DEVELOPING MAJOR PROJECTS IN BRAZIL

Report of seminar 178 held on 16th May 2013
at Institution of Civil Engineers, 1 Great George Street, London

SUMMARY
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<th>Speaker</th>
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<td>09:45</td>
<td>Coffee &amp; registration</td>
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<td>10:15</td>
<td>Chair’s introduction</td>
<td>Paula Walsh, HM Consul General Rio de Janeiro</td>
<td>British Consulate Rio de Janeiro</td>
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<td>10:25</td>
<td>Brazil’s pipeline of major projects</td>
<td>Victório Semionato, Vice President, Engineering</td>
<td>Mendes Júnior Trading e Engenharia S.A.</td>
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<tr>
<td>10:55</td>
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<tr>
<td>11:45</td>
<td>Doing business in Brazil</td>
<td>Andres Beran, Vice President – Sales Latin America</td>
<td>Fluor Ltd</td>
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<td>12:15</td>
<td>Avoiding legal risks in major projects in Brazil – an international counsel experience</td>
<td>Luiz Aboim, Senior Associate</td>
<td>Freshfields Bruckhaus Deringer</td>
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<td>12:45</td>
<td>Panel discussion</td>
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<td>14:30</td>
<td>Major projects in Brazil – a funder’s perspective</td>
<td>Rafael Marchesini, Manager, London Office</td>
<td>Brazilian Development Bank BNDES</td>
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<td>15:00</td>
<td>Discussion</td>
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<td>15:30</td>
<td>Challenges of delivering construction projects in Brazil</td>
<td>Victório Semionato, Vice President, Engineering</td>
<td>Mendes Júnior Trading e Engenharia S.A.</td>
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<td>16:00</td>
<td>A major Brazilian transport project – TAV</td>
<td>Jon Clyne, Associate Director</td>
<td>Halcrow/CH2M HILL</td>
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<td>16:50</td>
<td>Full panel discussion</td>
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<td>17:20</td>
<td>Chair’s closing comments</td>
<td>Paula Walsh, HM Consul General Rio de Janeiro</td>
<td>British Consulate Rio de Janeiro</td>
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<td>Drinks reception</td>
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PURPOSE
The objective of the seminar was to provide a clear overview of the pipeline of major projects in Brazil; to offer an understanding of how major projects are delivered differently compared to the UK, as well as an honest view of the challenges of delivering major projects in Brazil.

KEY MESSAGES
• Brazil will soon be the fourth largest economy in the world; it offers huge opportunities for those brave and pragmatic enough to do business there. But it is not for beginners and, as for all countries with an emerging economy, not for those with a short-term focus.
• A local partner is essential for building up local relationships and navigating the fiscal and regulatory frameworks. It should be noted that there are regulatory differences between individual states and individual cities, so even good local partners may not be able to see the whole picture.
• There is a clear will by the Brazilian Government to try to improve the infrastructure of the country. The establishment of the Brazilian planning and logistics company Empresa de Planejamento e Logística (EPL) has made the strategic planning of the logistics project pipeline clearer, but it is still a nascent organisation.
• The Brazilian Government is embracing the concession/PPP model for the majority of infrastructure investment – this is based upon the UK model and there is therefore a willingness to learn from us.
• The pipeline of projects is far greater than the local resources available to deliver it, so foreign participation is being sought, both in terms of financing as well as delivery.
• BNDES, the Brazilian Development Bank, has an important role in helping to fund projects of importance to the Government and therefore has a remit to offer equity funding and low interest loans to key projects.
• The taxation and bureaucratic burdens are far higher than in the UK and Europe, but must be navigated. Businesses will inevitably run into issues of taxation and labour.
• Historically, the country has been troubled with corruption. The tide of public opinion on this is changing and, whilst it still goes on, it is possible to do business in a manner which avoids it.
• English is only prevalent at the senior levels of organisations. All government departments will require local certifications and documentation in Portuguese, and often these need local accreditation.

KEY LESSONS
• Find a local partner with whom you have a shared philosophy, as well as good accountancy and legal representation.
• Do not underestimate the importance of due diligence, on partners, advisers and suppliers.
• Dedicate resources to producing a paper trail of compliance and evidence of contract changes.
• Do not underestimate the length of time and the amount of work it will take to secure permits and licences, or to progress supplies and equipment through the ports.
• The tax system is NOT the place to be creative.
• Plan Brazilian – listen, ask, understand; once you have made a decision, there is no turning back.
Infrastructure investment in Brazil has tripled over the last ten years, reaching $100 billion in 2012. Due to factors such as demographic changes and the demands of economic expansion the country has had to accelerate its infrastructure development – for example, between March and September 2013 the Government will make concession auctions for 7,500km of highways and 10,000km of railways, as well as extra airport and port capacity. There will also be further bidding rounds for oil and gas, hydro and wind power projects, and the installation of 23,200km of electricity transmission lines. EPL, the logistics company set up to deliver these projects, has the largest portfolio of infrastructure projects in the world.

Chaired by Paula Walsh, HM Consul General Rio de Janeiro, this full day seminar offered an insight into how the public and private sectors are planning to deliver these projects, and some of the issues that they face – for example, the intended infrastructure boost is coming at a time when the Brazilian economy is slowing down and the supply chain for major projects is stretched to its limits. This will pose corporate, financial and legal challenges to employers and contractors involved in delivering projects in Brazil in the coming years.

The first presentation of the day, given by the Vice President of Engineering at the Brazilian company Mendes Júnior, discussed why Brazil currently provides opportunities for companies involved with major projects.

Starting with an overview of Brazil’s geography and demographics, the presentation went on to look at how the economy had developed in recent years, and the subsequent demands placed upon the country’s infrastructure. For example, there has been an increase of over 200% in the trade flow with the rest of the world over the last decade. This has led to the need for improved infrastructure, to facilitate the import and export of goods through ports, railways, highways and airports.

A number of large infrastructure programmes have been announced over the last two years. The value of investment involved will be around R$470 billion (US$235 billion) in the coming years – and this excludes the major urban infrastructure works necessary for the 2014 World Cup and the 2016 Olympics Games.

The session provided a snapshot of these programmes from the perspective of the Brazilian construction engineering market – such as the size of investment, timescales, the role of the PPP model, how concessions are awarded, and some of the challenges. The programme areas discussed included highways, ports, airports, railways (including high speed rail), energy, transmission, sanitation, and oil and gas.
This session looked at the Brazilian market from the perspective of Fluor, one of the world’s most diverse engineering construction companies.

It was noted that Brazil is not an easy country in which to conduct business – the World Bank’s Ease of Doing Business Index ranks Brazil 130 out of 185 countries. For instance, the business culture and values are different and for the most part internally focused – although this is changing fast with the realisation that long-term growth is dependent on the ability to integrate into the global marketplace.

As part of an initiative to enter the Brazilian market, Fluor embarked on an evaluation and selection process to find a Brazilian joint-venture partner. Initial advice from consultants and organisations was varied and sometimes contradictory. The conclusion was that every opportunity is different, and there is no recipe to follow. With this in mind, the presentation outlined some of the most important elements that need to be considered when undertaking business in Brazil.

For example, a great deal of preplanning is required to make sure the right decisions are made; employ a reputable local business adviser to help with the process, and do not try and save money. Incorporating the business is another area that requires accurate advice and where it does not pay to save money.

As far as operating the business is concerned, governance must be defined in detail, particularly for partnerships. The majority of organisations involved in major projects are labour-intensive, and the labour market is another area that needs to be handled with care – most activities are unionised, with different union contracts for different sectors.

Above all, the need to study, understand and plan operations, both at the beginning and throughout the life cycle, must not be underestimated.

The third presentation, from Freshfields Bruckhaus Deringer, outlined how the global financial crisis and the slowdown of the Brazilian economy have squeezed the supply chain for major projects. It was explained that this has had serious consequences for both existing and upcoming projects. For example, delays due to labour shortages and other resources have led to an unprecedented number of contracts being terminated, and to very complex disputes which may disrupt or adversely impact the economics of major projects.

Against this background, the presentation looked at the need for more active risk avoidance and management by both contractors and employers. When the supply chain is stretched and competing for the same resources certain risks are common to employers and contractors. They fall broadly into five categories: corporate, operational, reputational, financial, and litigation/arbitration. Looking at each of these in turn, it was stressed that the organisation must be alive to the nature of the risks and their possible consequences, avoiding disputes wherever possible.

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Some of the questions asked by foreign clients seeking advice in relation to Brazilian projects were outlined, such as the principles of the Brazilian Construction Code, and the pros and cons of using Brazil as a seat for arbitration in a contract. This was followed with a detailed look at various measures that can be used to avoid disputes – for example the use of new or existing levers to improve delivery.

The presentation concluded by noting that there is no model solution to avoiding legal risks or disputes, while at the same time protecting project delivery. Bespoke strategic planning and preparation is required – for example designing an effective dispute resolution strategy for each project, or assessing the impact on project delivery before drawing on guarantees and bonds or terminating important contracts.

This presentation outlined the history of BNDES (the Brazilian Development Bank), and its role as both a development and financing institution within the Brazilian economy. This overview was set against the backdrop of the changes to Brazil’s institutional and political framework – for example, it was explained that after a long period of economic instability, Brazil has achieved a 20-year track record of relatively stable macroeconomic policies, with an independent central bank and strong fiscal regulations in place.

BNDES is a state-owned federal development bank. Founded in 1952, its mission is to foster sustainable and competitive development in the Brazilian economy, generating employment while reducing social and regional inequalities. As a development institution, it was explained that BNDES is a key instrument of the Federal Government for implementing industrial and infrastructure policy in Brazil. As a financial institution, it provides well over 50% of long-term financing for infrastructure projects. However, the bank has also been working with the Federal Government to develop the Brazilian capital markets, to encourage both foreign and domestic investors to invest in infrastructure securities.

Examples of areas in which BNDES provides finance include infrastructure projects worth over R$10 million, social programmes such as urban transport systems, and cultural projects, including historic building restoration. BNDES also manages the Amazon Fund, created by the Federal Government to raise funds to preserve and promote the forest’s sustainable development.

As a development bank, BNDES follows government guidelines, targets and objectives. To illustrate the basic framework for projects financed by the bank, the presentation outlined the guarantees and other conditions required as part of the support for an ongoing major hydroelectric scheme – the project is worth over £9 billion, of which BNDES is funding over £7 billion.
Building on his earlier talk, in this presentation the Vice President of Engineering at Mendes Júnior discussed some of the challenges and procedures involved in delivering major infrastructure projects in Brazil.

The importance of understanding the Brazilian construction market and the conditions in which companies operate was stressed. Taking advice from people locally is recommended – they can provide the information needed to prepare an accurate preliminary feasibility study. There are many areas of operation which pose potential risks for foreign companies operating in Brazil, and these should not be underestimated – for example the complexities of industrial relations, labour laws and the interpretation of tax law; environmental licence requirements at ports; or intervention from government agencies.

The different types of project sponsors (both public and private) were discussed, along with the structure of the contracts that currently operate in Brazil and the various forms of contracting process. This was followed with an overview of the complex legislation governing contracts, concessions and bidding for projects. Public clients are agents of the Federal Government, the provinces and municipalities, and sponsor major infrastructure projects such as urban infrastructure using PPP contract models and concession auctions.

Some of the ways in which design and construction companies can participate in the Brazilian market were outlined, such as acting as technical advisers or entering into partnership with a Brazilian company. It was noted that opening a branch office in Brazil is not straightforward, and Brazilian people are required locally to deal with the complexities and bureaucracy of the regional registration procedures.

Every year over seven million people travel between Brazil’s two largest cities, Rio de Janeiro and São Paulo. When the US$20 billion Trem de Alta Velocidade (TAV) high speed train link is up and running, a significant proportion of them will move from congested airports and highways, and onto state-of-the-art trains running at speeds of up to 350kph. The scheme has now been approved, and work on the 515km route is due to begin in 2014–15.

This presentation, from Halcrow/CH2M HILL, looked at the background to the TAV project, some of the challenges in developing the feasibility study, and what lessons could be learned that might be relevant for other major projects.

The study spanned the whole range of technical activities from traffic and revenue, and economics through to operation and engineering feasibility. Many of the challenges, such as changes in scope, unrealistic deadlines or language barriers might well be found elsewhere; others reflect the unique nature of working in Brazil – for example the lack of technical expertise in engineering, the technical challenges of working in a country with a very limited passenger rail network, or the complexities of the company registration procedure.
One of the lessons learned concerned the procurement process – existing models that might be applicable to a power or highway scheme were found not to be suitable for a project of this scale. Lessons learned from high speed rail projects such as High Speed 1 in the UK endorsed the need for a flexible procurement route map that is adapted to the context of the country.

The presentation concluded with a few observations about working in Brazil. For a foreign company it is important to have people in the resident workforce who have a good working knowledge of Portuguese. Also, since meetings with government are conducted in Portuguese, it is advisable to attend with a Portuguese speaker.

In summing up the proceedings the Chair noted that there is a clear infrastructure demand in Brazil, as well as a clear government will and finance available to meet that demand and expansion. There are also some very real challenges in delivering projects on time and on budget.

It was acknowledged that doing business in Brazil is not always easy – patience, good Brazilian partners and sound advice are essential criteria for success. However, for companies with a long-term focus it is worth putting in the effort, the time and the money to understand the Brazil context and to build partnerships.
AECOM
Active Risk
Babcock International Group
Bechtel Ltd
Brazilian Development Bank BNDES
British Consulate Rio de Janeiro
Capital Dynamics Ltd
CH2M HILL
CMS Cameron McKenna LLP
EC Harris LLP
Embassy of Brazil
Fluor Ltd
Freshfields Bruckhaus Deringer
Halcrow
Major Projects Association
Mendes Júnior Trading e Engenharia S.A.
Mott MacDonald
National Audit Office
PA Consulting Group
Parsons Brinckerhoff
PricewaterhouseCoopers
Risk Solutions
School of Construction and Project Management, UCL
Siemens UK plc
The Nichols Group
Transport for London
Turner & Townsend
UKTI
University of Leeds