



BANCO CENTRAL DO BRASIL

Highlights on licensing procedures for foreigners

(For more detailed information, refer to the National Financial System Manual, available at <http://www.bcb.gov.br/?NFSMANUAL>).

1 – LEGAL ASPECTS

Article 192 of the Brazilian Federal Constitution, along with Article 52 of the Transitory Provisions, requires a presidential decree to permit foreign investments in domestic financial institutions. Additionally, Article 18 of Law 4,595/64 determines how authorizations may be obtained for foreign institutions to operate in the Brazilian markets.

The aforementioned Article 192 provides that the national financial system be regulated by legislation passed by Congress, approved by a qualified quorum. Among other aspects, the conditions for foreign investments in domestic financial institutions must be defined.

Article 52 of the Transitory Provisions provides that until such conditions are established, new agencies of financial institutions domiciled abroad are not permitted in Brazil and, in addition, individuals and legal entities domiciled abroad are not permitted to increase their investments in the capital of financial institutions operating in Brazil.

However, Article 52 determines that those restrictions are not applicable when the investment is deemed to be of national interest, in which case a presidential decree is required.

2 – CENTRAL BANK'S AUTHORIZATION GUIDELINES

Below, a summary of the main conditions that must be met prior to the Central Bank's approval for a foreign financial institution to set up a branch in Brazil is presented. Such guidelines are based on Resolution 3.040, of November 28th, 2002, issued by the National Monetary Council, and Circular 3.317, of March 29th, 2006, issued by the Central Bank of Brazil.

According to Circular 3,317, of 2006, the following information must be provided to the Central Bank of Brazil in regards to applications filed by foreign counterparts to operate in the Brazilian financial sector:

- a) amount of foreign participation in the total capital of a local subsidiary of a financial institution (not applicable to branches);
- b) importance of the entrepreneurship for the Brazilian economy, listing all benefits that could be gathered by the local financial system, such as new technologies, greater variety of products and services, incrementing competitiveness and so on;
- c) detailed description of existing activities of the foreign investor in the Brazilian financial system, including any participation in local economic groups;
- d) relevance of the local operations to the strategic plans of the foreign investor, including added-value analysis on any existing operations in Brazil;
- e) risk rating classification of the applicant, including the entire economic group, if applicable;
- f) indication of any financial institutions that maintain direct or indirect relations with the financial institution domiciled abroad;
- g) indication of regulatory bodies that supervise the financial institution domiciled abroad, if applicable;
- h) other information considered relevant for the analysis by the Brazilian government on the issue.

Resolution 3,040, of 2002, sets down the conditions to be met both by Brazilian and foreign applicants to operate in the domestic financial system. The main aspects of these regulations are listed below:



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- a) the Central Bank of Brazil is responsible for authorizing the establishment and operation of multiple banks, commercial banks, investment banks, development banks, credit, financing and investment societies, real estate credit societies, mortgage companies, development agencies, leasing societies, security and stock broker societies, security and stock dealer societies, foreign exchange broker societies and micro-entrepreneur credit societies;
- b) direct controlling interests in the institutions listed above may only be held by:
 - i) natural persons;
 - ii) financial institutions and other institutions authorized to operate by the Central Bank of Brazil;
 - iii) other legal entities whose sole purpose is to invest in the equity of financial institutions and other institutions authorized to operate by the Central Bank (holding companies);
 - iv) commodities and futures exchange, in case of the establishment of a commercial bank to perform the central clearing and depositary functions of such exchange, render services to the exchange and to economic agents responsible by the operations carried out in it;
- c) in order to request authorization to establish a financial institution in Brazil, the organizing group must appoint a technically qualified person as a contact with the Central Bank in regards to the clarification of any issue related to the project. In addition, members of the future controlling group and qualified shareholders, i.e., those that own more than 5% of total capital, must be identified;
- d) all members of the future controlling group and qualified shareholders must authorize the Central Bank to obtain full access to their income tax data relating to the last three fiscal years, for the sole purpose of usage for authorization proceedings. Besides, the Central Bank must also be authorized to obtain information regarding the inventory of properties and rights and debts and mortgages. The absence of restrictions on the personal data mentioned above is essential to obtain the Central Bank's authorization for the operation of a financial institution in Brazil;
- e) the Central Bank, when it deems necessary, may require the publication of a statement of purpose by naturals and legal entities that form part of the controlling group of the financial institution;
- f) a detailed economic and financial feasibility analysis report must be made available to the Central Bank, containing at least a three year forecast of the financial institution's operations. It must comprise the following data:
 - i) market analysis, describing in what market segments the financial institution will be focusing on;
 - ii) it must include a per market segment analysis of the opportunities, weaknesses, threats and strengths of the institution in comparison to other competitors;
 - iii) for each market segment, the application must describe the main premises used in the business plan, such as growth rate, customers income, interest rate and so on;
 - iv) capital structure to be adopted by the financial institution, indicating the source of funds and assets/liabilities evolution over time;
- g) a detailed business plan must be made available to the Central Bank, containing at least a three year forecast of the financial institution's operations. It must comprise the following data:
 - i) organizational structure, clearly indicating the responsibilities and attributions of each organizational level;
 - ii) description of the main procedures for controlling risks associated with the financial institution's operations, such as operational risk, credit risk and market risk;
 - iii) internal and external auditing procedures and specifications;
 - iv) strategic goals;
 - v) definition of main products and services to be provided and public targeted;
 - vi) specification of the information technology infrastructure necessary to provide the desirable products and services to customers and to assure full compliance with the risk management policies to be adopted by the financial institution;



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- vii) definition of the time frame needed to initiate activities after authorization has been granted by the Central Bank;
- viii) description of the criteria to be utilized for selecting top management.

Finally, it is important to highlight the following aspects:

- a) studies developed by the Central Bank conclude that better supervisory practices tend to be facilitated if foreign groups operate in the Brazilian financial system by means of subsidiaries, rather than branches. The reason for this is the fact that subsidiaries are formally incorporated in the Brazilian financial system, being subject to the domestic legal and regulatory framework, potentially reducing cross-border regulatory problems, more likely to appear when foreign companies operate in Brazil as branches;
- b) there are no substantial differences between the legal and regulatory framework applicable to financial institutions controlled by Brazilian residents in comparison to financial institutions controlled by foreigners operating in Brazil (branches and subsidiaries). Therefore, both Brazilian and foreign financial firms must operate in compliance with the same basic set of rules.

3 – CAPITAL REQUIREMENTS

Minimum paid-in capital and net stockholders equity specified below shall be permanently complied with by financial institutions and other institutions authorized to operate by the Central Bank of Brazil (Article 1 of the Regulation annex II to Resolution no. 2,099/94, as amended by Resolutions no. 2,607/99 and 3,334/05; Article 5 of Resolution no. 2,828,; Article 5(I) of Resolution no. 2,874/01; Article 9 of Resolution no. 3,345/05; Article 5 of Resolution no. 3,426/06, Article 4 (I) of Resolution no. 3.567/08):

- a) seventeen million and five hundred thousand Reals (R\$ 17.500.000): commercial bank and multiple bank with commercial portfolio;
- b) twelve million and five hundred thousand Reals (R\$ 12.500.000): investment bank; development bank; corresponding portfolios of a multiple bank and savings bank;
- c) seven million Reals (R\$ 7.000.000): foreign exchange bank; credit, financing and investment society; real estate credit society; leasing society; and corresponding portfolios of a multiple bank;
- d) four million Reals (R\$ 4.000.000): development agency;
- e) three million Reals (R\$ 3.000.000): mortgage company;
- f) one million five hundred thousand Reals (R\$ 1.500.000): security and stock broker societies and security and stock dealer societies qualified to conduct repurchase operations as well as performing firm guaranty operations of security subscription for later sale, margin account or swap operation where there is assumption of any rights and obligations with the counterparts;
- g) five hundred and fifty thousand Reals (R\$ 550.000): security and stock broker societies and security and stock dealer societies conducting activities not mentioned in subparagraph (f) above;
- h) three hundred and fifty thousand Reals (R\$ 350.000): foreign exchange broker society; and
- i) two hundred thousand Reals (R\$ 200.000): micro-entrepreneur credit society.

Note 1: In the case of multiple banks, minimum capital requirements are dependent upon the types of portfolios held. The minimum capital requirement for such institutions can be figured out by the sum of each portfolio.

For instance, a multiple bank with a commercial bank portfolio and a leasing portfolio would have to meet the following minimum capital limits:

MINIMUM CAPITAL REQUIRED = CAPITAL REQUIRED BY PORTFOLIO 1 + CAPITAL
REQUIRED BY PORTFOLIO 2
MINIMUM CAPITAL REQUIRED = R\$ 17,500,000 (COMMERCIAL BANK PORTFOLIO) + R\$
7,000,000 (LEASING PORTFOLIO)



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MINIMUM CAPITAL REQUIRED = R\$ 24,500,000

Note 2 – Increase/Reduction on the Minimum Limits:

- a) in Brazil, the institutions may request installation of up to 10 branches without additional capital requirements. Beyond this limit 2 percent will be added to the required Paid-in Capital and Net Equity per branches in the states of Rio de Janeiro and São Paulo and 1% per branches in other states;
- b) the Paid-in Capital and Net Equity minimum limits for Banks is supposed to be added up by R\$ 6.5 million if relevant foreign exchange market operations are carried out. For further information, please see the *International Capital and Foreign Exchange Market Regulation – RMCCI* available on the Central Bank of Brazil website - <http://www.bcb.gov.br/rex/LegCE/Ingl/Ftp/RMCCI-I.pdf>;
- c) an institution with at least 90% of its branches located outside the states of Rio de Janeiro and São Paulo, including its head office, will have its Paid-in Capital and Net Equity requirements decreased by 30%.

Additionally, the Central Bank of Brazil has also defined minimum capital requirements in alignment to the ones proposed by the Basel Committee on Banking Supervision, since 1988, when the Basel Capital Accord was established.

In Brazil, banks are required to hold a capital base (PR) greater than the required capital base (PRE), which must be calculated taking into account, at least, the sum of the following portions, as stated in Resolution 3,490, of August 29th, 2007:

$$PRE = P_{EPR} + P_{CAM} + P_{JUR} + P_{COM} + P_{CAS} + P_{OPR}$$

where:

- a) P_{EPR} is the portion referring to exposures weighted by the risk weighting factor attributed to such exposures (see Note 3);
- b) P_{CAM} is the portion referring to exposures in gold, foreign currency and operations subject to exchange variations;
- c) P_{JUR} is the portion referring to the risk of operations subject to exchange rate variations and classified in the trading book;
- d) P_{COM} is the portion referring to the risk of operations subject to commodity price variations;
- e) P_{CAS} is the portion referring to the risk of operations in stock prices and classified in the trading book; and
- f) P_{OPR} is the portion referring to operational risk.

Note 3: As far the P_{EPR} is concerned, the parameters for its calculation were set down by Circular 3,360, of September 12th, 2007. The P_{EPR} is expressed by the following formula:

$$P_{EPR} = F \times EPR,$$

where,

$F = 0,11$ (eleven one hundredths);

EPR = summation of the products of the exposures by the respective risk weighting factors – FPRs (0%, 20%, 35%, 50%, 75%, 100% and 300%).