Practical Law™
MULTI-JURISDICTIONAL GUIDE 2014/15
OUTSOURCING

ACC Association of Corporate Counsel

Country Q&A

Outsourcing: Brazil overview

Paulo Rodrigues Brancher and Camila Gurgel Fasano de Guglielmo
Barretto Ferreira e Brancher – Sociedade de Advogados (BKBG)

global.practicallaw.com/6-501-5060

REGULATION AND REQUIREMENTS

National regulations

1. To what extent does national law specifically regulate outsourcing transactions?

National law does not specifically regulate outsourcing transactions. However, from a labour law perspective, a direct employment relationship between the customer and the supplier's employees is normally inferred in these arrangements (*Precedent No 331, Brazilian Superior Labour Court (Tribunal Superior do Trabalho)* (TST)) (*see Question 9*).

Sectoral regulations

2. What additional regulations may be relevant for the following types of outsourcing?

Financial services

There are no additional regulations relevant to a financial services outsourcing.

Business process

There are no additional regulations relevant to a business process outsourcing.

IT

There are no additional regulations relevant to a private IT outsourcing; however there are for government IT outsourcings (*see below, Public sector*).

Telecommunications

There are no additional regulations relevant to telecommunications outsourcing, although specific regulations apply to a public sector outsourcing of telecommunications (*see below, Public sector*). However, if the outsourcing concerns telecommunication services, the customer remains accountable to the Brazilian Telecommunications Agency (*Agência Nacional de Telecomunicações* (*Anatel*)) and consumers for the outsourced services.

Public sector

The Federal Constitution allows the federal government, states and the municipal districts to outsource certain public services, such as telecommunication and energy services, among others, through public concessions and permits.

Public services concessions and permits are regulated by Law No 8,987/1995 and Law No 9,074/1995, and must be preceded by a public bidding process (*Law No 8,666/1993*). The private party takes on the business risks under a public concession or permit, but the contract is subject to certain restrictions in the public interest, such as:

- The supplier is strictly liable to the public administration for the services provided, except in cases of *force majeure*.
- The public administration can unilaterally modify or terminate the agreement in the public interest.
- In contracts for essential services, the public administration has, among others, the right to temporarily take over the services and the relevant premises when the agreement is terminated to enable an uninterrupted service.

Any contract between an employee and the public administration entered into without a public contest has no effect and only guarantees the employee the right to receive (*TST Precedent No 363*):

- Compensation for the hours worked.
- Payment into the employee's severance fund account (*Contribuição ao Fundo de Garantia por Tempo de Serviço* (FGTS)).

Public and private partnerships (PPPs) are a special type of public services' outsourcing. The law allows more contractual flexibility in these types of projects. In a PPP, the public administration pays a service fee to suppliers and, depending on the contract, the supplier may also receive tariffs paid by consumers. The following limitations apply to PPPs (*Law No 11,079/2004*):

- The contract value must be over BRL20 million.
- The contract can only be for:
  - construction;
  - the supply of employees; or
  - the supply of equipment.
- The minimum term is five years.

There are also specific rules governing public sector outsourcings of IT and automation services (*Decree No 7,174/2010*). The preference order below must be followed for the government to outsource in this field of activity:

- Goods and services produced with technology developed in Brazil in accordance with the Basic Productive Process, as defined by the Brazilian government.
- Goods and services produced with technology developed in Brazil.
- Goods and services produced in accordance with the Basic Productive Process.

Micro and small-scale companies that meet the above requirements have priority over medium-sized and large companies that meet these requirements. When determining whether micro and small-scale companies are to be given priority over other public bid participants, the government will also consider criteria such as:

- Whether equivalent delivery dates can be provided.
- Support services.
- Quality.

- Standardisation.
- Compatibility.
- Performance specifications.
- Price.

The outsourcing of IT services that are classified as "common" (services that can be objectively defined in terms of quality and performance during the bid process) can be done through auction-type public bids as long as the participating companies comply with the Basic Productive Process. Public bids governed by the Public Bidding Law (Law No 8,666/93) (open competitive bids, price surveys and bids by invitation) must use the "method/technology and price" criteria to decide the winner.

In contrast to other outsourcings, in irregular outsourcings of employees by a private entity to the public administration, no direct employment relationship is formed between the public administration and the employees (*TST Precedent No 313*) (*see Question 9*).

Other

Outsourcings are subject to the Brazilian Federal Constitution guarantees and statutory consumer protection rules (*see Question 18*).

3. What further legal or regulatory requirements (formal or informal) are there concerning outsourcing in any industry sector?

There are no further legal or regulatory requirements concerning outsourcing transactions.

4. What requirements (formal or informal) are there for regulatory notification or approval of outsourcing transactions in any industry sector?

There are no requirements for regulatory notification or approval of outsourcing transactions in Brazil.

LEGAL STRUCTURES

5. What legal structures are commonly used in an outsourcing?

Service agreements

Description of structure. The most commonly used structure in an outsourcing is a services agreement that regulates the relevant terms and conditions. If the outsourcing is complex, it may be regulated by a set of agreements (including agreements for the transfer of assets). In addition, the outsourcing may be at the customer's or the supplier's premises. If so, agreements may become more complex and increase the risk of creating a direct employment relationship (*see Question 9*).

Advantages and disadvantages. This structure has the advantage of being cheap for the customer to set up and gives the customer more control over the price (as the agreement will specify either a fixed services fee or a determinable price). The disadvantage is that the customer may lose some control over the services provided, as the supplier has the expertise in the area. Although the customer can audit the supplier's work, it may not be able to control the quality of the services and details of the transaction.

Joint venture

Description of structure. Another possible structure is to incorporate a new entity as a joint venture, to which the supplier and the customer contribute capital, technology and/or assets. Under this structure, the customer may need to pay more to implement the outsourcing and to maintain the joint venture company than it would under another type of structure.

Advantages and disadvantages. The advantage of this structure is that the customer is able to participate more closely in the provision of services. The disadvantage relates to cost (*see above, Description of structure*) and difficulty in establishing the limits of liability of each contracting party in practice.

PROCUREMENT PROCESSES

6. What procurement processes are used to select a supplier of outsourced services?

Request for proposal

Typically, the customer determines internally which services or activities are going to be outsourced, and what its requirements for the outsourcing and supplier are. It then issues a request for proposal (RFP) to identify possible suppliers. The RFP describes in detail what the customer expects from the outsourcing.

Invitation to tender

The invitation to tender is often used by government entities subject to the provisions of the Public Bidding Law when contracting services and goods (*see Question 2, Public sector*). Government entities using this process must (unless the law provides otherwise) issue a call for bids describing, among other things:

- The service to be contracted.
- The requirements to be met by the bidder.
- The bid procedure.
- The date of bidding.
- A draft of the contract to be executed with the company that will provide the outsourced services.

Due diligence

After analysing bid proposals, the customer selects a few potential suppliers and carries out a due diligence process to verify which supplier is the most suitable for the outsourcing. Before due diligence, the parties sign non-disclosure agreements. Once a supplier is selected, the parties negotiate the agreement (or agreements) and then implement the outsourcing.

Negotiation

When the supplier and customer are private companies, both parties are free to lead the negotiation in the direction that best suits their interests. However, when contracting with a public entity, a supplier has no other rights of negotiation than those stated in the call for bids.

TRANSFERRING OR LEASING ASSETS

Formalities for transfer

7. What formalities are required to transfer assets on an outsourcing?

The customer may retain ownership of its assets used in the outsourcing, as this gives it more control and flexibility if it intends to change supplier. The customer can grant the supplier the right to use the assets in the outsourcing while retaining ownership. Where the supplier acquires assets from the customer or from third parties specifically for the outsourcing, the outsourcing agreement normally gives the customer an option to re-purchase the assets on the termination or expiry of the outsourcing agreement.

Immovable property

The transfer of title to immovable property must be in writing and the relevant transfer document (for example, the purchase and sale agreement) must be:

- Executed before a notary public as a public deed.
- Registered with the relevant real estate registry.

IP rights and licences

As a general rule, the transfer of IP rights must be in writing and, depending on the nature of the IP right, registration of the transfer with the Brazilian authorities is required, as follows:

- Trade marks, patents, industrial designs and geographical indications must be registered with the Brazilian Patent and Trade mark Office (*Instituto Nacional de Propriedade Industrial*) (INPI).
- Domain names must be registered with the Centre for Information and Co-ordination (*Núcleo de Informação e Coordenação do Ponto br*) (NIC).
- Plant varieties must be registered with the National Service for Plant Variety Protection.

Registration of software and copyright is not mandatory. However, if they are registered in Brazil, then their transfer must also be registered, as follows:

- Software transfers must be registered with the INPI.
- Copyright transfers must be registered, depending on the work, with specific national entities.

Generally, the transfer or assignment of IP licences must be in writing and, depending on the terms and conditions of the licence agreement, the consent of the other contracting party may be required. The following agreements must be registered with the INPI to be effective against third parties and to allow remittances abroad:

- Supply of technology and technical assistance.
- Trade marks, patents and industrial designs assignment or licence.
- Franchise.

Movable property

As a general rule, there is no specific formality required to transfer movable property in Brazil, although it is advisable that the assignment be made in writing.

Key contracts

The assignment of key contracts must be in writing and, depending on the terms and conditions of the agreements, the consent of the other contracting party may be required.

Formalities for leasing or licensing

8. What formalities are required to lease or license assets on an outsourcing?

Immovable property

There is no specific formality required for the lease of immovable property, but the agreement is subject to specific regulation and it is advisable that the lease agreement be in writing (*Law No 8,245/1991* and *Brazilian Civil Code (Law No 10,406/2002)*). For the lease agreement to be effective against third parties, it must also be registered with the relevant real estate registry.

IP rights and licences

Brazilian law does not set out any specific formality for most IP licences but it is advisable that a licence agreement be in writing. In addition, to be effective against third parties, certain agreements and licences must be registered with the INPI (*see Question 7, IP rights and licences*).

Where the licensor is a foreign entity, for those agreements and licences that must be registered with the INPI to be effective against third parties, registration of the licence agreement with the INPI is necessary to enable the remittance of payments abroad and the deductibility of payments by the Brazilian licensee for local corporate income tax purposes.

Movable property

Brazilian law does not require any specific formalities for leasing movable property, but it is advisable that the lease agreement be in writing.

Key contracts

Contracts cannot be licensed or leased, but only assigned. Subcontracting part of the obligations may be possible, depending on the terms and conditions of the relevant contract. If a customer does not want the supplier to subcontract, it is important to express it in the outsourcing agreement.

TRANSFERRING EMPLOYEES

Transfer by operation of law

9. In what circumstances (if any) are employees transferred by operation of law?

Initial outsourcing

On an outsourcing, the employees attached to the outsourced business do not transfer automatically from the customer (transferor) to the supplier (transferee). If the parties want them to transfer with the outsourced business, the customer must terminate their employment, following the proper procedure and paying the required severance pay. The supplier can then hire them. However, there is a risk that a direct employment relationship will still exist between the transferor and these employees if the following elements of employment relationship are present:

- Personal nature of the services.
- Subordination.
- Compensation.
- Continuity.

Employees do transfer by law in the following circumstances:

- **Group company transfer.** Employees automatically transfer as part of a business transfer between two members of the same group of companies.
- **Employer transfer.** Employees automatically transfer in the context of an acquisition, or transfer of the business (all assets and employees transfer and the same activities and core business are to be maintained). If the transferee replaces the transferor as the employer because it has assumed ownership of the transferor's business, it employs the transferor's employees automatically without having to re-hire them.

In these two cases, the transferee is the transferor's legal successor, and is responsible for any employment-related liabilities and obligations.

On an outsourcing, there is a risk that a direct employment relationship will be formed between the transferor and the

transferee's employees, unless the outsourcing relates to (*TST Precedent No 331*):

- Temporary employment agreements (Law 6019/1074).
- Security, cleaning and maintenance services.
- Specialised or expert services that are not related to the transferor's core business or corporate purpose, provided that there is no personal relationship nor any legal subordination between the transferor and the transferee's employee.

Change of supplier

On a change of supplier, the employees attached to the outsourced business do not transfer automatically from the old supplier to the new supplier. The old supplier must terminate their employment for the new supplier to be able to hire them, and in this case there is a significant risk that the employee will claim, or the labour authorities will infer, a direct employment relationship with the transferor. However, this does not occur on a group company transfer or an employer transfer (*see above, Initial outsourcing*).

Termination

On termination, the employees attached to the outsourced business do not transfer automatically from the transferee back to the transferor. The transferee must terminate their employment for the transferor to be able to re-hire them (except where a group company transfer or an employer transfer occurs (*see above, Initial outsourcing*).

For more information on transferring employees on an outsourcing, including structuring employee arrangements (including any notice, information and consultation obligations) and calculating redundancy pay, see Transferring employees on an outsourcing in Brazil: overview.

DATA PROTECTION AND SECRECY

10. What legal or regulatory requirements and issues may arise on an outsourcing concerning data protection?

Data protection and data security

General requirements. There is no specific and consolidated law on the collection and use of personal data in Brazil, but there is an important bill of law for personal data protection and privacy in progress at the Brazilian Congress. However, under the Federal Constitution, fundamental rights and guarantees apply in relation to the protection of privacy and personal data. Other legislation regulates specific aspects of data and privacy protection, including, for example, consumer protection, banking and tax secrecy laws. The Brazilian Internet Act (Law No. 12,965/14) reaffirms the principles of data protection and privacy in the use of internet. The right to privacy is a "personality right" that cannot be waived (*Civil Code*). Breaches of a natural person's right to a private life entitle the victim to compensation for damages (including moral damages). The court can also, at the victim's request, take action to stop or prevent any such breach.

Mechanisms to ensure compliance. Although most obligations and standards regarding personal data and its protection are contained in the CDC, its rules are commonly adhered to in other areas. As a result, it is strongly advisable, for instance, to make an individual aware that his/her personal data is to be included in any database. In addition, the outsourcing agreement shall set out minimum standards for data security, as well as supplier's liability in case of breach of data protection.

International standards. Compliance with international standards for data protection and security is not required, but there is an important project in public consultation in this area, the Personal Data Protection Draft Bill, which aims to protect the fundamental rights of individuals, particularly with regard to their freedom, equality and privacy in the processing of personal data.

Banking secrecy

General requirements. Financial institutions wanting to provide further services to customers can outsource their services provided that the outsourcing complies with:

- Central Bank Resolution No 3954/2011, which governs outsourcing by financial institutions.
- Law No 105/2001, which governs banking secrecy in Brazil.

All confidential information provided to companies by its customers must be kept secret, that is, the information can only be disclosed in situations permitted by law or with the authorisation of the customer. In relation to financial institutions, the disclosure of data and customer information can only be done in specific situations, for example (*Law No 105/2001*):

- The exchange of information between two banking institutions regarding their registry status.
- The disclosure of criminal offences to the Brazilian Central Bank.
- The disclosure of confidential information with the express consent of the interested party.
- The disclosure of information between a financial institution and a supplier providing outsourcing services. The supplier receiving the information must keep it secret. Note that the financial institution and the supplier can be held jointly liable for any disclosure by the supplier of banking data and information related to clients of the financial institution.

Mechanisms to ensure compliance. The most common way of ensuring compliance with secrecy requirements is to include a confidentiality obligation in an outsourcing agreement, which imposes a fine for breach of the obligation. A breach of the rules on banking secrecy, except in circumstances expressly permitted by law, is a criminal offence; anyone who breaches the law may be subject to a fine and up to four years' imprisonment (*Law No 105/2001*).

International standards. Compliance with international standards on banking secrecy is not required, but it is recommended.

Confidentiality of customer data

The Brazilian Consumer Protection and Defence Code (*Law No 8,078/1990*)(CDC) regulates the collection, storage and use of consumer databases. Consumers are entitled to secrecy in respect of any personal information they provide. In general, consumers:

- Must be informed, in writing, if their personal data is to be included in a database.
- Are entitled to access, at any time, the data to be included in the database, and can require the correction of any erroneous information. The owner of the database must make the correction and notify the consumer that this has been done.

If a business starts a database or keeps records that include information on consumers, it must notify those consumers in this respect, and explain how the personal data will be collected, used, stored, disclosed and otherwise processed.

Under the CDC, all the companies involved in the supply chain are jointly liable to the consumers for breach of consumers' rights.

SERVICE SPECIFICATION AND LEVELS

11. How is the service specification typically drawn up and by whom?

The services specification is initially drawn up by the customer in the request for proposal (RFP). During the course of negotiations with the supplier, the parties typically amend or add to the services

specification and description. The specification is then usually included in the relevant agreement. It is also common practice to include a customer's RFP as a schedule to the agreement.

12. How are the service levels and the service credits scheme typically dealt with in the contract documentation?

The service levels and key performance indicators are usually described in the relevant agreement (or a schedule to the agreement). Service credits schemes are usually included in the payment section and in a schedule to the agreement. The customer sometimes replaces the service credits scheme with non-compensatory penalties for failure to reach performance levels. In any event, service levels and service credits schemes are specific to each type of outsourcing and vary according to the customer's needs.

It is important that service levels:

- Are objectively measurable.
- Are based on availability, response times and so on.
- Have their breach measured by level of severity.

If not, it can be very difficult to enforce the service credits scheme and reduce the fees where the supplier does not perform its obligations according to the agreement. The parties should review the service levels from time to time to ensure that they meet the customer's needs.

The agreement may also provide for the payment of a bonus to the supplier if performance exceeds certain thresholds.

FLEXIBILITY IN VOLUMES PURCHASED

13. What level of flexibility is allowed to adjust the volumes customers purchase?

The parties are free to contract, provided that the limits stated by the Brazilian laws are observed. In principle, there is no limitation regarding the minimum and maximum volumes involved in this type of agreement.

Exclusive agreements are permitted if the relationship between the contracting parties does not constitute a violation of the economic order. The Brazilian Antitrust Act (*Law No 12,529/2011*) provides for the control of market structures and business conduct. The law prohibits conducts that could restrict commercial transactions or result in the abuse of a dominant market position.

CHARGING METHODS AND KEY TERMS

14. What charging methods are commonly used on an outsourcing?

Fixed price plus

The most common method used on an outsourcing is a fixed fee combined with other charges based on variation mechanisms (such as the number of employees, requests and so on).

Cost plus

It is also common to charge based on time and materials using a cost-plus model (or to use either of these plus a fixed price). In cost-plus models, the customer should be able to review the budget and the costs incurred.

15. What other key terms are used in relation to costs, including auditing and benchmarking mechanisms?

The parties normally agree on benchmarking to set the fees charged under the agreement and engage a third party to compare the contractual fees with those generally charged in the market.

The agreement may also provide for a lump sum payment to the supplier for the initial costs of implementing the outsourcing.

There may also be charge variation mechanisms (*see Questions 15* and *14*).

When fixed prices are used, the agreement may specify that the service fees are subject to indexation on an annual basis according to a particular index, such as the Index of Prices to Consumers (IPC).

CUSTOMER REMEDIES AND PROTECTIONS

16. If the supplier fails to perform its obligations, what remedies and relief are available to the customer under general law?

If the supplier fails to perform its obligations, the customer can:

- Suspend compliance with its obligations under the agreement.
- Terminate the agreement for cause (subject to compliance with the agreement's termination provisions).
- Seek indemnification for the damages caused to it arising from the supplier's breach, plus interest, indexation and legal fees.
- Seek specific performance. Depending on the nature of the services, a court can authorise a third party to provide the services on the supplier's behalf and then charge the supplier a services fee.

17. What customer protections are typically included in the contract documentation to supplement relief available under general law?

The following customer protections are typically included in outsourcing agreements:

- Penalties for breach or delay of key obligations.
- Audit rights.
- Periodic reports.
- Step-in rights for the customer to temporarily take over the outsourced services in cases of severe breaches by the supplier.
- Service levels (*see Question 12*).
- Minimum insurance coverage, depending on the type of agreement.
- The ability to review or adjust services fees based on service levels, benchmarking and so on.

WARRANTIES AND INDEMNITIES

18. What warranties and/or indemnities are typically included in the contract documentation?

Warranties and indemnities vary according to the type of outsourcing and the nature of the services being performed, but typical provisions included in outsourcing agreements are:

- Confirmation that the parties are validly existing entities and are authorised to enter into the agreement.

- Confirmation that the parties are independent contractors and that there is no employment, joint venture or agency relationship between them.
- Confirmation that each party is responsible for its own employees, and indemnification against an employee filing a lawsuit or complaint against the other party.
- Warranties of IP ownership and indemnities against IP rights' infringement.
- If products are supplied, warranties regarding the product's quality or use.
- Confirmation that the supplier will comply with applicable laws when providing the services.
- Warranties from the supplier that the services will meet the contractual specifications.
- Confirmation that the supplier has technical and operational structure to perform the agreement with no need of additional investments.

19. What limitations are imposed by national or local law on fitness for purpose and quality of service warranties?

A contracting party can reject a defective good or product, or demand a proportionate price reduction, within 30 days of delivery for visible defects, or 180 days from the day on which the defect is shown in the case of hidden defects (*Brazilian Civil Code*).

If the agreement sets a warranty period, this overrides the term provided for by the Civil Code for the buyer to make a claim. However, even while the contractual warranty is in force, a buyer or contracting party who is harmed by the product defect must notify the other party of the defect within 30 days of the defect becoming apparent. Failure to do so renders the warranty unenforceable.

Consumer contracts have minimum protection requirements (statutory warranties), and a strict civil liability regime governing damages caused by the product or service or for a product's imperfections. Statutory warranties cannot be waived, as a matter of public policy.

The consumer can claim against visible or easily verifiable defects of durable products within 90 days of the actual delivery of the product. For hidden imperfections or defects, the 90-day term starts when the defect is shown. If the supplier does not correct the imperfection within 30 days, the consumer can demand one of the following, at the consumer's option:

- Replacement of the product by another without defects of the same kind.
- Immediate reimbursement of the amount paid, with indexation. This does not affect the consumer's right to recover any losses and damages.
- A proportionate price reduction.

20. What provisions may be included in the contractual documentation to protect the customer or supplier regarding any liabilities and obligations arising in connection with outsourcing?

Customers have subsidiary liability in relation to services provided by a supplier and, as a result, may be held liable for any damages caused to clients or to third parties. A provision limiting the extent to which a supplier will indemnify its customer for losses incurred may be included in the contract as long as certain legal requirements are observed (*see Question 30*). Provisions regarding employee arrangements cannot be included (as responsibilities to employees cannot be limited).

INSURANCE

21. What types of insurance are available in your jurisdiction concerning outsourcing, and to what extent are they available?

There is no specific regulation concerning insurance issues on an outsourcing. Companies can, however, obtain insurance to cover potential liabilities arising from services and employee actions to be provided under an outsourcing arrangement.

As a customer has subsidiary liability for services provided by a supplier, and may be held liable for any damage caused to clients or third parties (*see Question 20*), it may wish to obtain insurance to cover these risks.

In addition, companies can obtain insurance to cover predetermined risks that may affect the company's business (*Civil Code*). However, if a company acts fraudulently to obtain insurance, the insurance agreement is null and void (*Article 762, Civil Code*).

TERM AND NOTICE PERIOD

22. Does national or local law impose any maximum or minimum term on an outsourcing? If so, can the parties vary this by agreement?

As Brazilian law does not regulate outsourcing, there is no mandatory minimum or maximum term applicable to the length of an outsourcing. The parties are free to agree a contractual term in the outsourcing agreement.

23. Does national or local law regulate the length of notice period required (maximum or minimum)? If so, can the parties vary this by agreement?

A party can terminate an agreement on written notice to the other party. However, if one party has made substantial investments to enter into and perform its obligations under the agreement, termination of the agreement by the other party can only occur after a notice period that is deemed reasonable in view of the characteristics of the agreement and the investments.

In fixed-term agreements, early termination without cause may entitle the party that did not terminate the agreement (terminated party) to indemnification for losses sustained. However, if the agreement gives any party the right to terminate without cause, the risk that indemnification will be required is reduced, provided that the notice period is reasonable in view of the agreement's term and the investments made by the parties. In agreements with an indefinite term, it is advisable to specify in the agreement that:

- Either party can terminate without cause.
- The notice period must be reasonable.

Termination for cause does not require reasonable prior notice, but it is advisable to include a period in the agreement during which any breaches can be remedied (if a breach is not remedied in the specified period, the agreement can then be terminated).

TERMINATION AND TERMINATION CONSEQUENCES

Events justifying termination

24. What events justify termination of an outsourcing without giving rise to a claim in damages against the terminating party?

Fundamental breach

As a general rule, a breach of contract justifies the termination of an agreement by the innocent party, provided that the breach is relevant.

Insolvency events

Although most agreements specify that insolvency or bankruptcy events terminate the agreement, this may be deemed unenforceable (*Bankruptcy Act No 11,101/2005*), in which case termination may give rise to a claim in damages against the terminating party.

Other

In an agreement for an indefinite term, termination without cause cannot give rise to a claim in damages against the terminating party provided that:

- The agreement specifies that either party can terminate it without cause.
- The prior notice period for the termination is reasonable in view of:
  - the investments made by the terminated party;
  - the length of time that the agreement remained in force; and
  - the impact that the termination may have on the terminated party's business.

25. In what circumstances can the parties exclude or agree additional termination rights?

Parties are generally free to agree on additional termination rights under the agreement, but a few restrictions apply, such as:

- There is a general contract law principle that a party cannot be forced to remain in a contract indefinitely. As a result, if the agreement does not contain a right of termination, a party may claim in court that the agreement is abusive and request that it be terminated. However, this does not affect that party's obligation to indemnify the other contracting party for damage caused by early termination.
- Prior written notice for termination should be reasonable in view of the investments made by the parties and the type of agreement involved (*see Question 23*).
- If only one party is granted the right to terminate the agreement, there is a risk that courts will find the agreement abusive and grant the other party the right to terminate it (the court analyses the facts on a case-by-case basis).

Any reason for termination that does not comply with the general principle of good faith may be deemed unenforceable under Brazilian law (depending on the facts).

26. What remedies are available to the contracting parties?

If the termination is due to force majeure or act of God, it will occur without payment of damages and losses. However, if the failure is due to a party's fault, that party will be subject to payment of a contractual penalty and/or indemnification for damages, including, in some cases, incidental damages and loss of profits.

IP rights and know-how post-termination

27. What implied rights are there for the supplier to continue to use licensed IP rights post-termination? To what extent can the parties exclude or include these by agreement?

The supplier has no implied rights to continue to use licensed IP rights after termination or expiration of the agreement, although the parties can allow for this in the agreement (*see Question 28*). If a customer does not want the supplier to continue using its IP rights, the inclusion of the correspondent prohibition in the agreement is strongly recommended.

28. To what extent can the customer gain access to the supplier's know-how post-termination and what use can it make of it?

The supplier generally retains title to its know-how, that is, confidential information disclosed by the supplier and protected under the agreement's confidentiality obligations. On termination or expiry of the outsourcing, the customer is usually required to stop using the know-how and maintain its confidentiality (although the parties can allow the customer to continue using some of the know-how).

If the supplier licensed the know-how to the customer under a separate agreement registered with the INPI, it is likely that the supplier will not be entitled to prevent customer from using the know-how after the termination of the agreement. This is because the INPI does not recognise the concept of a technology (temporary) licence and considers the technology to have been permanently transferred to the Brazilian recipient.

LIABILITY, EXCLUSIONS AND CAPS

29. What liability can be excluded?

Contractual liability is based on three requirements:

- Wilful misconduct or a negligent act or omission.
- Evidence of the damage caused.
- A connection between the negligent act and the damage.

Indemnification is only due if these requirements are met and, in this case, liability cannot generally be excluded. However, this only covers:

- Losses arising directly and immediately from the contractual breach.
- Profits that could have been reasonably obtained if the contractual breach had not occurred.
- Pain and suffering (moral damages).

Moral damages are only awarded for breach of contract where serious damage has been done to the image or personality rights of the other contracting party. Any other indirect, consequential or punitive damages are not available.

In IT contracts, contractual provisions are void if they purport to exempt either party from liability regarding claims brought by third parties as a result of software imperfections, software defects or copyright infringement (*Brazilian Software Act (Law No 9,609/1998)*).

Liability for torts, environmental risks, consumer contracts or the supply of products in the market place cannot be excluded under Brazilian law.

30. Are the parties free to agree a cap on liability? If so, how is this usually fixed?

Brazilian courts normally accept limitation of liability provisions in commercial contracts as valid and enforceable, provided that:

- Both contracting parties are legal entities and have negotiated the limitation.
- The limitation is reasonable, that is, the cap is not so low that it would be considered a disclaimer.
- There is a justification for the limitation and there is consideration or a reduction in costs in return for the limitation.
- Damages are not caused by a high level of negligence or wilful misconduct.
- The limitation does not violate Brazilian public policy rules (for example, a limitation on liability for damage to the environment).

The courts define reasonable limitation on a case-by-case basis, and do not uphold limitation of liability provisions that are excessively low in relation to the risks involved in the transaction. In addition, if there is a great discrepancy between the party's negligence and the damages caused, the courts may reduce the monetary compensation due (*Civil Code*).

The parties to an agreement can agree on contractual penalties or liquidated damages for delay in performance, partial performance or breach of contract. The enforceability of these provisions depends on the following:

- The parties must have agreed on the liquidated damages before the breach of contract occurred.
- Liquidated damages do not apply in cases of breach due to *force majeure* events, unless otherwise expressly agreed by the parties (*Civil Code*).
- Liquidated damages cannot exceed the contract price.
- Where the breached obligation has been partially fulfilled, or if the liquidated damages agreed to by the parties are excessively high in view of the purpose and the nature of the contract, the court will reduce the amount to be paid to the non-breaching party.

The parties can specify in the agreement that the liquidated damages clause does not prevent the claiming of additional indemnification for damages arising from a breach of the agreement. If so, the amount of liquidated damages specified in the agreement is deemed to be the minimum amount of indemnification available. If the damages exceed the cap, it is possible to recover additional indemnification from the breaching party.

Both supplier and customer are jointly liable for violations of consumer rights (*CDC*).

DISPUTE RESOLUTION

31. What are the main methods of dispute resolution used?

The dispute resolution methods mostly used in Brazil are the court litigation and arbitration. Arbitral awards rendered in Brazil have the same effects as a court judgment.

The main advantages of using arbitration to resolve disputes are the:

- Celerity compared to the Brazilian judiciary.
- Possibility of conferring confidentiality to the procedure.
- Judgment by specialised arbitrators with knowledge of international transaction structures and agreements.

If the parties elect arbitration, they gain considerable freedom to choose the governing law, the venue, the language of the proceedings, and also as to whether the arbitration will be managed by an institution or held in an *ad hoc* manner.

In addition, conciliation and mediation are also used in Brazil.

TAX

32. What are the main tax issues that arise on an outsourcing?

Transfers of assets to the supplier

Where the customer transfers assets to the supplier, the supplier is deemed to have received income equal to the assets' fair value, to the extent that the supplier does not pay fair consideration.

The customer is subject to income tax levied on any capital gain it receives.

However, the transfer of assets from a customer to a supplier rarely occurs in an outsourcing transaction. Instead the parties usually enter into a free lease or a loan.

Transfers of employees to the supplier

If employees are transferred to the supplier, the supplier is responsible for withholding payroll taxes and social security contributions, as well as paying and depositing other taxes and social contributions. The customer and supplier remain jointly liable for outstanding labour and social security debts.

VAT or sales tax

There are two forms of VAT in Brazil:

- **Federal Excise Tax (*Imposto sobre Produtos Industrializados* (IPI)).** IPI is levied on:
  - industrial products, when they leave the plant where they were manufactured; and
  - imported industrial products, on their import or resale by the importer.
- IPI rules allow the tax paid on previous transactions in a given production chain to be offset against future charges. In an outsourcing transaction that qualifies as a tolling arrangement (the customer purchases only the raw materials and sends them to the supplier for manufacturing, and the final products are returned to the customer's premises), it is possible to suspend the IPI levied on inputs sent by the customer to the supplier, provided that the industrial products return to the customer. If so, the customer does not receive an IPI credit to offset its sales and the IPI is ultimately charged on the sale of the manufactured product by the customer. IPI rates vary:
  - depending on how essential a product is for consumers and for the development of the country;
  - in accordance with the product's tax code, as determined by the harmonised system set by the Mercosul Common Nomenclature (*NomenclaturaComum do Mercosul* (NCM)).
- **State Sales and Services Tax (*Imposto Sobre Circulação de Mercadorias e Serviços* (ICMS)).** ICMS is another value added tax on sales and services, similar to IPI, payable on:
  - the importation of products into Brazil;
  - the sale or transfer of products within Brazil; and
  - certain communications and intra- and inter-state transportation services.

- ICMS rules allow the tax paid on previous transactions in a given distribution chain to be offset against future charges. It is a state tax and its regulation varies from state to state within Brazil. In an outsourcing transaction that qualifies as a tolling arrangement, most states suspend ICMS on inputs sent by the customer to the supplier, as long as the products return to the customer. If so, the customer does not get an ICMS credit to offset its sales, and ICMS is charged only over the amount related to the inputs and services added by the supplier. The remaining ICMS is then ultimately charged on the customer's sale of the manufactured product.
- In the case of imported products, the tax rate with regard to products that have more than 40% of imported contents is 4%, regardless of the state through which the product enters Brazil.
- The tax basis is the CIF value (Cost, Insurance & Freight), plus the amounts paid as Import Tax, IPI , PIS-Import, COFINS-Import and customs expenses, such as the Additional Freight Charge for the Renewal of the Merchant Navy (AFRMM).
- In the internal operations, ICMS is due at rates varying between 12% and 19%, depending on the state (in Rio de Janeiro the rate is 19%; in São Paulo, Minas Gerais and Paraná, 18%; and in other States, 17%).
- In interstate operations, the ICMS tax rate is:
  - 4% if the product is not submitted to industrialisation following its import;
  - 4% if the product is submitted to an industrialisation process following its import, but the imported content thereof continues to be more than 40%;
  - 12% or 17%, as the case may be, when the product does not have a similar national product.

Service taxes

Services provided by a supplier to a customer under the outsourcing agreement may be subject to municipal services tax (*Imposto Sobre Serviços*) (ISS). ISS rates can vary between 2% to 5%, depending on the nature of the service and the municipality in which the taxpayer is located.

Stamp duty

There are no applicable stamp duty taxes.

Corporation tax

There are no specific provisions on outsourcing that affect corporate income tax.

ONLINE RESOURCES

A wide number of the statutes and regulations referred to in this Q&A can be found at the following locations. English-language translations are not binding.

Brazilian Federal Constitution

W www.stf.jus.br/repositorio/cms/portalStfInternacional/portalStfSobreCorte_en_us/anexo/constituicao_ingles_3ed2010.pdf

Brazilian Civil Code

W www.wipo.int/wipolex/en/details.jsp?id=9615

Brazilian Consumer Defence and Protection Code

W http://brasilcon.org.br/arquivos/arquivos/cdc-en.pdf

Brazilian Internet Act

W www.planalto.gov.br/ccivil_03/_ato2011-2014/2014/lei/l12965.htm

Central Bank Regulations

W www.bcb.gov.br/?NORMS

Labour Laws

W http://portal.mte.gov.br/data/files/FF8080812CD2239D012CE0B73B226D28/manual_empregador_ingl.pdf

Federal Tax Code

W www.receita.fazenda.gov.br/principal/ingles/versao2/default.asp

Corporate Law

W www.cvm.gov.br/ingl/regu/law6404r.ASP

Practical Law Contributor profiles

Paulo Rodrigues Brancher

Barretto Ferreira e Brancher - Sociedade de Advogados (BKBG)
T +55 11 3897 0300
F +55 11 3897 0330
E brancher@bkbg.com.br
W www.bkbg.com.br

Professional qualifications. Brazil, 1996

Areas of practice. Corporate; telecommunications; IT.

Non-professional qualifications. Professor of Corporate Law, Intellectual Property and International Arbitration at the Catholic University of São Paulo; PhD in International Law, Catholic University of São Paulo.

Professional associations/memberships. World Intellectual Property Organization Arbitration and Mediation Center (WIPO Center); Arbitration Board of Sao Paulo – CAESP, Arbitrator; former Board Member of the International Technology Law Association – ITechLaw (2007-2013), former Chairman of the Brazilian Association of Information Technology and Telecommunications Law (ABDTIC) (2007-2008); former Board Member of the Brazilian Arbitration Committee – CBAr (2001- 2005).

Languages. Portuguese, English, French, Spanish

Camila Gurgel Fasano de Guglielmo

Barretto Ferreira e Brancher - Sociedade de Advogados (BKBG)
T +55 11 3897 0300
F +55 11 3897 0330
E guglielmo@bkbg.com.br
W www.bkbg.com.br

Professional qualifications. Brazil, 2007

Areas of practice. Contracts; IP; TMT.

Non-professional qualifications. LLB, Mackenzie Presbyterian University Law School (São Paulo, Brazil); LLM in Créations Immateriélles et Droit, Université Montpellier I (France)

Professional associations/memberships. Member of the Legal Data Processing Commission of the Brazilian Bar Association – São Paulo Section.

Languages. Portuguese, English, French