Brazil

Negotiated M&A Guide

Corporate and M&A Law Committee

Contact

Maria P.Q. Brandão Teixeira

BRANDÃO TEIXEIRA, REIS, VIEIRA PINTO ADVOGADOS
São Paulo, Brazil, 2017

maria.brandao@brandaoteixeira.com.br

I. INTRODUCTION

1.1. In the last 40 years Brazil has undergone a remarkable political and economic transformation which, with the support of globalization, has drastically changed the business local scenario and practices. Yet the last three years have dramatically and astonishingly changed the country and its business environment. Starting in year 2014, the most relevant investigation on corruption has become a turning point for Brazil and Brazilians hope this will be a point of no return. Business has suffered serious impacts and Brazilians are paying a high price for cleaning the wrong practices. Nevertheless, there is a growing expectation that the changes will come for better.

1.2. Until the final two decades of the twentieth century Brazil has been quite non-attractive for foreign investments but from 1990 to 2015 the growing Brazilian economy has completely changed the picture and has transformed Brazil into one of the most attractive countries to invest. In particular, the new millennium has seen the development of huge Brazilian conglomerates with relevant presence in the international business transactions and investments. Inside and outside the country, Brazilian and non-Brazilian corporations have done business and M&As have become usual business talk.

1.3. An apparently small and routine investigation in a car wash store in the city of Curitiba, in the State of Paraná, south of Brazil, in 2014, has triggered a giant investigation that resulted in the impeachment of the president, the imprisonment of some of the most powerful entrepreneurs in the country and some important deputies and senators. Similar investigations have been triggered in other countries of South America and Africa and have also resulted in impeachments and imprisonments. Police collaboration with other countries, in particular with Switzerland and the United States of America, but not only these two, have closed the loops and billions of dollars of the United States, in different currencies, have been recuperated. The most important Brazilian corporation, controlled by the federal government but listed in the São Paulo and the New York Stock Exchange, Petrobrás, has been the most relevant victim of corruption, the immediate loss calculated in more than USD 2 bilion. Employment has gone significantly down. In one year 13 million employees lost their jobs and the rate of unemployment in the country has increased in 10%. As a consequence, there has been a destructive impact in the consumption of the population and an increase of insolvencies and bankruptcies.

1.4. In mid-2017, when this article is being written, the political scenario is still far from recovering but the economy has started to improve. Petrobrás is now well and seriously managed and has recovered the grades from the classification of risk agencies. All conglomerates involved in leniency agreements, and their officers and directors that have done plea bargaining transactions with the public prosecutors, are now selling their business, or part of them, to pay the heavy fines and return their criminal gains. As a result, despite the heavy political environment, M&A transactions are pretty much on the top of priorities.

1.5. At this point, not only the sales led by the businesses affected by the “Car Wash” criminal disclosure are significant. As the business activity has been severely affected during these last three years, several companies have lost their in investment capacity and are eager for a partner or even to change hands. Bankrupt business that in the past have had a significant share of their market are also good bargains. Besides, significant transactions continue to be leveraged by means of private equity financing and areas like education, medical equipment, agribusiness, laboratories and software building continue to be on the loop of the investors. Very recently the Federal government has announced several privatizations in areas like airports, roads, oil exploitation and ports and there is a relevant expectation on the level of foreign investors to bid. Finally it is important to highlight that very important in the M&A market, nowadays, is the private equity investment done in “*start up*” business. Brazilian individuals are very active in the so called “*start up*” ventures and their need for investment requires M&A negotiations. On the contrary, real estate business and construction groups that in early 2000 have been incentivized and induced to invest are now adding losses and a prospective investor must be very careful in any investment proposal.

1.6. Legally speaking, the business involving mergers and acquisitions of private legal entities in Brazil is well established and grounded on a community of attorneys well prepared. While a few big law firms, ranging from 100 to 300 lawyers, lead the most significant transactions, several medium-sized or boutique law firms handle a myriad of mergers and acquisition business, more or less complex, from due diligence and NDAs through tax planning and regulatory filing. With due regard to the legal systems distinction, as Brazil adopts the civil code system, M&A processes and documentation strongly follow the same pattern originally developed in the common law countries (especially the United Kingdom and the United States of America) but are customized to fit local needs.

1.7. In this scenario, it is important to note that foreign investors may find certain cultural differences to be relevant in their first contact with the Brazilian market. Brazilians are very much informal (although they may try to be initially formal to please their foreign peers) and serious business negotiation may be carried on in a very relaxed manner. Also the language may be an initial barrier since a significant number of local businessmen with potential business for sale do not speak English, forcing negotiations to be carried out in two languages simultaneously. Therefore, local counsel with expertise in dual language negotiations may prove to be of the essence for a successful closing of a transaction.

1.8. Not only one, but several laws govern different aspects possibly impacted by an M&A transaction in Brazil. Although Brazil is politically formed by several States, the laws which may affect M&A transactions are mostly federal and therefore applicable all over the country. Exceptions may be found in respect to tax, real estate and environmental issues, that may be concurrently subject to laws enacted by the Federal Government, by the States and/or by the Cities where the business is/shall be developed. As a summary approach, the main statutory rules to be considered when discussing M&A are as follows:

(a) the Brazilian Constitution (enacted in 1988, as amended) generally provides for the guidelines of all legislation enacted by Federal, States and Cities governments and in particular provides for few limitations against foreign investments (as further detailed hereinbelow);

(b) the Brazilian Civil Code (enacted in 2002, as amended) rules on all aspects of civil acts and facts, including real estate matters, guaranties, contracts, indemnification for losses and damages and legal entities in general, except corporations ("*sociedades anônimas*");

(c) the Corporation Law ((1976, as amended) rules on corporations (closed corporations and public corporations) and pool of companies;

(d) the National Tax Code (enacted in 1966, as amended) and a series of other Federal, State and Cities laws on tax matters;

(e) the Antitrust Law (enacted in 2011, as amended) provides for the cases where notification to the antitrust authorities (including the antitrust court, CADE – "Conselho Administrativo de Defesa Econômica") is mandatory, and also rules on antitrust condemned practices;

(f) the Labor Laws Consolidation (enacted in 1943, as amended, including a relevant amendment enacted in July 2017) rules on any labor relationship which may be impacted by any M&A transaction;

(g) the Criminal Code (enacted in 1940, as amended) and a series of other Federal laws rule on misconduct, malpractice, mismanagement and other criminal actions that may either be discovered during the M&A process or result from the M&A negotiation, commitments and actions;

(h) the Forest Code (enacted in 2012, as amended) and a series of other Federal, State and Municipal laws that concomitantly rule on environmental matters, responsibilities and remediation liabilities; and

(i) the Anti-corruption law 12,846, enacted on 1 August 2013.

1.9. In addition, there are specific sets of rules to be observed when dealing with specific matters under an M&A transaction, to wit:

(a) the sanitary rules issued by ANVISA ("Agência Nacional de Vigilância Sanitária"), the Brazilian sanitary agency;

(b) the Consumer Code (enacted in 1990, as amended);

(c) the Trademark and Patent Law (enacted in 1996, as amended);

(d) the rules enacted by the Central Bank of Brazil (the "BACEN") in respect to exchange control of currency in and out of Brazil; and

(e) regulatory rules applicable to specific activities and coordinated by agencies which should be independent but are very much under the political influence of the federal government like aviation, transportation, pension funds, energy.

1.10. Very few restrictions on foreign investment remain in force in Brazil. Foreign investors will encounter some restrictions for investments in (i) nuclear energy, (ii) ownership and management of newspapers, magazines and other press vehicles, as well as radio and television networks; (iii) ownership of rural properties and business in frontier areas, (iv) fishing industry, (v) mail and telegraph services, (vi) concession of domestic airlines, (vii) aerospace industry, (viii) financial institutions and (ix) purchasing of new rural land (please refer to item 1.7 below). Some of these restrictions are absolute (i.e. are completely forbidden for foreigners) but in other cases foreign investors, either independently established or through joint ventures, may be allowed to perform restricted business (such as banking) subject to compliance with certain guidelines and obtaining presidential express approval. It is important to highlight that the area of health care has been restricted to foreign investment until 2015. On 20 January 201, however, law 13,097 was enacted and authorized foreign investments to be made in the area of health, including hospitals, clinics, etc.

1.11. Among the restrictions that are obstacles against the investment by foreigners in Brazil, it is important to highlight the restrictions set forth by Law No. 5,709/1971, invigorated in 2010 by Opinion AGU - 01/2008 (notwithstanding it being dated 2008, Opinion AGU - 01/2008 was published on August 23, 2010 at the Union Gazette by the Brazilian Public General Attorney with the approval by the President of the Republic). Law No. 5,709/1971 generally sets forth that foreigners and foreign legal entities can only own up to 1/4 of the area of a Municipality and individuals and legal entities of one same nationality may hold no more than 40% of such threshold area. Also, any foreign legal entity interested in purchasing a rural land must previously approve before the Brazilian Agriculture Ministry, and before the Brazilian Secretariat for Agriculture Reform (" INCRA"), an agricultural, livestock, industrial or colonization project to be implemented in the rural property to be acquired, clearly indicating such corporate purpose in its corporate documents. Act No.5,709/1971 is ruled by Decree 74.965/74 and both Act and Decree set forth detailed ruling to govern the restrictions and their limits. In practice, only exceptionally a Brazilian company controlled by foreigners or foreigners directly, individuals or legal entities, are authorized to purchase rural land in Brazil. Additionally, certain other related rulings were also invigorated in 2010, extending the restrictions imposed in Act No.5,709/71 to indirect rural land acquisitions such as those resulting from transactions involving the merger of companies or global M&A transactions or, further, change of corporate control and also the leasing of rural land, by foreigners. Foreigners that directly or

indirectly owned rural land in August 2010 can continue exploring such land legitimately. New purchases, however, are subject to the invigorated rules.

1.12. In principle, private M&A contracts are freely negotiated by the interested parties without any prior approval by government authorities except, where applicable, for antitrust authorities and transactions involving a small number of regulated industries. Except for very few situations, generally there are no distinctions applicable for foreign investors vis-à-vis local investors.

1.13. The Civil Code typically governs all contracts and transactions under Brazilian law, the only exception being labor contracts, which are governed by labor laws. Agreements governing M&A business combinations of private legal entities are therefore primarily governed by the Civil Code notwithstanding their additional compliance with other laws as it may be applicable.

1.14. Certain basic principles brought by the Civil Code must be generally observed when negotiating and preparing M&A documents, such as the principle of "communal function of the contract" (according to such principle, the freedom of the parties to enter into a contract is limited to the communal function of the contract itself) and the principle of "good faith and fairness" (according to such principle, the parties must act in good faith and with fairness not only at closing but also during the time of implementation of a contract). Other than that the Civil Code must be specifically observed as a guideline for drafting representations and warranties, indemnification and guaranty sections, for example, law and jurisdiction clauses shall be guided by the Introductory Law to the Civil Code and the Civil Procedure Code.

II. STRUCTURE OF THE TRANSACTION

2.1. When dealing with private legal entities, a great variety of M&A structures may be implemented in Brazil, most of which are also commonly used in other jurisdictions. In practice, such structures may also be used in conjunction one with the others, depending on the objectives and the demands of the parties involved, and also on specific business and tax planning. In an attempt to categorize the different types of combinations possible, there is the following:

- Acquisition of existing businesses (in certain cases followed by public tender offers), including the acquisition of:
    - an existing entity,
    - shares of an existing entity, followed by a joint venture structure,
    - assets and/or rights, including "establishments";
- Business Reorganization (usually combined with an acquisition structure), including:
    - Consolidation ("*fusão*", in Portuguese, whereby two or more companies combine, becoming a new legal entity, this being a very rarely implemented structure),
    - Merger ("*incorporação*", in Portuguese, whereby one company is merged into another and the latest shall be the only surviving company),
    - Spin-off ("*cisão*", in Portuguese, whereby one company is divided into two or more companies, under one same control),

- “Drop down” of assets and/or rights (including or not entire “establishments”) whereby such assets and rights are contributed as capital into a newly created entity or an existing entity;

- Shares merger or Roll-up (“*incorporação de ações*”, in Portuguese, whereby one corporation becomes a wholly owned subsidiary of another corporation),

- Group of Companies (whereby companies are united under common control);

- Joint-Venture agreements supported by shareholders agreements and/or other types of agreements;

- Contractual Pool of Companies (“*consórcio*” in Portuguese, whereby companies with complementing skills and expertise enter into a contractual arrangement to develop a specific project); and

- Private Equity investment in either regular existing companies that need investment or very small business named as “start ups”, including herein structured loans, lines of credit and facilities. .

2.2. The seller and the purchaser/investor (herein simply referred to as the “purchaser”) usually have different approaches in proposing the best structure to adopt. However, considering the several alternatives available and the current limited maneuvering opportunities towards totally avoiding tax burdens, most times it is not very hard for a purchaser and a seller to agree on the structure to implement. In the past, several loopholes in tax laws would significantly justify a choice for one structure or the other. Nowadays, however, after some initial discussions, it is rather easy for the parties to agree on the best path to take, sometimes the only possible alternative, sometimes predominantly with a view to satisfy the seller’s demands, sometimes primarily entertaining the needs of the purchaser. In few situations the due diligence review may indicate that an alternative structure shall be adopted and unless it presents any risk for one of the parties, the process may be adapted as necessary to the new structure.

2.3. The main reason why the choice of structure is not a problem is that under the Brazilian legal system the general rule is that before third parties and, most important, before government authorities and public bodies, a purchaser generally succeeds seller in all liabilities, *provided however* that the purchaser and the seller may contractually agree on seller’s obligation to indemnify purchaser in respect to losses and damages originating from acts, facts and omissions occurring prior to the sale/reorganization date. Accordingly, there is practically no difference in this regard if one compares the purchase of shares vis-à-vis the purchase of substantial assets. Although the choice of the structure may not be a problem, discussions on pre-closing liabilities and related guaranties generally consume most of the time and effort of the negotiators representing the seller and the purchaser. A direct consequence thereof is that a complete and thorough due diligence investigation is of the essence whenever the purchaser is not willing to assume past liabilities above a certain limit and seller is willing to define in advance the liabilities it will be responsible for after closing (and, therefore, any related holdback, guarantee or escrow as best addressed hereinbelow).

2.4. Given the characteristics above, unless purchaser is prepared to combine / to acquire and assume all past liabilities, an M&A process usually takes from 6 to 9 months to complete.

III. PRE-AGREEMENT

3.1. Usually the M&A process starts with a confidentiality agreement to protect both parties' proprietary information. It may, or not, include standstill and exclusivity obligations on the part of the seller and sometimes also on the part of the purchaser. In this respect, in the last two years purchasers have been very active and have avoided entering into exclusivity undertakings so as to be free to concurrently negotiate with more than one prospective seller. The practice, however, has proven to be detrimental to sellers as they waste money, time and effort when a purchaser gives up at the last moment. Confidentiality agreements usually survive the termination of the negotiations of the parties.

3.2. Negotiations following the confidentiality agreement may involve preliminary due diligence based on public information available in the name of the seller and/or the target company. In most cases such preliminary investigation, albeit being very limited in scope, has proven to be very helpful to the purchaser, first to confirm whether or not it is worth continuing negotiations and then, if negotiations actually continue, to guide the purchaser when drafting any Pre-Agreement (as defined below).

3.3. At a given stage of the preliminary negotiations it is quite natural that the parties determine the need to enter into a pre-agreement in the format of either a "Memorandum of Understanding", or a "Letter of Intent" or even a simple and more informal "Term Sheet" (all of them generally referred to herein as a "Pre-Agreement"). Notwithstanding the format, the content of each such documents is very similar and they have one sole purpose: to record the preliminary agreements reached so far by the parties and to set out the guidelines to be observed by them on the negotiations to follow, including due diligence review, subject to conditions precedent.

3.4. In our practice, whenever the parties consider whether or not to enter into a Pre-Agreement, a relevant first query frequently arises from foreign prospective purchasers: will it be a binding commitment towards completion of the transaction? The answer is "no" if the Pre-Agreement does not contain, in itself, the premises of a closed deal. In fact, according to the Civil Code provisions, a Pre-Agreement is binding on the parties strictly to the limits of its content. Therefore, a Pre-Agreement generally providing as referred to in item 3.3 above, and furthermore containing a repenting provision to the benefit of both parties and a limited term of validity (which may be automatically renewable, or not), only obliges the parties to negotiate in good faith endeavoring to reach, or not, final agreement. Accordingly, such a Pre-Agreement definitely does not oblige the parties to close a deal they are not ready or willing to do.

3.5. With due regard to our comments above, it is thus rather usual that the parties enter into a Pre-Agreement as a means to confirm their intent to continue negotiations and undergo a complete due diligence investigation. In this sense, a Pre-Agreement usually contains the following specific provisions:

- Object of the prospective transaction (share purchase, asset purchase, or others)

- Indicative price (subject to terms and conditions further to be agreed by the parties) and/or (in case of joint venture agreements) the estimated value of the investments that the parties intend to incur in a short term period (and in a long term period, if applicable) and funds raising projects as needed to cope with such prospective investments;

- Conditions precedent for closing (for example, final approval by the relevant boards, satisfactory negotiation of the final agreements, termination of the due diligence investigations with results that the purchaser may deem to be satisfactory, among others);

- Definitive agreements that the parties intend to enter into;

- Exclusivity provisions (if not included in the confidentiality agreement or in ratification thereof);

- Guidelines for and scope of the due diligence exercise;

- Preliminary agreement on which party shall be responsible for the pre-closing liabilities to be found in the due diligence;

- Agreement of the parties as to unknown liabilities;

- Preliminary agreement on the guaranties to be instituted by one party to the other (by the purchaser, regarding payment of the purchase price and by the seller, regarding pre-closing liabilities, if applicable);

- Whenever applicable, preliminary agreement of the parties as to specific joint venture provisions like put and call options, tag along, drag along and termination clauses;

- Antitrust matters and other specific authorization matters, if applicable;

- The parties´ liabilities towards costs to be incurred with the transaction;

- Language provisions (if the Pre-Agreement is signed in two languages – Portuguese and English, which language to prevail); and

- Law, jurisdiction and, if applicable, arbitration commitment.

3.6. For the Pre-Agreement to be valid and enforceable between the Parties it must comply with the same requisites applicable to agreements in general, in particular the basic principles set forth in Section 1.8 above.

IV. DUE DILIGENCE REVIEW

4.1. As mentioned above, unless the purchaser agrees in advance to assume all pre-closing liabilities, no matter what they are, due diligence on the target company (and sometimes on sellers and/or the targets' managers) is mandatory. The process is complex and usually is cost and time consuming.

4.2. Due diligence is usually carried out by (at least):

(a) one law firm (covering all fields of legal practice as, for example, civil, contractual, criminal, environmental, labor, real estate, banking, currency matters and BACEN regulations, tax, compliance, consumer, regulatory, licenses and permits, antitrust, intellectual property and information technology);

(b) one auditing firm (either a local branch of an international firm or a local one, to cover a tax and accounting review, including calculations and review of tax and labor regular payments and obligations); and

(c) one environmental expert firm (either a local branch of an international firm or a local firm with capacity to conduct local investigation on environmental contamination of soil, water and air).

4.3. Traditionally the parties would specifically be most concerned with tax and labor issues and liabilities, no matter the size of the transaction or the type of the industry at target. Nowadays, however, it must be said that environmental issues are in the first rank of all concerns and, in some cases, are even deemed more relevant than tax and labor matters.

4.4. In fact, Brazilian laws governing environmental liabilities, with a little variation depending on the Region, the State or the City where the target is located, are among the most complex, complete and strict anywhere in the world. Contamination of the soil, the water or the air are generally condemned as a civil infraction and as a crime, and this is the only case in Brazilian law where the legal entity itself may be deemed to be a criminal, which means that the officers and the members of the board (if existing) of the criminal legal entity are also deemed to be criminals. Environmental liabilities do not distinguish when the contamination was formed. Therefore, although the first specific law was enacted in 1965 (the Forest Code, mentioned in item 1.4 above), if the contamination was formed in years 1950 (when industrialization was actually launched in Brazil), it must be cleaned up. According to the law, the polluter is the party deemed responsible for the contamination and for cleaning it up. Notwithstanding, governmental authorities have the option to require remediation measures from the owner of the site whenever the original polluter is not known or does not voluntarily assume responsibility.

4.4.1. The hardest part in respect to environmental liabilities is that the remediation costs are usually unknown when the process begins and the environmental agencies (which may be Federal, State and Municipal (of the City) agencies, all of them acting concurrently) may either deny initial licenses or cancel existing licenses to operate if remediation is not implemented according to their standards. Considering the complexity of the subject matter, it is therefore very important to note that in practice environmental issues and conformity must be confirmed as early as possible in a due diligence process.

4.5. Given the recent developments on corruption investigations, compliance review is an important part of the due diligence review. Interview with employees, officers and directors, and check testing on policies, internal processes and controlling policies are a,

4.6. Regarding other aspects of a due diligence investigation, the following issues are deemed to be relevant and must be taken into account:

- In respect to basically all activities of the target and the seller it is possible to obtain public certificates which may either confirm the conformity of the target / the seller with a specific area or show the outstanding measures to be implemented for them to reach such conformity. Some of the public certificates may be required and obtained by any third party (including representatives of the purchaser) and some may only be required and obtained by the target / the seller themselves. It is therefore important that the list of required public certificates be submitted by purchaser to seller as early as possible in the due diligence process. As example, public certificates can cover outstanding taxes in the three spheres (Federal, State and Municipal), outstanding litigations before all courts (except arbitration panels, which are confidential), including civil, labor and tax different courts, guaranties, loans and other contracts and liabilities registered with public notaries and real estate development status before public bodies and real estate registry.

- In any case of a business reorganization and in case of certain acquisition structures, public clearance certificates in respect of payment of taxes and social charges by the target companies must be submitted to the Board of Trade as a condition precedent for the reorganization / the acquisition to complete.

- Brazilian labor laws provide for continuation of labor contracts and transfer of all past labor liabilities to the purchaser (as new controller of the acquired business) and/or to the surviving company or companies (as a result of any business reorganization).

- Brazilian tax laws provide that as a result of an acquisition or a business reorganization structure the purchaser (as new controller of the acquired business) and/or the surviving company or companies (as a result of the business reorganization) shall be fully liable for past liabilities, provided however that in case the seller remains in business (even in business involving different areas of activities) such liability shall only be subsidiary.

- Foreign equity investments in Brazilian companies and foreign loans are subject to control by the BACEN, which means that any funds entering and/or leaving Brazil for any purpose must be registered with the BACEN and the relevant registration must be annually up-dated by the Brazilian invested company. Registration is mandatory to allow capital return, payment of dividends and repayment of loans and interests. All such payments also have to be reported to BACEN by means of amendments to the original registration files on a case-by-case basis. In practice, all foreign currency exchange transactions are directly operated between the commercial banks and the local company and the banks are given authority by BACEN to confirm that the flow of funds in and out of the country meet all legal requirements. At any time BACEN may audit both the commercial banks and the local company to confirm that all transactions have indeed been legally supported and carried out. Statute of limitation for such auditing is 5 years.

- In case the purchaser is a foreigner, either an individual or a legal entity (including funds), it is important to confirm whether the target is subject to any restrictions against ownership by foreigners as mentioned in items 1.6. and 1.7 above.

4.7. Given the intricacy of the laws and the verification process, it is highly recommended that the seller meets with the firms in charge of due diligence several times while the process is undergoing in order to confirm any unexpected liability or key issue that becomes a deal breaker. In most cases, early discussions with the seller on the outstanding matters are necessary for the purchaser to confirm whether or not it will continue the process.

V. MAIN AGREEMENT AND ANCILLARY AGREEMENTS

5.1. Depending on which structure the parties decide to adopt (as referred to in item 2.1 above) a different definitive agreement shall be prepared and entered into. As examples of typical main agreement we would nominate the Share Purchase Agreement, the Asset Purchase Agreement, the Investment Agreement, the Subscription Agreement and the Joint Venture Agreement, in each case supplemented by other ancillary agreements as, for example, an Amendment to the Articles of Association (in the case of a limited company), the signature of a term of transfer or shares and a Shareholders Meeting Minutes (in case of a corporation - "*sociedade anônima*"), a Shareholders Agreement or a Voting Agreement and/or a Transition Services Agreement. Irrespective of the name of the agreement, all main documents usually contain similar provisions (as they are meant to rule on the interests of a purchaser or investor, on one side, and the interests of a seller or recipient of an investment, on the other side). For ease of reference herein we will generally use "Main Agreement" to address any main agreement together with its ancillary agreements, jointly considered, except where a specific reference is needed for clarification purposes.

5.2. As previously mentioned, the Main Agreement (as well as the ancillary agreements) must observe the general rules for contracts set forth under the Civil Code and further comply with specific legislation,

whenever applicable. For example, a Shareholders Agreement or a Voting Agreement prepared in respect of a corporation ("*sociedade anônima*") must comply with the Civil Code and also with the Corporation Law.

5.3. As from June 2011, when Law No.12,529/2011 ("Anti-Trust Law") came into force, all M&A transactions that meet a certain threshold set forth therein must be entered into subject to a very specific condition precedent: the transaction shall only be completed upon prior approval by the Brazilian Anti-Trust Tribunal, named CADE- Administrative Council for Economic Defense. For further information, please refer to Chapter VI hereinbelow.

5.4. Main Agreements usually are divided into the following major sections:

- Whereas clauses – under the Civil Code atmosphere, it is rather important to register in the preamble of any agreement the reasons why the parties wish to do business, the preparatory steps carried out by the parties prior to entering the agreement and other background information. Any such preliminary provisions shall be of importance in case ever the parties litigate and the judge is forced to understand the transaction as a whole.

- Object and indication of the ancillary contracts to be signed to govern certain specific aspects of the transaction (the ancillary agreements themselves are then detailed in another section).

- Closing provisions and Conditions Precedent – Based on the discoveries made during the due diligence and the negotiations of the parties, they usually agree on certain actions that must occur as a condition precedent for the transaction to close. Usually closing occurs within a certain limited period of time as from the date of signature of the agreement, which may vary from 15 days to 60 days depending on the time the relevant actions may take to be implemented. Examples of conditions precedent are, as applicable:

    - establishment of the escrow account
    - implementation of a corporate reorganization
    - remittance of funds to Brazil
    - establishment of the investment vehicle
    - notification to third party contractors
    - opening of new branches or closing of old branches
    - obtainment of new licenses, permits and/or authorizations
    - termination of employees
    - meeting regulatory provisions
    - antitrust filing matters
    - no corruption and other compliance commitments.

- Price and/or other financial aspects of the transaction – The financial aspects of an Main Agreement must be clearly and detailed stated. Provisions must contain a reference to:

    - the total price and how price was calculated

    - installments and maturity date of each installment

    - possible adjustment of the price based on inflation (under Brazilian law, only price to be paid in installments more than one year long may be adjusted by inflation)

    - interest to be paid

    - exchange rate to be used to convert funds into local currency (the "Real")

    - possible deductions

    - holdback and rules to govern the release of the holdback amounts, depending on the verification, or not, of liabilities that are held by the seller

    - establishment of an escrow account and rules to govern the use and the investment of the funds to be deposited therein and, also, how the escrow amount shall be released to either the seller or the purchaser, as the case may be (the covenants on the escrow shall also be object of an ancillary specific agreement as further detailed hereinbelow).

- Warranties and Representations – Sections on W&R generally follow the usual pattern of the common law agreements, including separate disclosure schedules. However, there are some standard qualifications that are frequently used in the common law agreements that do not have support under the Brazilian legal system. Therefore, if any such qualifications are included in the agreement (and most times they are included based on requests by the foreign party, that feels more secure by having them), they may be construed, by a Brazilian court, in an undesirable / unexpected manner. In this respect, we recommend foreigners openly discuss the matter with their local counsel, on a case-by-case basis, to be reassured that the agreement, under Brazilian courts, shall be construed as expected. Examples of such qualifications are:

    - "material" and "significant" as used in expressions as "material adverse effect", "material respect", "material fact" "significantly increase" – there are no legal definitions or case law precedent in Brazil indicating what should be the correct construction of qualifications using such expressions; the alternative solution is to clearly and objectively define in the agreement what they shall mean for purposes therein; and

    - "to the best knowledge" – there is no specific difference between this expression and the simpler expression "to the knowledge", except for the trivial meaning of the adjective "best"; however, the expression may be used if the parties agree that it can be literally construed, as written.

  Usually W&R must be valid and effective on the date of signature of the agreement and also on the closing date. It is rather common, also, that W&R survive the

agreement for (at least) the statute of limitation period applicable to the relevant matter. However, all such provisions must be clearly stated in the agreement as they do not originate from the law.

- Liabilities and Indemnification – All Main Agreements contain provisions governing the parties' mutual liabilities and mutual obligation to indemnify one another in respect to either past or future actions and contingencies, and also in respect to the undertakings under the transaction agreements themselves. Indemnification sections are meant to provide as to:

    - whether or not there is joint liability among co-sellers or co-purchasers

    - whether or not the liabilities of either party is limited in amount and/or in time

    - the roles of the indemnifying party and the indemnified party whenever a defense must be filed

    - procedures to be observed by the parties in case of indemnification demands

    - guaranties and how / when guaranties can be triggered

    - whether or not loss of profits are to be included as part of indemnification due

    - whether or not the penalty is a limitation to indemnification, or not (under Brazilian law, unless the agreement provided 0if the agreement provides for a penalty the party in breach may choose opt to pay the penalty instead of complying with the obligation)

- Covenants of the Parties – Some covenants are common to most types of Main Agreements, some are not, to wit:

    - Non compete – non compete undertakings are generally accepted by Brazilian law whenever certain circumstances combine: (i) either the party which undertakes the obligation not to compete is paid therefore (as part of the purchase price of the shares or the assets, for example) or the obligation not to compete is mutual and, therefore, no payment from one party to the other is needed (as in case of a Joint Venture Agreement), (ii) no person can be prohibited to compete in such a manner that such prohibition jeopardizes the capacity of such person to earn his/her leaving, and (iii) any non compete obligation must be limited in respect to the subject matter, the location and the time of validity (maximum time usually admitted is 5 years).

    - Confidentiality – Main Agreements usually contain confidentiality provisions that supersede any similar undertakings in previous agreements. Such provisions are usually further complemented to provide for restrictions on disclosing the transaction as a whole and/or parts of it

    - Pre-Closing Absence of Changes – It is common that the seller undertakes the obligation to conduct business of the target as conducted prior to the signature of the Agreement, until closing. It is not recommended, however, that purchaser starts participating on the management of the target prior to closing.

- Antitrust Filing – All Main Agreements where there is a combination of two businesses or the transfer of control of a relevant company to a new owner, must contain a provision clearly stating whether or not the parties understand that notification to the Antitrust Authorities is necessary and, if so, which party will bear the costs thereof. Additional comments to the Antitrust filing rules in Brazil may be found in the final section of this article.

- Transfer of Shares provisions – these are typical to Joint Venture Agreements and/or Shareholders Agreement (or Voting Agreements) and may include, as the parties may agree, put option, call option, drag along, tag along, preemptive right, right of first refusal, restrictions on transfer of shares, buy-sell arrangements, change of control consequences.

- Corporate Governance provisions – also typical to Joint Venture Agreements and/or Shareholders Agreements (or Voting Agreements), corporate governance provisions are necessary to set the rules on how the target will be managed and what shall be the role of each party in such management. Most of the provisions on corporate governance are also contained in the By-laws of the target, which, in that case, will be attached as an ancillary agreement.

- Future Contributions - again typical to Joint Venture Agreements and/or Shareholders Agreements (or Voting Agreements), but also to Subscription Agreements, are provisions governing the future contributions of the shareholders.

- Compliance – it is currently mandatory to include in any and all agreements, irrespective to its size or importance, a specific section expressly condemning and prohibiting corruption practices and other condemned attitudes and illegal actions.

- Ancillary Agreements, including Transition Agreements – Usually the Main Agreement contains a summary of the purpose of each ancillary agreement so as to make sure the whole transaction is consistent and the ancillary agreements are not deemed unreasonable. Possible ancillary agreements are referred to in item 4.4. below.

- Notification – Besides the usual notification section, it is also common for Brazilian contracts to contain the appointment, by a foreign party, of a Brazilian individual to represent the foreigner in any notification related to the matters under the agreement. This appointment is rather important in case the agreement is subject to Brazilian law and Brazilian courts (or arbitration in Brazil) so as to make sure notifications are delivered.

- Term, termination – Main Agreements are usually meant to be valid for the time necessary for all obligations therein to be fulfilled. However, there are some Main Agreements and some ancillary agreements that shall typically be valid for a limited period of time as, for example, a Shareholders Agreement or a Voting Agreement. Should that be the case, the Main Agreement shall be valid for an identical period of time, at least, to be consistent. Early termination is usually not permitted unless there is a breach by one of the parties that cannot be remediated and that makes the continuation of the relationship between the parties impracticable. Accordingly,

parties in breach are due to remediate their breach and hold the other party harmless for any consequences to said breach.

- Law – Whenever one of the parties is not Brazilian, the parties must agree upon the choice of law to govern the M&A Agreements (we are assuming that any agreement where the two parties are Brazilians, the applicable law shall be Brazilian law). In principle, considering that the target is a Brazilian legal entity and the contractual obligations must generally be complied with in Brazil, we usually advise our foreign clients that all agreements be subject to Brazilian law. Also, it is important to remark that Brazilian law is mandatory in respect to certain agreements (as, for example, By-laws and Articles of Association of Brazilian legal corporations and limited companies, Shareholders and Voting Agreements, Real Estate related agreements, local services agreements, local escrow agreements, environmental remediation agreements) and it is quite problematical to have some agreements subject to a foreign law and other agreements subject to local law. However, Main Agreements may, in principle, be subject to foreign law and, therefore, the parties may, in theory, decide to make that choice. Accordingly, we recommend the parties involved in an M&A discussion in Brazil to consult with their legal counsel to decide what is the best choice on a case-by-case basis.

- Dispute resolution - Jurisdiction / Arbitration – The choice of jurisdiction for dispute resolutions deriving from M&A Agreements is more complex than the choice of law. There are basically two decisions that the parties must take in respect to jurisdiction: (i) the choice of jurisdiction itself – whether the dispute resolution process will take place in Brazil or abroad, and (ii) the choice between traditional courts and an arbitration tribunal. In respect thereto, we would comment as follows:

    - if all the agreements are governed by Brazilian law, it is advisable that such agreements be subject to either Brazilian courts or an arbitration tribunal located in Brazil;

    - if the Main Agreement is governed by a foreign law, such agreement may be subject to a court abroad or to an arbitration tribunal located abroad but the ancillary agreements which are governed by Brazilian law shall be subject to either Brazilian courts or to an arbitration tribunal located in Brazil, causing any possible dispute resolution procedure to be very complex and possibly incoherent ;

    - as traditional court procedures are very much time consuming in Brazil, more and more M&A parties are considering the option of arbitration for disputes resolution in Brazil, notwithstanding the fact that an arbitration process is much more costly than a process before a traditional court;

    - in order to be enforced in Brazil, a foreign judgment enacted by a traditional court abroad or a foreign award enacted by an arbitration tribunal abroad must first be recognized by the Brazilian Superior Tribunal of Justice and the relevant procedure is complex, demanding and time consuming;

    - arbitrations conducted in Brazil must comply with Brazilian Law No. 9.307, of September 23, 1996, that has been conceived and written very much in line with the New York Convention provisions, dated 1959. The New York Convention itself was only ratified and endorsed by Brazil on July 23, 2002, by means of Presidential Decree No. 4,311. Brazil is also a signatory of the

Inter-American Convention on International Commercial Arbitration, entered into in Panama in 1975 and ratified by Brazil by means of the Legislative Decree No. 90/1995 and the Presidential Decree No. 1,902, of May 9, 1996. In principle, according to international interpretation rules, the Panama Convention should prevail in Brazil due to the fact that it was ratified and confirmed prior to the New York Convention. Notwithstanding, scholars understand that it seems defensible that, under certain circumstances, the New York Convention may be ruled as prevailing as it is more complete than the Panama Convention and, in fact, it may be applied where the Panama Convention is in omission.

- Language of the agreements - Another issue that seems to be trivial but may be of significant importance in M&A transactions involving one foreign party and one Brazilian party is the language in which the agreements (in particular the Main Agreement) will be written – either Portuguese and/or a foreign language (usually English). As a background information it is important to note that Portuguese is the official language of the country and all documents, contracts and titles must be written in Portuguese (and sometimes registered with public notaries) in order to be valid and effective between the parties and before third parties and, also, to be accepted in court. In this regard, it is key also to remark that certain agreements must be written in Portuguese only (as, for example, the By-laws of a corporation and the minutes of a General Shareholder Meeting or of a Board Meeting, contracts involving real estate developments and real estate property title) and some documents must be written in Portuguese but may also be written in two languages (in two columns, side-by-side) as far as the Portuguese version prevails (as, for example, Shareholders Agreements, Voting Agreements, Amendments to the Articles of Association of a limited company, Escrow Agreement, Transition Agreements). Any agreement only written in English must be translated by official sworn translators and registered in a public notary registry and, moreover, any agreement entered into abroad (either in Portuguese or in a foreign language) must be signed before a notary and the notary's signature must then be certified by the nearest Brazilian Consulate. Considering the risks of a literal and non-legal translation (by a sworn translator) of an agreement written only in a foreign language, we always recommend to our clients that agreements must be signed, whenever possible, in two languages concurrently, Portuguese and another language, in a two columns, side-by-side document, the Portuguese version to prevail in case of conflict.

5.5. Ancillary Agreements vary, of course, depending on the type of transaction. For easy reference, we would address some of the most commonly used:

- Escrow Agreement – Brazilian legislation does not provide for an escrow structure the way it is known and practiced in the common law jurisdictions. However, given the growth of M&A transactions in the country, certain banks (2 or 3 banks, only) have developed a specific product with the characteristics of a typical escrow agreement. The Brazilian escrow agreement, therefore, as currently conceived, is a service agreement whereby both parties of the transaction retain a bank to provide services similar to the typical escrow activities. The banks charge an annual fee for the escrow services and in practice the parties usually find the escrow fees too high and whenever possible they end up by choosing another alternative structure (a guarantee or a holdback, for example).

- Transition Services Agreement – Usually this is a local agreement, between two Brazilian companies, subject to Brazilian law and Brazilian courts and limited on time.

Transition Services Agreement may be entered, for example, with the seller (either an individual or a legal entity) for purposes of causing the seller to actually convey and transfer to the purchaser all the know how needed for the target business to continue without interruption.

- Shareholders Agreement or Voting Agreement – Shareholders Agreements are very much used in Brazil as part of Joint Venture documentation. They are governed by the Corporation Law and are meant to typically set forth the agreement of the signatory parties, while shareholders of the target corporation, in respect to the exercise of the power to control, the exercise of voting rights, the right to transfer shares and the right of first refusal in case of sale of shares. Shareholders are entitled to enforce the provisions of the agreement by means of specific performance actions and at the meetings of either the board or the shareholders any vote against the provisions of a Shareholders Agreement shall be disregarded and not counted. Voting Agreements are Shareholders Agreements that only rule on the voting obligations of the signatory shareholders and are used very seldom.

- Guaranty Agreements – Certain guaranties (as, for example, mortgage, fiduciary alienation, pledge of shares) must either be established by means of public deeds or registered before public notaries in order to be valid and effective. For such a purpose, they are governed separately in an ancillary agreement. Guaranty Agreements generally must comply with strict terms of the law, in particular the Civil Code.

- Agreements on the Environmental Remediation – Whenever applicable, the parties may enter into an agreement specifically to set forth the steps that will be taken to fund and implement the environmental remediation of a site sold or rented as part of the M&A transaction.

VI. ANTI-TRUST FILING

6.1. As mentioned in item 5.3 above, anti-trust filing is ruled by No.12,529/2011 (“Anti-Trust Law”) that became effective in June 2011. According to the Anti-Trust Law:

- Transaction must be submitted to the prior approval by CADE whenever:

    - At least one of the groups involved in the transaction has registered, in the previous fiscal year, either a gross turnover or a volume of business, in Brazil, equivalent or higher than BRL400,000,000 (equivalent, in late February 2014, to approximately USD 180,000,000), and

    - At least another group involved in the transaction has registered, in the last previous fiscal year, either a gross turnover or a volume of business, in Brazil, equivalent or higher than BRL30,000,000 (equivalent, in late February 2014, to approximately USD 13,000,000),

- Although signature of the Main Agreements may happen prior to approval by CADE, the Parties must obtain such approval prior to completing the transaction and, most important, exchanging business information,

- Filing process shall take no longer than 270 days,

- Penalties for breaching the law vary from BRL 60,000 (equivalent, in late February 2014, to USD 26,000) through BRL 60,000,000 (USD 26,000,000),

- In addition to the classic M&A transaction, the following structures shall also be submitted to CADE for prior approval: association contract (this is quite broad), pool of companies and joint venture (also too broad), and

- Transactions which are not deemed complex are subject to a "fast track" approval process, in which case approval is issued within 30 days, at most, from initial filing.

VII. START – UPS

7.1. Start-ups are quite dependent on third party investments and, therefore, are natural clients of M&A. However, their size and their early need to accept investors does not permit very complex and classical M&A arrangements.

7.2. In most cases the first investor in a "Start-up" is a so-called "angel investor" that invests in the new business and in the new ideas with no guaranty of return and no official partnership. "Angels" usually do a limited investment, in time and in money, and have the benefit of a future official partnership in beneficial conditions,

7.3. In a subsequent phase "Start-up" businesses are candidates to receiving short term loans that shall be converted into partnership upon certain conditions precedent. The lenders are granted the right of a higher grade of benefits if and when their loan is converted into shares. However, in most cases the lenders shall not receive repayment of their loans if ever the business of the "Start-up" does not mature and is closed.

7.4. When the business of the "Start-up" is proven to be successful it is converted into a corporation and all previous investors/lenders receive shares in proportion to their previous benefits arrangements. Then both the original members of the "Start-up" and the investors need a classical M&A to establish their long term relationship and terms and conditions for future investments and possible exit alternatives.

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