International Financial Services

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I. Brazil

The following is an update of significant legal developments in the banking and financial service areas and related capital market issues in Brazil during the year 2001.

A. ELECTRONIC BANK ACCOUNTS

The Brazilian Monetary Council (BMC), the governmental body charged with regulating Brazil’s national financial markets, approved Resolution No. 2817 on February 22, 2001. Resolution No. 2817 contains rules for opening and operating bank accounts exclusively by electronic means. This course of action represents a major step towards the development of electronic banking—it waives the usual checking of a customer’s personal data and the warranty requirements provided by Resolution No. 2025 of November 24, 1993. In passing this new Resolution, the BMC also successfully reduced the bureaucracy in banking services.

In fact, according to Resolution No. 2025, checking the original identity cards or any documents regarding, for instance, enrollment with the Taxpayers’ Individual Register of the Ministry of Finance, was mandatory. Resolution No. 2817, however, waived these formalities and allowed electronic validation through other financial institutions or directly through the Federal Revenue Department’s electronic system.

In this sense, we must highlight the recognition of the most important feature of any electronic interaction: the waiver of the notion that a document must be a printed matter to be perfectly valid. With the electronic banking expansion and improved security systems

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1. Resolutions (translated in Portuguese or English) issued by the BMC or Ministry of Finance are available at http://www.fazenda.gov.br (last visited July 30, 2002).
seen in the last decades, it is scarcely understandable that such a concept remains attached
to the existence of material support. It does not, however, mean that the data transfer
required to open a bank account via the Internet lacks the security provided by a signed
piece of paper.

Resolution No. 2817 establishes, among other things, specific procedures for opening an
account that must be duly performed throughout every step of the process. For example,
the holder of a bank account, whether an individual or a legal entity, must be a resident of
and domiciled in Brazil. The holder must also have a bank account with a financial insti-
tution duly authorized by the Central Bank of Brazil (Bacen) to operate in Brazil. It is
mandatory, therefore, that the application form to open such an account bears the identi-
fication of the financial institution with which the prospective accountholder has a previous
record in order to attest to the accuracy of any information handled throughout the elec-
tronic process.

Additionally, Resolution No. 2817 ensures liabilities of the financial manager of the in-
stitution where the electronic operation is carried out with regard to money laundering and
concealment of assets, rights, and values. This Resolution clearly requires the financial
manager to follow preventive procedures that restrain activities that might be associated
with crimes listed under Law No. 9613 of March 3, 1998, which technically describes all
felonies regarding the Brazilian financial system.

In addition to the above-mentioned provisions, Resolution No. 2817 requires that the
Web sites authorized by the Bacen—through which financial transactions may be under-
taken—meet certain criteria. Thus, such Web sites must clearly and accurately indicate the
corporate name of the financial institution or institution authorized by Bacen to make
electronic media available to customers. Further, they must specify what services are
charged and their respective charges, if any. And, in case further clarification is needed,
they must provide customers with telephone numbers, e-mail addresses, and mail addresses.
Additionally, all Web sites authorized by Bacen must ensure the secrecy of information and
safety of all electronic means available.

Even though Resolution No. 2817 deals with electronic issues in an incipient way, it is the
first indication of acceptance of exclusive electronic means in banking operations and will
certainly increase electronic transactions. Such an approach, for example, was adopted on
March 1, 2001, when the Bacen implemented the Electronic Statement Register—a registry
system known as SISBACEN (the Information System of Bacen) that electronically records
(1) every security placement in the international market, (2) direct currency loans, and
(3) fund raising transactions with securitization of exports. Resolution No. 2817, in short, is
the way authorities found to replace physical monetary means with virtual counterparts and,
therefore, reduce financial institutions' costs and bureaucracy in banking services.

B. The Independent Investment Agent in Brazil

The BMC decided to reestablish itself as a player in the domestic capital market as an
Agente Autonomo de Investimento—an independent investment agent. The BMC, addition-
ally, determined the scope of activity to be performed by such agent, the basic governing
rules of which are contemplated in Resolution No. 2838 of May 30, 2001 issued by
the Bacen.2

2. Resolutions issued by the Bacen are available at http://www.bcb.gov.br (last visited July 30, 2002).
As defined in Resolution No. 2838, an independent investment agent is an individual or legal entity formed by authorized professionals—and are under the charge of and employees of licensed institutions, which are those deemed to be participants in the Brazilian securities distribution system—whose role is the distribution and mediation of instruments, securities, shares of investment funds and derivatives, at all times. Pursuant to article 15 of Law No. 6385, of December 7, 1976, the Brazilian securities distribution system must include the following institutions:

(i) financial institutions and other companies engaged in the distribution of securities issues: (a) as agents of the issuing company; and/or (b) on their own account, subscribing to or purchasing the issue for market placement purposes;
(ii) companies engaged in the purchase of securities outstanding in the market, in order to resell them on their own account;
(iii) companies and independent agents engaged in the mediation in securities trading on stock exchanges or over-the-counter market;
(iv) stock exchanges; and
(v) entities of the organized over-the-country market.3

Similarly, the following activities require prior authorization of the Brazilian Securities and Exchange Commission, Comissão de Valores Mobiliários (CVM): (a) distribution of an issue in the market; (b) purchase of securities for resale on one's own account; and (c) mediation or brokerage on the stock exchange.4 Only independent agents and companies registered with the CVM may engage in securities mediation or brokerage activities outside the stock exchange. In order to perform his/its activity, the independent investment agent must:

(i) be duly certified as being able to act in such capacity by an entity licensed by the CVM, provided, however, that the performance of the distribution and mediation activities in the derivatives market is still conditioned on the approval in a specific exam that may evaluate the knowledge of the operation and inherent risks of such derivatives market;
(ii) obtain the CVM authorization;
(iii) enter into a contract for distribution and mediation with one or more of the licensed institutions referred to above;
(iv) act in the distribution and mediation exclusively as an employee of such institutions; and
(v) refrain from receiving or delivering to the investors, for any reason whatsoever, money, instruments, securities or any other amounts that can only be effected through financial institutions or through the Brazilian securities distribution system.5

C. CREDIT ASSIGNMENTS IN BRAZIL

On May 30, 2001, the BMC approved new rules regarding credit assignments in Brazil, which are now consolidated by means of Resolution No. 2836 issued by the Bacen. Pursuant to such Resolution, financial institutions duly licensed by the Bacen to operate in Brazil are

(last visited July 30, 2002).
4. Id.
5. Id..
expressly authorized to assign to other institutions of the same nature credits arising out of loan, financing, and leasing transactions. The negotiation of other types of credit documents is also allowed, such as bank credit certificates (including certificates issued by financial institutions evidencing bank credit certificates, in accordance with the Bacen Resolution No. 2843, dated June 28, 2001), mortgage certificates, and rural, commercial, industrial and export credit certificates and notes. Furthermore, Brazilian leasing companies may assign to other Brazilian leasing companies and financial institutions their credit rights arising out of leasing agreements. Such credit assignments may be effected with or without co-obligation of the assignor.

The purchase of credit rights derived from agreements with an exchange variation clause—a clause that enables the parties to reinstate the amounts expressed in Brazilian currency based on the floating rates of the United States dollar or any other convertible foreign currency—can only be made upon payment with proceeds of loans obtained abroad. The negotiation of credit documents with an exchange variation clause, however, may be effected by domestic proceeds.

The regulations do not allow the term repurchase of non-matured credits that have been previously assigned or the acquisition of credits with proceeds of acceptance of bills of exchange. Bills of exchange and other commercial instruments, such as trade bills (duplicatas) and promissory notes, are normally used in Brazil in connection with consumer credit finance transactions to fund purchases of goods and services by consumers or end-users.

Operations of assignment and acquisition of credits between Brazilian credit, finance and investment companies (financeiras), commercial banks and multiservice banks with commercial and/or credit, finance and investment portfolios, involving any of the transactions admitted by the Bacen as indicated above, may originate acceptance of bills of exchange by the assignee. The following conditions must be jointly complied with: the acquired credits must be derived from finance granted based on bills of exchange's acceptance agreements and, with respect to the assigned credits, there is no acceptance of bills of exchange by the assignor.

The Brazilian financial institutions and leasing companies are authorized to assign credits arising out of loan, finance, and leasing transactions to legal entities that do not participate in the Brazilian Financial System provided that: (i) the credit assignment must be made with no co-obligation of the assignor; (ii) no repurchase of the assigned credits is allowed, and (iii) the liquidation of the transaction must be made at sight. The credit assignment agreement must contain all the terms and conditions of the transaction and shall be made available to the Bacen at the assignor's headquarters. The assignor will have to include in its first balance sheet published after the credit assignment an explanatory note with the book value and the credit assignment value, as well as the impact on the company's net worth and the outcome of the transaction.

The prior authorization of the Financial System Organization Department, Departamento de Organização do Sistema Financeiro, of the Bacen is required in any credit assignment made to controlling, controlled or affiliated individuals, or legal entities. This includes companies located in Brazil or abroad, in which the assignor holds, directly or indirectly, individually or jointly with other partners, including as a result of voting agreements, partner's rights that ensure to such assignor, separately or cumulatively: (i) predominance in the company's resolutions; (ii) power to elect or dismiss a majority of the company's officers; (iii) effective operating control, characterized by common administration or management or by acting in the market under the same trademark or the same commercial name; or (iv) shareholding
control represented by the sum of the equity participation held by the institution, regardless of the percentage, with those owned by its officers, controlling partners and affiliated companies, as well as those acquired, directly or indirectly, through investment funds.

Brazilian financial institutions may acquire from or assign to other legal entities, whether or not such entities participate in the Brazilian Financial System, any credits arising out of export contracts negotiated in the domestic market. The credit assignment operations made by the Brazilian financial institutions and leasing companies are limited to those contemplated in Resolution No. 2836 and in the Bacen’s Resolution No. 2686 of January 26, 2000. These resolutions authorize the assignment of credits arising out of transactions performed by multiservice banks, commercial banks, investment banks, credit, finance and investment companies (financeiras), real property credit companies, leasing companies, mortgage companies, savings and loans associations, and the Federal Savings Bank (Caixa Econômica Federal) to special purpose corporations—companies formed with the sole and exclusive purpose of purchasing such credits. The acquisition by any such institutions of credit rights from entities that do not participate in the Brazilian Financial System is also allowed.

D. BRAZILIAN NON-FINANCIAL LEGAL ENTITIES MAY NOW INVEST ABROAD WITH SHARES OR OTHER ASSETS

The Collegiate Board of Bacen decided, by issuing the Circular No. 3037 on May 31, 2001, to authorize investments abroad by Brazilian non-financial legal entities, under the modality known as International Contribution of Shares or Other Assets. International contribution of shares or other assets means the payment of capital of a Brazilian company made by a non-resident investor by way of giving shares in a foreign company, based abroad, or payment of capital of a foreign company, based abroad, made by way of giving shares, by a resident investor, in a Brazilian company. If investments are made through international contribution of shares or other assets, concurrent exchange operations will be required relative to the entry of foreign investment and exit of Brazilian investment. Said concurrent exchange operations will be carried out without the issuance of payment orders, and liquidation will be prompt and net at the same bank. The amount of the concurrent exchange contracts may not exceed, in the currency, the lower amount obtained in the appraisals.

Circular 3037 issued by the Collegiate Board of Bacen lists the documents that the Brazilian companies must submit to the financial institution in charge of closing the foreign exchange transactions to implement an international contribution of shares or other assets. Among the documents listed in Circular 3037, the investor is required to submit an appraisal report issued by an entity accredited by CVM with respect to the value of the shares or assets involved in the transaction.

Accredited banks are allowed to carry out transfers abroad, on behalf of private non-financial legal entities, as Brazilian investments abroad, of up to U.S.$5,000,000 or the equivalent in any other foreign currency, for a minimum period of twelve months without the need to request prior authorization from Bacen. The restrictions imposed by the Bacen on this type of investment are: (i) any investments made by such economic group within a period of twelve months exceeding the maximum U.S.$5,000,000 value requires analysis by the Bacen, as provided in Circular 3037; and (ii) the prohibition of transactions resulting in cross participation between the Brazilian and the invested foreign companies.

The rules issued by the Bacen impose restrictions with respect to remittances abroad of dividends and capitalization of profits registered by the Brazilian company through the
equity method of accounting. The rules are an attempt to avoid outflow of funds from Brazil based on profits generated abroad, by the non-resident invested entity, when the proceeds earned by the non-resident company have not yet been repatriated to Brazil. The Brazilian investor is not allowed to: (i) remit profits or dividends and bonuses abroad when the underlying profits resulted from the application of the equity method of accounting on the net worth of the non-resident invested company, or (ii) to register in foreign currency, as foreign investment with Bacen, the amounts of profits registered through the equity method of accounting and capitalized in the books of the Brazilian company in favor of a foreign shareholder.

Upon the issuance of Circular 3037, Brazilian companies are also authorized to transfer title in Brazil of their equity interests acquired in non-resident companies. In this case, the Brazilian investor is required to inform the Bacen within thirty days of the transfer of title. In case of a sale of a liquidation of the investment in the non-resident company, the Brazilian investor is required to cause the immediate repatriation to Brazil of the amount invested abroad, in addition to any surplus resulting from sale or dissolution of the investment. Circular 3037, however, does not apply to the investment in foreign stock exchanges, investments in foreign financial markets, or investments in real estate located abroad, which is subject to specific regulations.

E. New Swap Transaction Rules

On July 26, 2001, the BMC issued new rules providing term and over-the-counter swap transactions, agreements traded in commodities future exchanges, and entities authorized to operate by the Bacen or the CVM. These new rules were made public by means of Resolution No. 2873 of the Bacen, dated July 26, 2001. For purposes of Resolution No. 2873/01, a transaction will be deemed to have occurred over the market if contracting thereof was not accomplished by means of auction sale or floor trading. Based on the definition in this Resolution, swaps are transactions effected for settlement, on a later date, that entail swap of financial income resulting from the application on assets and liabilities of reference rates or indices.

Under the terms of the new regulation, only certain financial institutions were authorized to effect over-the-counter and on their own account or account of third parties, term and non-standardized option swap transactions based on gold, exchange rates, currency indices, interest rates, commodities, price indices, interest rate indices, shares of public companies issue, share indices, simple or share-convertible debentures, and promissory notes issued by joint stock corporations (sociedades anônimas) designed for public offer. Financial institutions expressly authorized to effect such transactions are multi-service banks, commercial banks, the Federal Savings Bank, investment banks, brokerage houses, and securities dealership companies. Price indices shall have their series regularly calculated and be known to the public. Shares, gold, and commodities prices should be those charged under trade scenario consented to by the Bacen or CVM or ascertained as reference by methodology previously authorized by the regulatory bodies. Share indices shall be calculated based on shares that meet such requirements.

Additionally, Resolution No. 2873/01 establishes the obligation to register these transactions with systems run by stock exchanges, commodities futures exchanges or entities duly authorized to operate by the Bacen or the CVM, within their respective authorities,
to such activities that meet the tax and control requirements by such authorities (i.e., the Bacen and CVM). The following provisions apply to the commodities futures exchanges:

(a) Commodities futures exchanges shall include in their operating rules provisions allowing prevention or correction of unusual market conditions that may constitute violation of legal or regulatory rules, or that constitute inequitable practice, fraud or manipulation;

(b) Upon determination of any of the events provided in the previous item, it is incumbent on the commodities futures exchanges to make arrangements to restore the proper operation of respective market, and shall inform Bacen and CVM of any irregularity found and the corrective measures taken; and

(c) The commodities futures exchanges and their members are under the obligation to provide information, including information on the market under their management, as required by Bacen and CVM and the entities legally authorized to access such information.

Swap transactions addressed under Resolution number 2873/01 are conditioned upon the nomination, by the authorized financial institutions, of a technically qualified administrator accountable to the Bacen for such transactions.

CVM will interfere if the asset traded is based on security subject to Law No. 6385 of December 7, 1976 (which establishes CVM), that is, in the case of:

(i) shares, founders' shares, coupons thereof and subscription warrants;

(ii) securities certificates of deposit; and

(iii) other securities created or issued by joint stock corporations, at the option of the National Monetary Council. To date, several other securities have been authorized, namely: promissory notes issued by joint stock corporations and designed for public offer; stock portfolio indexes; securities put and call options; subscription rights; subscription receipts; real estate fund quotas; certificates of audio-visual investment; joint ventures for animal fattening purposes; certificates representing electric power term purchase and sale agreements; depositary receipts used in the placement of Brazilian companies' shares in the international market; certificates of real estate receivables (CRI); and securities or collective investment agreements that generate right to ownership, partnership or compensation, including those arising out of provision of services, whose earnings result from the efforts of undertaker or third parties, if such securities or agreements are offered publicly. Additionally, any derivative whose asset-object is among the securities listed above shall be indicated as securities, and other securities created or issued by joint stock corporations, so long as they are inserted in the concept of security and duly registered with CVM.

Another important aspect is that the Bacen and CVM may take measures and lay down complementary rules required to the performance of Resolution No. 2873/01, change the established conditions for swap contracting, and curb the performance of authorized financial institutions relatively to the transactions effected under Resolution No. 2873/01.

F. AMENDMENTS TO THE BRAZILIAN CORPORATION LAW

On November 5, 2001, Law No. 10303 was published bringing important changes to the Brazilian Corporation Law (Law No. 6.404 of December 15, 1976) and the Brazilian Securities Law (Law No. 6385 of December 15, 1996). These changes concern not only the privately- and publicly-held Brazilian corporations but also the Brazilian Securities Market. The changes will undoubtedly benefit minority shareholders in many ways.

Firstly, it is important to point out the several rules that govern when the new provisions will come into force vis-à-vis privately- and publicly-held companies.
(a) Corporations (Sociedades Anónimas) will have until March 5, 2003 (one year after the effective date of the Law—120 days after publication) to adjust their bylaws to the provisions thereunder.

(b) The Tag Along right granted to minority shareholders of publicly-held companies corresponding to 80 percent of the purchase price offered to the controlling shareholder will not apply to state-owned companies undergoing privatization that have their Invitations to Bid Notes published until October 31, 2001.

(c) Any change in the type and number of shares resulting from the new provisions under the Law shall not entitle shareholders to exercise their right to withdraw, unless it is carried out until December 31, 2002.

(d) The voting to non-voting right ratio (which reduced 66 percent non-voting to 33 percent and voting to 50 percent) of shares that companies can issue shall be applicable to companies incorporated after publication of the Law and to privately-held companies that apply for license to trade bonds and shares in the market.

(e) The election of members of the Board of Directors by minority shareholders (shareholders with voting rights representing 15 percent minimum of the total voting stock and shareholders representing 10 percent minimum of the total issued stock) is limited to a list of three names, prepared by the controlling shareholder until the first General Shareholders' Meeting of 2005.6

It is also worth mentioning that a Brazilian corporation can be classified as a public trade company even though it has not issued shares into the market. Corporations that issue debentures, for instance, have to apply for a license as a publicly traded company. In that respect, all the new rules applicable to publicly-traded companies will also be applicable to corporations that have been authorized to issue debentures or other bonds. Following is a summary of the most important changes brought about by this new law.

1. Public offer for acquisition of shares

As mentioned above, public offers for acquisition of control entails a tag along right for the minority shareholders corresponding to 80 percent of the value offered to the controlling shareholder. Furthermore, in case of public offers for acquisition of shares from minority shareholders and closing of the company's capital, a new procedure was established pursuant to which shareholders representing at least 10 percent of the shares not held by the controlling shareholder may challenge the value offered by the controlling shareholder and request a new appraisal of the company. The majority shareholder is also required to support the value offered based on one or more criteria for appraisal of the company mentioned in the new law. After the above-mentioned public offer, if less then 5 percent of the total shares issued by the company remains in the market, the shareholders' meeting may authorize the mandatory purchase of said shares by the company.

2. Voting and Non-voting Stock

The non-voting shares cannot exceed 50 percent of the total number of shares issued. The non-voting shares of publicly traded companies should receive preferential dividends in relation to voting shares. In case of privately held companies, the preferential dividend of 10 percent over voting shares was eliminated.

6. See id.
3. **Put Option**

The right granted by law to the minority shareholders to withdraw from the company by selling their shares to the company was increased to include the spin-off company, except if the spun-off assets are transferred to a company the main business activity of which is equivalent to the business activity of the original company. Furthermore, the put option may be exercised by the minority shareholder in case of a reduction in the mandatory dividend.

4. **Shareholders’ Agreement**

The enforceability of the provisions in the shareholders’ agreement is confirmed by the new law, according to which the Chairman of the Shareholders’ meeting or Board meeting should not take into consideration votes that violate voting arrangements provided in the shareholders’ agreement. The exercise of the controlling power was also included among the subjects that can be regulated in the shareholders’ agreement.

5. **Shareholders’ Meeting**

The time for calling shareholders’ meetings of publicly traded companies was extended from eight to fifteen days. Depending on the agenda of the meeting and upon request of the minority shareholders, said time may be extended by CVM’s decision for up to thirty days and its course can also be interrupted by an additional fifteen days.

6. **Board of Directors**

Shareholders representing a minimum of 15 percent of the voting shares are entitled to elect one Board member. Shareholders with non-voting shares, representing at least 10 percent of the issued stock are also entitled to appoint one Board member. Regardless of the number of members in the Board, the controlling shareholder will be entitled to elect the majority of Board members. The appointment of Board members who are not resident in the country is now allowed and Board members cannot hold officer offices in companies regarded as competition of the company.

7. **Arbitration**

The new law makes specific reference to the possibility of conflict resolutions among shareholders or between the company and any shareholder by means of arbitration. This change will undoubtedly benefit minority shareholders and the securities market to the extent that investors’ confidence increases and CVM has more powers to oversee the market. These changes should also benefit foreign investments into the Brazilian securities markets, since it grants additional rights to minority shareholders. On the other hand, the new set of shareholders’ protection rights might have adverse effects on foreign investors taking a majority stake in joint ventures with Brazilian shareholders. Even though the main reason for the enactment of the new law is to boost the Brazilian Securities market, there are economic and tax aspects that should also be addressed by the Brazilian Government in order to increase the investments (national and foreign) in the securities market. Indeed, economic and tax (incentives) changes usually have a much more effective result in boosting investments than changes in the law.

G. **NEW CHANGES TO THE BRAZILIAN SECURITIES LAW**

Law No. 10303 enacted on October 31, 2001, introduces changes not only to the Brazilian Corporation Law (Law No. 6404 of December 15, 1996, as amended) but also to
Law No. 6385 of December 15, 1976, which regulates the CVM and the Securities Market. The main changes introduced by Law No. 10303 were oriented to give more autonomy and extend the supervisory role of CVM. Several articles of Law No. 10303 were vetoed by the Vice-President (acting on behalf of the President) because of constitutionality concerns regarding the change of CVM into an independent Agency. Project No. 3115 of 1997, which was approved by the Congress and originated Law No. 10303, contained several provisions regarding CVM. It was stated, however, that the creation of regulatory agencies and their scope is subject to presidential initiative, pursuant to article 61 of the Brazilian Federal Constitution of 1988. Therefore, changing CVM into an independent agency could not have been originated from a law proposed by Congress.

In order to avoid constitutionality challenges after approval of Law No. 10303 or the debate about the constitutionality of the relevant articles, the articles were vetoed and immediately enacted in the form of Provisional Measure No. 8 of Oct. 31, 2001 (MP No. 8) and Presidential Decree No. 3995 of Oct. 31, 2001 (Decree No. 3995) regulating MP No. 8. MP No. 8 will have to be ratified by Congress within sixty days from publication. The ratification will not be very difficult considering that the same wording originally proposed by Congress in Law No. 10303 was maintained in both the MP No. 8 and Decree No. 3995.

Among the changes affecting CVM and the Securities Market, the following are worth mentioning:

- CVM is now an independent agency with its own budget and not subordinate to the Government. Until MP No. 8 and Decree No. 3995 were enacted CVM was an agency under the control of the Ministry of Finance, and therefore subject to the economic policy and political influence by the Federal Government. CVM will be managed by a president and four directors who shall hold such office for five years, and will be removed only: (1) in case of death, (2) in case of embezzlement and upon a final court ruling to that effect, (3) in case of resignation, or (4) in case of a breach in their judiciary duties as head of the agency. The President and the Directors will be appointed by the Brazilian President, subject to confirmation by the Congress.

- CVM is empowered to issue rules applicable to different types of publicly traded companies. It is important to clarify that until the enactment of the new laws rules issued by CVM were applicable to companies with publicly traded securities as well as to companies that issues debt instruments only, such as debentures. The level of disclosure and filings that will be required from companies applying to issue securities in the capital market will probably vary depending on the type of securities issued by each of them. The reduction in the report and disclosure requirements should boost the interest of companies in accessing the capital market.

- CVM supervisory jurisdiction was expanded to include acts carried out abroad and that have effects in Brazil, as well as acts performed in Brazil that have effects abroad.

- CVM will also regulate the future and commodities exchange as well as the over the counter market and the entities responsible for settlement of transactions with securities.

- CVM is entitled to request copies and has access not only to accounting records of companies authorized to issue securities but also to working papers of auditing companies that have always argued about the secrecy of such documents. The administrative procedures and related documents will constitute public record and will be available to the general public unless expressly protected by secrecy laws or when necessary to guarantee the right of defense or to protect the public interest. It is worth mentioning that the above concept of the protection of the public interest gives CVM broad discretion on secrecy issues unless the information is expressly protected by law.
CVM will also issue disclosure rules applicable to individuals with access to relevant information related to the capital market. Only managers (Directors and Officers) and the controlling shareholder were required to disclose relevant information. Now, not only minority shareholders and members of the companies' auditing committees will be required to disclose information but individuals considered to have access to sensitive information will be required to follow CVM's request for disclosure.

The independence of CVM to further regulate and supervise the market was well received as another step to foster the Brazilian Securities Markets, along with the changes introduced to the Brazilian Corporation Law. One of the changes proposed by Congress but vetoed after opposition from the Securities Market prohibited appealing to the courts from administrative decisions issued by CVM Board.7

II. Update on European Union Law

A. Electronic Commerce

The European Commission (Commission) published a Communication on E-commerce and Financial Services that set out a strategy to create a single market in financial services by 2005 through a program of convergence covering contractual and non-contractual rules.8 The objective of this Communication is to establish a policy framework that enables consumers and retail investors to access financial services available throughout the European Union (EU) while being fully protected.

How the e-commerce Directive interacts with existing financial services legislation is of central significance to the development of a clear and coherent policy in this field. The Commission commits to build any future policy on the approach set out in the e-commerce Directive, in order to:

(a) establish a fully functioning Internal Market for retail financial services;
(b) secure coherence between financial services legislation and the e-commerce Directive;
(c) secure coherence also between on-line and more traditional provision of financial services; and
(d) examine how the Internal Market clause will apply in areas where national rules significantly diverge and where further harmonisation might be necessary, to avoid exposing consumers and investors to legal regimes that may differ substantially from their own.9

More generally, in order to end the current fragmentation in retail financial markets, the Commission envisages a three-strand approach:

(a) A programme of convergence covering contractual and non-contractual rules. In the non-contractual sphere, harmonisation of key marketing rules in the proposed Distance Marketing Directive and approximation of the conduct of business rules protecting investors are of paramount importance. Additional measures are required at the sectoral level focusing on the provision of high quality and comparable information to consumers. This convergence of rules should pave the way for a country of origin approach to work in

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9. Id.
practice covering all financial services sectors and distance trading modes. For contractual obligations, a review of mandatory consumer protection rules is needed. The purpose of the review will be to identify the feasibility and the basis on which retail financial services governed by the law of one Member State can be freely offered throughout the European Union in a framework of legal certainty;

(b) Targeted measures to build consumer confidence in cross-border redress and internet payments. The Commission considers that access to redress is vital to consumer confidence. Ultimately the consumer will always have access to the courts, but for cost reasons this is often a last resort. A realistic alternative has been established (FIN-Net) which provides effective and rapid out of court redress on a cross-border basis. To address the lack of confidence in internet payment systems, steps are also proposed to improve security and provide consumers with a legislative safety net when making payments on-line within the Union;

(c) Enhanced supervisory co-operation. In an e-commerce environment, host state authorities are increasingly dependent on the supervisor in the country of establishment to monitor the cross-border provision of services at source. To keep pace with market developments, the Commission, together with Member States, will keep the arrangements for implementation and enforcement of European Union legislation under continuous review. In particular the Commission will examine the need for additional measures to: supervise the cross-border provision of certain non-harmonised services; establish technical means to meet money laundering requirements on-line and cross-border; and respond to the emergence of new risk profiles associated with e-commerce business models.]

The European Council endorsed the Commission's approach in May 2001, and the Financial Services Policy Group reported in August 2001 on the way forward. The Commission is expected to introduce some of the initiative foreshadowed in this document in the near future.11

The Commission has declared its intention to propose guidance to Member States on the application of Article 3(4)-(6) of the Electronic Commerce Directive in the area of retail financial services. Such guidance will aim to promote understanding of the regulatory framework and to facilitate a surefooted implementation of the place of establishment approach. The Commission hopes to be able to publish this document by mid-January 2002, before the Directive comes into force.

B. DATA PROTECTION AND SAFE HARBOR DEVELOPMENTS

On June 15, 2001, the Commission approved a Commission Decision (2001/497/EC) providing standard contractual clauses for the transfer of personal data to third countries not declared by the Commission as providing an adequate level of data protection (so far the Commission has declared that Switzerland, Hungary and the U.S. Safe Harbor System provide adequate protection).12 Member States were notified of this Commission decision on June 18, 2001. The Commission decision entered into force on September 3, 2001.

This decision does not by any means complete the work on contractual clauses. Its scope is limited to transfers of personal data from a controller established in the Member Com-

munity (Community) (the data exporter) to a controller established in a third country (the data importer). It does not cover data transfers to subcontractors established in third countries who merely process personal data on behalf of controllers in the Community. This category of data transfers does not require the same safeguards as provided for in the decision of June because the controller in the EU remains responsible vis-à-vis the data subject. But a very large proportion of international transfers from the Community are of this kind and the Commission is therefore preparing a further decision establishing standard contractual clauses for this purpose.

The Commission's services have been discussing such clauses for controller-to-processor transfers with the Article 31 Committee (Member States), the Article 29 Working Party (data protection commissioners), business associations and other interested parties since March. A text of the draft Commission Decision was posted on DG Internal Market's Website for consultation in July 2001 and comments have been received from the most interested business associations. A constructive meeting was also held with these associations in the same month. The Article 29 Working Party delivered a favourable opinion on the draft decision on September 14, 2001. The Article 31 Committee has also been invited to deliver an opinion and is expected to do so in the coming weeks. All efforts are being made to have these standard contractual clauses approved by the Commission quickly.

In addition, the Commission is respecting the undertaking it gave in its June decision to consider approving alternative sets of clauses put forward, for example, by business organisations. It is currently discussing with representatives of the organisations concerned a set of draft clauses submitted in September by a group of business organisations (ICC, CBI, EICTA, American Chamber of Commerce, Japan Business Council in Europe, ICRT, FEDMA, and UNICE). Like the standard contractual clauses approved in June, they are limited in scope to controller-to-processor transfers. If approved by the Commission, such clauses would exist alongside those adopted, not replace them. So far, however, only a preliminary exchange of views between the Commission services and business representatives has taken place (on October 11, 2001) and it would be premature to speculate about when the Commission might approve these clauses.13

C. Amended Distance Marketing of Consumer Financial Services Directive

The Council of Ministers (Council) reached a political agreement on a draft distance marketing of consumer financial services directive on September 27, 2001. All Member States voted in favour of the compromise proposal tabled by the Belgian presidency, with the exception of Luxembourg. This is considered a breakthrough in the difficult negotiations to reach an equitable solution for all stakeholders. The Council will adopt a “Common Position” shortly, without debate, and the consolidated text will go back to the European Parliament for a second reading. Final adoption may be possible by the summer 2002.

D. Proposed Pension Fund Directive

On October 16, 2001, Frits Bolkestein, Commissioner for the Internal Market, expressed his deep concern to the Council about the distinct lack of priority given to the proposed


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directive on occupational pension funds presented by the Commission one year ago. Mr Bolkestein indicated that the proposal would ensure a high level of protection for the rights of future pensioners while ensuring that institutions enjoyed sufficient freedom to develop an effective investment policy. "The measure was specifically identified as a high priority by the Lisbon European Council. The European Parliament has already adopted its Opinion, but in the Council of Ministers, the proposal appears to be going nowhere fast. Without this Directive, Europe's future pensioners run a greater risk of getting a raw deal." 

III. India


The Indian Government has recently introduced the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Ordinance, 2002 (Ordinance), which modified and incorporated the provisions of the Creation and Enforcement of Security Interest by Banks and Financial Institutions Bill, 2001 (the "Bill"), to alleviate the maladies in debt recovery scenario. The Ordinance seeks to codify and consolidate the law and practice relating to securitisation and reconstruction of financial assets and enforcement of security interests by banks and financial institutions without court intervention.

1. Securitisation or Reconstruction companies

The Ordinance permits establishment of securitisation companies (SC) or reconstruction companies (RC) to acquire the financial assets of defaulting borrowers. An SC or RC can raise funds for such acquisitions from qualified institutional buyers by issuing security receipts representing an undivided interest in such assets. Once an SC or RC acquires the assets from a lending bank or financial institution, it can enforce all of the lenders' rights and claims against the borrower. The functions of an SC or RC include management, sale or lease of a borrowers' business, re-scheduling of a borrower's debts and enforcement of security interests.

The Reserve Bank of India (RBI) will regulate and supervise SCs and RCs. Disputes relating to securitisation have to be settled by conciliation or arbitration under India's Arbitration and Conciliation Act, 1996.

1. Registration of security interests

The Ordinance provides for the establishment of a Central Registry to register and maintain particulars of all transactions relating to securitisation, reconstruction and creation of security interests in favour of secured creditors. Registration with the Central Registry is mandatory. However, it will not affect the priority or validity of charges registered under any other enactments.

2. Enforcement of security interest

The Ordinance provides that if any borrower who is liable to a secured creditor under an agreement defaults in repayment of the secured debt, the secured creditor can require the borrower, by a notice in writing, to discharge his entire liability within a period of sixty
days from the date of notice. If the borrower fails to do so, the secured creditor is entitled to take possession of the secured assets and sell them or take other steps to recover the amount due. In case of joint financing done by secured creditors, the secured assets cannot be transferred unless agreed upon by secured creditors representing not less than three-fourths in value of the total outstanding amount due.

Further, in the case *Dena Bank v. Bhikhabhai Prabhudas Parekh & Co.* (unreported), dated April 25, 2000, the Supreme Court of India held that the State Government has preferential right to recover its sales tax dues over the rights of the banks as the secured creditor. The Ordinance, however, does not have any provisions to protect the interests of the secured creditors in this kind of situation. Therefore, the secured creditors will not be in a better position even under the Ordinance, if some other law provides that certain dues will have priority over the dues of the secured creditors.

3. **Borrower in winding-up**

In case the borrower is a company in liquidation, the amount realized on sale of its secured assets is to be distributed as per the order of priority in § 529A of the Companies Act of 1956 (Act). However, if a secured creditor opts to realize its security under the Ordinance and remain outside liquidation proceedings, it will have to hand over the workmen’s dues to the official liquidator of the company from the sale proceeds.

4. **Taking possession of secured assets**

The Ordinance provides that for taking possession or custody of any secured assets, the secured creditor can apply in writing to the Chief Metropolitan Magistrate or District Magistrate, who has jurisdiction over the secured assets or the related documents.

5. **Immunity to secured creditors from legal proceedings**

As per the Ordinance, a secured creditor or any of its authorized representatives will not be prosecuted for any acts done or omitted to be done under the provisions of the Ordinance. The Ordinance further provides that no court or authority shall grant any stay or injunction in respect of actions taken or to be taken under the provisions of the Ordinance.

6. **Similar provisions under existing law**

Provisions similar to the Ordinance in respect of enforcement of security interest are provided under § 29 of the State Financial Corporations Act, 1951. However, this provision applies only if the borrower is an industrial concern within the meaning of that Act.

B. **Conclusion**

The rights under the provisions of the Ordinance are available to all the banks and financial institutions. Under the Ordinance, actions can be initiated against any borrower irrespective of its status. Further, setting up of securitisation and reconstruction companies will introduce a speedy and efficient debt recovery mechanism.

IV. **Turkey: 2001 Crisis, Before and After**

A. **Before**

In 1999 a financial crisis hit the Turkish economy. A stand-by arrangement with the International Monetary Fund (IMF) was established at the end of 1999 to support Turkey's
drive for economic stability and disinflation. The economic program implemented in accordance with the stand-by arrangement envisaged structural reforms and prudent fiscal policies along with a pegged exchange rate regime. The program was successful for some time, but the difficulties of maintaining the pegged exchange rate regime surfaced eventually and inevitably. Questions on the exchange rate system and some shifts in the reform agenda raised concerns on the strength of the program and the Government's commitment to it.

In 2000, the stance of the Government was tested in markets once again. The economic program proceeded with seemingly positive outcomes in the short run. Interest rates came down promptly below projected levels, leading to improved expectations and accelerated consumer confidence. The economy experienced a consumption boom owing partially to the appreciated currency, which in turn produced a very high current account deficit amounting to nearly $5,000,000,000 throughout the first half of the year. However, in the second half of 2000, the Government's commitment to implementing the ambitious structural reforms was being doubted and concerns on the sustainability of the current account deficit were rising. Delays in privatization of state-owned enterprises further contributed to the concerns on the future of the program. Given the high exposure to foreign exchange and interest rate risk, the financial sector was too fragile to withstand such pressure. Panic was the defining element in markets by November. This tension was, however, calmed down temporarily until February 2001 with the support of the IMF and prompt actions on the part of the Government.

B. FEBRUARY 2001

With the illiquid public banks causing pressure on short-term interest rates and disruptions in the market, the underlying fragilities of the financial sector were too deep to recover quickly from a crisis. Consequently, the financial situation of the economy could no longer be sustained and in February 2001, the turmoil in the markets caused the Turkish Lira to devalue by 40 percent overnight, and since February 2001 overall devaluation has reached 110 percent. In order to facilitate the recovery of the economy, the Turkish Government signed yet another series of stand-by and other agreements with the IMF.

C. AFTER

The attempt after February 2001 proved to be unrealistic and the Government was forced to allow the exchange rate to float. Uncertainty about the exchange rate, interest rate, and inflation hit the markets shortly. The Government had to address the decades-long inflation problem in the economy and put together another economic program to remove uncertainties in the market and lay the basis for growth. One of the key elements of the program under the agreements that were considered to be of high priority was the amending of various financial, commercial and other legislation as well as the adoption of new legislation and improvement of certain standards.

After managing the crisis for several months and trying to calm down the markets, Turkey in May announced the Economic Program for Transition to a Strong Economy, encompassing a reinforced structural reform agenda and tight fiscal policies. Fiscal policies have been directed at producing a very high public sector primary surplus to accommodate the increase in the debt stock due to the restructuring of the banking sector and to provide for the efficient use of resources in the public sector. The results of the economic program began
appearing by early August with a certain recovery in production, a decline in interest rates and a more stable exchange rate. Much has been done in attempts to restructure the economy. Between March and June of 2001, sixteen pieces of legislation or regulation was approved by the Parliament and put into force. They range from the deregulation of the electricity market to banking sector regulations. One piece of legislation was the amendment of the Banks Act with the goal of facilitating the strengthening of the economy. The banking system is being reformed by restructuring state-owned banks and regulating the banks whose administrations were assumed by a state agency, the Savings Deposit Insurance Fund (Fund). The amendments may be summarized as follows: providing consistency with EU standards; setting a ceiling for banks on equity participation in non-financial entities (i.e., with the new legislation, a bank is not permitted to acquire or hold more than 15 percent of a non-financial entity and such participation may not exceed 60 percent of its equity); redefining of credit to include derivative transactions including option agreements (i.e., option agreements and derivatives now fall under the definition of credits); loan loss reserves becoming deductibles from corporate income tax base (i.e., banks are permitted deduct loan loss reserves from their corporate tax basis); prerequisites for mergers and acquisitions of banks being set (e.g., provided that the sum of the assets of two banks do not exceed 20 percent of the entire banking sector, a merger or acquisition is not be subject to the Turkish Commercial Code or the Competition Law); granting of privileges to the Fund for the purpose of collecting receivables of the banks whose administrations it assumed; lending limits on a consolidated basis being set; and credit limits for effective monitoring and mitigating of risks being broadened.

The law of the Turkish Central Bank (Central Bank) was also amended. Among the amendments were attempts at keeping the Central Bank free from political influence and making it an autonomous body. It has been authorized to set and implement fiscal policy, keep inflation under control, and supervise banks and financial institutions. The Central Bank has been empowered to request all financial information it deems necessary from private and public entities. One of its tasks is to control the inflation and to set inflation targets in cooperation with the central Government. The Central Bank is prohibited from disbursing any loans or making advance payments to the Treasury or other public institutions. Further, the Government has revoked the permissions for operations of twenty banks and operations of these banks have been assumed by the Fund. Amendments have been made to encourage mergers and acquisitions in the banking sector.

Exemptions from corporate and income taxes have been granted in the event of a merger or acquisition under two conditions:

(i) Exemptions are granted until December 31, 2003 in the event of a merger or acquisition by or between solvent banks. However, a merger or acquisition is subject to the advance approval of the Banking Regulation and Supervisory Agency. The transactions for the merger or acquisition must be initiated within three months after approval.

(ii) If a bank merges with or acquires an insolvent bank under the control of the Fund, the acquirer is eligible to deduct the loss amount shown in the balance sheet of the insolvent bank for a term of up to five years from the date of the merger or acquisition.

The main emphasis of the structural reform process is to create a free and competitive
market in the country and scale down the Government sector and eventually attain and comply with EU standards. The Public Procurement Law and the Public Borrowing Law approved by Parliament are recent examples of this effort. Measures to promote foreign investment are taken. The foreign investment regulations have been reviewed and substantial changes are expected to take place. If these changes can be combined with a decreased inflation rate and stability in the country, increases in direct foreign investment in Turkey will be a more realistic expectation. In furtherance of the program, Turkey will also create an action plan and put it into force in line with the recommendations of the World Bank.

September 11, 2001 was also an impediment to the recovery of the economy. Following September 11, the exchange rate went up again, interest rates jumped, and the stock exchange declined. Furthermore, global recession expectations forced Turkey to make downside adjustments in short-term targets. While the gross national product shrank by 9.4 percent in 2001, new macro policies are expected to yield a growth rate of 3 percent in 2002. With the expected economic recovery and lower real interest rates, the targeted primary surplus should facilitate a decline in the public debt ratio over time. This, in turn, should lead to further declines in interest rates.

Under the expenditure management program supported by the World Bank, the Government has set a gross national product benchmark of 14.5 percent for 2002 for overall social spending in the public sector, including education, health, and social security. However, it is expected that this benchmark will be exceeded.

In order to attain sustainable growth, the Government plans to continue and further the structural reforms around three pillars for 2002 and beyond:

(i) Completing financial sector reforms: Remaining financial sector reforms are aimed at ensuring effective regulation of private banks, the eventual privatization of all state banks, and a more effective corporate restructuring framework.

(ii) Supporting more dynamic private sector development: Private sector development will be supported through initiatives to create a more stable and inviting investment climate, including administrative streamlining, rapid land access and site development, proactive investment promotion and regular Investors’ Council meetings and accelerated privatization. Privatization is one of the most important issues in the Government program. As part of the privatization agenda, the sales of the remaining shares of POAŞ (the petroleum retail distribution network) has been successfully completed; the sale of TÜPRAŞ (state petroleum refineries) is scheduled for the second quarter of 2002; the privatization of Teker (state monopoly for tobacco, alcohol and salt) will follow the enactment of the tobacco law; the privatization of electricity distribution and generation companies, Turkish Sugar Company factories, Turkish Airlines and Türk Telekom are to follow as allowed by market conditions.

(iii) Creating a smaller and more efficient public sector: The plan to reduce public-sector participation in the economy will be accompanied by measures to strengthen fiscal transparency and good governance. Turkey aims to modernize its economy with job creation being driven by a competitive and more productive private sector while limiting the Government’s economic role to effective market regulation in order to couple development with social justice. Turkey’s efforts in reducing the weight of public sector in the economy have begun to give way to a more transparent and business-friendly environment. It is hoped that the private sector will soon take the opportunity to attain the global business standards and to have the potential to compete in international markets. It is also hoped that the benefits of these reforms will become even more evident over the coming years; they might lead to rapidly rising living standards and prepare Turkey for full membership in the European Union.
Social consequences of the economic adjustment program are addressed by the Government as well. While the fiscal policy stance is very tight, real spending in the social sector will be increased in efforts to protect the most vulnerable segments of society.

In conclusion, it is expected that the recent stand-by arrangement with the IMF will improve the economic fundamentals of the country as well as continuing to maintain the reduction in the exchange rate and interest rates and the increasing in the stock market index. Looking ahead, under the circumstances, provided that private sector becomes strong, sound market institutions are maintained and the public sector functions well and in a transparent manner, Turkey can be optimistic and confident about the future of the economy. All these might be regarded as a sign that 2002 will be a starting year for total renewal and transformation of Turkey.