AbdulJaami, PLLC
International Commercial Transactions

Exporting Port Equipment to Brazil – Financing Your Goods; Minimizing Risk

Introduction

Brazil's infrastructure is currently operating at capacity and cannot support a significant increase in exports. The Brazilian government, well aware of this problem, took a huge step and allocated US$13.3 billion for transportation infrastructure investment in its 2000-2003 Bi-Annual Investment Plan. According to a May 2005 United States Commercial Service report, "although several terminal operators have made investments during the last few years…there are still **excellent export opportunities for U.S. companies that supply port equipment**."

This report provides information that will help you to maximize opportunities to export your product to Brazil. While the report was written specifically for U.S. manufacturers of port equipment who are interested in exporting to Brazil, the information that the report contains is in many respects broadly applicable to export transactions. The goal of the report is to provide you with a framework that allows you to profitably export your products.

Opportunities

Opportunity for Port Equipment Suppliers – May 2005

In May, 2005, the United States Department of Commerce Commercial Service (U.S. Commercial Service) released a market research report that focused on an excellent opportunity for U.S. port equipment manufacturers. According to the U.S. Commercial Service, "Brazil's booming agriculture exports are at risk due to bad infrastructure conditions and high operation costs at many ports." The report went on to say that **providers of the following equipment**: *cranes*, *spreaders*, *reach stackers*, *forklifts*, and *loading and unloading equipment* have the "**best prospects**." The Brazilian government's enactment of a port equipment tax incentive program, the *Reporto*, means that importers of port equipment save 20-40% over the FOB costs. The cost savings are an excellent motivator and should mean increased profits for those who can get their deals done. Visit www.buyusa.gov/brazil for a copy of the May 2005 U.S. Department of Commerce report and other associated reports.

Reporto and how can you take advantage of it

In August, 2004, the President of Brazil signed a law that creates incentives designed to increase investment in the modernization and expansion of Brazil's port infrastructure; the law went into effect December, 2004. The goal is to provide Brazilian port operators with a strong incentive to invest in new machinery and modern equipment. Specifically, certain port equipment is excluded from taxes including import tax (only new equipment), social contribution tax (Confins), social integration program tax (PIS/PASEP) and an industrialized products tax (IPI). Under *Reporto*, importers avoid taxes that range from 20 to 40 percent over the FOB value of port equipment.

This port modernization tax incentive program, the *Reporto*, is temporary and is currently scheduled to expire at the end of December, 2005. However, the government has the option of extending the program through December, 2006.

The following port equipment is included in the *Reporto* Program: locomotives, rail cars and tracks, weighing machinery, hoists, cranes, forklifts, loading and unloading equipment, elevators and conveyors, tractors, trucks and other vehicles used at the port for transportation of goods, and X-ray equipment. *Reporto*, does not include computer hardware and software or security equipment required under the ISPS code (see below).

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Brazil's Receita Federal to invest US$300 million between 2005 and 2006

In March 2005, Brazil's *Receita Federal* announced that it would reorganize its structure in order to improve Brazilian Custom's vigilance, modernize its services and comply with the International Ship and Port Facility Security Code (ISPS Code). Receita Federal estimates that it will invest US$300 million between 2005 and 2006 on this new program, which includes the purchase of scanners for Customs to analyze the content of containers and the modernization of its computer system.

To get a better sense of the extent of the upgrades that Brazil's infrastructure require, visit www.normangall.com, click on "Publications" and read "**Crossroads of transportation: Can Brazil's roads and ports overcome decades of neglect?**" Braudel Papers No. 19 (1997).

Also, visit www.focusbrazil.org.br/ccg to view U.S. Commercial Department reports about Brazil and opportunities.

Brazil – Basic Economic Overview

The 12th largest economy in the world, Brazil is the largest country in South America with a land mass that is slightly smaller than the United States'. With a population of approximately 180 million, Brazil has an 81% literacy rate and a work force that numbers 79 million. Brazilians speak Portuguese (not Spanish) and have a life expectancy of 63.5 years. More affluent Brazilians have studied the English language and attained at least a basic fluency. Brazil is a federative republic and has a governing system that bears some resemblance to that of the U.S. (3 branches: executive, legislative and judicial).

Brazil had a 2003 gross domestic product (GDP) of US$508.6 billion; services accounted for 59%, industry accounted for 32% and agriculture accounted for 9% of Brazil's 2003 GDP. In 2004, Brazil experienced a 5% growth in GDP and it is estimated that 2005 GDP growth will be 4-5%. In 2003, Brazil had a US$24.8 billion trade surplus with US$73.1 billion in exports and US$48.3 billion in imports. Brazil's major suppliers were: the European Union (the EU) (26.29%), the U.S. (19.82%), Argentina (9.68%), Japan (5.22%), and China (4.45%). Brazil's major markets were: the EU (24.8%), the U.S. (23%), Argentina (6.24%), China (6.2%), and Mexico (3.75%).

The currency is the Real and on 6/15/05 the Real to U.S. Dollar exchange rate was 2.44 to 1. In March of 2005, inflation was estimated to be 7.54%. In June 2005, Brazil's Selic Rate, the equivalent of the U.S. Discount rate, was 19.75% (the U.S. Discount rate was 3%).

Visit www.focusbrazil.org.br/ccg for more information about Brazil's economy.

10 Things You Can Do to Minimize Risks and Maximize Profits

- *Finance Your Transaction using Purchase Orders*: purchase order financing (PO financing), obtaining financing based on a purchase order from a company that the financier deems to be a credit worthy buyer, can be used to finance your transaction *before* you export (pre-export financing). The funds that you receive can be used to purchase materials from vendors or, if you're acting as an intermediary, purchase items for export. You, the manufacturer, generally receive a percentage of the full purchase order amount, with the remainder minus a discount (the financier's compensation for providing funds and taking on risk) advanced after the purchase order becomes an account receivable. The operative documents include the PO financing agreement, an assignment agreement and possibly a subordination agreement. PO financing can be a creative means of financing working capital. You remain responsible for collecting on the underlying receivables and, if the buyer fails to perform, repayment.

- *Increase Liquidity by Assigning Your Receivables*: a basic assignment of receivables involves you, the owner of the receivable, assigning the receivable to a third party and simultaneously receiving in exchange payment of the full value of the receivable minus a discount (the financier's compensation for providing funds and taking on risk). The benefits of an assignment of receivables are: (i) immediate cash payment without waiting for the maturing of the receivable and (ii) no longer having to worry about collecting on the receivable. The UNCITRAL Convention on the Assignment of Receivables in International Trade, adopted December 12, 2001, by introducing some measure of uniformity in the assignment of international receivables, increases your ability to obtain financing through assignment. Operative documents may include an assignment agreement, a security agreement and a promissory note.

- *Forfaiting – Obtain Financing While Laying-off Risk*: forfaiting (from the French term "à forfait" meaning to give up the rights to something) is a receivables assignment transaction where you, the manufacturer, sell medium-term receivables for the value of the receivable, minus a discount (the financier's compensation for providing funds and taking on risk) on a non-recourse basis (non-recourse means that if the importer fails to pay, you are not obligated to the financier). In a forfait transaction, the importer's obligation is usually represented by a letter of credit, bill of exchange or promissory note, that is backed by a bank guarantee. The receivable that is sold may be purchaser's obligation to pay the price of the sale, or a bank's obligation to pay the proceeds of a documentary credit. Although the financier typically does not have recourse to you, the manufacture, some forfait transactions allow for limited recourse in the event of fraud. Besides allowing you to immediately access funds, forfait transactions are attractive because they help you to eliminate your risk of non-payment (commercial risk) and currency risk (exchange risk) if there is any.

- *Decrease Risk – Guarantees*: a guarantee is a commitment by third-party to make a payment in the event of lack of performance by one of the parties of the primary transaction (either the exporter or the importer). Guarantees are relatively easy to obtain and can provide protection to either party. The following are common types of guarantees: (i) bid bond (tender guarantee): protects against an exporter's unrealistic bid or failure to execute the contract after winning the bid; (ii) performance bond: guarantees exporter's performance after a contract is signed; (iii) advance payment guarantee (letter of indemnity): in the case where an importer advances funds, guarantees a refund if exporter does not perform; (iv) standby letter of credit (a mix of a letter of credit and a guarantee): the issuing bank promises to pay exporter on behalf of importer. Guarantees are 100% independent of the underlying transaction and the legal status of the primary contract has no impact on the guarantor's obligation (if a contract is backed by a guarantee, and the contract is terminated because of an act of God, "*force majeure*", guarantor is still obligated to pay the guaranteed party).

- *Decrease Risk – Insurance*: various forms of insurance can be used to decrease your risk of loss during an international transaction. Transportation insurance can be used to protect you against loss of or damage to goods during

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transport; the degree of coverage varies. Credit insurance can be used to protect you against the insolvency of the purchaser or protracted defaults and/or political risks. A purchaser who makes an advance payment to you, the manufacturer, can purchase seller non-compliance insurance, a form of credit insurance, as a means of reducing its risk that you will not perform or will perform inadequately. Foreign exchange risk, the risk that you will experience loss due to currency fluctuations between the time you enter into an agreement and the time of performance, can be hedged through the use of foreign exchange risk insurance.

- *Government Resources*: Export Credit Agencies (ECAs) are public agencies that provide government-backed loans, guarantees and insurance to private companies for the purpose of increasing the private companies' ability to do business abroad. One way that ECAs fulfill their goal of supporting exports is by providing direct credits to either the importer or the exporter. An ECA can help an exporter to make a deferred payment sale (insurance is used to protect the seller or bank) or can help the exporter by extending a buyer credit to the importer, and by doing so, enable the importer to purchase goods from the exporter. The following list should provide some insight into ways U.S. ECAs can assist you:
    - **Small Exporters**
        - SBA Export Express loan program
        - SBA International Trade Loan program
    - **Working Capital Loans**
        - SBA Export Working Capital Program
        - Export-Import (Ex-Im) Bank Working Capital Guarantee Program
    - **Foreign Buyer Credit**
        - Ex-Im Bank loan guarantee
        - Ex-Im Bank Export Credit Insurance program
        - Ex-Im Bank Medium and Long-term fixed-rate loans
    - **Export Finance Matchmaker** (EFM) - For more information on the EFM, visit the *Export Finance Matchmaker* webpage at http://www.trade.gov/efm or contact the Office of Finance at (202) 482-3277.
    - **Credit Checks** - Department of Commerce International Company Profile (ICP)
    - **Private Export Funding Company** (PEFCO) - For more information, visit the PEFCO website at http://www.pefco.com or call (212) 916-0300

- *Contractual Protection – Choice of Law, Forum*: You benefit from a choice of law clause in three ways: (i) by choosing law you are familiar with; (ii) by choosing law that is favorable to you; and (iii) by keeping the decision in your hands instead of a judge or arbitrator. Forum selection clauses are equally important for similar reasons: (i) you can resolve your dispute in familiar surroundings; (ii) you can avoid being prey to the whims of a foreign judiciary; and (iii) you can save time and money. You should be aware that, if you have not explicitly stated the law that is to govern your agreement, but have included a forum selection clause, a judge/arbitrator may view that forum-selection clause as an indication that you decided that the selected forum's law would govern the agreement. The United Nations Convention on Contracts for the International Sale of Goods (the CISG; also known as the Vienna Convention)), should be taken into account when you are negotiating your sales agreement. Unless explicitly opted out of, the CISG governs certain international contracts for the sale of goods. If the seller's and the buyer's respective places of business are located in two different countries, both of which have ratified the CISG, then the CISG will apply to the contract. Although the U.S. has

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signed the CISG, Brazil has not and therefore the CISG will not automatically apply.

- *Commercial Terms – Incoterms and You*: the risk of transporting goods from you, the manufacturer, to the purchaser should be dealt with thoroughly in the sale agreement. International Commercial Terms (Incoterms) can be used to efficiently allocate responsibility for shipment, delivery, costs and point in time at which risk of loss passes from seller to buyer. Your state's Uniform Commercial Code (UCC) contains shipment terms that are commonly used domestically when goods are shipped by sea. However, in international trade, UCC terms generally take a backseat to the internationally well-known Incoterms. Exporters who use Incoterms have the ability to choose from 13 different commercial terms to describe each party's obligations with respect to delivery obligations, apportionment of risk and costs. The 13 terms are symbolized as follows: EXW, FCA, FAS, FOB, CFR, CIF, CPT, CIP, DAF, DES, DEQ, DDU and DDP. Incoterms can be used in contracts that are governed by the UCC, as long as express reference is made to their use.

- *Why You Should Always Specify Time and Place of Payment*: by clearly stating the time of payment, the place of payment and the currency of payment, exporter and importer ultimately make their lives easier. Lapses in memory, differing interpretations and the vagaries of a court can be avoided. Typically, where there is any doubt concerning the law that governs a sales agreement, the law of the place where payment is made is applied. It is important to carefully choose the time/date of payment; differences in time zones, national holidays and bank practices should be taken into account. Time of payment should be approached from two perspectives: (i) with regard to delivery of the goods (prepayment, at delivery or deferred payment) and (ii) with regard to successful completion of the contract (i.e. at what point after payment will buyer be acknowledged as having fully performed). Care should be taken to specify whether the payment term includes external costs such as shipping costs, insurance, duties and taxes.

- *Dispute Resolution – Mediation and Arbitration*: dispute resolution clauses should be approached with the goal of (i) gaining some control over the likely variables and in so doing decreasing risk and (ii) limiting the cost and time it takes to resolve a dispute. The need for relatively swift, efficient means of third-party dispute resolution has resulted in two practices, mediation and arbitration, gaining acceptance as forms of international dispute resolution and, in many cases, becoming preferable to litigation.

    - Mediation is a private, voluntary process, during which parties to a transaction employ an independent third-party who assists the parties resolve their dispute by acting as an intermediary and a facilitator. The benefits of mediation include: a process that is very flexible, control over time and expense, and maybe most importantly, preservation and possibly strengthening of the business relationship. Mediation is not an adversarial process and suffers if a party approaches it as a way of imposing its will on the other party or views the mediator as a judge or arbiter.

    - Arbitration is a non-judicial dispute resolution process that resembles litigation to some degree but is generally less time consuming, subject to some degree of control by the parties, and may be less costly. Parties usually become subject to arbitration by entering into an arbitration agreement or including an arbitration clause in a contract. Similarities to litigation include the collection and presentation of evidence, adherence to a process, and the arbiter(s) (analogous to a judge(s)). The appeal of arbitration is the

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degree of control parties have over the process. Procedure, location, selection of one or more arbitrators, whether or not the arbitration will be binding or non-binding and even the law that will be used to make the decision, are all subject to the decision of the parties to the arbitration agreement. The 1958 New York Convention, currently ratified by 128 nations, requires that the courts of the 128 nations recognize written arbitration agreements, refuse to litigate a dispute if it is covered by an arbitration agreement and recognize and enforce foreign arbitral awards. Both Brazil and the U.S. have ratified the New York Convention.

How We Help You

Export transactions generally have two main areas where headaches are particularly plentiful: (i) arranging the deal and getting the goods to the buyer; and (ii) securing payment. Here's how we help you successfully complete your transactions:

1. Contract stage: Our focus is international transactions and we bring that to bear when we help you negotiate and draft agreements that accurately reflect your business goals and take into account the legal complexities of operating in the international marketplace. Whether we draft agreements unique to your transaction or review and modify your agreements so that you are protected, we analyze the transaction from both a U.S. and an international perspective.

2. Payment/Financing: Whether you arrange outside financing or finance the buyer yourself (buy now, pay later), we provide you with legal advice that allows you to make intelligent business decisions. We use U.S. law to secure your rights in your products and protect you against buyer's default or inadequate performance. We maintain contacts with Brazilian professionals so that your protection extends to importer's jurisdiction.

3. Other: Our location in the heart of mid-town Manhattan allows us to network with other professionals, including insurance agents and financiers. We also maintain excellent relationships with professionals located in Brazil.

Contact Us

It is estimated that roughly US$1.6 billion in investment will be needed to bring Brazilian ports up to international standards. If you manufacture or export any of the following:

- cranes
- elevators and conveyors
- forklifts
- hoists
- loading and unloading equipment
- locomotives
- rail cars and tracks
- trucks and other vehicles used at port for the transportation of goods
- weighing machinery
- X-ray equipment

call or email Saboor H. AbdulJaami (1 646 435 0668) or sabduljaami@shajlaw.com to discuss the successful completion of your transaction. Be sure to say that you are calling or emailing regarding the "**Brazil Port Report**." We look forward to hearing from you.

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