

Beth Babich: Thank you for joining our podcast today covering changes in the Brazilian labor system. My name is Beth Babich, a Senior Manager in our Global Services consulting practice. Joining us today from Sao Paulo, Brazil is Danilo Mininel, a partner at Madrona Law. Hello Danilo.

Danilo Mininel: Hi Beth. Nice talking to you.

Beth Babich: So as everyone has probably been reading in the media here in the United States recently, there's a lot of political turmoil going on in Brazil. Just last year their President Dilma had been impeached and now there are talks and discussion of their current President Temer being charged with different scandals.

So there's been a lot of discussion about this in the United States but what this has really eclipsed is the different changes that are going on in the Brazilian labor system and court system to make it more favorable for businesses to do business in Brazil. Just recently a few weeks ago, major labor reforms have passed in Brazil, which is something we want to discuss today. But in addition to this, other things are coming down the line including pension reform, I believe Danilo, and what else?

Danilo Mininel: Yes. You're absolutely right. We've seen a very big effort by the Brazilian government to put in place and changes to legislation as part of these efforts of Temer to turn around the Brazilian economy, bring in investment, and really take the focus out of his supposed wrongdoings and the fact that this is very negatively affecting Brazilian image abroad. Of course, [inaudible 00:01:44] and see a lot of instability in Brazil and businesses in Brazil, but part of his effort is to try to bring in investment into Brazil and changes to the labor law. It's a very good example of this.

We, as you know, the labor code dates back from the 1940s, 1943 if I'm not mistaken. And besides that, which we're gonna be talking in a minute, we see the government bringing in some changes to the law also in connection with the mining code. We have a mining code from the '60s that just this week, three executive orders have been issued trying to update this code to create a new agency to govern the sector, changes in the royalties in the form that the royalties are calculated, bringing in more flexibility for licenses for new projects which is usually huge bottleneck for projects in the mining sector in Brazil.

Another big effort that we see government or President Temer doing is trying to increase collection of taxes. A couple of plans for payment overdue taxes installment have been brought just recently by the Federal government where the government reduces substantially interest and penalties. This is still under discussion between government and Congress but still it's a very, very relevant aspect for doing business in Brazil for companies already operating in Brazil that see this as a very good window for paying overdue taxes with a huge discount over time.

We have been seeing some very huge efforts actually in the state of Sao Paulo and some other states for expedited procedures for incorporating legal entities. Simple fire registration. This is another, as you know very well, and your clients usually face these problems here in Brazil, bottlenecks in the registration and incorporation of companies in the country.

And finally something I would like to bring up just as a note is that we see a lot of efforts by the Federal government for privatizing public companies and granting new concessions for some very large projects in [inaudible 00:04:13], power plants, [inaudible 00:04:15], oil and gas. You name it. The government has been putting a lot of effort into this. Last year, Temer went to China to try to bring in investments. Just recently he went to Europe. That was not so well received because that took place in the middle of the turmoil of these charges of corruption. But in any event, we see a lot of effort being put on these privatizations and concessions.

And one final interesting piece on this is that they're offering larger IRR on these projects that we're seeing in [inaudible 00:04:55] concessions and privatizations. So that's brought a lot of interest in foreign investors.

Beth Babich: Right, so and do you think that any of the impending charges against the current President is going to put the brakes on any of these things moving forward? Because a lot of the message that we hear in the US is just what's going on is so politically unstable, but all these great measures you being pushed through. So do you think that would have any impact on this or would actually, even if things move forward, it wouldn't have any impact at all?

Danilo Mininel: Yeah. These huge impacts you're gonna see hopefully in the economy here in Brazil, will be effective, mainly not because they will bring in or change the political scenario or the public opinion of President Temer but he's doing something else to deal with that. He's actually tried to cut some deals in the Congress so this measure or this complaint, it has to be approved by the Congress to move forward to the higher court here in Brazil, that will be blocked at the Congress most likely next week.

We see that Temer is very active in cutting deals or agreements with the Congressmen in terms of investments in their states or Municipalities in order to get their support in maintaining Temer in the Presidency. So besides all these measures or these actions he's taking, and which are at some level being very well received by the businessmen here in Brazil, usually the general population is not paying too much attention to this. What is really gonna change things in favor of Temer is the fact he's cutting these deals and agreements with the Congressmen so probably this whole process of him being subject to an investigation by the higher court here, SPF in Brazil, will be blocked by the Congress.

Beth Babich: Now, and just to dig into the recently the reformed changes just a little more, when I think about American business men and women, thinking about Brazil

doing business in Brazil, they oftentimes say to me that it's a very difficult country to do business in. Lots of regulations, so on and so forth. So to see some of these regulations, these changes, pass, it's kind of surprising. Everything from hours changes to reduction in vacation days of when you can take them, even when it comes to the unions. Things like that.

But something I found very interesting, and I know some of our clients have dealt with, are with labor claims, an ability for the court to actually assess court charges and legal fees to employees that bring about frivolous charges, that actually lose their case. I know clients that we have dealt with. It's something very different from, at least, in our legal system from a labor standpoint, how often labor claims are filed against in Brazil against companies. So to see this, this is actually something when we look at our legal system, we don't even see here in the US, where you're actually assessing those court fees onto that person that is bringing about a frivolous case.

So is that something that ... I know that when I've been reading the different labor law changes that there are some things that the President, that they find to be controversial that he may change by Executive order. What do you think are the most significant things of the labor law, especially for American businesses doing business in Brazil or businesses from outside of Brazil doing business in Brazil? What are the most most major things you see from the labor law changes that are here to stay, that are going to be there that won't be changed by the President in the coming months?

Danilo Mininel:

Yeah. Yeah. Well, commenting on your previous comment that these frivolous cases usually give [inaudible 00:09:09] to losses and still costs to the employers here in Brazil. What we have to consider is that Brazilian labor law has been ... The law we see today and which will be subject to this reform effective as of November this year, it has been very protective to employees. You're right. We see that if you file a labor claim in Brazil, you're going to get something out of it. And this is part of the culture here in Brazil, where the labor courts and employees have this very protective environment to the employee. So what we see now is a change in this culture. What we see now is a change in the law that will allow for more free negotiation of employment agreements.

It still preserves the rights and some of the main rights that the employees have been granted since the '40s here in Brazil. But when you deal with more complex labor relationships, or you deal with more qualified, let me put it this way, individuals, you're gonna have a lot more flexibility to freely negotiate an employment agreement in the terms of the agreement. We see also something that is very, very important. I would like to bring this up now, is that when we see the legal uncertainty of having the possibility of a court decision piercing the corporate veil of an entity an individual, that brings a lot of risks for doing business in Brazil for affecting other companies within the same group.

When we see businesses failing in Brazil, and all the succession for labor claims and labor [inaudible 00:11:11], doomed by that entity, being shifted or

redirected to other companies of the group, this now apparently, and this is what the law is, the reform is bringing, we're gonna see a more strict test for [inaudible 00:11:27] group in succession and for piercing of corporate veil to be put in place. Which is a very huge concern apparently in doing business in Brazil in dealing with labor issues. So if you have a labor claim not being fully paid, once you have a final decision, not mutually paid by the employer, you could see that being shifted to another company of the group or even to the shareholders of that group.

So this brings in a lot of uncertainty and risk of doing business in Brazil. And one of the main changes we saw now is that for that to take place, and more strict task will have to be performed.

Beth Babich: Right, so it's not [crosstalk 00:12:08]

Danilo Mininel: Something else that is very ... Go ahead.

Beth Babich: It's not really a question of doing an asset deal, or a share deal or anything like that. Basically, any liabilities that do exist are going to carry over to the successor company or the acquirer.

Danilo Mininel: Yeah, you're right. And besides that, we could see the shareholders being held liable for that, if and when the company doesn't have enough assets to go around. So as one of the solvency tasks, that is something that brings a lot of concern doing business in Brazil, is the fact that if you have labor exposure or contingencies or lawsuits ongoing, you're gonna have a problem with restricting those liabilities to the entity. Even if you didn't act with fraud, if there's no asset confusion, or any of the other elements or possibilities allowed by labor or by the laws here in Brazil for piercing of a corporate veil, the labor courts didn't really care about it. The labor courts simply go ahead and pierce a corporate veil and you would have to deal with obligations of another company affecting your healthy business.

So, we hope this is one of the things that will be changed and will be acknowledged and accept by the courts from now on, based on this reform.

Something else I would like to bring is a means of bringing certainty to the employment relationship is that from now on employee/employer will be able to have an annual release term of the obligations they have fulfilled in the previous year. And this is very interesting also for mitigating these risks of future claims, or overdue amounts and non-compliance of labor obligations and so forth. So, the union will still play a role in this specific case but still it's something that is not present today. And even if you have the waiver or a release by an employee in connection with [inaudible 00:14:19] labor obligations, that is not accepted by the courts. So this is something that again, brings certainty to labor relationships here in Brazil. It's very well received by businessmen here in Brazil.

Beth Babich: Right. And even going through some of the different changes, I noticed there's less reliance on the union, less [inaudible 00:14:46] involve unions, it seems like, where individuals can more freely negotiate employment contracts, so on and so forth. I think that's kind of appealing to American business men and women doing business in Brazil as well. That you are not having to negotiate every single thing with the labor union necessarily. Is that being well received by the public or is that something that's here to stay, the rejection of reliance on the union or dependence on the union so to speak?

Danilo Mininel: Yeah, that's been well received by the employers and still, we have a very strong influence by unions [crosstalk 00:15:26]

Beth Babich: Right.

Danilo Mininel: Employees, mainly blue collars and so in that sector, it has not been so well received. This has been told to [inaudible 00:15:35] reduction of the protection that the employees have been granted since the '40s and this has been brought as something bad for the employees. But, we know that the unions will still remain in Brazil. We'll probably see a reduction of the number of unions, the smaller ones that are very dependent on the union contributions paid by the union employees, which is no longer mandatory.

Beth Babich: Right.

Danilo Mininel: So this is what we're going to see, the unions still playing a role, important role, in securing and guaranteeing that the rights of the employees are observed. But they have been removed in some of the day to day issues. And I'll give you an example. Whenever you have a termination of an employment agreement here in Brazil, or an employment relationship, you have to get the union approval of that termination. So this has been removed. So union no longer has to play this specific role and the fact that now we have some changes that aiming at allowing more flexibility in the negotiation of the terms of the employment agreement between the employer and employee. This will also take some of the need or necessity of those collective bargaining agreements playing such a relative role in the relationship between the employees and employers.

So examples of this, you can have free negotiation of working hours, work break schedules, positions of trust, and what these are, and if the individual has taken a position of trust in the company. And under Brazilian law perspective, a position of trust is something that gives rights to a lot of benefits [inaudible 00:17:32] such as you no longer have to have overtime payment for that individual. You no longer have to control the work hours of that individual and so forth.

So all these changes will probably take some of the burden from the union of being so actively involved in the day to day issues of employment relationships, but still will keep it as a relevant player in securing and guaranteeing that the

rights of these employees are being observed. So this is something interesting that the law has brought, that so far has suffered a lot of heat from ...

Beth Babich: From the public [crosstalk 00:18:16]. I'm sure.

Danilo Mininel: [crosstalk 00:18:16] of course they're very much affected by this. But the businessmen are seeing this as something very positive, a change to the entire labor relationships and the labor code that we have today.

Beth Babich: It will be interesting to see how this all plays out just because of how ingrained the unionized culture is, in especially manufacturing and distribution kind of companies in Brazil, and just to see how that plays out. Because of course you have the law but now how the law's applied. So how do people really react in the marketplace? How do they really interact with each other?

So to see how this affects actual, the relationship between the unions, employees and employers, it will be interesting to see how that plays out. Do you believe that there's anything else more significant to bring up about the labor reform and the changes that are being made that are significant? Or do you think it's relevant to discuss some of the other things that are kind of coming down the line? Just as you were mentioning, there's other things going on besides just the labor reform changes, but actually expediting the business establishment process, municipalities working with the Federal government, the states working with the Federal government, to make it a more pro business environment.

What are some of the things that you see that you think are going to come through in the coming months that are most significant?

Danilo Mininel: Yeah. Just a few more highlights, final highlights on the labor reform.

Beth Babich: Okay.

Danilo Mininel: Which I think they are very important for people to keep in mind, is that in general we're gonna see a simplification of these procedures for dismissing employees, their relationship with the unions. We will have a reduction of the burden on the companies. For instance, for bonus payments, which is something that very much affects business in Brazil. Usually bonuses are considered part of [inaudible 00:20:17] compensation of individuals. And as a result of that, this creates a lot of increases in the full compensation calculation of individuals. Whenever we have to dismiss someone, those bonuses are part of the compensation and on the calculation basis. So this is all gonna change with the law.

And something else I would very much like to highlight here is that again, this is gonna be a change in the culture of Brazil and how labor [inaudible 00:20:47] applied, and applied by the courts. And we have a court system that has been

historically very protected towards the employees. And the first reaction we saw from the courts and the judges whenever we see them commenting on these changes, is that you're gonna have a hard time applying these changes and we'll probably have to see or wait a few years until these more [polemic 00:21:14] changes reach the higher courts, labor courts, and we have decisions that bind and reflect over the lower courts in connection with the application of this new law before we can see the actual application of these changes by the courts.

Beth Babich: Right.

Danilo Mininel: So [crosstalk 00:21:33] something interesting. It's gonna be a change in culture over time. And we hope, we all hope that this is really gonna stick to the minds of people and that we can see a better environment for businesses in Brazil in connection with employment relationships and employment law.

Beth Babich: Now it would be interesting to see how it does play out and the changes, when you look at Brazil, and these changes coming out of the legal system, it's amazing to see that these kinds of things can be passed actually.

Danilo Mininel: Yeah, absolutely right. And this environment we see right now of Temer really having to show that he's working towards creating a better environment for business in Brazil. We're turning around the economy. I think this is the perfect storm for this to happen. And a couple of more items for us to consider here, that Temer must change, and we'll probably do if he remains in the Presidency over this year and next year. We saw that there has been a lot of discussion on the simplification of the tax system in Brazil. As you know, this is even worse than the labor system in Brazil. So, indeed it's very complex. Creates a lot of uncertainty. Increases the cost of operating in Brazil.

So, even though this is not as mature as the labor discussions and the labor reforms were, people are expecting that Temer will be able to put this in place maybe next year. Something we also see that government will probably be focusing on is the fact that they are gonna come up with changes to the law for contracts by the public authorities in the government. So, you'll see, this is in the pipeline as well. We'll see that Temer will try to empower the public agencies that deal with energy, telecom, now mining sector and so forth. These agencies are gonna be given more power to regulation and to govern each of the specific sectors. And we will see a change most likely in the form that the government contracts with the private sector [crosstalk 00:24:14]

Beth Babich: And is that coming out of the corruption scandals moreso, or just for business? What is really the function of that happening in your opinion?

Danilo Mininel: That is a good question. Yeah, a good question. It's a little bit of both because we see that this environment public entities contract with the private sector allows for corruption to take place, allows for cartels and price fixing to take

place. We have been seeing for the last years, a very strong effort by the government and the agencies, mainly one of the entities very much active in this [inaudible 00:24:55] the anti trust authority that has been very active in fighting price fixing practices and so forth in many, many sectors.

Part of the carwash investigations have given rise and showed that some of the main players in the, for instance, construction sector in Brazil have been fixing prices. And there's strong indications of those practices in other sectors as well. So, part of these efforts for the Brazilian government now to change the way it negotiates and contracts with the private sector is also a reflex of this and a reaction to what carwash operation has been shedding light on, that this has to be simplified. It has to be changed. It has to have more clear rules governing the relationship between government and private sector.

Beth Babich:

And for those listening in, the carwash scandal that Danilo refers to, is if you've seen any of the corruption and scandal things come out in the United States about Brazil, this is what they've been talking about. It's the government contracts where literally people were funneling money through a carwash in the capital of Brazil to launder money that they were getting through government contracts. So, and this is something that has been going through the court system.

So I think probably the biggest thing we can talk about is what are really the takeaways from all this for companies that are either currently doing business in Brazil or are looking at doing business in Brazil? So of course, companies that are currently operating in Brazil, I think one of the biggest takeaways is to work with your legal counsel. If you do not currently have legal counsel or your tax advisers, labor regulation advisers. What do these changes mean for your business and how is it going to impact you to know what are the changes? How to apply them? What they mean?

Most likely I would think that this means less oversight in terms of monitoring the labor regulations for your business. Of course, I think another takeaway is for businesses currently operating in Brazil is, and Danilo you can comment as well, if you're looking at contracting more individuals, so on and so forth, is now the right time? I think that is something that people should be looking at as well. If they were holding off on contracting individuals or looking at really if they were looking at thinning out their workforce even, is now a better time to do that than previously?

Danilo Mininel:

Yeah and mainly rethinking the way companies contract employees in Brazil. So, you're right. This is the right time to start thinking about this, planning on how to contract for instance, individuals for high paid jobs, for even rethinking as you said, your HR departments, which are now, as we all know, very costly in terms of maintaining a large number of people just to handle with union and labor obligations.

We hope that this reform will, over time, not immediately, and we're gonna see this in the long run, you reduce the costs for operating in Brazil. We will allow for companies to more freely negotiate terms of employment with individuals in Brazil and we'll bring more certainty to doing business in Brazil. And we all hope over a longer period of time, these new practices and these new laws specifically will give rise to last contingencies and a lower burden on companies and potentially on individuals or companies acquiring assets or businesses in Brazil which will very much help for foreign investment to come to Brazil over time.

Beth Babich: Right. So, those companies that have been looking at Brazil as a potential market to do business in or are being asked by their customers to have a presence in Brazil, is this now a better time to start thinking about making that dive into the Brazilian market? It seems like it to me, and as we progress through more labor changes or tax reform changes, I think the landscape is only gonna get better, in my humble opinion. And I'm sure you're feeling the same way Danilo.

Danilo Mininel: My humble opinion as well. This is what's gonna happen. People are seeing Brazil as a better environment for investing. Let's hope that the tax reforms really take place and the whole scenario and environment in the Brazilian market gives rise and calls attention to these investments. The FX rate is really positive at this point for investments.

Beth Babich: [inaudible 00:30:08]

Danilo Mininel: And all these changes, we hope, will again create a momentum for investors who decide to come into Brazil, either to start new businesses in a more simplified regime or structure, set up companies in a more expeditious way, or even acquire existing businesses and enjoy some of these changes at this point, that will simplify the operations and reduce costs in Brazil.

Beth Babich: Well, as Brazil moves to these changes that they're going through right now and more changes come to tax codes, labor laws, so on and so forth, we'll continue to report on this, leave our clients updated on what's going on. And for any additional information, of course you can visit www.plantemoran.com, or www.madronalaw.com.vr.

Danilo, thank you for your presence today, and your input, your thoughts. It's been very helpful to have someone that we've worked with with many of our clients locally, discussing what is going on in Brazil, how things are progressing, how things are being received in the market there. It's been very helpful to talk to you. Very informative. Thank you for your time and your participation.

Danilo Mininel: Thank you Beth. Was a great pleasure. Thank you.