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BRAZIL'S CURRENT MARKET AND BASIC M&A PROCEDURES.

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ADVOGADOS

This brief article has the scope of providing its readers with information regarding recent Brazilian social, political and economic highlights, all with the objective of outlining the basic Mergers & Acquisitions procedures currently observed in Brazil. Thus, the text was divided into two sections. The first aims at providing an insight into the current Brazilian Market. The second describes the main procedures regarding our M&A market.

I. Current Brazilian Market

In the last 5 years, Brazil's economy has improved its GDP (Gross Domestic Product) and overall employment. Additionally, its middle class population hit record highs. Brazil has also past the phase of being the "must go" destination for investments, especially among the BRICS (i.e., Brazil, Russia, India, China and South Africa) and has become a more complex, yet full of opportunity, market.

Brazil is now recognized as a mature country with solid macroeconomic indicators. Its fast expanding internal consumer market makes the country one of the most promising emerging economies in the world. In addition to this, in 2014 there is a presidential race to which there is no predictable result, despite the indication contained in some polls demonstrating that Mrs. Dilma will remain acting as president until 2018.

In addition to this, there is an increase of awareness demonstrated by the population, as perceived by the public demonstrations occurred during July 2013. Mainly, the protests were against public expenditure, the lack of investments in infrastructure and education, as well as contrary to huge international events scheduled for Brazil (e.g., 2014 FIFA World Cup and the 2016 Summer Olympics Game). These events provide an insight into the opportunities and next challenges for the local population and foreigners, who intend to expand and do business in Brazil.

In this complex scenario, Brazil shall remain undoubtedly an attractive place for investments, especially when compared with the Eurozone, USA and other South American countries. Part of the continued appeal is that Brazil's economy is its corporate fragmentation. In other words, there are many mid-sized family businesses. This state of affairs makes room for corporate consolidation and restructuring, with possible efficiency gains for a potential investor, interested in entering into the Brazilian Market by means of equity acquisition.

For foreign investors, buying this type of company is particularly interesting, as their pre-existing licenses and sometimes surprisingly strong brands can give you immediate access to markets that would otherwise require significant expenditures in regulatory approvals, as well as expensive marketing campaigns.

It is important to mention that Brazil adopts the free flow policy in regard to its currency. This might give an edge for foreign investor since recently the American dollar has increased its relative value in comparison to the Brazilian national currency (i.e., the 'Real' or simply R\$). This may cause the Brazilian assets to seem depreciated and to appear more attractive to foreign investments.

Recently released indicators endorse this opinion. According to a report by a large accounting firm in Brazil, there was a 5.2% year-on-year increase on the number of transactions during 2013 compared with 2012. Of the total of 811 transactions announced in 2013, 291 (only 36% of the total) disclosed the amount

involved in the transaction, in the sum of US\$ 88 bn. Of the total amount of transactions, 40% involved foreign investors, making Brazil the second hottest investment destination globally.

II. M&A Procedures in Brazil

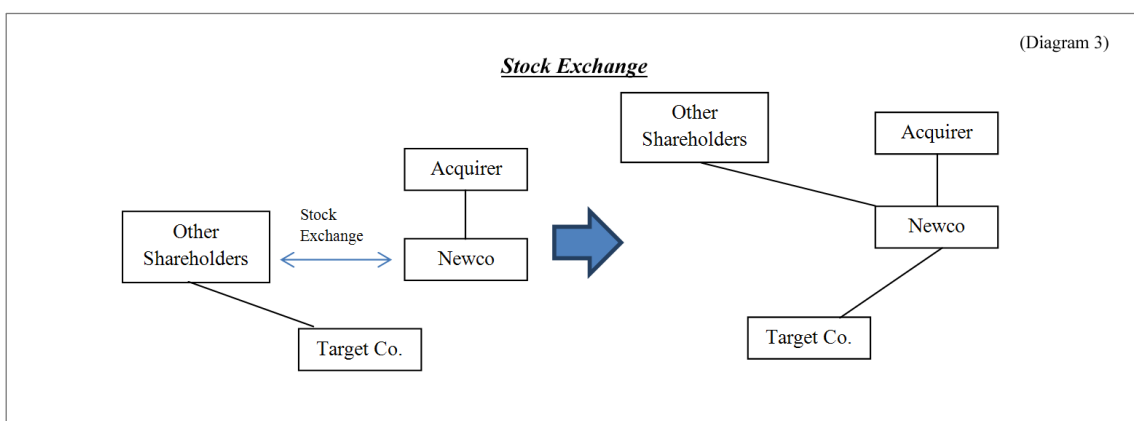
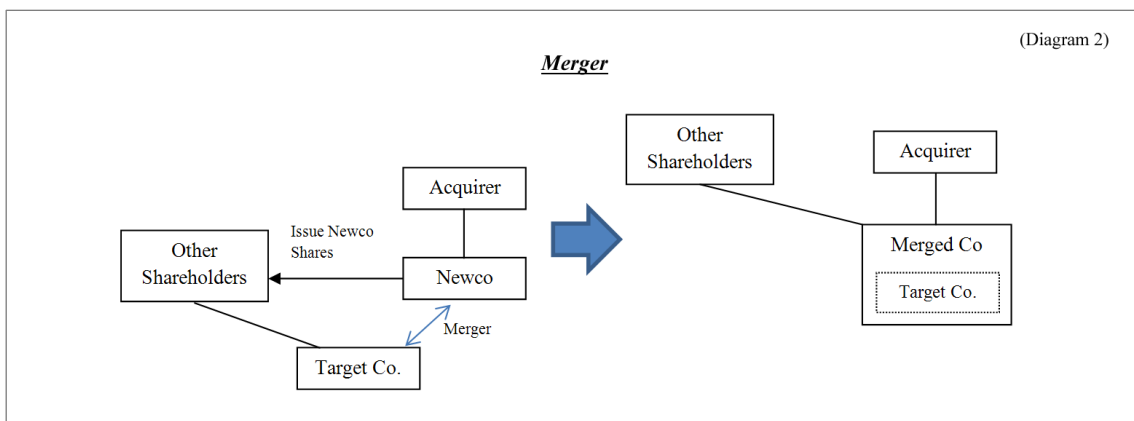
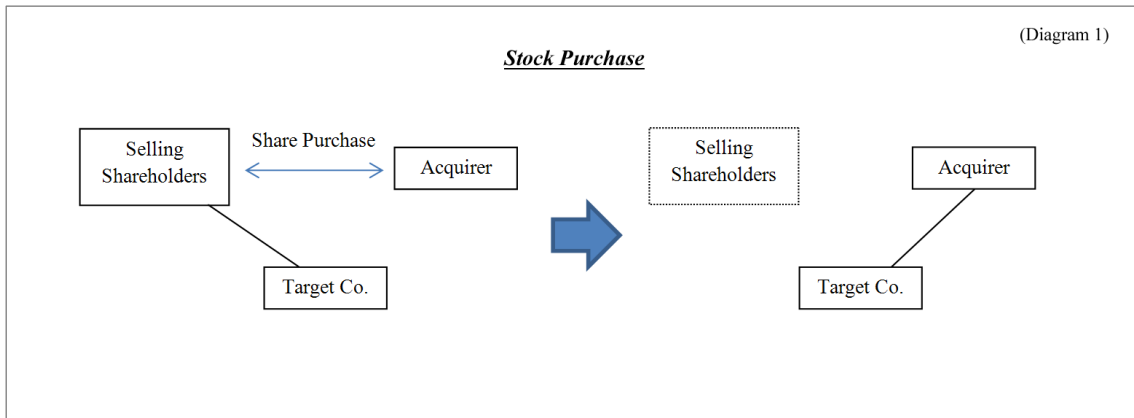
One of the challenges entrepreneurs face, especially foreign investors, is to understand the rules and regulations regarding Mergers & Acquisitions procedures in Brazil. For this reason, it is recommended, while still in the initial phase, that the parties draw up the basic premises of the intended deal, signing documents that ensure transparency and convergence of interests. This is usually done by a Letter of Intent ("LOI"), which usually is associated with a Non-disclosure Agreement ("NDA").

An LOI will indicate which kind of transaction is intended between the parties.

A. M&A Transaction Structures in Brazil.

Basically, there are four main transaction structures for M&A operations in Brazil. The more common of which is the acquisition of a target company's equity by an investor (Diagram 1). Mergers are also common place (Diagram 2). In this type of transaction, a corporate vehicle incorporated in Brazil by an investor acquires a target company, integrating the latter's assets into its own structure. Additionally, it is not uncommon to arrange an operation based on an exchange of shares among investors and investees (Diagram 3). Finally, some transactions are "asset deals" that are structured around the acquisition of a

single asset or group of assets, such as a trademark or industrial plant.



Due to the Brazilian corporate fragmentation described earlier, restructurings and turn-around operations are commonly implemented. This procedures aim at providing a company with a more efficient legal structure. In this sense, it may involve all types of

operations described in the above paragraph, as well as less popular types of operations such as a split off, wind down and drop down.

In accordance with the Brazilian Corporate Law (Law No. 6.404/76), a "split-off" is an operation whereby a company transfers a portion of its assets to one or more corporations already in existence or formed for this purpose; the company splitting off shall become extinct if all its assets are transferred, or if the transfer is only partial, its corporate capital shall be split-off but the company itself will remain in existence.

On the other hand, a "wind down" is similar to a dissolution where some of the company's assets will be divided for distribution among its shareholders. A "drop-down" is a more complex structure, which involves the incorporation of a new entity by the Company, with the contribution of some of assets in order to segregate a specific line of business. Despite the fact the final result be similar from the partial split-off, due to regulatory reason, drop down may be more convenient.

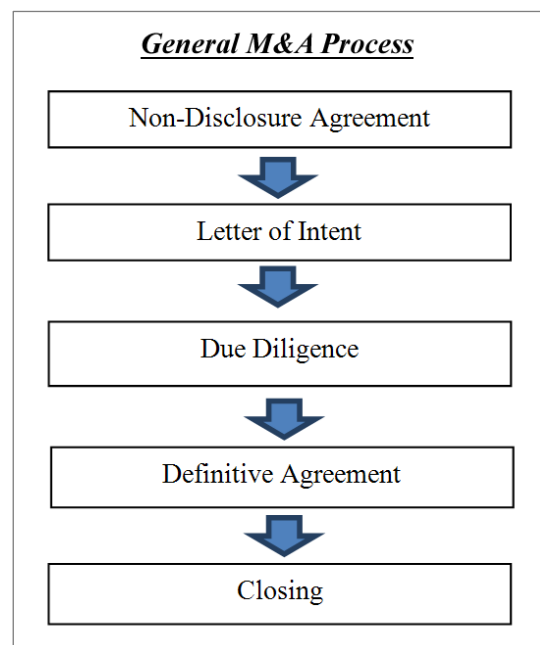
Lastly, please note that in Brazil, a simple transference of business (in Portuguese called "trespasse") is not commonly used. Basically the "establishment" (and not the company) is sold in this operation. An "Establishment" is a legal concept which describes the place of business and business operations conducted in such place. This operation, if performed without due attention to the law, has the potential to generate up debts and insolvency.

B. General Steps of M&A in Brazil and CADE Examination.

It is important to notice Brazilian law does not contain specific laws that outline M&A procedures, although there are general rules in corporate and contract law. In

addition, the internationally adopted usages and practices have been incorporated into Brazilian transactions, allowing different formats and methodologies.

Usually, when the initial phase of defining the basis of negotiation has been concluded, including the execution of LOI, the process moves into the stage for submission of documents and information to lawyers, auditors and specialized consultants, known as due diligence, to verify the situation of the target company. Once the Due Diligence report has been completed and the issues that came to the fore have been discussed, the parties are ready to proceed to the final stages of the negotiations. This is when the parties start to negotiate the definitive agreements, such as the Share Purchase Agreement (SPA), which is the document aimed at regulating the liabilities and duties of each partner.



It is important to note that there are certain foreign investment restrictions in Brazil which could affect the

general M&A procedure described above. Since this topic is complex and requires close attention, it will be addressed in another opportunity.

We would like, however, to point to another matter which will affect the general timeline of M&A. That is, depending on the context of the initial documents for an M&A operation, the intended transaction might have to be submitted to the Brazilian System for the Defense of Competition (also named CADE). From a very high level point of view, the Antitrust Law (Law 12.529/2011) defines in its Section 90 the following transactions as acts of concentration: (i) the merger of two companies that were previously independent from each other; (ii) the acquisition of total or partial control of one or more companies, by one or more companies, directly or indirectly, by means of purchase or exchange of shares, partnership rights, legal titles or other securities convertible into shares, or tangible or intangible assets, contractually or by other means; (iii) a merger of one or more companies into a third company; and (iv) the execution of an associative agreement, consortium or joint venture, by two or more companies.

Further, the Antitrust Law specified in its Section 88 that the acts of economic concentration (as defined in Section 90) which cumulatively fulfill the following requirements shall be submitted to CADE's examination : (i) at least one of the groups involved in the transaction has declared in its last balance sheet annual gross revenue or the total sales volume in Brazil equal to or greater than R\$ 750,000,000.00, in the year preceding the transaction ; and (ii) at least one of the other groups involved in the transaction has

declared in its last balance sheet annual gross revenue or the total sales volume in Brazil equal to or greater than R\$ 75,000,000.00, in the year preceding the transaction.

The initial decision regarding an approval of the deal structure takes an average of two to three months, depending on the complexity and the circumstances of the transaction envisaged. Should the deal be rejected, a period of six months to a year may be expected for a final administrative decision.

In the end, it is important to mention that closing deals in Brazil is not for the beginners and for the inexperienced. It requires resilience, deep due diligence, as well as a profound understanding of the Brazilian Law and its complex regulatory landscape. While there is no doubt that Brazil has reached a high level of political stability in the last generation, its government is still unfortunately subject to a fast changing legislation (especially in regard to tax law), protectionist measures that seek to do anything from cooling the flow of hot money into the country, to shielding local companies from international competition.

It is important to mention that this brief article is not intended to deplete this complex subject, quite the contrary. It intends to start a dialogue by giving a glance of this complexity and trying to explain in a very summarized form how the M&A transactions are conducted in Brazil.

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Mr. Fernando Zanotti Schneider works in the area of business law, notably in the corporate area involving foreign investment, structuring of business, mergers & acquisitions and capital markets. He is the leader of the Corporate area of Abe Advogados and has acquired a vast experience in assisting international clients in green fields operations, joint ventures and sell side and buy sides deals in Brazil. Specialist in Corporate Agreements Law at Fundação Getúlio Vargas and graduated at the Pontifícia Universidade Católica de São Paulo (Pontifical Catholic University of São Paulo - PUC/SP), since 2006. Fluent in Portuguese, English and Spanish.

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