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**KLA – KOURY LOPES ADVOGADOS
ESTABLISHING A BUSINESS ENTITY IN BRAZIL**



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ESTABLISHING A BUSINESS ENTITY IN BRAZIL



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The two most common types of legal entities adopted in Brazil are the limited liability company (“Limitada” or “Ltda.”) and the corporation (“S.A.”). These are the most attractive types of companies since they are the only types of companies in which you may find, at the same time, all the following advantages: (i) the liability of the equity holders is generally limited to their equity interest (subject to certain specificities described below); (ii) they can be used for any type of business (i.e., services, industry, commerce); and (iii) they do not have minimum capital requirements (sometimes they do, but by reason of the activities conducted, not by reason of their corporate type).

In 2011, a new type of entity, called Eireli (“Empresa Individual de Responsabilidade Limitada”, or Limited Liability Individual Entity) was introduced in Brazil. The Eireli works similarly to a Limitada, but its equity interest is held by a single partner, individual or legal entity (Brazilian or foreign), provided that (i) in case the partner of the Eireli is an individual, he/she may not be a partner of any other Eireli, and (ii) the capital stock of the Eireli must be equivalent to at least one hundred

times the minimum wage in Brazil - which currently amounts to BRL 954.00 (approximately USD 230).

1. **Limitada x S.A.: Summary of the most relevant characteristics and the basic differences.**

The Ltda. is governed by the provisions of the Brazilian Civil Code, law 10,406/02 (the “Civil Code”), and the S.A. is governed by the Corporation Law, law 6,404/76 (the “Corporation Law”). The Articles of Association of a Ltda. may provide that the Ltda. shall be subsidiarily governed by the Corporation Law, in which case such law will apply whenever the Civil Code regulations are silent on any subject.

An S.A. may be either publicly or closely held. A publicly held S.A. must be registered with the Brazilian Securities and Exchange Commission (“CVM”), and has its stock traded in the Stock Exchange. A closely held S.A. is a private entity, which does not issue shares to the public. For purposes of this article, we will consider only the characteristics of a closely held S.A.

The charts below present a comparative analysis of the most relevant characteristics and the basic differences between a Ltda. and a S.A.

**COMPARATIVE CHART BETWEEN THE LTDA. AND THE S.A.**

A. General Aspects: In general, the main differences between a Ltda. and a S.A. are the following:

	LTDA.	S.A.
Holders	Holders of the Ltda. are called partners.	Holders of the S.A. are called shareholders.
Governing Documents	The Ltda. is governed by the Articles of Association (“Contrato Social”).	The S.A. is governed by the By-laws (“Estatuto Social”).
Capital Stock	Capital is divided into quotas, which ownership is reflected in the Articles of Association. All quotas must have voting rights and an indicated par value.	Capital is divided into shares, which ownership is reflected in the company’s corporate books, and may also be represented by certificates (no longer a common situation). There may be preferred shares with no or limited voting rights, and there may be shares with or without a par value.
Transfer of Interest	Articles of Association must be amended for the quotas to be transferred. Transfer of quotas to a third party may be opposed by partners representing more than ¼ of the capital stock.	Transfers of shares are registered in the company’s corporate books. No need to amend the By-laws.
Securities	The Ltda. may not issue debentures, warrants and other securities or convertible bonds.	The S.A. may issue debentures, warrants and other convertible bonds (even a closely held S.A., no need to be publicly held).
Minimum Capital	No minimum capital must be paid in at the time of formation of the Ltda.	10% of the subscribed capital must be paid in at the time of formation of the S.A.
Dividends	No minimum dividend payment required. Payment of dividends may be pro-rata or not to the partners’ equity interest.	A minimum dividend must be provided in the By-laws. Payment of dividends must be pro-rata to the shareholders’ equity interest.
Management	At least 1 individual, resident in Brazil.	At least 2 individuals, residents in Brazil.
Publications	No need to publish financial statements and minutes of Meetings in newspapers, if the Ltda. is not considered as a “large size company” (please see details below).	Publication of financial statements and minutes of Meetings in newspapers is required, with few exceptions.



B. Partners/Shareholders and Capital Stock

	LTDA.	S.A.
Partners /Shareholders	Minimum of 2 partners required, individuals or legal entities, Brazilian or foreign. The foreign partners must be represented by a Brazilian resident and will be required to obtain a taxpayer registration number. For the representation in meetings or assemblies, the Brazilian resident must be either one of the other partners or a lawyer.	Same as in the Ltda. In relation to the representation, foreign shareholders may be represented by another shareholder, an officer or a lawyer, all residents in Brazil.
Liability	Until the capital is fully paid in, the liability of the partners is limited to the total amount of the capital. After the capital has been fully paid in, the liability of the partners is limited to their equity interest.	The liability of the shareholders will be limited to their equity interest, whether or not the company's capital stock is fully paid-in.
New Partners/ Shareholders	The admission of a new partner may be opposed by partners representing more than ¼ of the capital stock. In addition, the Articles of Association or a partners' agreement may impose limitations and/or rights of refusal for the transfer and sale of quotas.	The By-laws or a shareholders' agreement may impose limitations and/or preference rights for the sale of shares.
Capital Contribution	May be paid in cash (national currency), credit or assets.	Same as in the Ltda.
Capital Increase/ Preference Rights	Only possible if 100% of the prior capital subscriptions have been fully paid in. Partners have the right of first refusal for the subscription of newly issued quotas, pro-rata to their equity interest.	Only possible after ¾ of the current corporate capital is paid in. Shareholders have the right of first refusal for the subscription of newly issued shares, pro-rata to their equity interest.
Amendments to the Governing Documents	The following actions, among others, require the amendment of the Ltda.'s Articles of Association, subject to the approval of partners representing 75% of the capital: <ul style="list-style-type: none"> • change of the corporate name, address, purposes or duration • changes to the capital stock (increase or reduction) • changes to management provisions • super majority requirements 	Same as in the Ltda., but the changes to the By-laws require approval of shareholders representing 51% of the capital stock.



C. Management

	LTDA.	S.A.
Structure	Minimum of 1 manager.	Board of Officers with at least 2 members (mandatory). May also have a Board of Directors with at least 3 members (optional).
Characteristics of Managers	Managers may be partners or non-partners and must be Brazilian residents (no nationality requirement).	Members of the Board of Officers must be Brazilian residents (no nationality requirement). Members of the Board of Directors may be foreigners and/or non-residents (no nationality requirement). The foreign Directors must be represented by a Brazilian resident for purposes of receiving service of process and such power of attorney must be valid for 3 years following the date the Director ceases to be a Director of the S.A.
Board of Directors	There are no specific requirements for a Board of Directors in a Ltda. and it is not common to have such type of board in a Ltda. If provided in the Articles of Association, such board, in practice, would have a “consulting” function.	In general, not required, but if existing, the Board has a more “robust” purpose, with exclusive functions assigned by law. One-third of the members of the Board of Directors may simultaneously be members of the Board of Officers.
Control of the Management by Partners/Shareholders	Certain matters (such as spin-offs, mergers, liquidation, etc.) depend on the approval of the partners. Additional limitations to management’s authority may be inserted in the Articles of Association.	Certain matters (such as spin-offs, mergers, liquidation, etc.) shall be submitted to the decision of the Board of Directors (if existent) and the Shareholders Meeting. Additional limitations to management’s authority may be inserted in the By-laws.
Election	Managers are always elected by the partners.	The members of the Board of Directors are always elected by the shareholders. The members of the Board of Officers are elected by the Board of Directors, if existent, or directly by the shareholders.
Board of Auditors	Not mandatory. It may be provided for in the Articles of Association and, if so, shall be composed by 3 or more members and their alternates. Members may be partners or non-partners and must be Brazilian residents (no nationality requirement).	Mandatory, but the shareholders may decide, at each Annual Shareholders Meeting, if it will be convened or not. When convened, shall be composed by 3 to 5 members, who may or not be shareholders, cannot be an officer or a director and must be Brazilian residents (no nationality requirement).



D. Other Characteristics

	LTDA.	S.A.
Partners’/Shareholders’ Meetings Quorum	Most important decisions require a quorum of ¾ (75%) of the capital (including amendments to the Articles of Association, capital contributions, changing the purposes of the Ltda., amalgamation, merger, dissolution, or termination of liquidation of the company). Other decisions, such as approval of the financial statements, may be approved with a majority vote. Articles of Association and partners’ agreement may establish super majority decisions.	Decisions taken by majority vote. The By-laws and shareholders’ agreement may establish super majority decisions.
Meetings’ Calls	The Articles of Association may establish its own procedure to convene the company’s meetings, except if the company has more than 10 partners, in which case the call notices shall be published 3 times, 8 days in advance for the first call and 5 days for a second call. A Meeting’s call may be waived if all partners attend the Meeting.	Call notices for Shareholders Meetings shall be published 3 times, 8 days in advance for the first call and 5 days for a second call. A Meeting’s call may be waived if all shareholders attend the Meeting.
Publishing Requirements	For the time being, the need to publish financial statements is under discussion. There is a debate about whether Ltda. that are considered as “large size companies” should be required to publish their financial statements. “Large size companies”, pursuant to a legal definition, are a company or group of companies under common control that had, in the prior fiscal year, total assets exceeding BRL 240,000,000.00 or annual gross revenues exceeding BRL 300,000,000.00. Ltda. which do not fulfill these conditions are not required to publish the financial statements. Minutes of Partners Meetings or Articles of Association, except in specific cases must be published (such as merger, spin-off, capital reduction and transformation into another corporate type, among others).	Financial statements, Minutes of Shareholders’ Meetings and incorporation documents must be published with the Official Gazette and another newspaper with great circulation.
Audited Financial Statements	Only required for “large size companies”, as defined above.	Only required for (i) publicly held, and (ii) “large size companies” as defined above.
Case Law	No recent case law, since the new Brazilian Civil Code was enacted in 2002. Therefore, case law on Ltda.’s is not yet consolidated.	The S.A. Law was enacted in 1976 and, therefore, case law on S.A.’s is more consolidated.



2. Necessary Information

The formation documents of the Brazilian entities shall necessarily contain, at least, the following information:

- (a) Partners/Shareholders. Name and identification of the partners/shareholders. Foreign partners/shareholders need to obtain a taxpayer registration in Brazil (which is a simple procedure).
- (b) Name of the Company. In the case of the Limitada, it must include the company's main activity.
- (c) Purposes of the Company. Tax aspects should be observed when specifying the activities to be conducted by the company.
- (d) Complete Address. It is necessary to establish the full address of the head office and branches (if any).
- (e) Term of duration. May be either determinate or indeterminate.
- (f) Capital Stock. Amount of the capital, necessarily in Brazilian currency. The capital stock may be paid-in in national currency, credits or assets (in case of the S.A., if payments are in assets, such assets shall be subject of an evaluation report prepared by an expert, usually an accountant).
- (g) Quotas/Shares. Number of quotas (Limitada) or shares (S.A.) held by each partner/shareholder and how these quotas/shares will be paid in. Usually (but not mandatorily), the quotas or shares have the par value of BRL 1.00. In the S.A., it is possible to establish that the shares have no par value. The shares of the S.A. may be either ordinary or preferred shares, which preference is related to

either political or economic advantages. Preferred shares may or may not have voting rights, provided that the number of non-voting shares is limited to 50% of the total shares issued by the S.A. The Limitada may also have preferred quotas, although this is not usual since the Civil Code expressly prohibits quotas with no voting rights.

- (i) Manager. Appointment of the individuals who will act as (i) managers of the Limitada (at least one, who shall be resident in Brazil); or (ii) officers of the S.A. (at least two, who shall be resident in Brazil) and, if applicable (iii) directors of the S.A. (at least three, who do not need to be resident in Brazil).
- (j) Dividends. Provision on how dividends and losses will be allocated among the partners/shareholders.

3. Formation Procedures.

- 3.1. Limitada:** A Limitada is formed in Brazil through the filing of its Articles of Association with the Board of Commerce of the State where the company will have its headquarters. The Board of Commerce of the State of São Paulo takes approximately two to three weeks to file the Articles of Association. After the Articles of Association are filed, the Limitada will be considered as validly existing in Brazil. There is no need to publish the Articles of Association.
- 3.2. S.A.:** An S.A. is formed in Brazil through the filing, with the Board of Commerce of the State where the company will have its headquarters, of the Minutes of Shareholders Meeting approving the formation of the S.A. and its bylaws. After registration, the Minutes must be published at the State Official Gazette and another newspaper of the city



whereby the company's headquarters are located. The S.A. also needs to open and registry certain corporate books, as legally provided.

4. Registrations.

After its formation, the Brazilian company shall obtain the following basic additional registrations, whenever applicable:

- (a) Federal Taxpayer Registration (CNPJ/MF):
- required for all companies. The registration is obtained simultaneously with the registration with the Board of Commerce, upon the company's incorporation. After such registration, the company will be able to open a bank account and sign contracts. Estimated time for conclusion: approximately 2-3 weeks.
- (b) State Taxpayer Registration (required only for companies involved, directly or indirectly, in the manufacture or sale of goods). The registration is obtained simultaneously with the registration with the Board of Commerce, upon the company's incorporation. After such registration, the company will be able to issue invoices related to the manufacture or sale of goods. Estimated time for conclusion: approximately 2-3 weeks, or more in case of manufacturing companies, industries or other similar companies.
- (c) Municipal Taxpayer Registration (CCM - required for all companies). Estimated time for conclusion: approximately 5 days.
- (d) Municipal Service Tax Registration (ISS - required for companies involved, directly or indirectly, in the rendering of services). After such registration, the company will be able to issue invoices related to the rendering of services. Estimated time for conclusion: depends on each Municipality requirements, but average timing is 15 days.
- (e) Ministry of Labor and Social Security registrations (required for all companies). Estimated time for conclusion: approximately 5 days.
- (f) Brazilian Central Bank (required for all companies with foreign partners/shareholders). Estimated time for conclusion: approximately 2 days.
- (g) SISCOMEX (Integrated System of Foreign Trade - required for companies operating in foreign trade in Brazil, performing imports or exports), for the obtaining of an import license called "Radar" – Registration System for Tracking the Activities of Foreign Intermediaries. The granting of a Radar license is subject to the confirmation of the existence, the substance, and the financial and operating capacities of the company. There are three different types of import license: (i) "Express", (ii) "Limited" and (iii) "Unlimited":
 - (i) Express Radar. The Express Radar is only applicable to (i) publicly held S.A.; (ii) financial institutions; (iii) companies solely or partially held by the government; and (iv) companies operating export transactions which aggregate amount in any deemed period of six consecutive months is lower than or equal to USD 50,000;
 - (ii) Limited Radar. Under the "Limited" type of Radar, the company may import only up to USD 150,000 per semester. Such kind of Radar is indicated for companies that will import or export lower volumes. The procedure to obtain the



"Limited" Radar is simpler and only requires the submission of an application request to the Brazilian Federal Revenue Customs Agency. The concession of "Limited" Radar is faster and is not heavily dependent on proof of financial capacity.

- (iii) Unlimited Radar. The "Unlimited" type allows unrestrained freedom to operate foreign trade, but a recurring analysis on the financial capacity of the importer will be performed by customs authorities – regularly based on the level of taxes collected in Brazil – in order to continuously confirm the unlimited permission to import.

Other specific registrations may be needed depending on the activity to be performed by the company. The registrations are part of the standard routine of a company formation and the whole procedure takes approximately forty-five (45) days, if there are no manufacturing/industrial activities included in the company's purposes. The time for conclusion provided above is an estimated only, which depends entirely on the internal procedures of the applicable governmental entities.

5. Basic Tax Aspects to be Considered.

5.1. Taxation: Brazilian legal entities are individually taxed, without the possibility of tax consolidation, and may be subject to taxes at the Federal, State and Municipal level of government, according to their activities:

- (a) All legal entities are subject to income taxes (Corporate Income Tax - IRPJ and Social Contribution on Net Profit - CSLL). The most common regimes of assessment of these taxes are the so-called

Deemed Profit and the Real Profit, as further detailed below.

- (b) PIS and COFINS contributions are also generally due by all companies. Their regime varies according to the income tax regime. They can be calculated in a simplified manner, with lower rates (3.65%), but without offsetting credits, if the company opts for the Deemed Profit regime, or in a more complex system, with a higher rate (9.25%), but with the possibility of offsetting certain credits, if in the Real Profit regime. PIS and COFINS are also due upon importation of goods and services at a combined rate of 11.75% and credits may be booked depending on the regime the importer is subject to.
- (c) Import Duty is collected upon customs clearance of goods imported into Brazil. The taxable base is the CIF value of the goods. The rates are usually defined in a schedule based on the Harmonized System and ordinarily vary from 0% to 35% (goods considered to be "essential" are subject to lower rates while superfluous goods are taxed at higher rates). The amount paid upon customs clearance is not recoverable by the importer in the form of a credit and consequently becomes part of the cost of the imported product. Brazilian importation rules follow WTO standards, including in what respects valuation of goods.
- (d) The IPI is an excise tax charged on a value-added basis and is imposed on the importation of goods, on their subsequent sale and on the



sale of products arising from industrial processes. The taxable basis is the CIF value the goods and Import Duty in case of importation, or the value of the transaction on subsequent sales. Rates are also provided for by a schedule based on the Harmonized System, ranging from 0% to 45% (as to the Import Duty, it follows the “essentiality” principle).

- (e) The ICMS is a State tax charged on a value-added basis upon importation and sale of goods. On transactions taking place within the boundaries of any given State (importation and intrastate transactions), the tax is entirely due to such State. Sales across State lines impose the split of the tax between the State of origin and the State of destination. The general mechanism for this split is the determination of an interstate rate (4%, 7% or 12%) that is lower than the regular rate for intrastate transactions (usually 18%), allowing the destination State to collect the difference on the subsequent sales or the balance derived from the difference between the interstate and the intrastate rates when the acquirer is the end-user of the product (i.e., there is no subsequent transaction with the good)¹.

¹ Many products or transactions are subject to what is called the ICMS Substitution Regime (ICMS-ST), under which one participant in the production and consumption chain (usually the manufacturer or importer) anticipates the payment of the tax due across the entire chain, based on certain statutory presumed profit margins. After the entity appointed by the law as the “substitute taxpayer” makes payment of the tax, all subsequent transactions within the State boundaries are exempt from it. In the event of subsequent interstate

- (f) The ISS (Municipal Tax on Service) is due upon the importation and the rendering of services and its rates vary from 2% to 5%.
- (g) Payments abroad are usually subject to a 15% withholding income tax, or 25% if to tax havens or if related to services. Other taxes may levy depending on the nature of the remittance. Dividends are tax free in Brazil, irrespective of the domicile of the beneficiary.
- (h) The most relevant labor-related taxes are Social Security Contribution of 20% on payroll and Employment Security Fund – FGTS of 8%, also on payroll.

5.2. Tax Regimes: There are two basic regimes for calculation and payment of the Corporate Income Tax (IRPJ) and the Social Contribution on Net Profit (CSLL), namely the “Real Profit Regime” and the “Deemed Profit Regime”.

- (a) Real Profit Regime. Companies with total gross revenues greater than BRL 78,000,000.00 per year must assess income tax according to the Real Profit Regime, which is based on quarterly or annual balance sheets. They may not opt for the Deemed Profit Regime (a simplified system of taxation based on a statutory percentage of gross revenues).

Other companies subject to the Real Profit Regime of taxation, irrespective of the revenue level,

transactions, the ICMS must be paid again by the seller and the amounts previously paid by the substitute taxpayer and ultimately collected from the seller become a credit to the seller.



are those: (i) involved in financial activities (banks, leasing companies and other financial institutions) or factoring; (ii) that have profits or capital gains arisen from foreign sources (income from foreign trade or services excluded); (iii) that enjoy tax benefits (exemption or reduction of income tax); (iv) that had made payments under the estimated system during the tax year.

- (b) Deemed Profit Regime. Under this regime, calculation of taxes is simplified. First, the company must determine its basis, which it does by applying a statutory percentage to its gross revenues (32% for services, including the assignment of rights, and 8% for the sales of goods). The resulting amount is the basis, to which the tax rate will apply.

The rates are the same as in the Real Profits Regime, that is: (i) IRPJ of 15%, with an additional 10% on the profits that exceed BRL 20,000.00 per month (i.e., profits of BRL 240,000.00 per year are taxed at a 15% rate, and the exceeding amounts are taxed at a combined 25% rate); and (ii) CSLL of 9%.

- 5.3. Transfer Pricing on Foreign Loans and Thin Capitalization Rules: All foreign loan agreements in Brazil are subject to transfer pricing rules, according to which the interest paid to related parties is deductible up to an amount which does not exceed the amount corresponding to:

- (a) the market rate of Brazilian bonds issued abroad in US Dollars, for

transactions in US Dollars with fixed rate;

- (b) the market rate of Brazilian bonds issued abroad in Brazilian Reais, for transactions in Brazilian Reais with fixed rate;
- (c) the Libor rate for 6-month deposits in the currency of the corresponding agreement² or in US Dollars for agreements signed under a currency for which a specific Libor rate is not available, for other transactions; or
- (d) the specific rate stipulated by the Treasury Ministry, for transactions in Brazilian Reais with floating interest rate³.

In the first three cases above, the maximum interest rate is increased by a 3.5% spread.

Thin capitalization rules impose additional restrictions on the interest paid on loans to related foreign companies. In general, interest paid to foreign related parties is deductible only if, cumulatively:

- (a) it consists of a necessary expense for the entity; and
- (b) the amount of the indebtedness with a related company does not exceed twice the amount of the participation of the related entity in the equity of the Brazilian entity (or twice the net worth of the entity if

² At the moment, Libor rates are only available for deposits in US Dollars, Euros, Pounds Sterling, Swiss Francs and Japanese Yen.

³ This alternative is not in effect because the Treasury Ministry has not stipulated an interest rate in this case. Thus, controlled foreign loans concluded in Brazilian Reais with floating rate will be tested against the Libor rate for 6 months.



lender does not hold any participation).

Thus, besides observing transfer pricing rules, the Brazilian companies shall pay attention to specific debt/equity ratios, as follows: **(a)** a debt/equity ratio of 2 to 1, in general, or **(b)** a debt/equity ratio of 0.3 to 1, in cases the related entity is domiciled in a blacklisted jurisdiction or is subject to a privileged taxation regime.

The debt/equity ratio above must be tested every month, considering both the amount of accrued interest, as well as the net equity of the previous year or month (if available). In this sense, profits accumulated during the year may reduce the debt/equity ratio.

Notwithstanding the above, when the company verifies that the ratio is about to reach the limit stipulated by law, it is possible to convert part of the loan into equity. This procedure is simple to implement, but it may trigger IOF (Tax on Financial Transactions) in some cases. It may also anticipate the withholding income tax if a portion of due interest is also converted into equity or the recognition of exchange variation gains or losses (in cases where the company elected the cash basis regime).