

Paraguay

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Asuncion

On August 15 2003, Paraguay inaugurated a new administration under President Nicanor Duarte Frutos. Unlike his predecessors, President Frutos proposed major changes to the economic and political situation. Tax reforms presented to Congress, a letter of intent with IMF, the renewal of the Supreme Court – with the removal of six of its nine members – and other changes to the judiciary system, a new internet-based government purchase system and other administrative anti-corruption measures are signs of progress. One of the results has been a 44% increase in tax collection rates compared to a similar period a year before.

Paraguay is a full member of Mercosur, together with Argentina, Brazil and Uruguay. Mercosur is the largest commercial area in South America, with more than 11 million square kilometers, 200 million consumers and a combined GDP of more than \$1 trillion. Paraguay recently obtained a special treatment for origin rules within Mercosur for 10 years (beginning in 2004). By this agreement, goods made in Paraguay need to be added with just 40% of their final (cost) value, between any or all the four country members of Mercosur in order to be considered Made in Paraguay (up to 2008) – that means zero duties on imports of Paraguayan products into the Mercosur countries. From 2008 to 2014, this percentage will rise from 40% to 50%. General rules applied to the other Mercosur countries require the addition of at least 60% of the value in the region (20% higher). That makes Paraguay an interesting option for the production of those products or components currently imported into the region.

Paraguay and IMF

On December 15 2003, the IMF executive board approved a 15-month standby arrangement for Paraguay to support the country's economic programme. This programme is intended to create better conditions for sustained economic growth and poverty reduction, addressing long-standing governance problems by improving the efficiency and transparency of government operations. Fiscal surplus is one of the programme's goals and, as tax collection this year has shown a 40% average improvement compared with last year, success seems more likely. The programme

also aims to attain structural reforms in the public sector and the public banking system.

This arrangement is opening the doors for new credits from international agencies, mainly for infrastructure improvement. Some of these disbursements have already been made and the balance is expected for 2004.

Protecting foreign investors

Foreign Investment Law 117/91 gives foreigners the same guarantees, rights and obligations enjoyed by Paraguayan investors. Paraguay has signed the Multilateral Investment Guarantee Agency Agreement (Miga) of September 13 1991. The Miga, created under the umbrella of the World Bank, insures investors against risks such as expropriation, currency inconvertibility and damages caused by revolution, war or civil strikes. A similar agreement with the Overseas Private Investment Corporation of the US is in effect. The US agency has lifted restrictions regarding investments in Paraguay in recognition of its progress.

Dispute settlement: arbitration

Paraguay is a party to several international conventions and treaties intended to protect foreign investment: the World Bank Centre for Settlement of Investment Disputes as an independent international agency was ratified under Law 944/82; the Inter-American Convention on International Commercial Arbitration was ratified as Law 611/76; and the New York Convention for the Enforcement of Foreign Arbitral Awards and Judgments was ratified as Law 1.879/02.

Immigration

Nationals and foreigners are equal before the law. Foreigners can become residents if they comply with formalities and requirements established in the 978/96 Law. Foreign directors, managers and employees can apply for residence in the country, and a special temporary visa is granted to Maquiladoras employees.

Investment and exports promotion programme

The Investment Promotion Law 60/90

Paraguay actively promotes foreign investment in the industrial and service sectors. Investment projects require a presentation to the Investment Council, which is responsible for evaluation. Formal approval needs a bi-ministerial resolution, signed by the

Ministry of Industry and Commerce and the Ministry of Finance. Some of the benefits of this law are: exemption of 95% of the corporate income tax on net profits for five years (and in some cases up to a maximum of 10 years) (the general tax rate is 30%, reduced to 1.5%); total exoneration of importation duties on capital goods (including VAT in some cases); duty free importation of raw materials and other inputs could be granted (application required); remittance of profits abroad is free (general withholding tax rate is 5%); exoneration of municipal taxes and tax on loans are available under certain conditions.

Maquiladoras in South America: The Maquila Law 1064/97

The Maquila Law regulates the manufacture of goods for export. Some services are also eligible as long as they are exported. The Maquila Law requires a manufacturing contract between a non-resident person or company with a Paraguayan counterpart, and presentation of an investment proposal to the Maquila Council for its approval by bi-ministerial resolution (again, signed by the Ministry of Industry and Commerce and the Ministry of Finance).

Among the benefits of the Maquila programme are: substitution of the corporate tax on net profits (30%) by a 1% tax on national value added. The import taxes and duties on capital goods, raw materials, parts, components and inputs – including VAT – are suspended, and a guarantee for the same value is required.

Duty free areas

The introduction and storage of goods in the Paraguayan territory is permitted through the duty free areas, with suspension of all import taxes. They must operate in private properties and be approved by presidential decree. Commerce, industry and services could be performed in those areas. The tax rate is 0.5% on invoices, and no other tax applies as long as the goods are not sold in Paraguayan territory. There are two duty-free areas in the eastern area, near the borders with Brazil and Argentina.

Taxes

The most important aspects of the tax legislation in Paraguay are:

- *Corporate tax on net profits*
The tax rate on corporate net profits is 30%. Financial entities pay this tax only when profits are distributed, not if they are re-invested or incorporated as reserves.
- *VAT (IVA)*
The rate is 10%. It does not apply to bank loans, deposits and its interest.
- *Tax on acts and documents*
This applies to obligations, acts and contracts evidenced by documents. Acts involving financial intermediation are taxed. The rate is 1.5%.

Lowering taxes: The tax reform law project

Partial approval of the new tax code has been given by the Chamber of Deputies, but approval by the Senate is still pending. Discussions are still being held, but there is general consensus on the structure of the reform and its importance.

If approved, the tax on non-distributed net profits will be reduced to 15% during the first year of the Law's application and to 10% from the second year and after (the current rate is 30%) and remittance of profits abroad will be taxed by an additional 15% – the latter not applicable to companies covered by the Investment Promotion Law, which is set to continue in force. Personal income tax should be introduced with a 10% rate, and VAT rate will stay at 10% for most products and services, with a reduction to 5% for printed materials, interest on loans, assignment of use of goods and real estate sales. Agricultural products are exempt. Withholding tax on interest paid abroad will be 7% during the first year of the Law's application and 6% from the second year and after.

The Maquila Law (1064/97) will retain all of its benefits. The Investment Promotion Law (60/90) will continue in force but without the exoneration of 95% of the taxes on net profits for five years, meaning that instead of paying 1.5% for five years – and 30% from the sixth year and after – there will be a permanent 10% tax rate.

Better climate for investment

Paraguay's new government has launched an ambitious reform programme intended to raise economic growth, reduce poverty, and improve governance. First results are encouraging and a better climate for investment can be felt. New agreements set the best conditions ever to take advantage of the country's Mercosur membership. Confidence, transparency and internal broad consensus are being actively sought both by government and civil society organizations. Hopefully, Paraguay is entering a new era.

Corporate and commercial

Recommended firms

Tier 1

Fiorio Cardozo & Alvarado

Estudio Juridico Gross Brown

Estudio Mersan

Moreno Ruffinelli & Asociados

Peroni Sosa Tellechea Burt & Narvaja

Vouga & Olmedo

Fiorio Cardozo & Alvarado

Fiorio Cardozo & Alvarado advises on banking, gas and oil, telecommunications, tax, civil, and labour law, and has managed to remain active despite the recent drought of foreign investment in Paraguay.

In banking – where Fiorio Cardozo has excellent local relationships – the firm assisted mobile telephone company Nucleo in relation to local guarantees regarding the restructuring of its foreign debt, and represented Bank of America in connection with the purchase of debt issued by a local trust. Highlights of its M&A deals, meanwhile, were advising Financiera General and Financiera Familiar on their merger, and providing counsel to Louis Dreyfus in respect of its purchase of four cotton ginners in Paraguay.

The firm has an impressive international client roster, including ABN Amro, the Export-Import Bank of China, McDonald's, AT&T, Nestlé and GlaxoSmithKline.

Leading lawyers

Rafael Marcelo Alvarado

José María Cardozo Saguier

Key contact partner

Rafael Marcelo Alvarado

Estudio Juridico Gross Brown

Estudio Juridico Gross Brown is described as “a boutique specializing in banking,” and has long been the leading Paraguayan firm for banking and finance transactions, although it is also more than capable of advising on commercial and labour law, insolvency, and oil and gas. Its client roster has recently suffered a slight blow, however, after ING Bank's decision to cease its activities in Paraguay and Citibank's move to drastically reduce its operations in the country.

Most of the largest deals Gross Brown acted on last year were, as might be expected, in the banking and capital markets sectors. For example, the firm advised Citibank in relation to the sale of its retail and consumer assets in Paraguay, and represented a syndicate of banks in a restructuring package of Telecom/Personal Mobile Phone's \$75 million debt. Gross Brown further advised a banking syndicate that included ABN Amro and Vereins & West Bank on a \$30 million pre-export financing loan to local agro-exporters, and provided advice to the Shell Group in connection with the sale of its forestry business to a private Argentine group. Among the firm's other

clients are Lloyds Bank, Lehman Brothers and British Aerospace.

Jorge Gross Brown leads the four-partner firm, and is widely considered one of the leading banking lawyers in Paraguay. Atilio Gomez Grassi is another well-regarded banking specialist, who also handles labour law and litigation cases.

Leading lawyers

Jorge Gross Brown

Atilio Gomez Grassi

Key contact partners

Eduardo Gross Brown

Jorge Gross Brown

Atilio Gomez Grassi

Estudio Mersan

Estudio Mersan was founded in 1944 by Carlos A Mersan, who still practises at the firm as a tax and administrative law specialist. This four-partner family firm is “rather small and does mainly intellectual property work” but “works with some good local clients”. Outside of tax and intellectual property, it occasionally advises on corporate, banking and administrative law.

Estudio Mersan is a member of the Bomchil Group, an affiliation of Latin American law firms from 17 different jurisdictions in the region.

Leading lawyer

Carlos A Mersan

Key contact partner

Carlos A Mersan

Moreno Ruffinelli & Asociados

Moreno Ruffinelli “has more local than international clients,” according to one source, but is nevertheless making successful progress in adding multinationals to its client roster. Among those the firm has advised are the International Monetary Fund, Shell, Siemens, Credit Lyonnaise, Kodak, Credit Suisse and the World Bank.

A diverse team of 19 senior lawyers gives Moreno Ruffinelli the capacity to provide comprehensive counsel on diverse areas of corporate, banking and litigation law. The team is headed by founder José Antonio Moreno Ruffinelli, former legal adviser to the Paraguayan Central Bank and Ministry of Foreign Affairs and an authority in banking and commercial law. Managing partner José Antonio Moreno Rodríguez is also widely praised for his expertise in capital markets and foreign investment issues.

Highlights of the transactions the firm has acted on this year include the restructurings of Chinatrust Commercial Bank and Philips Paraguay. The firm continues to provide advice to the International Finance Corporation in a transaction valued at about \$30 million, and recently advised on setting up the first sports trust in Paraguay.

Leading lawyer

José Antonio Moreno Rodríguez

Key contact partners

José Antonio Moreno Ruffinelli

Carlos D Ruffinelli

María del Rocío Penayo Zarza

Peroni Sosa Tellechea Burt & Narvaja

Peroni Sosa Tellechea Burt & Narvaja was strengthened in 2003 when Enrique Sosa rejoined the firm after serving as Supreme Court Justice. His move back to private practice reinforced an already excellent legal outfit whose leading light is the hugely respected Guillermo Peroni, an expert adviser on privatizations and foreign investment matters. Peroni Sosa is a regular adviser to the Paraguayan government on development strategies, and works closely with Congress when the government requires assistance on drafting new legislation. In total the firm comprises seven partners and 12 associates.

Despite the stagnant economy and consequent lack of foreign investment in Paraguay, Peroni Sosa has advised on a few noteworthy transactions, principally in banking and oil. For example, the firm acted on the acquisition of Forestal Yguazy when it was sold by Shell Forestry to an Argentinean investor. It has also worked for oil prospectors CDS, providing advice on a state licence for mineral exploitation.

Peroni Sosa is the sole Paraguayan member of international law firm network Lex Mundi, and also belongs to international law firm network Club de Abogados.

Leading lawyers

Guillermo Peroni

Enrique Sosa

Vouga & Olmedo

Vouga and Olmedo has strength in depth in all areas of commercial and corporate law. The two leading partners at the firm, Gustavo Olmedo and Rodolfo Vouga, founded the firm in 1976 and are both noted for their experience and aptitude in providing solid advice on banking, M&A and foreign investment matters. The firm also has arguably the strongest litigation department in Paraguay.

In recent times Vouga & Olmedo has represented Brazilian oil corporation Petrobras on a number of public bids, and also advised PricewaterhouseCoopers in connection with Coca-Cola's purchase of 96% of Paresa Bottling. The firm's other notable clients include Merrill Lynch, Bear Stearns and Dresdner Bank.

Leading lawyers

Gustavo Olmedo

Rodolfo Vouga

Key contact partner

Rodolfo Vouga