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# MERGERS & ACQUISITIONS

*BRIEF STUDIES*

Almeida
CORPORATE LAW

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## INTRODUCTION

Mergers & Acquisitions are increasingly gaining importance in the globalized economy, being one of the reasons responsible for the reallocation of the investments in economy and the execution of corporate strategies, representing an alternative for the adequacy of the company's size and organizational structure to the market and to the global economic scenario.

A significant part of the top merger & acquisitions transactions in Brazil, especially after the 1990's decade, had participation of Almeida Advogados, whether advising the buyer, or the seller. Its strong expertise in the area classifies it as one of the most respectable law officers in merger & acquisitions' consulting.

In accordance with a PricewaterhouseCoopers' report, in 2008, 639 corporate transactions happened in Brazil, with an increase of 4% of the control acquisition ones, in comparison with 2007, being the most common deals, representing 66% of the year's transactions.

Almeida Advogados has taken part of several merger & acquisitions transactions, especially on 2008, when the sum of all amounts involved on such projects was higher than US$2.5 billion.

**Summary of the 2008 Transactions (until July):**

| | Values | Transaction | Almeida Advogados' Client |
|---|---|---|---|
| **1** | Initially US$ 100 million. Total Estimated Investment: US$ 1 billion | Capitalization | Argentine grains' Exporting Company |
| **2** | Approximately US$ 800 million | Acquisition | Mining Companies' Holding |
| **3** | Approximately US$ 750 million | Acquisition | Mining Companies' Holding |
| **4** | US$ 310 million | Acquisition of project for the construction of a harbor | Mining Companies' Holding |
| **5** | US$ 300 million | Restructuring | Energy Supply Company |
| **6** | US$ 280 million | Restructuring | International Investment Funds |
| **7** | US$ 55 million | Capitalization | Information Technology Company |
| **8** | R$ 48 million | Acquisition | Technology and Computer Services Company |

| | | | |
|---|---|---|---|
| **9** | Approximately R$ 6 million | Capitalization | Information Technology Company |
| **10** | Approximately US$ 1,8 million | Acquisition of all quotas ob Brazilian subsidiary company, with buyback option | International Images Agency |
| **11** | Approximately R$ 3,5 million | Purchase and Sell of equity interest | Investment Fund focused on small and medium information technology companies |
| **12** | Undefined | Restructuring | Communications Company |
| **13** | Undefined | Acquisition | International Investment Fund |

**Summary of the 2007 Transactions:**

| | Values | Transaction | Almeida Advogados' Client |
|---|---|---|---|
| **1** | Approximately US$ 5 million | Control Acquisition | Technology and Sustainable Development Company |
| **2** | Undefined | Acquisition of Equity Interest | Large Brazilian Food Company |

A merger & acquisition transaction is considered as successful when results in benefits to both seller and buyer, reason why its success is directly related to the quality of the legal services rendered.

Therefore, as important as the decision to carry out a merger & acquisition transaction, with all of its results, is the performance of lawyers with creativity and great legal knowledge, able to materialize the desires of the involved parties.

Aware of the importance of this subject and its consequences on the national economy, Almeida Advogados now presents twelve essays regarding merger & acquisitions, with the analysis of its most relevant matters.

With these studies, Almeida Advogados does not intend to discuss all the infinite legal matters related to merger & acquisitions, but only to provide to the reader the some interesting matters related to such fascinating subject.

Have a good reading!

## 1. MERGER, CONSOLIDATION AND SPIN-OFF TRANSACTIONS

The so-called M&A transactions ("mergers and acquisitions") consist of, from the corporate point of view, in addition to transactions relating to the purchase and sale of outstanding shares and/or quotas and direct investments represented by the subscription of new shares and/or quotas, the corporate transactions relating to the merger, consolidation and spin-off of companies, the latter in the total and partial types.

Such transactions may be the main alternative of any M&A transaction, or also, in the majority cases, ancillary methods used in connection with the transactions relating to the purchase and sale of ownership interest or new subscription of shares, and are used for the creation of corporate structures, segregation of activities, structuring of a tax planning adequate to the estimated investment, among others.

The merger and consolidation transactions are similarly set forth in the Brazilian Corporations Law and the Civil Code. The spin-off transactions are solely set forth in the Brazilian Corporations Law, which does mean that the spin-off transaction is not applicable to limited liability companies.

In general, it is possible to state that the merger transaction, pursuant to the Brazilian Corporations Law and the Brazilian Civil Code, is the transaction whereby one or more companies (merged companies) are merged into another company (merging company). As a result of the merger transaction, the merged companies are extinguished, and the merging company is the successor thereof in connection with any and all rights and obligations[2].

The consolidation transaction, also pursuant to the aforesaid laws, is the transaction whereby two or more companies are combined and extinguished as a result of any such transaction, to create a new company, which will be their successor in connection with any and all rights and obligations [3].

The legislation, for both transactions, in the same manner as in the spin-off transaction described below, sets forth rules in connection with the preservation of the rights of creditors of the companies to be extinguished, in the event of merger or total spin-off, or the rights of creditors of the spun-off companies, in the event of partial spin-off .

In this regard, pursuant to Article 232[4] of the Brazilian Corporations Law and Article 1,122[5] of the Civil Code, the companies involved in any merger and consolidation transaction should necessarily disclose the actions relating to the transactions and wait for a period of 60 (sixty) days, in the event of publicly-held companies, and a period of 90 (ninety) days, in the event of limited liability companies, for purposes of presentation of any declaration by the creditors. After any such period, and without any statement by the interested parties, the actions should be registered with the Trade Board.

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[2] Law nº 6.404/76, art. 227.
[3] Law nº 6.404/76, art. 228.
[4] Art. 232. Up to 60 (sixty) days after the disclosure of the actions relating to the merger or consolidation, the former creditor adversely affected by any such transaction may bring a claim before the court in connection with the cancellation of the transaction; after the end of the period, the creditor should relinquish any unexercised right.
[5] Art. 1.122. Up to 90 (ninety) days after the disclosure of the actions relating to the merger, consolidation or spin-off transaction, the former creditor adversely affected by any such transaction may bring a claim before the court in connection with the cancellation of the transaction.

The Brazilian Corporations Law, with respect to the spin-off transaction, defines it as the transaction whereby the company transfers parts of its net equity to one or more companies, which will be incorporated or are already incorporated for such purpose[6].

The spin-off transaction may be total or partial. The spin-off transaction should be considered as total if the spun-off company transfers its total net equity to one or more existing companies, and is subsequently extinguished. The spin-off transaction should be considered as partial if the spun-off company solely transfers a part of its net equity to one or more existing companies and continues to operate with the remaining portion of the net equity.

In addition to the corporate differences existing between merger, consolidation and spin-off described herein, it should be pointed out a key difference in what concerns the succession of rights and obligations between any such transactions.

In the merger, consolidation and total spin-off transactions, considering the fact that the original companies are extinguished as a result of such transactions and their registrations are cancelled, including before the Ministry of Finance, the companies that receive the net equity are the successors in connection with any and all rights and obligations, including those of tax and labor nature. On the other hand, in the partial spin-off transaction, the original company that allocates a portion of the net equity and transfers such net equity to another company, continues to operate and is the holder of any rights and obligations.

In this regard, Article 233 of the Brazilian Corporations Law sets forth that the partial spin-off may establish that the companies that absorbed a portion of the net equity of the spun-off company will be solely held liable for the obligations transferred to such companies, without any joint liability among each other or before the spun-off company. Therefore, any creditor which credit was recorded prior to the spin-off transaction may challenge the determination with respect to the credit, provided that upon delivery of notice to the company within a period of 90 (ninety) days counted from the date of disclosure of the spin-off actions. In the event of lack of challenge within any such period, the actions may be registered with the Trade Board.

Considering the matter of succession in connection with any rights and obligations set forth herein, the partial spin-off transaction is many times the most adequate to support the purchase and sale of a portion of the transactions of any given company or even new investments for the development of any given area of activity because the partial spin-off transaction allows to protect the rights and obligations of third parties without any type of succession and also provides for a advisable continuity of activities of the original company.

On the other hand, the merger and consolidation transactions are largely adopted in connection with companies comprising the same group in a manner to accelerate procedures and reduce costs.

Finally, the individual analysis of each intended transaction and the intent of the parties involved are critical for the recommendation and implementation of the corporate transaction that is more appropriate to each case.

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[6] Art. 229. The spin-off transaction is the transaction whereby the company transfers parts of the net equity to one or companies, which will be incorporated or are already incorporated for any such purpose, and the spun-off company is liquidated, in the event of total transfer of the net equity, or the share capital is divided, in the event of partial transfer of the net equity.

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## 2. THE IMPORTANCE OF THE PRELIMINARY DOCUMENTATION IN MERGER & ACQUISITION TRANSACTIONS

Each of us most likely already took part in the beginning of any negotiation process in which the general terms and conditions necessary to organize a corporate or commercial transaction are drafted. Such terms and conditions usually encompass the definition of obligations of the interested parties, and any other complementary terms and conditions.

The preparation of preliminary documents that summarize the transaction to be performed, or the company to be incorporated, is a normal practice prior to the preparation of an agreement comprising the aforesaid terms and conditions. Such preliminary documents are extremely important for the clear, swift and objective development of the deal.

Among the preliminary documents, three types of documents are most commonly adopted: the letter of intent, also referred to as LOI, the memorandum of understanding, also referred to as MOU, and the investment agreement, also referred to as term sheet. The typical subject matter observed in the three documents is the establishment of the terms and conditions for the preparation of an agreement. However, such documents present key differences that determine the circumstances when they should be used.

The letter of intent is normally used when there is an imminent transaction, but the interested party has yet no information on the condition of the company to be acquired or invested. Therefore, in general the execution of the letter of intent is carried out after the accounting and legal due diligence.

The memorandum of understanding is similar to the letter of intention in the sense that the memorandum of understanding clearly establishes the terms and conditions necessary for both companies to reach an agreement. However, the memorandum of understanding is usually used whenever there is any intent to incorporate a new company or carry out joint activities, circumstances which partially differ from a purchase and sale transaction per se.

The investment agreement or term sheet describes the legal and financial terms and conditions of the investment and quantifies, by means of numbers and any other indicators, the value of the transaction. This document, if agreed upon by the parties, is used as a basis for the preparation of any and all legal documents that support the investment. The structure of a term sheet is likely to be more complex and is executed after the performance of the due diligence.

The preliminary documents can be non-binding or binding. The non-binding documents contain the preliminary terms and conditions of the transaction and are not binding upon the involved parties. The binding documents are binding upon the parties and already describe the preliminary structure of any future Agreement. The terms and conditions thereof should be included in the final documentation to be entered into for the investment or transaction.

The preliminary documentation phase is exceptionally important in any merger & acquisition process, taking into consideration that, in light of the Civil Code, any such documents have

the legal nature of a preliminary agreement that may be binding upon the parties and result in, consequently, the right to execute the final agreement[7].

The preliminary agreement or pre- agreement is so relevant that, once registered with the competent authority, the judge may, upon request of the interested party and in order to fulfill the intent of the breaching party, consider it as a final agreement[8]. For this reason, the preliminary agreement should be similar, to the greater extent possible, to the final agreement to be entered in the conclusion of the corporate transaction.

The preliminary documents may be prepared by the interested company itself, by means of its controlling shareholders or officers and directors, the leader of a group of investors ("leading investor") and, are generally addressed to the investor and the controlling shareholders of the target company.

Among the various benefits of such documents, we may observe the following: *i)* include the primary terms and conditions of the transaction; *ii)* forthwith encourage the parties to declare, in writing, the intent thereof with respect to the investment, thereby reducing the chances of negative surprises; *iii)* help the discover of any potential obstacles to the transaction ("deal breakers"); *iv)* accelerate the investment process; *v)* facilitate the preparation of final agreements, among various other benefits.

The most common provisions set forth in the preliminary documents in addition to the qualification of the parties involved are: a) a summary of the proposed investment; b) terms and conditions of the offer (due diligence, tax and accounting analysis); c) allocation of the resources invested; d) schedule of the investment; e) rights of the investor and the parties; f) definition of the percentage rate for purposes of approval of specific matters (veto); g) non-competition among the founding shareholders, officers and directors and key employees; h) withdrawal rights and general rights; i) terms and conditions for the closing; j) confidentiality and exclusivity for a defined period; l) any other provisions, taking into consideration the nature of the transaction to be performed.

Another important matter related to the preliminary documents refers to the adjustment of the terms and conditions set forth therein. This because each jurisdiction has own rules which requires the adjustment of the documents based on the jurisdiction of the investor and the invested company with the resulting company. The typical terms and conditions that are normally included in the preliminary documents refer to: tag along; drag along; redemption; anti-dilution; right of first refusal; put option; call option; and others.

At last, it is worth to point out that the parties elect to adopt the Arbitration Process for the resolution of any potential controversies and that, even in the events of transactions carried out in Brazil, the parties normally adopt the Common Law policies in detriment to the Civil Code.

Such inclination is explained by the greater experience of the foreign investors with any such process thereby allowing greater flexibility in connection with the closing of the corporate transaction.

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[7] **CC, art. 463.** Upon conclusion of the preliminary agreement, as per the provisions set forth in the preceding Article, and provided that no termination clause is included therein, any party shall have the right to require the execution of the final agreement and establish a term for execution by the other party.
[8] CC, art. 464.

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Considering the importance of the Due Diligence, especially in cross-border deals, a deeper analysis of this important step of merger & acquisitions transactions will be the subject f the following chapter.

## 3. DUE DILIGENCE IN CROSS BORDER ACQUISITION DEALS

A Due Diligence process is one of the most remarkable characteristic of the modern counseling. As complex transactions enlarged the boundaries of global businesses, corporate creativity is bound only to the legal possibilities of its creators, where legal counseling erupts its original limits to become another active partner in drawing the very basic aspects of any deals.

We, at Almeida Advogados, believe that the full role of the best practice of law is played by being at both sides of creativity and consciousness: the art of outlining the environment for the business free flow, alongside the duty to evaluate all risks involved: to assist and to foresee.

We know for sure that there are multiple perspectives involving both of these commitments, nonetheless the Due Diligence process as a whole must be held as a keystone in the perspective of consciousness.

Due Diligence process is an art per se to evaluate all the legal aspects involving a certain company, to determine whether or not each business practices are susceptible to eventualities, to be able to understand how fragile or strong certain corporate relations may be and still, never lose track of the players' interests and needs. To master a Due Diligence is somehow to master the very outline of the corporate life.

In the present global business scenery, it is not possible to conceive the execution of an acquisition deal without conducting a Due Diligence process, both in order to verify all potential or effective contingencies and liabilities of a target company, as well as to accurately evaluate its assets and worthiness.

From this second standpoint, the seller has a great interest in proving the real value of the target company, among all areas a company must be evaluated from. Undoubtedly, the solidity of the evaluation of a target company is a strong bottom limit in negotiating prices, alongside good evaluation results.

From the other standpoint, and amongst the most important criteria for the buyer, there are the need of plainly understand the target company and to correctly evaluate the risks involved, and only a Due Diligence process is capable of such analysis and capable of avoiding exterior or cosmetic aspects of a certain company.

### 3.1. Due Diligence Concept

The Due Diligence process is a collective term for a number of procedures and standards involving the investigation or audit of a certain company, all directed towards its most accurate evaluation.

The term has its origins probably in the Securities Act of 1933, by the U.S. Securities and Exchange Commission, which had as basic objectives to guarantee that investors receive financial and other significant information concerning securities being offered for public sale, and to prohibit deceit, misrepresentations, and other fraud in the sale of securities. Such liabilities would be avoided once dealers have disclosed to the investors the information gathered as a result of the exercise of a “reasonable diligence”.

The term spread out through the broker-dealer community and was quickly adopted to identify the efforts of analysis and evaluation of any investment, becoming the conducting of due diligence investigations a standard practice throughout the business environment worldwide.

Interestingly, the due diligence process may be conducted by both parties in order enable both to verify the risk and value of a certain investment, as well as to verify the investor’s capability to purchase and to comply with the obligations and liabilities arising from the investment itself.

### 3.2. Due Diligence Scopes

The primal scope of a Due Diligence is to evaluate a certain target of an investment by analyzing any aspects that can be revealed or to harm its value. Since the Due Diligence is majorly a risk management activity, the activities conducted in Due Diligence processes are mainly oriented to reveal the liabilities, contingencies, problems and exposure to damages or losses arising from the regular performance of the target’s business.

In view of such risk analysis and evaluations, the Due Diligence process varies for different transactions, in example, the acquisition of an Information Technology company may not require the analysis for possible environmental damages.

The most relevant areas of concern may include the financial, legal, labor, tax, intellectual property, environment, real and personal property, market or commercial situation, IT, as well as insurance and liability coverage, debt instruments review, immigration, international transactions among many others.

Nevertheless, the crucial aspect of an accurate analysis exceeds the simple verification of the actual status of any aspect, relying on the ability of foreseeing any arising, potential or collateral contingencies that such aspect may generate and being able to evaluate the probability of damages or loss in the future. Therefore, the analysis of each area of concern should be performed by experienced and specialized consultants.

### 3.3. Due Diligence Structure

A Due Diligence process mainly comprises the review and analysis of documents, contracts, archives, accounting records and any other type of information required for the analysis of the chosen aspects. Therefore it is a process that can take place in either investor or investee location and that nowadays can be conducted even virtually, by using digital data rooms in which the scanned documents are stored and using computers to have access to it.

Depending of the particularities of each transaction, it may be necessary to conduct field researches, interviewing officers and employees, gathering information of the target’s sites and locations, and to include the analysis of proceedings where the target is involved within each court office.

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A Due Diligence process is usually conducted by lawyers, but it can include accountants, engineers, financial advisors and any other expert professionals who may be able to understand and more accurately evaluate each proposed aspect.

Although it is widely recommended that the Due Diligence wideness be as comprehensive as possible, analyzing every aspect of the intended investment, it is possible to reasonably adequate its range for the most sensible aspects involved in a certain transaction, decreasing the time-frame needs of the project as well.

Once a Due Diligence process is majorly conducted over an entire company or group of companies, another important aspect of such process is to clearly identify the documents flow and to set the confidentiality among the parties and agents involved in the transaction, as well as the responsibilities arising from delivering or supplying of documents, the control over the access to the documents, and the duties and tasks of each party, each consultant and agent.

The period of time a Due Diligence requests is often connected to its wideness, and such time-frame, as described above, usually contributes for its definition. Along with the available time-frame, the resources dedicated to the Due Diligence are another usual limitation to its range, nevertheless, as each transaction may present more relevant issues to evaluate, a more adequate Due Diligence may result in an acceptable safety margin, where other losses and damages may not compromise the whole investment to be done.

### 3.4. Due Diligence Result

The result of a Due Diligence is mainly a report and an opinion.

The report is a summary of all information gathered throughout the Due Diligence process, concentrating all evaluated areas and all aspects involved, as it acquire its form from a relation of all documents and information in which the analysis is based on, a description of the scope and limits of the Due Diligence process, all aspects involved, the selected areas of concern and a full brief of all gathered data such as numbers, dates, names, main aspects, main exposure, prices, risks, margins as well as any other information deemed to be relevant of each analyzed document or information. Nonetheless, the true value of a Due Diligence process is the opinion arising thereto.

Once all analyzed aspects have been evaluated specifically by the professionals involved in each area of a Due Diligence process, the most important task is performed, to understand the very outline of the proposed business, to perceive all interests involved in the transactions, to evaluate and foresee the gathered risks, to comprehend the investment as whole and to, finally, judge from a legal and commercial standpoint whether the proposed investment may prosper.

The opinion expressed as result of a Due Diligence process is one of the most important instruments for the corporate players to evaluate, to judge and to decide any transaction.

### 3.5. Cross Border Due Diligence

In respect of the above, it is within cross border transactions where a Due Diligence process finds its higher importance.

Since every country has its own legal system, it is almost impossible for a foreigner to correctly evaluate all aspects of a company such as financial, legal, labor, tax, intellectual property, environment, real property, insurance coverage, among many others aspects.

Furthermore, to evaluate certain aspects of an investment relying solely upon the rules and standards of another legal system and culture, can usually lead to misconceptions, distortions and imprecise conclusions, turning a highly non recommended investment in an attractive one or vice-versa.

Being absolutely aware that each country has its own particularities, its own requirements and concerns, a short brief of Brazilian legal system and most common singularities are presented below.

### 3.6. Due Diligence in Brazil

Considering the diversity of legal and administrative particularities of each country, especially in a continent size and federatively structured country such as Brazil, it is essential that a Due Diligence process be conduct by local legal consultants, whose expertise may comprise all the territory involved in a certain transaction.

It must be taken into consideration that Brazil has a Federative System comprised by three different government spheres, at federal, state and municipal levels, all capable to legislate in autonomous ways over many areas, according to the limits set forth in the Brazilian Federal Constitution.

In order to perceive the extension of such system, Brazil has today five thousand, five hundred and sixty two cities, divided into twenty six States and a Federal District, which legislates at both state and municipal levels, resulting in an enormously extent legislative production, filled with uncountable particularities and, very often, pierced by concurring standing for enacting legal rules among the three spheres.

In respect of such concurring standing, it should be further considered that there is a hierarchy between the federal, state and municipal instances, in reason of which the federal legislation outstand state and municipal ones and the state legislation govern the municipal one. Meanwhile, conflicts amongst such different legislations is very often found, which may lead to a great impact in the transaction, if not correctly observed, and alerted.

With regards to the environmental legislation, for example, the federal government may legislate in concurrence with states and the Federal District, enacting absolutely autonomous rules, thus regulating markets and setting specific policies to be fulfilled by companies and corporations in the performance of regular business.

Along the same path there are the regulatory agencies, entities connected to the indirect administration and which main scope are to rule activities under the infrastructure sector, previously executed by the state and now transferred to privately held companies.

In view of the above matters, a Due Diligence conducted exclusively under federal legislation or disregarding the particularities of the region involved in the transaction, or additionally, the standards and policies from state agencies shall inevitably hold distortions that may compromise the whole transaction.

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This is one of the reasons why foreign firms and companies are recommended to procure a local partner and consultant, who may offer the commitment and capacity to precise and accurate analysis of the aspects of a certain investment within Brazilian jurisdiction.

Besides the Due Diligence usually adopted in merger & acquisitions transactions, a due diligence specifically focused in possible environmental contingencies is gaining importance in such corporate transactions.

## 4. ENVIRONMENTAL DUE DILIGENCE

The recent drafting creation of an intricate environmental legislation in Brazil that provides for the imposition of severe liabilities and applicable penalties to the companies and respective its officers and directors, caused the parties interested to carry out any corporate transaction to be prudent in connection with the performance of a previous due diligence of any and all legal and environmental matters concerning the companies involved.

In this regard, the legal due diligence relating to the environmental liabilities, both potential and actual, is critical for the implementation of any merger & acquisition transaction, to the extent that no transaction, albeit even a small one, is not considered as reliable without the performance of an environmental due diligence.

The Brazilian environmental legislation provides for a number of matters that may materially affect the parties involved in any merger or acquisition transaction, both by virtue of the applicable penalties, which penalties are, with no exception, material and critical, and by virtue of the broad extent of the chain of liability of the parties involved and the lack of any statute of limitation in connection with environmental damages.

The penalties applicable on violations of environmental regulations are severe. The fines charged, on monetary basis, may reach the value of R$ 50,000,000.00 (approximately US$ 21 million), without prejudice to any potential obligation to indemnify any affected third parties, and also, recover the damages caused. In addition, motions to stay injunctions of activities (whether temporary or permanent), demolition or veto prohibitions to contract with governmental programs authorities are expressly set forth in the law.

As though the penalties of administrative and civil nature described in the preceding paragraph were not sufficient, causing cause damages to the environment may give rise to the imposition of criminal penalties of criminal nature, both on the individuals and the legal entities and respective officers and directors.

The large variety of potential agents that can be responsible for the to which the liabilities for the occurrence of damages could be attributed is another reason for the imposition of severe penalties. The liability for environmental damages is considered as strict and joint, a distinctive attribute of the Brazilian environmental law, that is, under a stricter analysis, any and all persons who contributed, in any manner whatsoever, to cause the damage, notwithstanding regardless of any guilty, could be held liable for the remediation thereof.

Also, as a third topic of stringency to be discussed, a large majority of the Brazilian courts understands that the obligation to recover environmental damages caused and indemnify the affected parties do not become time-barred ever and, not rarely, it is possible to come across

lawsuits brought filed against the owners of contaminated lands, which contamination has occurred decades ago and was caused by the former owners of the those lands.

In view of the foregoing, the risks (actual, potential or hidden) related to environmental problems in connection with corporate transactions may have material impacts – both financial and criminal – on the companies involved and their respective officers and directors.

For this reason, an environmental and legal analysis, the so-called Environmental Due Diligence, is critical for the identification of the actual situation of a company subject to merger, acquisition or any other methods of modification of companies.

By means of any such analysis, which comprise the legal and technical matters of the companies involved, it is possible to identify and quantify the environmental risks and contingencies existing in connection with the transaction. Thus, an Environmental Due Diligence report becomes an indispensable tool for a proper decision-making process in connection with corporate transactions, to the extent that any such report permits the parties involved to set prices and analyze any and all liabilities.

The previous performance of Environmental Due Diligences is strongly advisable with respect to any process for the company's modification or purchase of assets, thereby representing a tool for the making of decisions at the same time as it holds the officers and directors harmless from and against any and all criminal charges arising out of any potential or hidden matters.

Among the many reasons that may lead to a merger & acquisition transaction, one is being largely used as an alternative to avoid the impact caused by the tax burden deriving from the exercise of the taxpayers' business activities, especially in countries where such burden is extremely high, such as Brazil. Is the tax planning.

## 5. MERGERS & ACQUISITIONS AS METHODS OF TAX PLANNING

Any consolidation, spin-off and merger transaction is generally carried out with highly economic purposes aiming at the fulfillment of market interests existing among the parties involved.

However, any such transactions may also be used as tax planning methods, which can be defined as a group of measures and actions adopted by the taxpayer in order to reduce the tax burden deriving from the exercise of the taxpayer's business activity.

The consolidation, merger and spin-off transactions, as corporate reorganization methods, are governed by Law nº 6.404/76 (Brazilian Corporate Corporations' Law).

The consolidation is the transaction whereby two or more companies are combined for purposes of incorporation of a new company, which will be the successor company of those two or more companies in connection with any and all their rights and obligations.

The merger is the transaction whereby one or more companies are merged into by another company, which will be the successor of those one or more companies in connection with their rights and obligations.

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On the other hand, the spin-off transaction is the transaction whereby the company transfers parts of its the net equity thereof to one or more companies, which are incorporated for any such purpose or are already incorporated, and the spun-off company is liquidated, in the event of total transfer of the net equity, or its the share corporate capital thereof is divided, in the event of partial transfer of the net equity.

It is a common practice, by the Tax Authority, to challenge any such corporate transactions, if the transactions are carried out with the purpose of tax planning, under the allegation that the purpose thereof should be to prevent the payment of due taxes. For this reason, it is extremely important to analyze and separate distinguish the principles definitions of tax avoidance and evasion.

The tax avoidance seeks to prevent or reduce the tax burden levied on the taxpayer by means of valid transactions primarily used for any such purpose. The tax evasion, in other hand, is illegal, as such method seeks to conceal, from the Tax Authority, the occurrence of any triggering events, by means of fraudulent transactions.

In order to prevent the validity of any a tax planning, the Tax Authority generally adopts the principle of violation of rights, whereby the actions, facts, agreements and transactions, set forth in the tax legislation as taxation basis, should shall be construed in accordance with their economic results thereof and not in accordance with their legal nature thereof, that is, the Tax Authority relies upon the assumption that similar economic circumstances should shall necessarily be imposed similar taxation basis.

Nevertheless, any such principle clearly violates the individual autonomy, by means of a legal governmental intervention, which allows possibility of any Judge or Inspector to interpret construe the fact and regulation without taking into consideration the principles that governing the tax legislation, such as the legal conduct and safety, among others.

There are, however, circumstances in which the tax planning could be declared as illegal by the Tax Authority.

The principle theory that better defines and classifies any such circumstances is the simulation principle. The simulation, in the tax area, consists of forging a factual or legal situation that averts the imposition of the tax.

The Civil Code describes, in Article 167 thereof, the events of simulation; the Tax Authority, outside the scope of any such events, shall have no authority to declare the invalidity of the tax planning.

In view of the foregoing, it is possible to conclude that the tax planning, if carried out on preventive manner in order to cause any future corporate transactions or actions to be carried out in a manner less burdensome to the taxpayer, shall not constitute tax fraud.

Therefore, the adoption of any consolidation, merger and spin-off transaction, as tax planning methods, by the taxpayer constitutes a perfectly reasonable option to reduce the tax burden deriving from the exercise of the its economic activity thereof, thereby permitting the taxpayer to evade the voracity for the collection of taxes by the Tax Authority.

Besides the tax matters, labor and social security aspects cannot be ignored on these corporate transactions, once their analysis is very important to the evaluation of the viability (or not) of the deal.

## 6. LABOR MATTERS AND ITS IMPACTS ON MERGER & ACQUISITION TRANSACTIONS

The analysis of the labor matters between the parties for any merger & acquisition transaction turns out to be an exceptionally critical issue, in particular for the successor company that will take over the commercial activities of the merged company.

This because, in the Labor Law, the so-called labor succession[9] is usually a consequence of corporate transactions of such nature.

The labor succession will take place whenever the purpose of the successor company is not changed, and the employees will be held in the same positions and the same services continue to be rendered or may continue to be rendered.[10]

Any merger & acquisition transaction will have impacts on: a) the employee; b) the merged company; c) the successor company.

The employee has full guarantee as both the doctrine and jurisprudence set forth that the employment agreement is entered into with the company in lieu of the individuals who ultimately manage the company[11]. That is, the employee has a contractual relationship with the company and not with theirs shareholders[12].

With respect to the merged company, in general, any such merged company shall not hold any liability, whether jointly or subsidiary, taking into account the undertaking, by the successor company, of the role of new employer[13].

With respect to the successor company, it shall be primarily affected by the labor succession, as such company shall be held liable not solely for the employment agreements in full force and effect but also for the employment agreements already terminated – before and after the succession, of which liability shall comprise any and all labor rights[14].

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[9] The Consolidated Labor Laws ("CLT"), in Articles 10 and 448, sets forth labor succession as:
**Art. 10.** Any change in the company's legal structure shall not affect the employees' vested rights.
**Art. 448.** The change in the company's ownership or legal structure shall not affect any employment agreements entered into the respective employees.

[10] GOMES, Orlando; GOTTSCHALK, Edson. *Curso de Direito do Trabalho.* 18ª Ed. Rio de Janeiro: Forense, 2007. p. 315.

[11] NASCIMENTO, Amauri Mascaro. *Curso de Direito do Trabalho.* São Paulo: Saraiva, 2001. p. 680.

[12] MARTINS, Sérgio Pinto. *Direito do Trabalho.* 16ª Ed. São Paulo: Atlas, 2006. p. 62.

[13] Jurisprudence exception: OJ Nº 225 (SDI 1, TST). CONCESSION AGREEMENT OF PUBLIC UTILITY SERVICES. LABOR LIABILITY. (new wording, DJ 04.20.2005). Execution of concession agreement of public utility services, whereby one company (concessionary company) grants to the other company (second concessionary company), wholly or partially, by means of leasing, or any other method set forth in the agreement, on temporary basis, assets owned by the first aforesaid company: I – in the event of termination of the employment agreement after the commencement of the validity period of the concession, the second concessionary company, in the capacity of successor company, shall be held liable for any rights deriving from the employment agreement, without prejudice to the subsidiary liability of the first concessionary company in connection with any labor obligations undertaken up to the concession date; II – with respect to the employment agreement terminated prior to the commencement of the validity period of the concession, the liability for the employees' rights shall be solely borne by the preceding company.

[14] JORGE NETO, Francisco Ferreira. *Sucessão Trabalhista.* Privatizações e Reestruturação do Mercado Financeiro. São Paulo: LTr, 2001. p. 121.

The discussion of the principle of liability raises doubts or questions in connection with the validity and efficacy of the clause that sets forth the liability as a guaranteed method agreed upon between the parties involved.

The labor doctrine is unanimous to assert that the contractual clauses that restrict the liability of the parties in connection with the undertaking of labor obligations are not taken into consideration in the Labor Law as, in view of the principles related to the piercing of the corporate veil of the employer and the maintenance of the employment relationship, in addition to the rules expressly set forth in the CLT, there are rules that should not be breached by virtue of the company's sale.

Outside the scope of the Labor Law, upon the sale of a company, the parties understood that, in principle, the liabilities were not included therein. In the event of sale of the company only, the debts were not transferred, except if otherwise agreed upon by the parties, upon consent of the creditor or in accordance with the legislation. Therefore, the inclusion of a clause in the agreement was necessary for purposes of establishment of the buyer's liability for the succession. Currently, pursuant to the Civil Code[15], the buyer of the company will be the seller's successor in connection with any obligations regularly accounted for.

Therefore, such liability restriction clauses may eventually be binding upon both the buyer and the seller, as such clauses arise from of a civil agreement. However, the validity thereof should be restricted to such subject matter and should not have, as stated, any impact on the labor matter as the succession represents a public policy matter.

The liability of the shareholders and former shareholders for labor and social security obligations is a delicate subject matter.

The piercing of the corporate veil of any company, in the opinion of the Brazilian labor courts, in order to have access to the assets of any shareholder and former shareholder is entirely feasible for purposes of guarantee of payment of the values due to the employees[16].
Therefore, in view of the foregoing, the analysis of, upon performance of a meticulous due diligence, the labor obligations of the company to be acquired is extremely important in any merger & acquisition transaction, under penalty of incurrence of significant losses by the buyer company.

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[15] Art. 1.146. The buyer of the company shall be held liable for any debts incurred prior to the transfer, provided that any such debts are regularly accounted for and the original debtor shall continue to be held jointly liable for a period of one year counted from, with respect to overdue credits, the disclosure and, with respect to any other credits, the maturity date.

[16] LIABILITY OF SHAREHOLDER AND FORMER SHAREHOLDER FOR LABOR AND SOCIAL SECURITY OBLIGATIONS – PURSUANT TO THE CIVIL CODE. Principle of piercing of the corporate veil. Maintenance of the foreclosure against the company's former shareholders. The labor legislation protects the employee's right to receive the values arising out of the employment agreement, by virtue of the imposition of the Principle of Piercing of the Corporate Veil. Accordingly, in the event the foreclosure brought against the company or its current shareholders is not successful, the maintenance of the claim brought against the former shareholders is valid. TRT 2nd Region. 2nd T. Proc.: 20080715448. Ac.: 20080969911. Reporter: ROSA MARIA ZUCCARO. DOESP: 11/11/2008.
LIABILITY OF SHAREHOLDER AND FORMER SHAREHOLDER FOR LABOR AND SOCIAL SECURITY OBLIGATIONS – PURSUANT TO THE CIVIL CODE *FORECLOSURE – LIABILITY OF FORMER SHAREHOLDERS. "The withdrawal, exclusion or death of any shareholder shall not hold any such shareholder, or the heirs thereof, harmless from and against the liability for any prior corporate obligations, up to a period of two years after the approval of the company's resolution; neither in the two first cases, for any subsequent obligations and for an equivalent period, so as long as the approval is not requested.* TRT 2nd Region. 3rd T. Proc. 20080451149. Ac.: 20080969024 . Reporter: ANA MARIA CONTRUCCI BRITO SILVA. DOESP:11/11/2008.

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## 7. SOCIAL SECURITY IMPACTS ON THE MERGER & ACQUISITION TRANSACTIONS

The social security matter, as expected, also affects the merger & acquisition transactions, and attracts the interest of, in this regard, the companies involved in any such types of corporate transactions.

Upon the Reform of the Social Security, carried out by virtue of the Constitutional Amendment nº 20/1998, many companies started to adopt the private pension plan as an incentive method for the employees. In the private pension plan, the employer and the employee work together on the social security matter with a view to create a private pension investment fund that will be used as supplementary retirement contribution to the employee.

The private pension plan is beneficial to the employer, as the value contributed to any such plan is not included in the salary and is considered as a type of strategic compensation. In turn, the benefit will represent a future source of income to the employee or, at minimum, a type of saving in the event of future dismissal, with or without cause.

Taking into consideration that the private pension plan, as a type of strategic compensation, started to be largely adopted by the companies, in the events of corporate transactions, the matter of the social security impacts became a significantly important item in the audit conducted prior to any such transactions, or due diligence, as any such audit is normally known.

The companies, either in the merger or the acquisition transaction, should be aware of and be deeply informed about the social security plans of each other, in particular the financial condition of the investment funds, as well as the responsibilities of definition of the obligations undertaken.

The plan's deficit may be allocated among all parties contributing to the plan. Thus, the company, in the capacity of sponsor, will also take part in the balance, which may occur by means of extraordinary contributions made in installments during the relationship period, or in one single installment.

The identification of the imbalance is dynamic, primarily because the actuarial assumptions that support the private pension plan are changed on disorganized manner. This requires the auditors to have knowledge on the general rules of the private pension plan, in particular the financial and actuarial assumptions adopted in the preparation thereof.

This is one of the reasons based on which, the companies, in any audit process, should try to be familiar with the details of the benefit and funding plans and understand the possibilities to change and mitigate the deficit thereof.

It should also be pointed out that many plans are impracticable, mainly due to the original structure. The modification of the rules is an extremely complex task, to the extent that such modification involves inalienable rights of the participants. This is one factor that, by itself, demands a precise analysis by the buyer, as the buyer will have to bear the risk arising out of a poorly defined private pension plan with costs to be levied on the payroll.
Therefore, the buyer should be cautious and analyze the private pension plan obligations of the acquired or merged company before the acquisition or merger of any such company, in a manner to prevent any such future buyer to be confronted with future and concealed liabilities.

A merger & acquisition transaction is considered as successful when the legal advisory is able to foresee eventual contingencies which, if previously known, would prejudice the transaction. In this sense, the use of the right contractual strategies can avoid future surprises, usually against the clients' interests.

## 8. CONTRACTUAL STRATEGIES IN MERGER & ACQUISITION TRANSACTIONS

Any merger & acquisition transaction encompasses two primary steps, namely: the legal actions that comprise the acquisition of ownership interest and those aimed to guarantee the protection of the assets of the parties involved in any such corporate transactions.

The first step includes, for example, the purchase and sale of shares; the subscription of shares; the definition of common clauses in agreements of any such nature, such as price, collaterals, confidentiality, non-competition, indemnification, resolution of disputes; representations of warranties; among others.

In the second step, the Shareholders' Agreement is the primary instrument used to govern the relationship among the shareholders during the exercise of the corporate rights thereof.

The purchase and sale of shares is the easiest method used in connection with the direct acquisition of the control of any company. Based upon such method, the buyer pays a given price for each share issued by the target company, which is generally calculated based on the equity value increased by goodwill. This method refers therefore to the acquisition of ownership interest by means of the purchase of outstanding shares held by the current shareholders of the target company.

On the other hand, the subscription of shares is an acquisition method, whereby the buyer subscribes the capital increase in the target company, by means of the issuance of new shares, at the agreed percentage rate, either for the acquisition of the shareholding control or not. Therefore, the subscription of shares corresponds to the acquisition of ownership interest upon the subscription and payment of recently issued shares.

Among the aforesaid common clauses, one that is worth mentioning is the non-competition clause, whereby the sellers, upon the sale of total shares, agree not to compete with the buyers in the target company's market for a defined period and in a defined territory. Another clause that should be pointed out is the clause that sets forth the method based on which the disputes potentially verified after the conclusion of the transaction should be resolved. The arbitration process is, in general, the most commonly adopted method, once it provides celerity for the resolution of disputes.

The representations and warranties (Representations and Warranties) are also a key subject matter verified in the first steps. Such representations and warranties are statements included in the share purchase and sale or subscription agreements, provided by the parties and relating to past and present facts and/or matters concerning the subject matter of the agreement, in order to establish important aspects arising therefrom, such as the price and obligations of the parties.
The purpose of the Reps and Warranties, as the representations and warranties are known, is to allow the involved parties to analyze the terms and conditions of the transaction and oblige the other party to satisfy any such terms and conditions, under penalty of being held liable for, in general by means of the payment of indemnification, any breach thereof and/or

misleading representation and warranty. Such terms and conditions include, for example, those that provide for the capitalization, litigation, assets, environmental matters, among any other potential liabilities verified.

The second step of any merger & acquisition transaction focus on the preparation of instruments which purpose is to guarantee the protection of the assets of the parties. The shareholders' agreement is the main instrument in the second step and is expressly set forth in the Brazilian Corporate Law[17].

The holders of majority or minority ownership interests in companies adopt the shareholders' agreement to govern the relationship among any such holders in connection with the exercise of their respective rights. In general, the shareholders' agreement provides for both matters of political nature, such as voting rights, and matters of equity nature, such as share sale commitments.

Such instrument is also used when a joint venture it the result of any corporate transaction, as well as in the events in which the majority and minority shareholders are not included in the same economic group.

For example, any matters of political nature govern: the method based on which the target company's business will be managed, upon definition of the officers' and directors' powers and restrictions in connection with the performance of specific actions, such as, for example, the performance of actions not related to the corporate purpose, such as the granting of guarantees, pledges, among others.

The shareholders' agreement may also establish the criteria to be adopted in connection with the selection and election of the company's management for purposes of definition of their respective duties; and, also provides for the voting rights of the shareholders in the target company in connection with matters involving the definition of goals and business and/or the approval of any matters relating to the target company.

The clauses of equity nature, in turn, will define the criteria for the trading or disposal of the shares issued by the target company, both to any of its shareholders or to any third parties. Such clauses provide for: a) the Preemptive Right in connection with the acquisition of the shares issued by the target company; b) the Tag-Along[18]; c) the Drag-Along[19]; d) the Put and/or call options[20].

In view of the foregoing, it is possible to conclude that, as important as the decision to perform any merger & acquisition transaction with any and all impacts arising from the acquisition of ownership interest, are also the legal actions which purpose is to guarantee or protect the assets of the involved parties are also significantly important.

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[17] Art. 118 *et. seq*. of Law 6.404/76 (*caput* with wording defined by Law 10.303/01).

[18] Means the right of joint sale, by any given shareholder(s), of the ownership interest(s) thereof in the share capital of the target company, in the event any other given shareholder(s) decide(s) to sell the ownership interest(s) thereof to any interested third parties.

[19] Means the right of any given shareholder(s) to impose the sale of shares of the share capital of the target company held by other shareholders to a third party or group of buyer third parties, which sale will be carried out together with the sale of the shares held by the shareholder(s) that exercised any such right.

[20] Means the right to purchase or sell a volume of any given asset based on a previously established price within any given period of time. The options constitute methods to control the ownership interest and permit the shareholder to drastically increase and/or decrease the ownership interest thereof in the target company.

The success of any merger & acquisition transaction is directly related to the excellence of the legal advisory services rendered, which entails the work of creative professionals with extensive legal expertise, capable of fulfilling the needs of the involved parties.

Given that many merger & acquisition transactions are international deals, it is necessary to point out some aspects regarding the investments' flow and its registration with the Central Bank of Brazil.

## 9. INVESTMENTS' FLOW AND REGISTRATIONS OF FOREING CAPITAL

Law nº 4131/62 ("Foreign Capital Law") established the Superintendence of Money and Credit ("SUMOC"), which, together with Banco do Brasil and the National Treasury, such agency had at time, authority to carry out the registration of the inflow of foreign capital in Brazil.

The aforesaid Law remained effective until the enactment of Law nº 4595/64, which provided for the creation of the Central Bank of Brazil, a federal governmental agency part of the National Financial System, that resulted in the extinction of SUMOC, and also the transfer of SUMOC's authority to BACEN.

Pursuant to Circular Letter n.º 2997/00, the equity interests hold in the capital of companies located in Brazil, owned by individuals or legal entities resident, domiciled or with head office abroad, whether fully paid up or acquired, as well as the allocated capital of foreign companies authorized to conduct activities in Brazil, are subject to registration with the BACEN.

The equity interests hold by non-resident investors acquired in the financial and capital markets, as well as the earnings deriving there from, shall not be subject to registration, under this type of registration.

Any and all subscription and payment, swap, transfer of ownership of shares/quotas, as well as any mergers, spin-offs and consolidations, provided that, by virtue of any such transactions, there is inflow or outflow of foreign capital to/from Brazil (change of ownership interest of foreign investor) shall be subject to such registration.

The performance of the registration relies upon a routine consisting of the following steps: a) registration of the user with the Central Bank System ("SISBACEN"); b) registration with CADEMP; c) registration with RDE; and, d) registration of Transactions, which encompasses the supply of financial information, the registration of events and, finally, the submission of annual information.

The user, in order to be granted access to the SISBACEN, shall send the following documentation to BACEN's IT department: 1) form of application of registration; 2) documents that confirm the authority of the signatories to the registration application. This registration step will be concluded upon the delivery of the aforesaid system access code and password.

For purposes of registration of foreign capitals in the RDE sub-systems (Direct Foreign Investment, Registration of Financial Transactions and Foreign Investment in Portfolio) the

involved parties, whether individuals or legal entities, Brazilian or foreign, are required to obtain the registration with the Registry of Companies in the DECEC Area ("CADEMP").

In the event of direct foreign investment, for example, the foreign investor, whether individual or legal entity, upon registration in the RDE-IED sub-system, will receive a number corresponding to the respective relation between Brazilian recipient / foreign non-resident, in which any and all information concerning the participation of the foreign shareholder, the inflow of funds as direct foreign investment and the remittances of profits and dividends to the foreign shareholder shall be registered.

The process shall be concluded by means of the registration of transactions, in which the recipient's financial economic information that should contain the balance sheet/trial balance sheet prepared within up to 30 (thirty) days counted from the event date, the information on any accrued earnings and accumulated losses, reserves, shares held in treasury, and any and all accounts of the equity, in addition to the information on any and all assets and liabilities accounts, shall be informed.

The registration of the event shall be required upon the verification of the occurrence of new investments, transfer of ownership of assets in Brazil, sale of shares or corporate reorganization, among other events established by BACEN.

At last, up to the 30$^{th}$ (thirtieth) day of April of each year, the Brazilian companies that have foreign capital shall provide updated financial and economic information to BACEN, under penalty of prohibition to carry out any subsequent registrations.

BACEN also provides for administrative penalties in the events of: submission of inaccurate or incomplete information within the regulatory period, submission of information after the regulatory period, failure to submit any information, as well as submission of any false information. The value of the fines may vary from R$ 25,000.00 (twenty five thousand Brazilian reais) to R$ 250,000.00 (two hundred and fifty thousand Brazilian reais).

It should be pointed out that other penalties may also be imposed, such as the potential suspension or cancellation of the registration, criminal charges against the accuracy of the information provided, and also, the prohibition to remit profits, dividends, interest attributed to equity and repatriate investments, in the event of mismatch between any such profits and remittances and the information registered in connection with the foreign investment.

Some merger & acquisition transactions may direct impact the competition, in view of the possibility of market control. In these cases, such transactions may only occur after their approval by the Brazilian competition defense system.

## 10. THE ROLE OF CADE N THE DEFENSE OF COMPETITION

The Administrative Council of Economic Defense ("CADE"), as the governmental agency in charge of the defense of competition, adopts internal regulation and rules for the analysis of any merger & acquisition transactions, whenever any such transactions result in significant market share concentration or any potential restriction to free competition.

The control of the market by itself is not prohibited by the Brazilian legislation, which in fact, regulates the market domain that results in any potential prejudice to the free trade and competition.

Pursuant to Law nº 8.884/94[21], the companies participating in any merger & acquisition transactions shall notify the Brazilian competition defense system, which consists in the Economic Law Department of the Ministry of Justice (SDE), the Economic Monitoring Department of the Ministry of Finance (SEAE) and CADE, in connection with any and all transactions performed or to be performed in the Brazilian territory, whether by means of consolidation or merger of companies, incorporation of any company to exercise the control of companies or any other type of corporate organization that:

*i)* implies in the participation of any company or group of companies in any key market resulting in a market share at the percentage rate of 20%; or *ii)* in which any of the participants has recorded annual gross revenues, in the most recent balance sheet, equivalent to R$ 400,000,000.00 (four hundred million Brazilian reais).

For a better definition or explanation of the aforesaid economic criterion, CADE issued the Precedent nº 1 in 2005: "Upon the application of the criterion set forth in Article 54, § 3, of Law nº 8.884/94, the annual gross revenues solely recorded in the Brazilian territory by the companies or group of companies participating in the concentration action shall be critical[22]".

CADE, in addition to the economic criterion, also establishes a market criterion in what concerns regulation.

Such market criterion consists of the "obtaining of economic benefits" by means of the "control of the market in which the company participates", whether as compared to the competitors or the consumers of products or services.

According to the definition of key market set forth in the Merger Guidelines of the U.S. Department of Justice, a milestone in the Brazilian legislation and jurisprudence, the market advantage results in the holding of such power on "economically important markets – that is, markets that could be subject to the exercise of the market power", in particular the power to control the definition of its prices.

In a recent decision, CADE established that any transactions where the billing criterion is not attained, as well as any transactions involving an economic agent which, prior to the conduction of the transaction, already held a market share equivalent to or greater than a percentage rate of 20% in any given key market, but in which key market the another party has not conducted any activities, should not require the analysis of CADE and any other agencies comprising the Brazilian System of Competition Defense.

Therefore, the transactions exceeding the limits set forth in Law 8.884/94, which are not informed or which, even though informed, delivery of notice is carried out after the term set forth in the aforesaid law, will subject the parties involved in the concentration act to the imposition of a monetary fine that may vary from 60,000 (sixty thousand) to 6,000,000 (six million) UFIRs, to be applied by CADE, without prejudice to the initial of an administrative proceeding.

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[21] Art. 54, § 3.
[22] Published in the Federal Official Gazette on 10.18.2005, nº 200, Section 1, page 49.

Despite of the severity of Law 8.884/94, there are no doubts that the defense of competition in Brazil was encouraged by the enactment of the aforesaid law, once that the Defense of Competition, prior to its change into a governmental authority, was a mere supporting role in the Brazilian economic environment. Currently, in view of the seriousness by means of which the competition matters are handled, Brazil plays an important role in the international economic environment, in particular if compared to the majority of the other Latin American countries.

After the discussion of all of its steps, after the conclusion of a merger & acquisition, the post-closing actions are very important.

## 11. THE IMPORTANCE OF THE POST-CLOSING ACTIONS

Any corporate transaction will solely be considered as concluded between the parties after the execution of the applicable contractual instruments.

It is important to point out though that the agreements entered into between the parties should not be subject to registration, other than in events in which the approval of CADE (Administrative Council of Economic Defense) is required.

Nonetheless, the terms and conditions set forth in any such instruments will affect the corporate documents as a result of the transaction performed and, such corporate documents should be the ones actually subject to registration with the Trade Board of the State wherein the involved company's or companies' head office is located.

In what concerns the corporate transactions arising out in connection with publicly-held companies, it should be explained that any such corporate transactions should also be registered in their respective corporate books, such as, for example, the Book of Registration of Minutes of the Annual Shareholders' Meeting; the Book of Registration of Shares, the Book of Registration of Transfer of Shares, the Book of Registration of Minutes of the Meetings of the Board of Executive Officers and the Book of Registration of Shareholders' Attendance, among others.

With respect to the obligation to register, the Brazilian Corporations Law provides for the disclosure of various corporate actions, in particular those affecting third parties, in the Official Gazette of the State wherein the company's head office is located, as well as in any regional widely-circulated newspaper. On the other hand, the limited liability companies are not subject to any similar legal obligation and are solely required to carry out the registration with the applicable Trade Board.

In the event the transaction involves foreign companies investing in a Brazilian company, the registration of the investment transaction with the Central Bank of Brazil, in the RDE-IED system (Electronic Declaratory Registration – Direct Foreign Investment) will also be required.

Such measure should be adopted within a period of up to 30 (thirty) days counted from the registration of the transaction documentation with the Trade Board of the State wherein the company's head office is located and, upon the application, it must be submitted, the certificate issued by aforesaid entity, together with the articles of incorporation and powers of

attorney of the foreign company, all duly certified, legalized, translated and registered with the registry office in Brazil.
In addition to the aforesaid governmental agencies, the corporate documents relating to M&A transactions should also be registered with any and all agencies with which the involved companies are also registered, for purposes of disclosure of any and all results arising there from that may affect not solely any third parties but also the Public Authorities.

Such registrations should be carried out after the registration of the actions to be performed with the Trade Board, it being understood that the registration with the Federal Revenue Office should be necessarily carried out prior to the registration with the Central Bank of Brazil.

Among the public authorities that should necessarily be informed are: the Federal Revenue Office, the Social Security System Institute (INSS) and the Severance Pay Fund (FGTS), in addition to the governments of the City and the State where the head office is located, the Real Estate Registry Office, in some circumstances, and any other agencies, however the case may be.

The matter relating to the press release is a delicate subject matter and should be conducted by both parties, upon the previous approval of the draft of the press release. The content of the press release is discrete in most of the times and does not contain the values involved in the commercial transaction.

It should be pointed out though that there will be no need of previous notices in connection with an ordinary quota or share purchase and sale transaction. The corporate actions to be adopted are simpler and solely require an amendment to the articles of incorporation (in the event of limited liability companies) or the modification to the corporate books containing the new ownership of the shares (in the event of publicly-held companies).

Finally, it is opportune to remind that the parties are not hold harmless from and against the performance of any obligations upon the execution of the documents. In this regard, a number of other obligations, deemed as supplementary, will also demand the efforts of the involved parties for a sizeable period of time (many of them for a period of 5 years), for which reason the selection of an appropriate legal advisor constitutes a factor of critical significance for the success of transactions of any such nature.

Despite of the fact that, usually, the merger & acquisition transactions are very time expensive and demands high investments of the involved parties for their conclusion, usually, the company that arises from this long process becomes a target for acquisition proposals, which sometimes are not desired by the parties. This scenario required the creation of control methods, in order to avoid the so called hostile takeover bids.

## 12. THE POISON PILLS AS CONTROL METHODS AGAINST HOSTILE TAKEOVER BIDS

The translation of certain terms, such as poison pills, are always not accurate and, in many circumstances, the term should be kept in its original language.

However, for purposes of better understanding of this press release, we adopted the term "*pílulas envenenadas*" to translate the English term (poison pills), which is largely acknowledged.

Within the scope of the Brazilian Corporate Law, *"pílulas envenenadas*", or poison pills, correspond to clauses included in the bylaws of publicly-held companies, which purpose is to reduce, restrict or prevent the hostile acquisition of the shares issued by such companies in order to preserve the company's original purposes and to protect the goals of its founding shareholders.

A hostile takeover bid or its attempt is verified whenever any party interested to acquire the target company submits a tender offer for purposes of acquisition thereof, regardless of the interest of the target company's management to either sell the company or not.

The possibility to acquire the controlling power is often verified in companies with widespread corporate capital. In such events, an alternative adopted by the founding shareholders or shareholders in the bylaws are precisely the control methods by means of clauses that prevent the concentration of powers on the hands of one single controlling shareholder, in order to preserve the decentralization of powers and guarantee the preservation of or compliance with the company's original purposes.

In Brazil, the poison pills became popular as of 2005, when various companies with listed shares on the stock exchange, by means of Initial Public Offerings, or IPOs, as such offerings are normally called. Clauses adopted to protect against widespread shareholding were included in the bylaws of some of the new companies with shares listed on the stock exchange, even in the cases of companies that elected to keep the position of a controlling shareholder.

Such clauses provide for the conduction of a public offer of shares (OPA) by shareholders that intend to exceed any given percentage rate of ownership interest in the share capital.

Despite of the increasing adoption of the poison pills in Brazil, many experts consider that the development of the poison pills is still in the early stages in Brazil, as Brazil does not have a capital market as developed as the foreign capital markets. The policy adopted in Brazil is the concentration of shares, whether in one single shareholder or in a group of shareholders.

If, on one side, the poison pills are viewed under a positive perspective, some opponents understand that its adoption may result in the inadequacy of the companies' pricing process and could penalize those with any intention to invest in the company.

One of the reasons used to try to explain the steady reduction of the adoption of the poison pills in the United States and Europe is that the most excellent defense against any hostile takeover bid is to give the management the opportunity to conduct a bidding process in an attempt to receive proposals that guarantee the shareholder the best price for the shares thereof or the assurance that the current management team is capable to generate more value than any potential buyer[23].

[23] HESSEL, Camila Guimarães. Sophisticated, *poison pills win over each time more powers to prevent takers of control.* Revista Capital Aberto, year 4, nº 47, July 2007, p. 26

Likewise in Europe and in the United States, among the methods adopted to mitigate the results of the poison pills, Brazil has adopted a method which establishes that the adoption of the poison pills should be subject to the approval of the annual shareholders' meeting.

Another example consists of the elimination of the goodwill levied on the price established in connection with the conduction of the OPA. This is exactly what happened with, for example, Positivo Informática which established the limit for the conduction of the OPA at the percentage rate of 10% OPA, thereby determining that the value of the offer should correspond to the greater unit price of the share in the two preceding years.

Contrary to anything stated herein, there are examples of companies that, in addition to establishing low percentage rates in connection with the limits of the poison pills and goodwill at the percentage rates between 20% and 50%, still try to protect any amendments to any such clauses upon the adoption of provisions that, for example, impose the joint obligation to conduct the OPA[24] on the shareholders that approve any amendments thereto.

Finally, there are also companies that establish methods prior to the adoption of the poison pills in an attempt to prevent the increase of the ownership interest of the interested parties. In this regard, before reaching the percentage rate necessary for the conduction of the OPA, some given companies sets forth, in the bylaws, that the holder of shares at any given percentage rate that wishes to acquire new shares should solely carry out any such acquisition by means of auction on the stock exchange[25].

A large portion of the law's operators defends that the adoption of the poison pills arises from the legislation's gap in connection with certain subject matters, in the case under discussion, in what concerns the protection against the widespread shareholding. However, and notwithstanding the reasons that give rise to the adoption of the poison pills, it is irrefutable that the poison pills continue to constitute an example of a medicine extremely effective against hostile takeover bids for the preservation of the original purposes of any company.

[24] ibidem, p. 24.
[25] ibidem. p. 26.

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## 13. CONCLUSION

The above studies aimed at discussing the main subjects related to Mergers & Acquisitions, such as: its preliminary documents; due diligence and environmental due diligence; the tax, labor and social security impacts of such transactions; investments' flow and the registration of foreign capital; the role of CADE on the defense of competition that arise from such deals; the importance of the post-closing actions and, finally, an analysis of the control methods against hostile takeover bids.

Almeida Advogados is a law firm focused on corporate environment, whose main premise is to understand the businesses of each of its clients, the nuances of each market, the corporate culture and the purposes of each company. From the legal point of view, such focus allows us to structure and materialize our clients' projects in a safe and economical way.

Born from the union of competent professionals, committed with the legal practice, whose activities are focused on the rendering of legal services in the areas of corporate legal consultancy, risks' management and general litigation consultancy, to Brazilian and foreign companies, Almeida Advogados has an important role in several merger & acquisitions transactions, by providing full legal advisory to buyers and sellers, advising or managing Due Diligences, risks' analysis, draft and negotiation of agreements, corporate restructurings, draft of shareholders' agreements, and any other measures required on this kind of deal.

Aiming to participate and assist the implementation of new businesses, reducing the related risks, Almeida Advogados has conducted several investments' projects in Brazilian Information Technology companies, especially to North-American and South-American investors, as well as many acquisitions involving the agricultural industry, investing on Brazilian companies, and also Brazilian companies investing on foreign companies.

Almeida Advogados remains at your entire disposal for any clarifications regarding the mergers & acquisitions.

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