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Corporate M&A

Brazil
Law and Practice

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BRAZIL

Law and Practice

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1. TRENDS

1.1 M&A Market

When most of the world came to a halt in the first quarter of 2020, the impact on M&A activity in Brazil was deeply felt. While the world awaited developments and consequences of the pandemic, M&A activity slowed down severely and only picked up in a consistent manner in the last quarter of 2020.

As the new reality settled in, and investors became less risk averse, the devaluation of the local currency (Brazilian Real) created sought-after investment opportunities. Not only M&A but also venture capital activity made a full-fledged comeback (both markets remain very busy in the first months of 2021).

Furthermore, the second half of 2020 witnessed a surge of IPOs in the most varied industries as well as within the services sectors. The increase in the number of IPOs in the first quarter of 2021 seems to indicate that IPOs will continue to be a relevant source of funding.

SPAC deals served as a by-product of and a disruption to the enhanced IPO activity, as such transactions may be considered as a capital-raising alternative to IPOs.

The Wider Economy

During 2020, the COVID-19 pandemic acutely affected the Brazilian economy, and its effects and the continuing uncertainty are likely to extend beyond 2021. Numerous sectors and subsectors of the economy were severely impacted, and a wave of insolvencies ensued; as a direct consequence, distressed M&A became a consolidated practice. The reform of the insolvency legislation (approved in December 2020) broadened and affirmed the legal protection available to purchasers of distressed assets (no succession) and extended the protection to the purchase of the insolvent company itself.

1.2 Key Trends

A great part of 2020 was marked by an unprecedented level of engagement with ESG (environmental, social and governance) matters, which created both opportunities and risks. Maximising ESG-related synergies and mitigating ESG risks, notably risks related to climate change, greenhouse gas emissions, waste, diversity, and labour practices among other matters, became material concerns to M&A, venture capital and private equity transactions. ESG factors can be expected to increasingly influence how investors select potential targets and business partners.

Further, the pandemic-accelerated changes brought forward years of digital transformation. Therefore, tech M&A was a trend in 2020 and is still a trend in 2021. Cloud computing, SaaS and IT security businesses will continue to be potential targets from a B2B perspective, while streaming services, e-commerce, online entertaining, such as gaming, as well as any other tech business related to remote work and home orders will also continue to play an important role for B2C businesses.

Fintech

While Brazil is one of the most regulated markets when it comes to banking activities, fintechs are the ultimate trend. The ecosystem of fintechs is diversified, and such entities operate in several market segments: credit, payments, financial management, loans, investments, private financing, insurance, debt negotiation and crypto-assets and ledgers (“Distributed Ledgers” or DLTs). A new regulation came into force in 2020 permitting the creation of two new types of credit fintechs: direct credit companys (SCDs) and peer-to-peer loan companies (SEPs). Both SCDs and SEPs are allowed to attract investment through a fast-track procedure, since the

authorisation process by the Central Bank is faster than for other traditional financial institutions. In addition, since 2019, it is no longer necessary to issue a presidential decree to increase participation by individuals or legal entities residing abroad in the capital of financial institutions headquartered in Brazil.

The Financial Crisis

As the financial crisis deepens, the business consolidation witnessed in 2020 (health care, education, agribusiness) is likely to continue and expand to other sectors during 2021.

Venture capital and private equity transactions are expected to continue to fund and develop start-ups (venture capital transactions were second to M&A in number of deals in 2020).

Data Protection

Even though the Brazilian General Data Protection Law (LGPD) came into force in 2020 and put verification of compliance with the new legal requirements in the road map of due diligence, its full effects will only really be felt through 2021. Conditions precedent already came to include amendments of contracts with clients and suppliers to reflect specific data protection provisions and Codes of Conduct were drafted. Adoption of proper governance and compliance with and monitoring of privacy programs will certainly ensue.

The Petroleum Industry

Moreover, according to the strategic plan (2021-25) of the state-owned Brazilian multinational corporation in the petroleum industry – Petrobras, its divestment of assets strategy will remain ongoing in 2021 and subsequent years. The divestment will comprise the sale of several oil and gas assets in key segments, including onshore and shallow water fields and refineries. Petrobras' divestment process will represent a relevant investment opportunity in the short and mid-term.

1.3 Key Industries

As a direct consequence of the pandemic, health care related M&A were the most significant transactions during 2020 (by amounts involved), resulting in a clear consolidation of such market (laboratories and hospitals). Conversely, as technology gained importance in our current "new normal", technology related deals were far more numerous.

Following the worldwide trend, and for the same reasons, the adverse economic impacts of the pandemic were most strongly felt in the tourism industry (hotel and airlines) as well as catering, entertainment, and culture sectors.

Delivery services, on the other hand, boomed during 2020 and proved to be key to the survival of quite a few sub-sectors, including the middle and small food industry market.

Retail, initially greatly impacted by the lockdown, reinvented itself by investing in and focusing on online sales.

2. OVERVIEW OF REGULATORY FIELD

2.1 Acquiring a Company

Unlisted Companies

In Brazil, M&A deals involving private (unlisted) companies represent by far the majority of the transactions and M&A can be generally divided into equity deals and asset deals.

The typical M&A step plan is pretty similar to those followed in other markets: after negotiations reach a certain point, a Term Sheet or MOU is executed, establishing the basic business terms. Due diligence then follows (focus and

breadth vary from deal to deal and according to the target's business). Drafting and negotiation of agreements may happen concurrently or after due diligence has been concluded. Common market practice dictates that, in private deals, the purchaser drafts the agreements.

Acquisition of distressed assets (distressed M&A) follows a different set of rules since assets need to be acquired at a public bid. The above does not prevent negotiations with interested parties from taking place before the bid (even exclusivity rights may be granted although, in reality, such rights only serve to establish the asset's minimum price and grant the potential purchaser the right to match higher offers during the bid).

Listed Companies

M&A deals involving listed companies are also subject to specific rules and regulations set primarily by the Brazilian Securities Exchange Commission (*Comissão de Valores Imobiliários* orCVM). Purchases of listed companies are conditioned on other shareholders' tag-along rights (buyer shall also make a tender offer to purchase the remaining voting shares, for a minimum price equivalent to 80% of the price paid for the controlling shares or 100% of such price if the company is listed on Bovespa's Novo Mercado). Alternatively, buyer may offer to the remaining shareholders, the option to keep their shares, upon payment of a premium in the amount equivalent to the difference between the shares' market value and the price offered for the controlling shares.

Acquisitions are often preceded by corporate reorganisations (of target or sellers), segregation of assets and incorporation of a purchase vehicle by buyer (specific purpose company). Corporate reorganisations often also occur post-closing, by purchaser combining the purchased entity with another company from purchaser's corporate group. In such cases, the surviving entity is usually the entity with most tax benefits, or the entity with more regulatory enrollments.

Challenges for Investors

One of the main challenges for investors acquiring businesses in Brazil is the succession of liabilities. Whether the business acquisition is structured as an asset deal or equity deal, the buyer may be considered liable for the acquired business' past liabilities.

Further, in relation to labour and tax matters, other companies of purchaser's economic group (entities under the same management or control) will be considered to form an economic group and all legal entities of an economic group are jointly liable for all labour and tax obligations of any other entity of the same economic group.

The above considered, seller's indemnification obligations must be very clearly defined (ideally, to include any and all past liabilities of target, until the end of the statute of limitations).

Succession of liabilities does not apply to the purchase of distressed assets. In this case, the assets (including shares) will be segregated and transferred to an UPI (Brazilian acronym for Isolated Productive Unit). The purchaser of an UPI is legally exempt from previous liabilities involving the asset, the seller or other companies of seller's economic group.

Brazilian legal system is based on codified regulation (instead of common law) and interpretation of agreements' provisions (in case of disputes) are supposed to be based on the parties´ intentions and good faith principles instead of the strict language of a provision.

2.2 Primary Regulators

The primary regulator of M&A activities in Brazil is the Brazilian Securities Exchange Commis-

sion (*Comissão de Valores Imobiliários* or CVM), a federal agency which regulates and supervises the stock market activities and players.

The Brazilian antitrust authority (*Conselho Administrativo de Defesa Econômica* or CADE) is responsible for preventing abuses and enabling free competition and therefore also plays a very active role in the M&A market.

If the target is a listed company, and the transaction involves either a tender offer or a corporate reorganisation, the transaction may be voluntarily submitted to the M&A Committee (*Comitê de Aquisições e Fusões* or CAF), a private association, with a voluntary, self-regulatory nature formed to ensure fair conditions in tender offers and business combinations involving publicly-held corporations. Formed by the most relevant participants of the securities market in Brazil, CAF is inspired by the British Takeover Panel (and is actually considered the Brazilian Takeover Panel) and supported by the International Corporate Governance Network.

Finally, when a target entity is involved in regulated activities (financial institutions, oil and gas, telecommunications, etc), other regulatory agencies will also play a relevant role (specific approvals may be necessary).

2.3 Restrictions on Foreign Investments

There a few but important activities that must necessarily be exercised by Brazilian nationals or controlled by Brazilian nationals or entities. Some restrictions also extend to the management of such entities.

Prohibitions (foreign capital investment is prohibited) include:

- activities involving nuclear energy;
- health services (with exceptions established by law);
- post office and telegraph services; and
- aerospace industry (launching of satellites, vehicles and aircraft; manufacture and commercialisation of the same are permitted).

Restrictions (foreign capital investment limited by legal requirements) include:

- for reasons of national security, certain limitations apply to the acquisition of property in border areas;
- the incorporation of financial institutions and increase of foreign investment in existing entities must be approved by the Brazilian Central Bank;
- ownership of newspapers and broadcasting companies is restricted to 30% of total and voting capital and certain positions (management, programming, etc) must be occupied by Brazilian nationals (native-born Brazilians or naturalised for over ten years); and
- mining activities and generation and transmission of hydroelectric energy must be developed by entities incorporated and validly existing in Brazil (incorporation of a Brazilian company is therefore mandatory).

Further to the above, in Brazil, the Union has the monopoly of oil and gas activities including, amongst others:

- the exploration and production of oil and natural gas;
- the refining of petroleum of domestic and foreign origin;
- the import and export of basic products and by-products related to oil and gas; and
- the maritime transportation of crude oil of domestic origin, or of basic products of oil produced in Brazil, as well as the transportation through pipelines, of crude oil, its products and natural gas.

The current oil and gas framework provides a hybrid regulatory system, which authorises the development of oil and gas exploration and production economic activities under:

- concession regime;
- production sharing agreements (PSA) for pre-salt and other strategic areas; or
- transfer of rights agreements, executed between the Union and Petróleo Brasileiro S.A. – Petrobras (mixed-capital company controlled by the Brazilian Federal Government).

2.4 Antitrust Regulations

The Administrative Council for Economic Defense (CADE) is the agency in charge of the enforcement of competition laws in Brazil (primarily governed by Law No 12,529/2011 - the Brazilian Competition Law).

Brazil adopts a suspensory merger control regime, under which the parties can only consummate and implement a reportable transaction after obtaining final antitrust approval (antitrust clearance is therefore a mandatory condition precedent for the closing of such transactions). Between signing of the deal and CADE's final clearance, the parties must comply with a standstill obligation and remain fully independent; transfers of assets and/or employees, the exchange of sensitive information and the exercise of any kind of influence on each other's business may be considered "gun jumping" and subject the parties to severe penalties.

Three-Prong Test Conditions

A transaction will be considered reportable, and therefore filing for CADE clearance will be mandatory, if all conditions of a three-prong test are satisfied:

- the effects test – if the transaction or agreement will produce effects in Brazil (effects will be produced in Brazil if:
  (a) the transaction takes place in Brazil; or
  (b) even though the transaction takes place abroad (foreign to foreign), the target (or the new company) has or will have direct and/or indirect presence in Brazil (where a "direct presence" may be characterised through the existence of a local subsidiary, distributor, sales representative, and an "indirect presence" could be exemplified by export sales to the country));
- the revenues test – if at least one of the groups involved in the transaction generated gross revenues in Brazil (including export sales) in excess of BRL750 million, and at least one of the other groups involved generated gross revenues (including export sales) in Brazil in excess of BRL75 million, both in the fiscal year immediately preceding the transaction; and
- the concentration test – if the transaction will trigger a market concentration under the Brazilian Competition Law ("concentration" being:
  (a) acquisition of control;
  (b) acquisition of certain minority stakes or assets;
  (c) joint ventures; or
  (d) certain collaborative/co-operative agreements and consortia, except if created for the purposes of a given tender process launched by the public administration).

Failure to file for CADE clearance and gun jumping will subject the parties to penalties ranging from BRL60,000 to BRL60 million. CADE may also declare any acts deemed gun jumping as null and void. Furthermore, the delivery of misleading or false information, documents or statements is punishable by a pecuniary fine ranging from BRL5,000 to BRL5 million and denial of

antitrust approval due to lack of sufficient information.

2.5 Labour Law Regulations

According to the Brazilian labour law, mainly the Brazilian Labour Code (CLT), labour rights and obligations shall remain unaltered whether a company is merged, acquired, or if its original corporate structure is modified.

Accordingly, ownership change resulting from M&A transactions or corporate reorganisations shall not affect the employment contracts (terms, conditions, rights and obligations) of the target's employees unless such modifications are more beneficial. Hence, salaries and benefits cannot be reduced or suppressed (salary reductions are prohibited by the Federal Constitution). Employment agreements executed in breach of the above may be considered null ab initio.

Employees may file labour claims until the second anniversary of the termination of their employment contracts (dismissal date), to claim labour rights related to the five-year period immediately preceding the filing date of the claim.

It is very important for investors to take into consideration that under Brazilian labour law:

- entities under the same management or control are considered to form an economic group;
- all legal entities of an economic group are jointly liable for all labour obligations and charges of any employee who works for any other entity of the same economic group; and
- in a labour claim, a former employee may involve and obtain condemnation of all entities of an economic group.

Further, Labour Courts often determine the piercing of the corporate veil and seizure of partners', shareholders' and managers' assets to cover unpaid indemnification. Indemnification provisions related to labour matters must therefore be airtight.

2.6 National Security Review

Although Brazil does not formally adopt a national security review, for reasons of national security, certain activities and industry sectors are prohibited to foreign investment or permitted with restrictions. Prohibitions extend to a few but crucial activities involving nuclear energy, health services, post office and telegraph services, and aerospace industry.

Restrictions (limitations imposed by specific legislation) apply to acquisition of property in border areas, incorporation of financial institutions and increase of foreign investment in existing entities, ownership of newspapers and broadcasting companies, and mining and generation and transmission of hydroelectric energy.

3. RECENT LEGAL DEVELOPMENTS

3.1 Significant Court Decisions or Legal Developments

Unsurprisingly, 2020 was marked by intense litigation.

Insolvency cases abounded, triggering a wave of distressed M&A transactions, which volume is expected to significantly increase during 2021, partially due to changes to the Brazilian Bankruptcy Law (enacted in December 2020 and in force as of 23 January 2021). The most relevant and impactful change is the clear affirmation that the purchase of shares or assets segregated from the insolvent company into an UPI (Brazilian acronym for Isolated Productive Unit) will protect the buyer of the UPI from succession for past liabilities of the acquired business.

Dispute resolution (both in court as well as arbitration) was also much sought after to resolve many disputes related to the economic crisis, such as breach of contract, shareholders disputes, and collection claims.

3.2 Significant Changes to Takeover Law

In recent years, no significant change to takeover law or regulations was implemented in Brazil and the prior tender offer requirements are still applicable: a mandatory tender offer, if the company has controlling shareholders, or a voluntary tender offer, if the company's capital is widespread and control is diluted.

No change to such rules is envisioned for 2021.

4. STAKEBUILDING

4.1 Principal Stakebuilding Strategies

As most listed companies in Brazil have controlling shareholders, stakebuilding prior to launching an offer is commonly privately negotiated, between the potential purchaser and the controlling shareholders (the legally established tag-along right attributable to the minority shareholders must be observed).

Otherwise, stakebuilding may also occur through corporate reorganisations, such as the merger of companies or the merger of shares.

When stakebuilding, it is common for bidders to acquire shares of the target company in a percentage below the disclosure threshold before making a tender offer. This strategy ensures that the information about the purchase does not become public, and the company's valuation is not affected. However, before conducting the tender offer, the bidder shall disclose the price paid for the shares of the controlling shareholder or its related parties in the previous 12 months.

4.2 Material Shareholding Disclosure Threshold

In Brazil, any transaction that results in a shareholder holding 5%, 10% or other multiple of 5% of shares of any type or class (or rights on shares, or certain securities or derivatives under securities), of a listed company, must be informed to the company.

If the transaction results in the change of control or in the management of the company, or leads to a mandatory tender offer, the transaction shall also be informed to the market.

The market must also be informed of the approval of any tender offer that has been submitted to registration by CVM, any control acquisition and the negotiation, by the company, of its own equity, or of equity of its controlling or controlled entities.

The company's controlling shareholders or management may request the waiver of the disclosure obligation if the disclosure may put the company's rightful interest at risk.

4.3 Hurdles to Stakebuilding

The 5% disclosure threshold may only be altered if to establish stricter conditions and a lower threshold may be imposed by the company's corporate documents.

Poison pill-like provisions may also be included in companies' bylaws to determine that, when a transaction would result in the buyer holding a significant percentage of the company's equity interest (for example, 20% or 30%), such buyer must make a tender offer to the other shareholders. Such provision, although usually construed as irrevocable, may be challenged in court, under the allegation that it may affect the shareholders' rights to sell their shares.

4.4 Dealings in Derivatives

Dealings in derivatives are permitted in Brazil, provided that certain rules are followed. Moreover, the sale of derivatives without a tender offer is possible but, during the offer period, the offeror and its related parties are prohibited from negotiating derivatives involving the same class of shares of those being negotiated.

4.5 Filing/Reporting Obligations

The filing and reporting obligations for derivatives dealings, under securities and competition law, are the same applicable to the acquisition of shares: any acquisition or disposal of "relevant equity interest" in a listed company must be disclosed to the company.

Pursuant to CVM rules, a transaction involving 'relevant equity interest' means a transaction resulting in the equity holding by a person, or group of persons, of shares of a listed company (or rights on shares, or certain securities or derivatives under securities), being increased or decreased in 5%, 10% or 15%, or any subsequent 5% variations. When any such transaction results in the change of control or in the management of the company, or leads to a mandatory tender offer, it shall also be informed to the market.

Furthermore, the approval of any tender offer subject to registration with the CVM, the acquisition of control and the negotiation, by the company, of its own interest, or of interest of its controlling or controlled entities, must be informed to the market.

4.6 Transparency

Any share dealings involving a listed company that could result in the company's change of control must be informed to the market.

Moreover, although the applicable regulation does not require a buyer of a controlling stake to make any statements or declarations in relation to its intention regarding the control of the company, CVM requires that any fact involving a listed company and deemed relevant must be broadly and immediately disclosed to the market.

Pursuant to CVM regulation, a "relevant fact" is any act or fact (including any deliberation by the shareholders' meeting, or by the company's management, or any political, technical, business or financial-economic act or fact) occurred to or related to the company's business, that may reasonably affect the valuation of the company's equity interest and/or the investor's decision to acquire new shares or dispose of shares.

5. NEGOTIATION PHASE

5.1 Requirement to Disclose a Deal

A deal involving a listed company must be disclosed when definitive documents are signed, even if the transaction is subject to suspensive or resolutive conditions, and again when the conditions have been met and the deal closed.

Deals involving the delisting of the company and the approval of tender offers subject to registration by CVM shall only be disclosed when the decision has been made (when the company has been delisted or the tender offer has been registered by CVM). However, if the information becomes public prior to delisting or CVM approval, disclosure must immediately be made.

5.2 Market Practice on Timing

Market practice on timing of disclosure of the transactions usually abide by legal requirements since breach would trigger penalties.

Early disclosure, prior to completion of the transaction, although not barred by CVM regulation, is not customary since the possible impact of early

disclosure normally prevents the parties from doing so (market conditions and the potential transaction itself could be adversely affected).

Public companies with high governance levels usually make disclosures in earlier stages.

Moreover, when a transaction is subject to antitrust approval, any disclosure prior to such approval must be strictly made, according to the applicable rules (until antitrust authorities' final clearance, the parties must comply with a standstill obligation and remain fully independent and evidence of breach of such obligation may be considered "gun jumping" and subject the parties to severe penalties).

5.3 Scope of Due Diligence

M&A deals typically start with negotiation of business terms and conditions and, as soon as a Term Sheet or MOU has been executed, reflecting such terms, due diligence starts (focus and breadth vary from deal to deal and according to the target's business).

Tax and labour potential and actual contingencies (including ongoing or threatened litigation), as well as environmental compliance and licenses and registrations are primary focuses.

In most cases, due diligence also comprises civil and consumer aspects, commercial and financial contracts, corporate matters, intellectual property, real estate, and, more recently, data protection (the LGPD came into force in 2020). Compliance also became a "must" in the wake of Operation Car Wash.

Inevitably, the COVID-19 pandemic affected the length and efficiency of due diligence processes due to lack of personnel to provide information, restrictions on transit and increased delay on the issuance of official documents by public authorities.

5.4 Standstills or Exclusivity

Standstill agreements, whereby a bidder receives a premium against a commitment not to make a hostile takeover offer, or increase its equity interest in the company, are not common in Brazil, given that such rights and obligations would violate the legal principle establishing that all investors shall be treated equally. Standstill agreements could also be construed as a violation of the fiduciary duties of the company's management, since their object is the preservation of the company's current control regardless of whether maintaining the company's control is in the best interest of the company.

Listed Companies

Transactions involving listed companies are subject to a mandatory standstill in the negotiation of securities of the target, upon occurrence of a "relevant fact" subject to disclosure until the actual disclosure of such fact (a "relevant fact" is any act or fact that may reasonably affect the valuation of the company's equity interest and/or the investor's decision to acquire new shares of the company). The mandatory standstill is also compulsory during the 15-day period preceding the disclosure, by the company, of its quarterly and annual financial statements.

Further, during the 12 months subsequent to a tender offer, the controlling shareholders of a company and related parties are, in general terms, prevented from conducting tender offers for shares of the company and during the tender offer period, the bidder and its related parties are prevented from negotiating shares of the same class and type of the shares to be acquired or derivatives under such securities.

Exclusivity

It is normal for purchasers to request and be granted exclusivity rights, even when the target is not a listed company. Exclusivity, as a rule, is limited in time and often renewed.

Exclusivity may also be granted in distressed M&A deals, even though such right is actually a "right to match" the offers of other potential purchasers during the bid for the sale of the distressed asset.

5.5 Definitive Agreements

The execution of share purchase agreements or other documents reflecting terms and conditions of tender offers, although permitted, is not common; shareholders agreements, regulating the relationship between shareholders or groups of shareholders, are occasionally executed.

When the transaction involves non-listed companies, the execution of purchase agreements and shareholders agreements, among others, is the rule.

6. STRUCTURING

6.1 Length of Process for Acquisition/ Sale

The process for acquiring or selling a business in Brazil varies depending on the size and complexity of the target's business, number of players involved in the transaction, scope and length of the due diligence and the need for approval by regulatory or antitrust authorities. A fair estimate of timing would be between six and 12 months, counted from the execution of the Term Sheet or MOU.

Although the COVID-19 pandemic negatively impacted the length of due diligence, due to lack of personnel to provide information, restrictions on transit and increased delay on the issuance of official documents, discussion of drafts agreements and the actual closing of transactions became more efficient through remote interactions and electronic signing of documents.

6.2 Mandatory Offer Threshold

In Brazil, a mandatory offer threshold applies only in a few specific cases.

When the purchase of shares represents a takeover, the bidder shall put a tender offer for the acquisition of the remaining voting shares for a minimum price equivalent to 80% of the price paid for the controlling shares (or 100% of such price if the company is listed in Bovespa's Novo Mercado). Alternatively, the bidder may offer to the remaining shareholders the option to keep their shares, upon payment of a premium in the amount equivalent to the difference between the market value of the shares and the price paid for the controlling shares.

In the absence of a takeover, when a bidder acquires more than two thirds of the outstanding shares of the same of class or type, the bidder must be willing to buy the remaining shares of the same class or type, if the holders of such shares so require, for the same price of the tender offer.

6.3 Consideration

Although most acquisition deals in Brazil are paid in cash, the exchange of securities is also permitted, as long as such securities are tradeable in Brazil. A combination of payment in cash and securities is also possible.

Transactions involving the payment with securities must be previously registered with the CVM and only exceptionally, CVM may permit payment with securities not tradeable in Brazil (in the event of takeover offers and other special cases).

Cash consideration is not necessarily a synonym of fixed price. Not only price adjustment mechanisms (most commonly, working capital and net debt adjustments) but also price installments

(calculated based on PAT, OPAT and EBITDA for future years) are common.

6.4 Common Conditions for a Takeover Offer

Brazilian regulation expressly permits the imposition of conditions on takeover offers, which conditions shall be expressly established in the tender offer documents and may not depend on direct or indirect actions of the bidder. Usual conditions are:

- corporate approvals from buyer's shareholders/board of directors;
- regulatory and antitrust approvals; and
- approvals by relevant third parties, such as strategic clients and financial institutions, who shall commit not to terminate in advance their contracts with the target company by reason of the change of control and absence of material adverse changes.

In certain situations, the takeover offer may include conditions related to change of certain provisions of the target's corporate documents, such as the shareholder exclusion and poison pill provisions.

Except when a condition is legally required (such as the antitrust approvals), any takeover offer condition may be subsequently waived by the buyer.

6.5 Minimum Acceptance Conditions

Tender offers are also subject to different approval thresholds as well as acceptance conditions:

- a tender offer for delisting a company must be approved by holders of at least two thirds of the outstanding shares;
- in the case of takeover offers, buyer shall either purchase the shares of the minority holders who exercise their tag-along rights, or pay them a premium for remaining in the company, in the amount equivalent to the difference between the market value of the shares and the price paid for the controlling shares; and
- voluntary tender offers for acquisition of control may be conditioned by the recipients of the offer on the effective success of the tender offer (a tender offer is considered "successful" upon unconditional acceptance of holders of shares which, jointly with the shares held by the bidder and its related parties, can ensure bidder's control of the company.

6.6 Requirement to Obtain Financing

In Brazil, it is possible, and even common, to condition business combination offers on the obtaining of financing by bidder. The condition must be expressly disclosed in the offer and its compliance may not be dependent exclusively on direct or indirect actions of the bidder.

6.7 Types of Deal Security Measures

Although no legislative change was enacted in 2020 to create or increase deal security, none was revoked or modified either.

Tender offers may be protected by requiring the bidder, when the offer has been accepted, to deposit the payment funds in escrow, to ensure that the transaction will be liquidated.

In private transactions, break-up fees are not uncommon.

A much sought-after protection in distressed M&A transactions is the "stalking horse" whereby a bidder (the stalking horse bidder) makes a binding offer for the distressed assets, setting, therefore, the low end of the bidding range. It is customary to grant the stalking horse bidder the right to match higher offers made during the bid.

6.8 Additional Governance Rights

In Brazil, control of a company can be established not only by holding the majority or totality of the voting capital of a company, but also by means of voting agreements, veto rights, supermajority approval for certain matters and the right to control the management of a company.

Furthermore, protections established in a duly executed shareholders' agreement (filed at the company's headquarters) are subject to specific performance and therefore breach of obligations contained therein (eg, the obligation to vote in a certain way in certain circumstances), will be remedied by court (in the example above, the court would determine the vote to be considered as if it had been cast according to the rules of the agreement) instead of settled in monetary terms.

6.9 Voting by Proxy

Shareholders can vote by proxy, provided that certain rules are complied with:

- the proxy must be granted to another shareholder or manager of the company or to an attorney; or, if the company is listed, the proxy may also be granted to financial institutions;
- the proxy must be valid for up to one year (unless the proxy is granted pursuant to the terms of a shareholders' agreement, with powers to expressly approve or disapprove any specific matter); and
- the proxy must be specific.

6.10 Squeeze-Out Mechanisms

Holders of less than 5% of the company's shares may be squeezed out if, after a successful tender offer for delisting the company, such shareholders do not accept the tender offer. In such event, the company's shareholders may approve the redemption of all such outstanding shares. The liquidated funds shall be made available by the company to the shareholders, in a financial institution approved by CVM. The price for such shares shall be the same price paid to the shareholders who accepted the tender offer.

6.11 Irrevocable Commitments

It is possible to obtain irrevocable commitments to tender or vote by principal shareholders of the target company, as long as certain conditions are met, such as agreement by the parties on the valuation of the company and other aspects of the transaction. Irrevocable commitments are usually undertaken at the final stages of a transaction and commonly subject to exclusivity clauses. In the absence of exclusivity rights, the shareholders shall be free to accept a better offer.

7. DISCLOSURE

7.1 Making a Bid Public

Under Brazilian law, whenever the target company is listed, a deal is required to be disclosed, by means of a public notice, when definitive documents are signed, even if the transaction is subject to suspensive or resolutive conditions, as well as when the conditions are met and the deal closes.

Delisting of a company and approval of a tender offer subject to registration with the CVM must only be disclosed when approved provided however that if the information becomes public prior to that, disclosure must be immediately made, informing the nature of the transaction and its then current stage.

7.2 Type of Disclosure Required

If at least one of the companies involved in a business combination transaction that involves issuance of shares is a listed company, the market disclosure must contain, at least, the main conditions of the transaction, such as:

- the identification of the companies involved in the transaction, and a brief description of their activities;
- main benefits, costs and risks of the transaction;
- how the swap of shares will occur;
- whether the transaction must be submitted to the approval of Brazilian or foreign authorities;
- the financial statements of the companies involved; and
- any other relevant information (appraisal reports, financial statements, minutes of board meetings and any other documents related to the transaction).

7.3 Producing Financial Statements

If at least one of the companies involved in any business combination is a listed company, all companies involved in the transaction must disclose their financial statements, all drawn up on same base date. The shareholders meeting that will vote to approve/reject the transaction must take place no later than 180 days counted from the base date.

The financial statements must be audited by independent auditors, and prepared in accordance with Brazilian law, the CVM regulations and Brazilian GAAP.

7.4 Transaction Documents

Further to mandatory disclosure of financial statements by all companies involved in a business combination deal, all transaction documents must be disclosed to the CVM and, when applicable, to the antitrust authorities and/or regulatory authorities, as the case may be.

8. DUTIES OF DIRECTORS

8.1 Principal Directors' Duties

Under Brazilian law, directors (as well as managers and legal representatives) are bound by fiduciary duties owed primarily to the company and, subsidiarily, to the shareholders. The interest of the company shall always prevail over the private interests of the shareholders.

The fiduciary duties comprise, without limitation:

- the duty of care, pursuant to which managers must conduct their duties employing the care and diligence which an honest and prudent person customarily undertakes in the administration of their own affairs;
- acting in accordance with the law and with the company's corporate documents; and
- the duty of loyalty, pursuant to which managers must not take part in any corporate activity in which they have an interest and that conflicts with the interests of the company.

In a business combination, directors have the fiduciary duty to give their opinion about the proposed deal, in good faith and in the best interest of the company. If there is a conflict of interest, such conflict shall be immediately informed to the other directors.

8.2 Special or Ad Hoc Committees

Although recommended from a governance standpoint, the creation of ad hoc committees in business combinations is not common practice. In Brazil, such committees are created by the shareholders, not by the board of directors, but the board may suggest their creation, which shall then be submitted to the shareholders' approval.

Ad hoc committees have solely advisory powers and do not replace in any way the board of directors (under Brazilian law, the functions of a corporate body may not be delegated).

8.3 Business Judgement Rule

Brazil is a civil law country with its legal system based on codes. Courts and arbitration cham-

bers therefore decide the merits of a dispute in accordance with the applicable Brazilian law and shall not act as amiable compositeurs or decide the merits of a dispute ex aequo et bono.

Accordingly, the judgment or opinion of boards of directors may be taken into consideration by a court or arbitration chamber when reviewing a case but cannot form the basis of the court decision or arbitration award. Neither courts nor arbitration chambers may defer their decision powers.

8.4 Independent Outside Advice

The company's shareholders hold the decision-making powers on business combinations and the function of the board of directors is only advisory. Nevertheless, before opining in a proposed business combination, diligent directors commonly request the advice of legal, financial and accounting advisors which will review and report on the positive and negative impacts of the transaction and their consequences on the company.

8.5 Conflicts of Interest

Conflict of interest of directors, managers, shareholders and advisors are subject to judicial and administrative scrutiny. Conflict of interest can be defined, according to its nature, as a formal conflict and a material conflict.

A formal conflict of interest is a conflict that may be verified a priori, and as such is presumed, eg, a formal conflict of interest may be presumed if, in a potential transaction, a director has a personal interest in the deal, regardless of whether such personal interest is conflicting or converging with the company's interest.

A material conflict of interest is a conflict verified a posteriori, in which case the possible existence of a conflict is verified on a case by case basis, eg, after a director advised the shareholders in favour of a transaction, the question would be whether the director put his/her interest over the company's interest and, also, whether such fact has caused an actual damage to the company.

Currently, most of the CVM's administrative decisions are based on the formal conflict theory.

9. DEFENSIVE MEASURES

9.1 Hostile Tender Offers

Hostile tender offers are uncommon in Brazil, mainly because the capital of most companies is not widely held and therefore acquisition of control is often privately negotiated between the buyer and with the controlling shareholders of the company.

The last important hostile take-over attempt occurred in August 2020, involving two of the major players in the real estate development market in Brazil, Tecnisa and Gafisa, both family-controlled companies.

Gafisa held an equity interest in Tecnisa and made proposals for the combination of their businesses, all considered hostile. As a first step, Gafisa increased its equity interest in Tecnisa from 3% to 5%, then requested the amendment of Tecnisa's bylaws to change its poison pill provision. By way of defence, Tecnisa's controlling shareholder entered into voting agreements with other shareholders, to increase its controlling power and obstruct the approval of a takeover offer at the shareholders meeting.

In January 2021, Gafisa's interest in Tecnisa was reduced to 4.92%. However, neither company has discarded the possibility of an "organic" combination of the businesses.

9.2 Directors' Use of Defensive Measures

In Brazil, the company's shareholders have the exclusive power to approve takeovers and, accordingly, whenever necessary, defensive measures shall be used by the shareholders, not by the directors who may, nevertheless, advise and assist the shareholders on the use of such measures.

9.3 Common Defensive Measures

The most common defensive measure against a takeover of a listed company is the poison pill.

Unlike other jurisdictions, the poison pill provision commonly used in Brazil does not grant the shareholders of the hostile takeover target the right to purchase additional shares of the company for a lower price; instead, when the takeover offer results in the bidder holding a significant percentage of the company's equity interest (for example, 20% or 30%), the Brazilian poison pill compels the bidder to put a tender offer to acquire the totality of the remaining shares of the target company.

Other defensive measures, such as Golden Parachute provision and Crown Jewel Options, are uncommon in Brazil.

9.4 Directors' Duties

The board of directors may advise the company's shareholders on the convenience or necessity of using defensive measures but cannot enact them.

Advice by the board of directors must describe all aspects that may be relevant for the shareholders to make an enlightened business decision.

When issuing an opinion or implementing any defensive measures, as determined by the company's shareholders, the directors must exercise their fiduciary duties, acting with loyalty and diligence, and disclosing any possible conflict of interest.

9.5 Directors' Ability to "Just Say No"

Since only the company's shareholders can accept or refuse a tender offer, directors are not entitled to "just say no" and take action to prevent a business combination.

10. LITIGATION

10.1 Frequency of Litigation

M&A related litigation is neither a regular occurrence nor a rare event. Disputes tend to be subject to arbitration rather than courts and the recurring objects of disputes are breach of representations and warranties, unpaid indemnification, and earn-out price calculations.

10.2 Stage of Deal

Most frequently, disputes arise after closing, but 2020 was a peculiar year and broken deal disputes were filed as well as disputes over the applicability of MAC – Material Adverse Change provisions to indemnification of losses arising out of the COVID-19 pandemic.

10.3 "Broken-Deal" Disputes

It is too early to tell since jurisprudence has not yet been formed. Court decisions have been challenged by appeals and most cases therefore still await second level decisions.

11. ACTIVISM

11.1 Shareholder Activism

In a rapidly changing world, the relationships between companies and their shareholders as well as consumers have been evolving fast.

Social networks are playing a massive role in promoting discussions and engaging minority shareholders and, consequently, impacting the value and volatility of shares (during 2020, a major Brazilian retail company dismissed a large number of employees but, driven by livestream panels and discussions on Twitter about the company's values and initiatives to reduce impact on workers and consumers, its share price rose by 400%).

As the definition of "generating value" to shareholders switches to a broader spectrum, companies are gradually starting to focus on social and environmental issues and activists are closely monitoring the companies' actions and progress.

Most activists in Brazil still target monetary related issues but a new category of activists, epitomised by ESG (environmental, social and governance) activists, has come to prominence, as large institutional stockholders require greater transparency and accountability from companies and extend their agenda to diversity and inclusion.

11.2 Aims of Activists

Social change and sustainability motivate several groups of shareholder activists. Encouraging companies to divest from politically sensitive and polluting companies as well as from companies with unfair labour practices is pretty much on such activists' agendas.

11.3 Interference with Completion

Activists do not often try to actively prevent the completion of announced deals.

Felsberg Advogados is a full-service law firm founded in 1970 and defined by its ability to combine experience, tradition and excellence with efficient, fast and focused service, offering innovative solutions in a constantly changing world. The corporate and M&A department is headed by six partners. The firm assists Brazilian and foreign clients from the incorporation of companies to the structuring, due diligence and negotiation of acquisitions, disposals, and joint ventures. The M&A team is supported by a partner specialising in competition law, with years of experience in dealings with the Administrative Council for Economic Defense (CADE), investigations into anti-competitive practices, and settlement negotiations. More recently, the department created a specialty sub-group, Innovation, StartUps and Venture Capital, dedicated to advising all agents in the ecosystem, including investors (private equity and venture capital), start-ups receiving rounds of investments, as well as seed accelerators, financial institutions and the government.

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