethanol	6,578	7,873	9,716	9,587
Metallurgic products	16,100	23,047	11,104	8,931
Machines e equipments	8,724	9,671	6,256	5,836
Paper & Pulp	4,726	5,834	5,001	4,965
Coffee	3,856	4,733	4,251	3,774
Electrical equipments	5,712	6,500	4,694	3,554
Footwear & Leather	4,389	4,064	2,764	2,624
Others	36,150	38,771	35,377	
Total	160,649	197,942	152,995	116,169

Source: Secretaria do Comércio Exterior (Brazilian Trade Balance Consolidated Data Report)

(*) From January to September. Total exports in 2010 reached US\$ 201.9 billion.

Imports (in US\$ million)	2007	2008	2009	2010(*)
Capital goods	25,120	35,929	29,690	29,787
Oil and fuel	20,068	31,466	16,745	18,923
Consumption goods	16,024	22,525	21,523	22,377
Intermediate goods	59,409	83,277	59,689	61,069
Total	120,621	173,197	127,647	132,156

Source: Secretaria do Comércio Exterior (Brazilian Trade Balance Consolidated Data Report)

(*) From January to September. Total imports in 2010 reached US\$ 181.9 billion.

Petrobras (oil), Vale (iron ore) and Embraer (aircrafts) are amongst the companies with largest exports and imports transactions.

Exports by company (US\$ Millions)	2006	2007	2008	2009
Petrobras	11,087	13,626	19,299	12,307
Vale	5,990	7,904	13,531	10,826
Embraer	3,269	4,737	5,733	4,053
Bunge Alimentos	2,267	3,055	5,023	4,344
ADM do Brasil	801	1,224	2,593	2,770
Sadia (Brazil Foods)	1,316	1,776	2,424	1,873
Samarco Mineração	1,087	1,279	2,228	1,461
Cargill Agrícola	1,606	1,759	2,205	2,336
Mercedes - Benz do Brasil	-	1,424	2,109	1,234
Volkswagen do Brasil	2,279	2,126	2,002	1,479
Other	107,769	121,738	140,794	110,312
Total	137,471	160,649	197,942	152,995

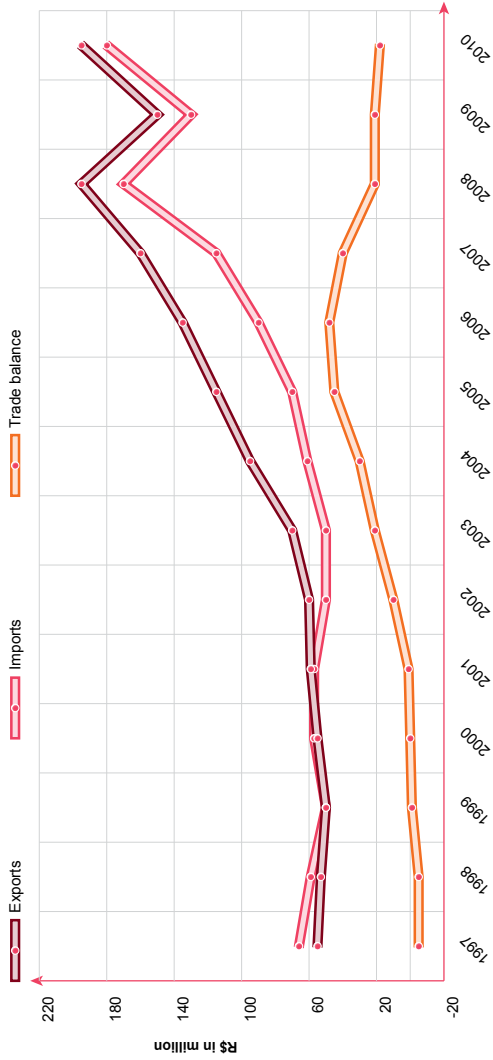
Source: Secretaria do Comércio Exterior

Imports by company (US\$ Millions)	2006	2007	2008	2009
Petrobras	11,207	15,374	24,087	12,555
Embraer	2,217	2,957	3,766	2,580
Alberto Pasqualini - REFAP	2,015	2,324	3,536	2,105
Bunge Alimentos	294	1,241	2,777	414
Cisa Trading	734	1,376	1,833	1,320
Motorola Industrial	1,946	1,866	1,667	711
Mercedes - Benz do Brasil	-	1,047	1,589	967
Samsung Eletrônica da Amazônia	901	1,046	1,554	1,478
Copesul - Cia Petroquímica do Sul	1,102	1,316	1,524	153
Volkswagen do Brasil	783	1,079	1,458	1,313
Other	70,197	90,991	129,408	104,051
Total	137,471	160,649	197,942	152,995

Source: Secretaria do Comércio Exterior

Brazil is gradually increasing its participation in global international trade.

Brazilian trade balance evolution - 1997 to 2010



Source: Banco Central do Brasil

Europe and the US have been the main foreign direct investors in the last five years. The manufacturing and services sectors received respectively 39% and 46% of the total investment in 2009. Foreign direct investors showed a sharp increase of approximately 60% in 2010, totaling R\$48.5 billion.

Foreign direct investor

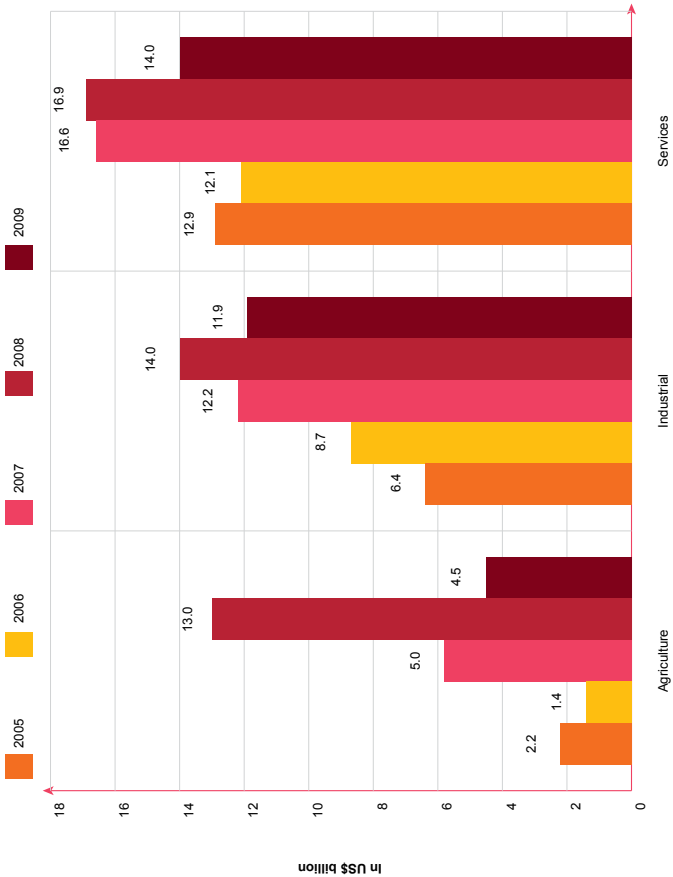
In US\$ billion	2004	2005	2006	2007	2008	2009	2010(*)
Netherlands	7,705	3,208	3,495	8,116	4,624	5,722	
United States	3,978	4,644	4,434	6,039	6,918	4,878	
Spain	1,055	1,220	1,514	2,164	3,787	3,415	
Germany	795	1,269	848	-	-	2,459	
France	486	1,458	745	1,214	2,856	2,136	
Japan	243	779	648	465	4,099	1,673	
Canada	593	1,435	1,286	819	1,438	1,371	
Cayman Islands	1,522	1,078	1,974	1,604	1,555	1,092	
Chile	22	103	27	716	263	1,027	
United Kingdom	275	153	395	1,004	641	1,025	
Austrália	6	926	117	494	1,153	707	
Norway	27	43	339	256	176	667	
Luxembourg	747	139	745	2,855	5,937	537	
British Virgin Islands	245	255	280	372	1,047	403	
Other countries	2,568	4,810	5,385	5,832	8,356	3,331	
Total	20,265	21,522	22,231	31,948	42,850	30,444	48,500

Source: Brazilian Central Bank

(*) Split by year not available

Note on above table: data is driven by the country of origin of the investing entity, and therefore does not necessarily reflect the original country source of funds.

Foreign direct investments by sector



Source: Brazilian Central Bank

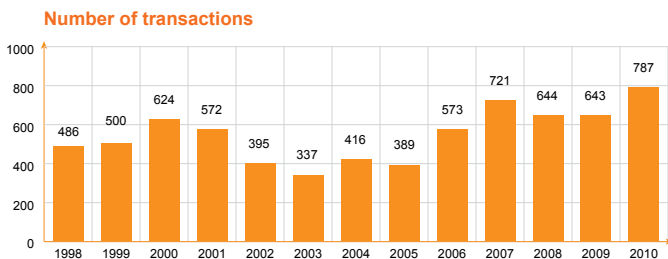
3 *M&A and Private Equity Activity*

3.1 2010 M&A Activity and the 2011 Outlook

During the 1990s, Brazil began to welcome increasing numbers of foreign investors, following a series of liberalizing structural changes, including moves towards a more open economy, privatization and deregulation of key sectors. The country then experienced several years of flux resulting from a number of crises in other emerging economies and high levels of foreign and domestic debt. This was combined with uncertainty over the direction of economic policy following the election of the Lula government that many commentators believed would lead Brazil back to a condition of unstable exchange rates, erratic growth and low levels of M&A activity and Foreign Direct Investment. Instead, the Lula government continued the sound economic policies of its predecessors and a period of strong growth commenced that, with the exception of the hiatus following the 2008/2009 downturn, continues until today.

Following the slowdown, there was a return to growth in the number and size of transactions: in 2010, 787 business deals announced during the year, a record in country's history. A deal value was revealed for 273 of these transactions, giving a total of approximately US\$63 billion, or an average of US\$233 million per announced deal. In comparison with former periods, 2002 to 2005, with an average of 384 transactions per year and 2006 through 2009, with an average of 645 transactions per year, 2010 set a new benchmark. Even compared to 2007 (a very strong period for the wider global economy with high liquidity, a high level of investment and active capital and mergers and acquisitions markets), 2010 represented an increase of 9% in M&A volume in Brazil.

Growth is being accompanied by an expansion of both the type and origin of investors, as well as the nature of targeted sectors.



Source: PwC Corporate Finance

The 2010 record in the number of announced transactions reflects the excellent state of the Brazilian economy and demonstrates the political and social maturity of the country, despite international developments in the post-crisis era.

In a year which was undermined by uncertainties about the performance of international economies, Brazil emerged stronger and more attractive to investors, largely due to its speedy recovery relative to larger and more mature economies like the USA and the Eurozone countries. Private equity players reinforce themselves as they act as an alternative for companies seeking new capital resources and opportunities to consolidate sectors. Apart from its main objective in increasing value, private equity stimulates Brazilian companies in mid and long term planning, besides continually seeking best practices in management and operations.

In a year of Presidential elections, and even given that Brazil still has structural deficiencies in some areas, including in infrastructure and in the lack of qualified labor, and that there are important discussions surrounding interest policies and government spending, the one thing that is clear is the increased maturity and attractiveness of the country as a whole and increasing developments in M&A.

This booming M&A market is testament not only to Brazil's rebound from the global downturn, but also to its underlying strength. While international market sentiment about M&A recovery this year has swung between optimism and skepticism, in Brazil there is a positive momentum in what looks to be sustained activity – largely influenced by the context described above. Strategic and financial investors have created historical record levels of deal-making, supported by a solid macroeconomic context and tremendous consolidation opportunities. Confidence – a key driver for M&A activity – has been further boosted by low unemployment rates, access to credit and the approximately 40 million new consumers in Brazil (Brazil's new middle income class). Middle market M&A activity remains strong and is expected to drive M&A in 2011.

Majority stake transactions account for 52 percent of all announced transactions, while non-controlling positions account for 32 percent, indicating a long-term investment strategy. Strategic and financial investors are both participating aggressively in the fast developing Brazilian economy. An annual and more detailed monthly analysis of deal flows will demonstrate that M&A activity in Brazil is at high levels, the monthly average number of business deals having risen from 54 in 2008 and 2009 to 63 this year

A multi-sector and multi-region deal profile has been seen this year, with the leading sectors by deal volume being IT, Consumer Products (including Food/Agribusiness & Beverages, Healthcare and Cleaning Products), Mining, Services (Healthcare, Education and General Services) and Chemicals/Oil & Gas. Next in significance come Financial Services, Logistics, Retail and Infrastructure/Construction. The largest sector (IT) holds some 9% of total deal activity in terms of volume, the other sectors following close behind.

Additional information on the profile of the Brazilian M&A market

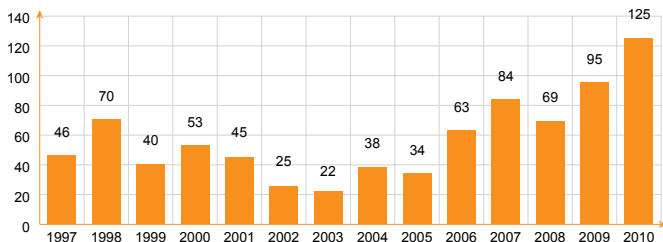
Buyers

- Local and multinational firms
- Private equity and buy-out funds
- Government and private pension funds
- Distressed debt conversions

Targets

- Private companies
- Family owned
- Privatization
- Carve-out of acquired non-core businesses
- Non-core or distressed businesses of multinational companies

Transactions with deal value over US\$ 100 millions



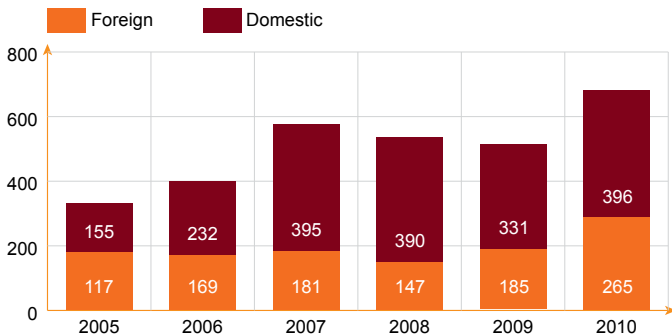
Source: PwC Corporate Finance

Foreign and domestic capital participation in M&A activities

Brazilian investors participated in 396 business deals, 60% of acquisitions (controlling and minority stake deals). In 2009 the number was 331 deals, so the numbers for this year represent an increase of circa 19%.

Foreign investors took part in 265 transactions (a record number for foreigners), or 40% of the business deals. The incentive to invest in Brazil is evident when one observes the level of participation of foreign investors in the total transactions where there was a constant increase (43%). Such a movement should reinforce the new momentum attained, particularly in terms of stable, transparent growth, demonstrated by the Brazilian economy.

Aquisition deals by origin of buyer (*)



Source: PwC Corporate finance report

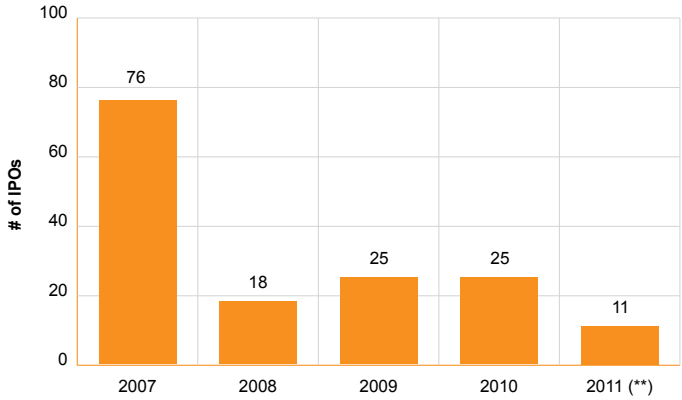
(*) Transactions released on press. It does not include agreements

IPO activity

Eleven Brazilian companies came to market in 2010 (plus 14 follow-ons), against six in 2009 and four in 2008. Brazil's record year for IPOs was 2007, when 64 companies raised 55.6 billion Brazilian Real (\$33.3 billion).

Whilst the 2009 highlight was the Latin American record-breaking Banco Santander (Brasil) S.A. IPO, which raised US\$7.6bn, in 2010 investors focused on the record US\$70 billion share offering by Petrobras, the government-controlled oil producer.

IPO's by year (*)



Source: BMF/Bovespa

(*) Include "follow on" transactions

(**) Until 20 March 2011

3.2 Private Equity

Private Equity in Brazil continues to gains momentum

While worldwide private equity-backed M&A activity was severely affected in 2009, in Brazil Private Equity activity reached record levels. After making up 30 percent of the business deals announced in 2009, it reached 42 percent of the deals announced in 2010. This share, which was 15 percent in 2007 and 20 percent in 2008, reflects aggressive Private Equity investment strategies and the consolidation of various sectors. This disparity has occurred in a market where the Private Equity industry is not reliant on financial leverage and is therefore less affected by the international credit crisis and liquidity constraints.

Capitalized and with some US\$15bn available for investments, a significant part of Private Equity activity in Brazil has involved consolidation opportunities in “cash for investments” deals. The largest investors this year are in the food and drink segments, along with real estate construction, consumer goods, IT, education and the financial and energy sectors. Additionally, deal size has started to increase from the small- to mid- market transactions that have historically dominated the market.

The Brazilian private equity market has been stimulated by a combination of factors that have strengthened the country’s position not only as an emerging market alternative to China and India, but as an attractive current alternative to more developed markets that have experienced a much slower return to growth. A combination of factors, such as increasingly sophisticated and liquid capital markets (which have seen 181 IPOs and follow-ons

over the past five years, 2007 being a record year with 76), new financing instruments and existing exit alternatives (such as sales to strategic players, capital markets/ IPO or sales to other PEs or funds of funds), along with the continuing demonstration of political and economic stability have opened the eyes of foreign Private Equity investors to Brazil, which is now regarded as a serious player in the global market.

The presence of the large funds that have traditionally operated in Brazil (like AIG, Advent, GP, Banco Pátria and Gávea) has continued to grow alongside the entrance and/or confirmation of interest in the country (as published in the media) of firms including Blackstone, Carlyle, GE Capital, One Equity Partners, Morgan Stanley, Apax Partners and CVC. All these players are competing for investment opportunities with other local and international funds as well as with strategic investors.

Brazil has a multi-sector profile in M&A

Strengthened by the dimensions of resources and the extensive possibilities in the country, M&A activity is spread across several sectors. IT showed the most activity, representing 9% of the total amount announced, most of it in the software segment and in network systems. The fragmented nature and need for investment in this sector is attractive for M&A.

Food, Chemical & Petrochemical and Mining are responsible for 24% of the total amount of business deals. Services, Banks and Retail together represent 20% of the deals announced. Other sectors, such as Public Services, Real Estate and Construction, Transportation, Education and Agribusiness, were responsible for 46% of the deals announced, with 365 transactions.

The approach of the Private Equity industry in Brazil is wider and funds in Brazil tend to be more flexible in terms of interest to be acquired and investment size. The typical deal size remains low, although a number of larger business deals are increasingly being seen.

Who is already investing?

Approximately 140 Private Equity and Venture Capital firms have invested in Brazil through over 230 investment vehicles. Private equity investors more than trebled their share of the Brazilian M&A market over the past four years, reaching a share of 42% in 2010. Some of the Private Equity investment highlights in 2010 were:

- Carlyle acquires shares in CVC
- IdeiasNet sold Media Factory
- BTG acquires shares of Rede D'or
- BTG invests US\$ 147 million in Textília
- Apax acquires 54,25% in Tivit
- Carlyle acquires Qualicorp
- BTG acquires Rosário Distrital
- Blackstone acquires shares in Patria
- 3G acquires Burger King
- JP Morgan acquires 55% of Gávea
- Actis invests US\$58,8 million in XP Investimentos
- Kinea acquires a minority participation of Grupo Multi and Yazigi
- IdeiasNet sold Netmovies
- International investors invest in BTG
- Carlyle acquires Scalina

What to expect for the near future in the Brazilian M&A Market?

Expectations are that the Brazilian M&A and investments context will continue to mature and reach new levels. Capital markets are also expected to return to pre-crisis levels and market specialists expect some 40 IPOs in several sectors, from Consumer Products to Construction and from Industrial Products to Retail and Finance. Benefitting from less reliance on financial leverage and therefore less exposure to liquidity constraints, as well as the expected slow return to growth across the rest of the world and the continuingly successful differentiation of Brazil as an alternative investment prospect, the investment outlook is positive. 2011, and onwards, should see new records of overall M&A activity as well as new PE entrants.

The main sectors of investment will continue to be Food and Consumer Goods, Healthcare, Education and Outsourcing Services, Real Estate, Energy and Finance, with consolidation in all these sectors continuing to be a key driver. Infrastructure, given Brazil's structural deficiencies, and Oil & Gas are also sectors likely to see to improvement in activity. Companies in Brazil are facing a transformation period. With better corporate governance and accounting procedures in place (IFRS has been mandatory for large companies since December 2010 and a more simplified and optional set of rules has been established for mid-size companies), most companies are experiencing the challenges of having a local company that is being transformed into a regional, then a national and finally an international operation.

4 Culture

This section presents an overview of Brazil's culture from the point of view of investment.

Language

Brazil's official language is Portuguese. There are no significant local dialects or other derivations from the official language, but a number of words and phrases vary from those used in Portugal. English is the most used foreign language in the business community.

Religion

The predominant religion is Roman Catholicism. Many other religions are also practiced, since immigrants of different creeds have settled in Brazil. The constitution guarantees freedom of religion.

Education

The government offers free state and subsidized private educational facilities from primary school through university, with full- or part-time curricula. The government also subsidises national apprenticeship training programs as preparation for various industrial and commercial sectors, as well as an educational program to reduce illiteracy among adults. About 90 percent (2008) of the adult population is considered to be literate. The general level of education requires considerable improvement. Approximately 9.5 percent of enrolled students go on to higher education.

Improvements in the public's education levels have been observed, compared to the previous decade.

Living standards

The standard of living of a large proportion of the population is very low, while that of the top stratum is extremely high. Whilst improving, this income gap between the rich and poor has been a constant preoccupation of successive governments. Basic social indicators underscore the differences in regional development.

GDP per capita was approximately US\$11 thousand in 2010.

Cultural and social life in Brazil

With its mixed background of Portuguese, Italian, German, Japanese, East European, Middle Eastern and African immigrants, Brazil offers a wide diversity of cultural and social activities depending on the region of the country. Most major cities support cultural institutions. Leisure and recreation activities are mainly outdoors, taking advantage of the favourable climate. Many social clubs in Brazil offer extensive sports and social facilities.

The attitude of local business community towards foreign investment

In general, the attitude of local businessmen towards foreign investment is welcoming. Certain sectors have exerted strong lobbying pressure in order to protect their activities, including the imposition of trade barriers and the establishment of restrictions on foreign investment. In the past, such political pressure was quite successful but since the early nineties, the government has gradually improved this situation as it seeks to generate more efficiency and competitiveness in the business environment.



Workforce attitude towards foreign investment

If foreign investment and management can be seen to bring jobs and compete on an equal basis with Brazilian businesses, the attitude of the workforce tends to be welcoming.

Cultural perception of Due Diligence

The need for a potential investor to perform detailed analysis and due diligence has been accepted by sellers of local businesses in Brazil. However, the purposes of due diligence are not always clear in the minds of local businessmen and the staff of target companies. It is sometimes thought to be some form of audit work or to be limited to an analysis of the company's financial, tax and legal positions.

The existence of generally less homogeneous accounting and reporting systems, and less sophisticated financial and accounting departments in medium and small sized Brazilian companies, renders the preparation of due diligence information and the execution of due diligence exercises generally more difficult and time-consuming than in more developed countries.

5 *Accounting Principles and Audit Requirements*

Audit requirements and practices

Investor considerations

- Public/listed “S.A.” corporations are required to publish their annual financial statements.
- The annual financial statements of all listed companies and all “large companies” (entities with total assets of over R\$ 240 million or annual revenue over R\$ 300 million) must be audited by an independent auditor registered at the Brazilian Securities Commission (CVM).
- Financial institutions and other entities under the jurisdiction of the Central Bank, as well as insurance companies, are required to publish annual and semi-annual audited financial statements.
- The quarterly financial information of listed corporations and financial institutions must be filed with the appropriate regulator (the CVM or Central Bank) and reviewed by an independent auditor.

Statutory requirements

Digital books and records

In January 2007, Federal Decree 6022 instituted the Public Digital Bookkeeping System – SPED, a tool that unifies the activities of receipt, validation, storage and authentication of documents and books which integrate the taxpayer’s commercial and fiscal bookkeeping, through a single, computerized flow of information and the use of digital certification.

SPED is an integrated initiative of the federal financial administration for three different areas: the Digital Fiscal Bookkeeping (*Escrituração Fiscal Digital - EFD*), Digital Accounting Bookkeeping (*Escrituração Contábil Digital - ECD*) and the Electronic Invoice (*Nota Fiscal Eletrônica - NF-e*).

The Accounting SPED – ECD tool is intended to replace the issue of hardcopy accounting books with softcopies. The general journal (*livro diário*), general ledger (*livro razão*), auxiliary books and the trial balances and balance sheets will be generated as part of a set of digital documents. The project includes the presentation of information for the federal, state and, hereafter, municipal tax authorities, as well as for the National Registration Department of Commerce (Departamento Nacional de Registro de Comércio), the Central Bank (BACEN), SUSEP and the Brazilian Securities Commission (CVM). These accounting books must be delivered on the current deadlines.

Audited financial statements

The annual financial statements of the following entities must be audited by independent auditors registered at the CVM, the Central Bank and other government agencies, as applicable:

- Listed corporations
- “Large companies” (as defined above)
- Financial institutions and other entities under the jurisdiction of the Central Bank
- Investment funds
- Stock exchanges
- Insurance companies
- Private pension funds

Financial institutions and insurance companies must also have their semi-annual financial statements audited. The quarterly financial reports of listed entities supervised by the CVM must be reviewed by independent auditors.

When a private corporation does not have independent auditors, the company's audit committee (*conselho fiscal*) may appoint them at the corporation's expense if it is believed that this is necessary for the fulfilment of its responsibilities.

Even when not required by regulation or bylaws, banks and other financiers frequently require audited financial statements from borrowers.

The tax authorities do not require audited financial statements.

Internal auditors cannot be used as statutory auditors.

Auditing standards

Brazilian accounting and auditing standards were recently converged with the International Financial Reporting Standards (IFRS) issued by the IASB and International Standards on Auditing (ISAs) issued by the International Federation of Accountants (IFAC) through the International Auditing and Assurance Standards Board (IAASB).

As part of the accounting standards convergence process the local standard setter (CFC) issued several accounting pronouncements (CPC's) since 2009. These new standards apply to the audits of financial statements for periods ending on or after 31 December 2010.

The information here is not a comprehensive source for assessing and understanding audit requirements and practices. We strongly advise you seek help from your accounting consultants when assessing these matters.

Accounting principles and practices

Investor considerations

- Law 11,638, enacted in 2007, modified the Brazilian Corporate Law and legislation regarding the Brazilian securities market and the CVM. Although the accounting professionals, standard setters and regulators were already committed to seeking convergence with International Financial Reporting Standards (IFRS), these modifications to Brazilian Corporate Law were necessary to provide the flexibility and agility to move forward in that direction.
- Although the convergence process is underway and several new Brazilian accounting pronouncements have been issued to that end, full convergence with IFRS has not yet been achieved. Several differences still remain for the 2010 calendar year.

- Listed companies, financial institutions and insurance companies must prepare their 2010 consolidated financial statements in full compliance with IFRS as issued by the IASB. Their stand-alone unconsolidated financial statements, however, will still be prepared in accordance with accounting practices adopted in Brazil. Other companies are not required to adopt IFRS and may prepare their financial statements in accordance with accounting practices adopted in Brazil.
- We strongly advise prospective investors to seek for help from accounting consultants when assessing potential differences in accounting practices during due diligence investigations.

6

Tax Issues

Preliminary comments regarding the tax environment in Brazil

The tax system is highly regulated and extremely complex and it is difficult, if not impossible, to structure a transaction in order to avoid or eliminate succession liability.

There are also a number of other factors which increase the risk in this area, including the nature of the legislation (sometimes with an emphasis on form rather than substance of transactions), the frequency of tax audits performed by Federal, State and Municipal authorities, the incidence of relatively high penalties and interest charges in the event of non-compliance and an enforcement process which is difficult to predict (and at times arbitrary).

It is also important to consider the fact that the statute of limitations for most taxes and social charges in Brazil is of five years. In case of fraud, the statute of limitations period does not apply.

During the statute of limitation period, a company can be inspected by the federal, state and municipal tax authorities regardless the fact that a certain tax or fiscal period have already been examined. In other words, even though a certain tax or period were already submitted to inspections, it does not mean that the taxpayer cannot be afterwards inspected and assessed by the tax authorities, to the extent that statute of limitations period is still in place.

With respect to succession liabilities in Brazil, the responsibility to pay current and previous tax and labour liabilities, both known and unknown, generally follows the legal entity, based on the concept that the owner of the operating assets or the acquirer of the business unit retains the capacity to generate income and hence, pay the tax or labour liabilities. As a result, whether in structuring the transaction as an asset or a stock acquisition, the buyer steps into the shoes of the previous owner with respect to all tax and labour liabilities and contingencies.

Penalties - Tax debts may be subject to penalties from 20% to 150%. For federal taxes, if the taxpayer voluntarily pays the tax debt before initiating any tax inspection, the penalties shall be imposed at 20% of the tax debt. The penalties are increased to 75% in case the payer is assessed by the relevant tax authorities and to 150% in case of fraud. Both penalties (75% and 150%) can be reduced up to 37.5% and 75%, respectively, if the taxpayer decides not to challenge the assessment made by the tax authorities and pays the tax debts assessed.

Tax treatment for foreign investors

As a general rule, local and foreign investors are treated equally as regards investment and tax benefits. There are no special Federal tax incentives to attract foreign investors, with a few exceptions such as the capital gain taxation.

Stock acquisition

The most common means used by foreign companies to invest in Brazil is through the acquisition of a Brazilian target entity through the purchase of its shares.

This acquisition method has several tax and labour implications for the buyer. From a legal standpoint, the business unit retains its identity in all respects including its taxpayer identification number. As a result, the buyer will step into the shoes of the former owner and be subject to, and primarily liable for, any known and unknown tax and labour contingent liabilities. In addition to this, the buyer will be also primarily liable for any fines and penalties imposed by the tax authorities regardless of whether such fines or penalties relate to target activities prior to or after the transaction. When acquiring the stock of a Brazilian Target Corporation, caution must therefore be exercised so that the major tax and labour contingent liabilities can be identified, measured and analyzed, so that the buyer can factor the cost of the liabilities into the overall investment decision.

Provided that certain conditions are met, foreign investors can benefit from an acquisition structure according which the tax “goodwill” paid for the acquisition of interest in a Brazilian company is tax deductible over a five-year minimum period. For Brazilian tax purposes the tax goodwill would consist of the positive difference between purchase price and the net equity value of the acquired interest in the Brazilian company. Please see further comments in the next pages.

Purchase of assets and assumption of liabilities

A foreign investor may, for a variety of business reasons, structure the acquisition of a Brazilian Target Corporation as an asset purchase of the business unit (operating assets), and assume part or all of the related liabilities. Unlike a stock acquisition, the acquirer will be secondarily liable for the income tax liabilities but will be primarily liable for VAT taxes (ICMS, PIS, COFINS and IPI) and labour liabilities. In addition, it is not common to structure a transaction as an asset acquisition in Brazil because the transfer of assets will typically trigger additional VAT taxes (ICMS, PIS, COFINS and IPI).

Types of investment mechanisms in Brazil

Besides the private deals, a foreign investor has mostly two other alternatives of investing in a Brazilian Corporation, which are often used. They are (i) acquiring shares directly on the Brazilian stock exchange market and (ii) investing on FIP (Equity Investment Funds). Accordingly, under certain circumstances the capital gains on the disposal of such investments made in the Brazilian Corporations are not subject to local taxation, provided they meet certain requirements, as per local tax and corporate legislation.

In summary, capital gains derived from sales of shares of listed companies on the Brazilian Stock Exchange (Bovespa) are subject to taxation at a 0% rate when the foreign investor is not located in a jurisdiction considered by the Brazilian tax authorities as a low tax jurisdiction (“tax havens”) and the investment was made in accordance with the Brazilian Monetary Council (i.e. investors qualified by the Resolution 2,689, issued by the Brazilian Central Bank).

In regards to an foreign investment through a FIP, in summary, non-residents investors may be granted to a 0% taxation provided that certain conditions are met such as: (i) 90% or more of the FIP’s portfolio must consist of shares, convertible debentures or warrants issued by Brazilian companies; (ii) debt instruments cannot exceed 5% of the total FIP’s portfolio; (iii) FIP quota holders (individually or together with related parties) must not hold 40% or more of the total quotas issued by the Brazilian FIP (iv) FIP quota holders (individually or together with related parties) cannot benefit for 40% or more of the income arising from the FIP; and (iv) a direct foreign quota holder of the FIP cannot be domiciled in a tax haven.

CFC rules

Brazilian resident companies are taxed on worldwide income. Foreign branch profits are taxed as earned and foreign subsidiary profits are taxed when distributed or made available to the Brazilian controlling company. Profits are considered available to the Brazilian controlling company at the time the CFC closes its financial statements at the end of its fiscal year.

The CFC's profits are subject to Brazilian corporate income taxes at the combined rate of 34%. Double taxation is avoided by means of foreign tax credits.

There are no tax breaks to encourage the location of multinational companies' headquarters and administrative offices in Brazil and/or the use of Brazil as a base for offshore financial operations.

Investing directly from abroad X Investing through a Brazilian vehicle

The advantage of investing in Brazil through a Brazilian vehicle is that this alternative may allow a potential tax deduction in Brazil of eventual tax goodwill paid upon the acquisition, which is not possible in Brazil if the acquisition is directly from a company abroad.

Note that, in theory, the existence of an intermediary holding company is neutral from a pure tax perspective, as dividends distribution is not subject to taxation. However, it may naturally bring some additional administrative costs to the group as well as determine an additional taxation of any interest on net equity paid by the operating company to the holding entity by the PIS and COFINS (two social contribution on revenues levied at a 9.25% combined rate).

Tax Goodwill Amortisation

In order to benefit from the tax goodwill deduction for local tax purposes the acquisition of interest in a Brazilian company is made through the incorporation of a Brazilian vehicle company or through an existing Brazilian entity. For Brazilian tax purposes, tax goodwill is the difference between the purchase price and the corresponding net equity of the target company.

The tax goodwill amount paid in the acquisition of interest in a Brazilian company, after the merger of the Brazilian vehicle into the operating entity (or vice-versa), if paid due to the future profitability of the acquired company, may be deducted for local tax purposes in a 5 year (minimum) to 10 year period (maximum).

One relevant requirement that has to be observed where using the tax structure above, among others, consists of providing evidence that the acquisition structure is supported by consistent economic reasons (business purposes). The evidence that the structure was established with the only purposes of reducing the tax burden may jeopardize the tax goodwill deduction.

As from January 2008, the goodwill concept changed for local corporate and accounting purposes. For accounting purposes, the cost of the investment acquired would have to be allocated to the fair value of the assets and liabilities of the acquired company and, if part of such acquisition cost could not be allocated, the remaining amount would have to be recorded in as an intangible asset, not subject to any amortization, named goodwill. Accordingly, there are rumours that the relevant authorities are discussing potential changes with respect to tax goodwill amortization for local tax purposes. Some rumours indicate that the tax goodwill amortization period would be no longer based on a 5 to 10-year period but would be in line with the accounting rules above.

In this case, the benefits arising from the tax goodwill would be subject to a longer period of amortization, if any. There are also rumours indicating that the tax benefit would be simply ceased.

Thin Cap rules

Interest paid or credited by a Brazilian entity to a related party abroad (individual or legal entity), which was not constituted in a tax haven or in a jurisdiction with privileged tax regime, may be deducted for income tax purposes if the interest expense is viewed as necessary for the activities of the local entity and the following requirements are met:

- I. the debt amount granted by the foreign related party (which has participation in the Brazilian entity) does not exceed twice the amount of its participation in the net equity of the Brazilian entity;
- II. the debt amount granted by a foreign related party (which does not have participation in the Brazilian entity) does not exceed twice the amount of the net equity of the Brazilian entity;
- III. the total debt amount granted by foreign related parties as per (i) and (ii) does not exceed twice the sum of participation of all related parties in the net equity of the Brazilian entity; or in case debt is only granted by related parties that do not have a participation in the Brazilian entity;
- IV. the total debt amount granted by all of these related parties does not exceed twice the amount of the Brazilian entity's net equity.

If one of the mentioned 2:1 ratios is exceeded, the portion of interest related to the excess debt amount is not deductible for Brazilian income tax purposes.

Similar provisions are also applicable to interest paid or credited by a Brazilian entity to an individual or legal entity (whether or not a related party) resident or domiciled in a tax haven or in a jurisdiction under privileged tax regime. In this case, the interest expenses is deductible for Brazilian income tax purposes if it is viewed as necessary to the company's activities, as referenced above, and the total amount of the Brazilian entity's debt with any foreign party resident or domiciled in a tax haven or in a jurisdiction under privileged tax regime, does not exceed 30% of the Brazilian entity's net equity.

The two above-mentioned limits (2 to 1 and 0.3 to 1 debt to equity ratios) also apply to cases where a guarantor, representative or any other intervening party is a related party or resident of a tax haven / privileged tax regime jurisdiction (respectively).

The Law also provides that amounts paid, credited, delivered, used or remitted under any title, directly or indirectly, to related or unrelated individuals or legal entities which are resident or domiciled in a tax haven or in a jurisdiction under privileged tax regime are deductible for Brazilian income tax purposes if all of the following conditions are met: (i) the effective beneficiary of the payment is identified; (ii) there is evidence that the beneficiary has operational capacity (i.e., substance); and (iii) there is adequate documentation to support the relevant payments and the corresponding supply of goods, rights or utilization of services.

Brazilian Double Taxation Treaties Network

Brazil has a limited network of Double Taxation Treaties entered with other countries (around 30). It includes Austria, Belgium, Canada, China, South Korea, Denmark, Spain, France, Netherlands, Italy, Japan, Luxembourg, Norway, Portugal and Sweden among others. Brazil does not have tax treaties entered with USA and UK, but have Reciprocity Agreements entered with such countries which allow, in theory, the utilization of tax credits derived from payment of income tax in the other country.

In terms of potential reductions on the withholding income taxation, the benefits allowed by the Treaties are limited. The advantage is much more related to Tax Credit allowed in one and the other country.

The adoption of a determined country to be used as a Holding Company for a Brazilian investment varies from case to case depending on the specific details of each case. However, in general terms, The Netherlands, Spain, Luxembourg and Austria are considered to be advantageous jurisdictions mostly because of the Tax treaties entered with Brazil and vis-à-vis the specific clauses related to tax credits availability.

Corporate legislation

Brazilian corporate legislation has been changed through Federal Law 11,638/07, which affected significantly accounting practices in Brazil as from January, 1st 2008. The main goal of this new rule was change the Brazilian GAAP towards the IFRS. As a consequence, such changes had tax implications as well.

In December 2008, through the Provisional Measure n° 449, Brazilian Government introduced the Transitory Tax Regime - “RTT” in order to neutralize the potential tax effects derived from new accounting methodologies brought by Law 11.638/07. In summary, according to the RTT, corporate taxpayers would avoid any adverse tax effects derived from the new corporate legislation, i.e. ensuring that the company could be taxable as if the corporate and accounting rules valid up to December 31, 2007 were still in force (related exclusively to the tax perspective).

Background information on the main taxes and contributions in Brazil

The main Federal, State and Municipal taxes are as follows.

Taxes	Statutory Rates	Comments
Corporate Income taxes - Corporate Income Tax (IRPJ) and Corporate social contribution net income (CSL)	25% ¹ and 9%	IRPJ and CSL are determined based on the calendar year, with monthly tax payments, and are generally computed on the basis of annual or quarterly taxable income.
Taxes on revenues - Contribution for the Social Integration Program (PIS) and Contribution for Social Security Financing (COFINS)	1.65% and 7.6% ²	<p>PIS and COFINS are levied on gross income. Companies are entitled of PIS and COFINS credits on the acquisition of certain inputs and services (non-cumulative methodology similar to a VAT³).</p> <p>PIS and COFINS contributions apply on the imports of goods and services to non-residents.</p> <p>Export revenues are tax exempt.</p>
Federal Excise Tax (IPI)	Various rates ⁴	<p>IPI is paid by manufacturers on behalf of their customers at the time of sale, either to another manufacturer who will further the manufacturing process or to the retailer who sells to the end user. When manufactured products are sold between producers, the IPI is imposed. However, the subsequent manufacturer is allowed a credit against its IPI liability, equal to the IPI paid to its suppliers (non cumulative tax).</p> <p>IPI is also imposed on import of goods. Export revenues are tax exempt.</p>
Import tax (II)	Various rates ⁵	Import tax is levied on the CIF price and is a cost to the company (not recoverable).

¹ IRPJ is charged at the rate of 15% plus a surcharge of 10% on annual taxable income in excess of R\$ 240,000 (approximately US\$ 120.00).

² Higher rates are imposed in certain sectors (such as automotive).

³ Certain companies pay PIS and COFINS under the cumulative system, which imposes a lower rate combined rate of 3,65% but does not enable the taxpayer to record any tax credits on acquisitions.

⁴ The rate is defined by the product's tax code according to the Harmonized System.

⁵ The rate depends on the degree of necessity and is defined by the product's tax code according to the Harmonized System.

Taxes	Statutory Rates	Comments								
Value-added tax on sales and services (ICMS)	17, or 18% internal rate ⁶	<p>ICMS is a State tax calculated on the circulation of goods and on the rendering of interstate and inter-municipal transportation services, communication and on electricity, even when the transaction and the rendering of services start in another country. The tax is only assessed on the increase in the price of the product in each part of the circulation process.</p> <p>ICMS is also imposed on imports. Export revenues are tax exempt from ICMS.</p> <table border="0" data-bbox="477 412 876 511"> <tr> <td></td> <td style="text-align: right;">%</td> </tr> <tr> <td>Intrastate transactions</td> <td style="text-align: right;">17 to 18</td> </tr> <tr> <td>Interstate transactions</td> <td style="text-align: right;">7 to 12</td> </tr> <tr> <td>Most imports</td> <td style="text-align: right;">17 to 18</td> </tr> </table>		%	Intrastate transactions	17 to 18	Interstate transactions	7 to 12	Most imports	17 to 18
	%									
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Interstate transactions	7 to 12									
Most imports	17 to 18									
Service Tax (ISS)	2% to 5%	<p>The ISS is a municipal tax levied on gross revenues for certain services as per the Federal Government.</p> <p>In general, the service tax is levied by the municipality in which the Company is headquartered. There are some exceptions to this rule for services involving assembly, construction, demolition, among others</p> <p>ISS also applies on the import of services.</p> <p>ISS is not levied on exports of services, except when the services are rendered in Brazil or the results of these services are applied in Brazil.</p>								
Withholding Income Tax (IRRF) - Dividends	Not taxed	Dividends are no taxed no matter the location of the recipient.								

⁶ ICMS internal rate corresponding to 17%, except for the States of São Paulo, Minas Gerais and Paraná, whose tax rate is 18% and Rio de Janeiro, whose rate is 19%. Some products exceptionally trigger a higher rate (in case of cosmetics industry) or a lower rate (in case of automotive industry).

Taxes	Statutory Rates	Comments
<p>Withholding Income Tax (IRRF) (Cont'd)</p> <p>- Interest</p>	<p>15%⁷ or 25%⁸</p>	<p>Interest expenses payable to related parties located abroad are subject to transfer pricing and thin capitalization rules.</p> <p>In regards to the transfer pricing rules, the loan contract should be registered with the Brazilian Central Bank (BCB) otherwise the maximum interest rate for this non-registered loan (i.e. the deductible maximum interest rate) should not be higher than a Libor (in US Dollars, for six months) plus 3% interest rate.</p> <p>The Brazilian Central Bank usually accepts (and provides the register) loan contracts which interest rates are consistent to the market rates.</p> <p>If the loan is borrowed from a lender located in a low tax jurisdiction or from a lender party subject to privileged tax regimes the thin capitalization and transfer pricing rules apply even if the lender is not a related party.</p> <p>Interest related to domestic loans is subject to the Brazilian withholding income tax at a 22.5% to 15% regressive rate, depending on the time where interest are paid (e.g. interest paid in less than 180 days are subject to a 22.5% tax rate, from 181 to 360 days - 20%, 361 to 720 days - 17.5% and more than 720 days - 15% tax rat).</p> <p>Domestic loans are also subject to the IOF (tax on financial, exchange and insurance transactions) at a 0.38% plus a 0.0041% daily rate (limited to 365 days or 1.5%), levied on principal amount of credit still not liquidated. In other words, the IOF would be levied at a 1.88% rate if the debt consists of a long-term (more than one year) loan contract.</p> <p>Long-term international loans (more than 720 days period) are subject to the IOF at a 0% rate. Short-term international loan (less than 720 days period) are subject to the IOF (levied only on the loan principal amounts) at 6% rate. Please see further comments in this Section regarding the IOF taxation.</p>

⁷ These rates are effective unless otherwise specified by tax treaty.

⁸ Payments of any type made to tax havens, defined as jurisdictions that do not tax income or tax income at a rate lower than 20%, and classified by the Brazilian local tax authorities as Tax Haven according to the "Blacklist", will be subject to withholding at a rate of 25%.

Taxes	Statutory Rates	Comments
<p>Withholding Income Tax (IRRF) (Cont'd)</p> <ul style="list-style-type: none"> Royalties and services 	<p>15%⁹ or 25%¹⁰</p>	<p>In the case of royalties, the royalty contract has to be approved by the National Institute of Industrial Property (INPI) and filed with the Brazilian Central Bank.</p> <p>Deductions for royalties are generally limited up to 5% of net sales of the relevant products or services; the percentage depends on the type of product or activity.</p> <p>Royalties for the use of trade marks and trade names, for whatever type of production or activity, when the use of the mark or name does not result from the utilization of a production patent, process or formula, are deductible up to 1% of net sales.</p> <p>In addition to the withholding income tax, royalties and service fees paid to foreign parties are subject to the Contribution for Intervention in the Economic Domain (CIDE) at the rate of 10 percent and to the PIS and COFINS at a 9.25% combined rate. These are taxes borne by the Brazilian service contracting company.</p> <p>Fees corresponding to services provided by foreign parties are subject to the Municipal Service Tax (ISS) at a 2% to 5% rate.</p> <p>Besides the withholding income tax, remittances or payments of royalties or service fees to abroad are subject to the IOF at a 0.38% rate. This taxation is imposed due to the conversion of the amount of royalties and service fees from Brazilian Reais into foreign currency. Please see further comments in this Section regarding the IOF taxation.</p>

⁹ These rates are effective unless otherwise specified by tax treaty.

¹⁰ Payments of any type made to tax havens, defined as jurisdictions that do not tax income or tax income at a rate lower than 20%, will be subject to withholding at a rate of 25%.

Tax Consolidation

The Brazilian Tax Laws do not contemplate the possibility of consolidated returns and/or group relief. Therefore, the entities from the same group are not allowed to consolidate the income and deductions of the members in order to submit to taxation the net income of the group. Considering this, each Company of the group must separately file its annual income tax returns to the local authorities.

Tax losses carry forward (IRPJ and CSL)

There is no time limit for the carry forward of tax losses. However, the taxable profit of each year can only be reduced by tax losses up to a maximum of 30%. Furthermore, it is neither possible to carry back tax losses nor transfer tax losses to other Brazilian companies. Tax losses of an acquired company cannot be carried forward to be offset against the taxable income of a new activity if the following two conditions are simultaneously met:

- a) modification in the ownership of the company; and
- b) modification in the activity of the company.

Interest on capital

Entities are allowed to remunerate their shareholders by way of interest on capital payments, subject to certain limitations (i.e., limited to TJLP - Long Term Interest Rate - and limited to 50% of current or accumulated profits). This payment is deductible for corporate income tax purposes and for social contribution on net income purposes, as well. These payments are subject to a 15% withholding tax (or 25% for tax haven jurisdiction).

During the first quarter of 2011, the applicable TJLP rate was 6% per year.

Payments made to tax havens' beneficiaries

Any payments directly or indirectly made to beneficiaries resident or incorporated at tax havens are not tax deductible, except when the following requirements are cumulatively observed: (i) identified beneficiaries; (ii) operational capacity of the non resident to perform the transaction; and (iii) payments, receipt of goods, rights an use of services are evidenced with proper documentation.

Capital gains

Capital gains derived from the sale of Brazilian assets (including shares) by non-resident shareholders are subject to the withholding income tax at a 15% rate (unless otherwise specified by international tax treaty), even if both vendor and buyer parties are domiciled abroad. In case of sale of shares, capital gain will correspond to the difference between the purchase price of the shares and the amount of foreign capital, in foreign currency, registered within the Brazilian Central Bank.

As a general rule, the local buyer is responsible for withholding and paying the withholding income tax levied on the capital gain earned by a foreign vendor. When both parties, buyer and vendor, are not located in Brazil, the local attorney-in-fact representing the foreign buyer in Brazil is the responsible for withholding and paying the withholding income tax.

Capital gains earned by foreign parties located in low tax jurisdictions (tax havens) are subject to the withholding income tax at a 25% rate.

Repatriation of capital in excess of the cost of the non-residents' investments in Brazil is subject to capital gains tax at 15% (or 25% for tax haven jurisdiction).

Capital gain derived from the sale or transfer of shares by a Brazilian resident company is subject to the Brazilian Income taxes (IRPJ and CSLL) at 34% combined rate.

Provided that some requirements are fully met, there are capital gain exemptions in case of the transactions are carried out by foreign investors, such as: i) in our local Stock Exchange Market; and ii) in private deals when it is structured through a local FIP (Equity Investment Fund).

Individuals domiciled in Brazil are taxed at the rate of 15% on capital gains.

Financial Transactions Tax (IOF)

As a general rule, foreign exchange transactions made in order to allow payments to non residents, considering royalties, technical services, and other payments, including the reimbursement of costs, are subject to IOF.

The regular IOF rate for foreign exchange transactions (both inbound and outbound) currently applied corresponds to 0.38%. Investments made through the Brazilian stock market or via Equity Investment Funds (FIP) are currently taxed by the IOF at a 2% rate, only on the inflow of foreign capital into Brazil. The return of investment is not subject to IOF. The IOF may not be avoided if the payment requires a foreign exchange transaction from Reais to a foreign currency, or from a foreign currency into Reais.

IOF is also levied at various rates, on loans and credit operations, securities transactions, foreign exchange transactions and insurance policies.

IOF at a 6% rate is charged on foreign loans with an average maturity of less than 720 days. All other long-term foreign loans are subject to IOF at 0% rate. The average maturity is determined based on the balance of the loan relative to the number of days of the outstanding balance of the related loan.

Other taxes on payments to non-residents

A Brazilian company with royalty, license or service agreements with foreign entities must pay a 10% Economical Domain Intervention Contribution (CIDE) based on the amounts paid abroad.

PIS and COFINS contributions, ISS and withholding income tax also apply on the payment of services to non-residents.

Tax Havens and Privileged Tax Regimes

Most payments (except dividends) made to tax havens, defined as jurisdictions that do not tax income or tax income at a rate lower than 20%, are subject to a withholding income tax at a rate of 25%. Indeed, Brazilian local tax authorities issue from times to times a “Blacklist” where the countries/jurisdictions classified as Tax Havens are referred to.

The Brazilian IRS released (on June 4th, 2010) a Normative Instruction (IN 1,037/2010) changing the Brazilian tax havens Blacklist.

Tax Havens’ Blacklist (according to the IN 1,037/2010)



Andorra, Anguilla, Antigua and Barbuda, Aruba, Ascension Island, Bahamas, Bahrain, Barbados, Belize, Bermuda, British Virgin Islands, Brunei, Campione D’Italia, Canal Islands, Cayman Islands, Cook Islands, Costa Rica, Cyprus, Djibouti, Dominica, French Polynesia, Gibraltar, Grenada, Hong Kong, Isle of Man, Kiribati, Labuan, Malaysia, Lebanon, Liberia, Liechtenstein, Macau, Madeira Island, Maldives, Malta, Marshall Islands, Mauritius, Monaco, Montserrat, Nauru, Netherlands Antilles, Norfolk Island, Niue, Pitcairn Islands, Panama, Queshm Island, Saint Helena, Saint Kitts and Nevis, Saint Pierre and Miquelon, Samoa, Samoa Island (American), San Marino, Seychelles, Singapore, Solomon Islands, St. Lucia, St Vincent and Grenadines, Sultanate of Oman, Swaziland,

Switzerland (suspended from the list), Tristan da Cunha, Tonga, Turks and Caicos, United Arab Emirates, US Virgin Islands and Vanuatu.

A second list of “Privileged Tax Regimes” has been created. This list encompasses the following regimes/entities:

- Uruguayan SAFIs;
- Danish Holding companies which do not perform significant economic activities;
- Dutch Holding companies which do not perform significant economic activities (suspended from the list);
- ITCs (Iceland);
- Offshore KFT (Hungary);
- US State LLCs, which interest are owned by non-US residents;
- Spanish ETVEs (suspended from the list); and
- ITC and IHC (both Malta).

Before the Normative Instruction (IN 1,037/2010) there was not a Blacklist of privileged tax regimes. After the IN 1,037/2010 some potential adverse tax consequences should be considered for parties subject to the foreign privileged tax regimes listed above.



In summary, the current understanding of the consequences of the IN 1,037/2010 is that the rules regarding the non-deductibility of payments (interest, services, royalties etc), transfer pricing and thin cap rules are applicable to payments made to and transactions performed with companies or persons located in the jurisdictions listed in the updated tax havens' Blacklist and also to foreign beneficiaries subject to the privileged tax regimes there listed.

For the purpose of the taxation of the Brazilian withholding income tax, only the companies or persons located in the foreign jurisdictions comprised in the tax havens' Blacklist (not in the Blacklist of privileged tax regimes) would be affected. It means that the IN 1,037/2010 would not affect the existing rules regarding the withholding taxation levied on capital gains, foreign investments made via the Brazilian capital market by qualified investors (which are exempt from taxation on capital gains), etc. for foreign companies or persons subject to privileged tax regimes.

7 *Work Force and Labour Charges*

Labour Relations

Labour and management relations

Employer and employee relations are dealt with principally in the labour laws (CLT) enacted in 1943 and subsequent legislation. The labour laws are applicable to all employees in regular registered employment, except for individuals in public employment or domestic labour, who have separate regulations. The labour laws make no distinction between skilled and unskilled workers or between those engaged in manual, office or professional work. Therefore, all types of workers are generally referred to as employees. A change in the legal structure or ownership of an employer does not affect the rights acquired by employees under the labour laws.

Extensive social security laws and labour regulations govern employer-employee relations. However, foreign investors have not experienced much difficulty in the way of labour problems, mainly because they follow local standards and practices.


Background information on labour practices and main social charges in Brazil

Employer's payroll costs in Brazil


Remuneration

Salary and labour rights

Employers are entitled to monthly salary, which may be increased by overtime, night shift additional payment and unhealthy work condition additional payment, among others.



After a 12-month period, employees are entitled to a 30-calendar day paid annual vacation, which must be taken within the subsequent 12 months and compensated at an amount equivalent to 1 month salary plus and 1/3 of bonus.



At the end of each year, employers must pay employees a Christmas bonus (on 13th salary) annual bonus equivalent to 1 month salary.

In addition to the amounts paid to employees as salary, any other amounts which are paid on a regular basis are, for all legal purposes, considered as part of the employee's salary and are, in general, taken into account in the calculation of vacation, 13th salary and the amount that must be deposited in FGTS, as well as termination payments.

A fringe benefit is an additional item granted to an employee in excess of the employee regular salary. Pursuant to the applicable labour legislation, the grant of an award or of any other benefit (such as vehicles) to an employee may be considered a fringe benefit, for the reason that any incentive award or benefit may represent an additional payment and consequently, compensation to the employee. In such cases, the total amount of the employee's earnings (including taxable fringe benefits) shall form the taxable basis for the contributions that should be borne by the employer.

Taxes and contributions on payroll

Social Security Contribution (INSS)

Employers' social security contributions correspond to 20% of the gross payroll (monthly compensation paid to all employees).

Payment of insurance by employers against labour accidents is normally due at rates which vary from 1% to 3% of the total remuneration paid to employees, depending on the "level of risk" presented by the type of activity of the company.

Employers are also required to pay a monthly contribution as the "education salary allowance" equivalent to 2.5% of the total remuneration paid to employees.

Additionally employers have also to contribute to other governmental entities, such as: Inca, SESC, SESI, among other, which respective contribution may reach up to 3.3%

In addition, employers are also responsible for withholding and collecting the INSS on behalf of their employees (who are also subject to INSS at lower and progressive rates).

FGTS

Under the FGTS system, employers must monthly deposit, on the employees' behalf, in a blocked bank account, an amount equivalent to 8% of the remuneration of each employee. The 8% destined to FGTS is borne by the employer, without any discount on the employee's salary.

In case of employee's dismissal, the company will have an additional 50% cost calculated on the balance of the employee's FGTS deposit.



8

Environmental Issues

This section discusses the environment in Brazil. In general, the rules are strict but there are significant opportunities for business.

Environmental impact on businesses

Business in Brazil has to take into account several environmental issues which may become relevant risks if not adequately managed. On the other hand, there are many environment-related aspects in Brazil that may result in real opportunities, such as the abundance and quality of natural resources, the country's climate, the overall concern with environmental protection and the corresponding Brazilian environmental legislation, which is among the most advanced in the world.

Protecting the environment

Key “green” concerns in Brazil include the deforestation of the native and old-growth forests in the biologically rich Amazon Rain forest and other regions, and soil loss due to erosion. The main “gray” areas of attention are the lack of sewage collection, solid waste management, urban, industrial and non-point-source pollution of rivers, lakes, estuaries and shoreline, air pollution in and around some major cities, and questions related to the recovery of mining areas.

Main legislation and regulation

Brazilian legislation extends over a wide variety of environmental issues concerning licenses, zoning, pollution prevention and control and inspection procedures.

Environmental crimes are subject to fines of up to R\$50 million (some US\$30 million)

The environmental legislation was effectively introduced in 1981, when the National Environmental System - SISNAMA – was implemented, including all agencies responsible for the environmental quality. More recently, in 1998, new legislation was passed (the “environmental crimes law”) defining pollution and forest destruction as crimes punishable with heavy fines and, in some cases, jail sentences. These fines can reach amounts up to R\$50 million (equivalent to more than US\$ 30 million).

Furthermore, the acquirer of a Brazilian company or business might become fully or partially responsible for present and past environmental liabilities attached to the acquired asset. The penalties might include not only the fine but also the cancellation of the operating license and the obligation for the recovery of the impacted area. Additionally, in many cases, the issue is made public, thus affecting the company’s reputation. Given this scenario, environmental due diligence prior to acquisition is highly recommended.

Projects for the construction of a new plant or production site must be submitted for approval by the Brazilian environmental authorities. The location and activity will determine the environmental license that should be obtained at federal, regional or local levels. For activities considered as having high environmental impact, a more detailed study of environmental impacts and mitigation (named EIA-RIMA) is required before installation is allowed.

Every plant in operation must obtain an environmental license issued by the Federal Environmental Agency (IBAMA). The license has to be periodically updated (the period varies according to the plant’s location).

Pollution control

Pollution has become a serious concern in many areas and consequently it is now one of the main issues both political and economically. Federal and State governments have developed programs and controls aiming at preventing or reducing pollution, mainly in the more industrialized areas.

The treatment of waste with the purpose of avoiding or reducing pollution must be considered in the installation of new production sites in Brazil or evaluated when acquiring a business.

CONAMA is the federal agency responsible for establishing federal criteria for pollution control. Other state agencies are required to take environmental regulations into account when examining applications for incentives and financing of investment projects. Non-compliance with pollution control regulations may result in the suspension of tax benefits, credit restrictions or even the closing-down of operations.

Sustainability: a growing issue in Brazil

Good environmental management became a relevant business issue as from the discussions at the Rio Environmental Summit in 1992, when the concept of sustainability (i.e., the adequate integration of environmental management, social responsibility and the related economics/value added) gained higher presence in the agenda of the public and private sectors as well as of a major part of the global population.

In many sectors, good environmental management is no longer a competitive advantage but a condition on the ability to compete not only in the global market but also in the Brazilian market.

9 *Our M&A Specialists and Post-Deal Services in Brazil*

PwC in Brazil

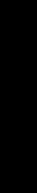
Our 16 offices in Brazil

Offices

- Barueri
- Belo Horizonte
- Brasília
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- Florianópolis
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- Rio de Janeiro
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- São José dos Campos
- São Paulo
- Sorocaba

The Brazilian firm of PwC was formed in 1915. Since then, we have been the leading professional services organization in the country.

- We have more than 140 partners and directors in Brazil, drawing on the experience of nearly 4,100 professionals.
- With 16 offices, we cover the entire Brazilian territory.

- 
- Our “Deals” (Transaction Services and Corporate Finance) group comprises:
 - 26 Partners and Directors
 - 78 Senior Managers and Managers
 - 128 Consultants
 - All partners, directors and staff are segmented into industry sectors: Financial Services, Consumer and Industrial Products, Agribusiness, Telecom, Media, Technology, Government Services.
 - On the Post-Deal side, we have a team of over 150 M&A Pre and Post-deal professionals who provide solutions to all critical aspects of an integration process. Our Synergy Track and 100-Day plan methodologies allow us help clients capture the deal value with the lowest cost and in the shortest timeframe.

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