stituting an illicit commercial practice within the meaning of the regulation. In In re U.S.—Japan Agreement on Semi-Conductor Chips[22] the Commission requested a GATT formal consultation procedure, alleging that the agreement at issue illegitimately resulted in raised prices of semiconductor chips to the Community and in discriminatory access to the Japanese market being given to U.S. exporters to the detriment of Community exporters. Clearly both disputes are ones in which the Regulation could ultimately be used against the United States.

Latin America*

The major legal developments in Latin America continue to reflect the severe external debt problems of the region. As discussed below, these problems have produced recent changes in the foreign exchange legislation of Brazil and Venezuela. In addition, significant developments have occurred in the area of taxation. Below we summarize such developments in Colombia and Venezuela.

I. Brazil

On February 20, 1987, the Brazilian exchange control authority, *Banco Central do Brasil* (the Central Bank), issued regulations restricting the payment of interest in U.S. dollars and other non-Brazilian currency to non-Brazilian banks (Central Bank Resolution No. 1263 and Central Bank Circular No. 1131). These restrictions mainly affect medium to long-term loans (i.e., over 360 days) and similar obligations of Brazilian borrowers to non-Brazilian banks outside Brazil.

The new regulations provide that a Brazilian borrower and the Brazilian banks authorized to deal in currency exchange transactions must follow a specific deposit procedure in paying certain interest owed to non-Brazilian banks. For purposes of these regulations, "Brazilian banks" include branches and subsidiaries of non-Brazilian banks chartered to operate in Brazil. To understand this procedure, it is useful to begin by considering the general Brazilian exchange control rules on remittances of interest in non-Brazilian currency from Brazil (the Exchange Control Rules).

22. Press Release IP(86)468.

*Excluding Argentina and Mexico. This report was prepared by Sebastião Mattos, Michael Mensik, and Thomas Studwell, Baker & McKenzie, Chicago, Illinois.

Under the simplest loan mechanism established by the Exchange Control Rules, a Brazilian resident debtor and his non-Brazilian bank lender should obtain prior approval of the terms and conditions of their loan agreement from the Central Bank. Otherwise, the non-Brazilian lender will not be entitled to receive payments of interest and principal in non-Brazilian currency. This approval is issued in a document called a "loan certificate." This certificate specifies, among other things, the amount borrowed in non-Brazilian currency, the principal and interest payment schedules, and the applicable rate of interest. When an interest installment becomes due, the Brazilian borrower presents the loan certificate and Brazilian cruzado equivalent of the interest amount owed to the non-Brazilian lender to a Brazilian bank authorized to deal in currency exchange transaction. After reviewing the certificate (and, in some instances, obtaining a prior clearance from the Central Bank), the Brazilian bank converts the cruzados into non-Brazilian currency (e.g., U.S. dollars) for remittance to the non-Brazilian lender abroad.

The recently issued regulations retain this basic procedure, but add a significant new step. After the Brazilian bank converts the cruzados into non-Brazilian currency (e.g., U.S. dollars), the new regulations provide that the Brazilian bank may not remit the non-Brazilian currency interest installment to the non-Brazilian lender abroad. Instead, this installment (denominated in U.S. dollars or other applicable non-Brazilian currency of payment) must be deposited in an account opened with the Central Bank in the name and for the benefit of the non-Brazilian lender. These non-Brazilian currency amounts are indefinitely blocked in Brazil.

The Central Bank and relevant non-Brazilian banks and financial institutions presumably will eventually reach an agreement on when and how these blocked deposits (as well as future interest and principal payments) will be remitted abroad. As of the date of these remarks, however, no such agreement had been reached.

II. Colombia

On December 23, 1986, Colombia enacted Law 75/86, which introduces far-reaching changes in the Colombian tax legislation (the Tax Reform Law). In general, the Tax Reform Law applies to the 1986 and subsequent tax years. It unifies and reduces certain tax rates, as well as eliminates many exemptions, deductions, and tax credits. In addition, the Tax Reform Law adds various previously tax-exempt organizations to the tax rolls.

A. Foreign Companies

The Tax Reform Law establishes a general unified income tax rate of 30 percent for foreign companies deriving income from Colombia. It increases the tax rate applicable to dividends remitted to foreign companies, which formerly were subject to withholding tax at the rate of 20 percent (unless the foreign company is organized in a tax haven country, in which case the applicable dividend withholding tax rate was 40 percent). However, because the withholding tax on most other categories of income (e.g., interest, royalties, and rental payments) previously was 40 percent, the Tax Reform Law should benefit most foreign companies deriving income from Colombia.

This general observation must be qualified at least in two respects. First, the Tax Reform Law will not benefit foreign companies deriving income in Colombia through a branch or quota company (*sociedad de responsabilidad limiteda* or S.R.L.). Under prior law income derived through a Colombian branch was subject to remittance tax at the rate of 20 percent. Income derived through an S.R.L. was subject to remittance tax at the rate of 14 percent. The rates applicable to such income presumably will rise to 30 percent under the Tax Reform Law. Second, the Tax Reform Law also will adversely affect certain foreign companies that previously were benefitting from a certain reduced tax on payments for so-called "technical services."

B. Colombian Companies

Under prior law a Colombian corporation (*sociedad anonima* or S.A.) was subject to income tax at the rate of 40 percent, and a Colombian S.R.L. was subject to tax at the rate of 18 percent. The Tax Reform Law establishes a single tax rate of 30 percent for both types of companies. In addition, it establishes a tax exemption for dividends or profits received by Colombian companies (or individual residents) from other Colombian companies, subject to certain reporting and accounting requirements.

C. Capital Gains

The Tax Reform Law establishes a unified rate of 30 percent applicable to capital gains (i.e., *ganancias ocasionales*) realized by Colombia or foreign companies. Under the prior law the applicable rate was 40 percent for foreign companies and Colombian S.A.'s and 20 percent for Colombian S.R.L.'s. The Tax Reform law also repeals certain previously available exemptions (e.g., the reinvestment exemption) and modifies the rules on adjustments of tax basis.

D. Miscellaneous

The Tax Reform Law introduces a series of changes applicable to Colombian citizens or residents. It also adds certain previously tax-exempt organizations to the tax rolls, repeals various previously available tax deductions and credits, and grants amnesties for omitted assets and past due returns and income taxes. In addition, the Tax Reform Law contemplates certain changes in the stamp tax and sales tax and proposes certain changes in the import taxes (other than import duties). In particular, it increases the stamp tax rate on private documents from 0.45 percent to 0.5 percent. This tax now applies to agreements executed outside of Colombia that will be performed or generate obligations in Colombia. The Tax Reform Law, however, establishes that certain types of documents will be exempt from stamp tax (e.g., offshore loans and patent, trademark, and trade name applications).

III. Venezuela

In the last quarter of 1986 and the first quarter of 1987, Venezuela enacted significant new tax and foreign exchange legislation.

A. Tax

The new Income Tax Law (the 1986 Law) was published on October 3, 1986, and is applicable to all tax years beginning after October 16, 1986. The 1986 Law introduces a number of important changes from the prior income tax law relevant to foreign companies doing business in or with Venezuela. In a major departure from the principle of strict territoriality—historically a cornerstone of Venezuelan income tax legislation—the 1986 Law subjects to Venezuelan income taxation certain passive income derived by Venezuelan residents and domiciliaries from sources outside Venezuela. Thirty-five percent of the gross amount of such passive income (primarily rents, dividends, interest, royalties, annuities, and trust income) is deemed net taxable income and is subject to a flat tax of 40 percent, yielding an effective tax rate of 14 percent. In addition, the 1986 Law characterizes as Venezuelan source income fees and other compensation derived from the performance outside Venezuela of activities relating to the import of goods and services. Thirty percent of payments from Venezuelan importers to persons outside Venezuela who provide certificates of price, quantity, or quality is deemed net taxable income, subject to taxation at the applicable marginal rates.

The 1986 Law also changes the marginal income tax rates applicable to corporations. The five marginal rates contained in the prior law are reduced to three in the new law: 15 percent applicable to net taxable income of Bs. 0.01 to Bs. 500,000; 35 percent applicable to net taxable income of Bs. 500,001 to Bs. 5,000,000; and 50 percent applicable to net taxable income in excess of Bs. 5,000,000. Under the prior tax law, the maximum rate of 50 percent was not reached until taxable income exceeded Bs. 20,000,000. In addition, the new law increases from 15 percent to 20 percent the withholding tax applicable to interest paid to nondomiciled foreign financial institutions in respect of loans and other credits.

The 1986 Law introduces the principle of consolidation to Venezuelan income tax legislation. The net gains and losses of corporations engaged in the same activities and controlled by the same persons are required to be consolidated for the purposes of determining the applicable income tax rates. Regrettably, the consolidation provisions are unclear and imprecise. Until the income tax authorities issue further clarification, the consolidation rules will likely result in frequent disputes with the tax authorities.

The 1986 Law provides that payments to foreign suppliers of technical assistance or technological services are not deductible if the assistance or services could have been obtained within Venezuela. The taxpayer is required to provide evidence to the tax authorities of its efforts to obtain such services within Venezuela. This rule creates an obvious disincentive to the import of technology, which is already subject to regulation under the Venezuelan Andean Pact rules.

B. Foreign Exchange

On December 8, 1986, the Venezuelan Government enacted Decrees Nos. 1,379 and 1,380 and revised Exchange Agreements *(Convenios Cambiarios)* Nos. 1 and 2. This legislation, with implementing regulations promulgated in the early months of 1987, established significant changes in the Venezuelan foreign exchange rules.

A new controlled exchange rate of Bs. 14.50 to the dollar was created. This rate is applicable to payments for all imports of goods or services other than medicine, food, and other essential items designated by the Finance Ministry, which still may be imported at the rate of Bs. 7.50. In addition, private sector exporters are now obligated to sell the foreign currency proceeds of their exports to the Central Bank at the rate of Bs. 14.50 to the dollar. Exporters may not receive payment for their exports in Venezuelan currency.

The 14.50 rate is also applicable for the conversion into bolivars of new direct foreign investments and foreign credits and the registration of foreign investments and reinvestments. The Central Bank will sell foreign currency at the 14.50 rate for remittances of dividends and royalties, for payments of principal and interest on foreign loans registered after December 8, 1986, and for capital repatriations in respect of foreign investments registered after December 8, 1986. The purchase of foreign exchange at the preferred rate for such remittances will require the prior authorizations from the Office of the Superintendent of Foreign Investments