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Private Equity

Brazil: Law & Practice

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Law and Practice

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1. Trends

1.1 M&A Transactions and Deals

The Brazilian private equity market started strong in the first quarter of 2020, with Brazilian private equity firms aiming at taking advantage of the capital markets boom at the time. However, due to the COVID-19 pandemic, private equity firms were forced to slow down both investments and divestitures during the second quarter in order to assess the impacts of the pandemic and provide full technical and financial support to their portfolio companies.

After the initial paralysis resulting from the pandemic, the private equity firms are now actively looking for investment opportunities and for divestitures.

In case of divestitures, due to the strong rebound of the global and Brazilian capital markets, they still tend to be made via initial public offerings or follow-on offerings.

From the investment side, Brazilian private equity funds have been focusing on investments in more resilient industries, such as tech and healthcare, which will continue to have attractive investment opportunities.

Other possible outcomes for 2020 are:

- acquisition of the Brazilian business units of multinationals that are seeking to divest their subsidiaries to strengthen the financial health of their headquarters; and
- investments in public companies with proven business models that need capitalisation (Private Investment in Public Equity – PIPE), considering the devaluation of many stocks.

1.2 Market Activity

In 2020 Brazilian private equity deals are spread across different sectors, with deals most concentrated in the tech, healthcare and financial industries. Investments in certain sectors that have stood out during the COVID-19 pandemic, such as remote healthcare, home entertainment and multi-channel retail, are also expected to excel in 2020.

2. Legal Developments

2.1 Impact on Private Equity

A few legal developments have impacted the Brazilian private equity industry in the past three years, and more are expected to be approved in the second semester of 2020.

Economic Freedom Law

The Economic Freedom Law (Law No 13,874/2019), which was enacted in September 2019, has the purpose of promoting economic activity by reducing bureaucracy related to doing business in Brazil and increasing freedom within private relations and, thus, diminishing government intervention in private activity. This Economic Freedom Law also provides, among other matters:

- the possibility of Brazilian limited liability companies having a single quotaholder;
- a new chapter of the Brazilian Civil Code on investment funds, providing for the possibility of limiting the liability of investment fund shareholders and facilitating the incorporation of investment funds; and
- simplification of the procedures for the obtaining of licences and permits.

Social Security Reform

The Social Security Reform, which was approved in October 2019, was considered by many people the first step to organise the Brazilian government accounts. Such reform, together with a major reduction of Brazilian interest rates, made traditional investment options based on fixed income less attractive to local investors, who took a bigger role on recent IPOs and follow-ons.

The Normative Rule No 606 of the Brazilian Securities and Exchange Commission (CVM), issued in March 2019, regulates incentive funds for investment in infrastructure, which grant to its shareholders a more favourable tax regime, provided certain requirements are met.

Labour Reform

The Labour Reform came into force in November 2017 and, since then, it has succeeded in significantly reducing labour disputes before courts. Great part of such reduction is due to the inclusion of a new article to the Brazilian Consolidation of Labour Laws, which states that the defeated party in a lawsuit must pay the prevailing party's legal fees. As such, dismissed employees are now less impulsive in filing labour claims, which represents a reduction in labour litigation of Brazilian companies.

In addition to the above-mentioned legal developments, another future structural reform to monitor in 2020 is the Tax Reform. Aiming at simplifying and debureaucratising of the overly complex and burdensome Brazilian tax legislation, the Tax Reform will benefit both foreign and local investors.

3. Regulatory Framework

3.1 Primary Regulators and Regulatory Issues

The primary regulatory bodies for private equity funds and private equity transactions are as follows.

The Brazilian Securities and Exchange Commission (CVM)
The CVM regulates not only investment funds but also their administrators and portfolio managers, which must meet certain requirements in order to provide such services. CVM regulation must also be observed whenever the transaction involves public companies and/or offerings.

The Brazilian Antitrust Agency (CADE)
CADE approval is a condition precedent for the closing of transactions in which one economic group involved in the transaction had an annual gross turnover above BRL750 million in Brazil in the preceding fiscal year, and at least one other economic group involved in the transaction had an annual gross turnover above BRL75 million in Brazil in the preceding fiscal year.

Regulatory Agencies
Regulatory agencies are utilised whenever the target company develops activities in a regulated sector (eg, insurance, pharmaceuticals, energy, telecom, oil and gas, etc) and/or the transaction is likely to require the approval or notification of the transaction to the regulatory agency.

The Brazilian Central Bank
The Brazilian Central Bank is involved whenever the transaction involves direct foreign investments and/or local financial institutions.

4. Due Diligence

4.1 General Information

Private equity investors usually carry out a thorough due diligence, engaging local legal counsel and auditors (depending on the activities developed by the target company, a technical due diligence may also be carried out – eg, environmental, real estate, operational or IT). In general, this process involves the review of the documentation and information made available directly by the target company or by the financial advisors, who got the mandate of the project. Upon request, advisors may also carry out independent search about the target company on public records.

Even though the scope depends on the nature and industry of the target company, a legal due diligence typically involves the analysis of the target company's:

- corporate aspects;
- civil, tax and labour materialised contingencies (please note that analyses of non-materialised contingencies are usually carried out by the auditors engaged by buyer);
- commercial and financial contracts;
- intellectual property;
- real estate;
- insurance;
- regulatory aspects;
- environmental aspects;
- compliance; and
- data protection.

Since the enactment of the Brazilian Anti-Corruption Law (Law No 12,846/2014) and of the Brazilian General Data Protection Law (Law No 13,709/2018), compliance and data protection have become focus areas in legal due diligences, specially to those involving target companies that hold close interactions with public authorities and store, transfer, process or otherwise have access to personal data.

Once the legal due diligence is finalised, a legal due diligence report is prepared (often in a "red-flag" format), summarising legal counsel's main findings – notably any hurdles to the closing of the transaction (eg, third party and government notices and consents), relevant materialised contingencies that could lead to a price adjustment or indemnification, and other restrictions that could impact the valuation of the target (exclusivity, non-compete and early termination provisions, among others).

4.2 Vendor Due Diligence

Although not a rule, there is a relevant number of transactions in which a vendor due diligence is prepared. When a private equity fund conducts a vendor due diligence, it normally focuses on selected matters, over whose narrative it desires to have a better control. Vendor due diligence reports are usually provided to potential buyers on a non-reliance basis. As for buy-side due diligence reports, they usually contain provisions stating that they may only be disclosed to third parties upon authorisation of legal counsel, who normally only provides reliance to its client.

5. Structure of Transactions

5.1 Structure of the Acquisition

Most Brazilian private equity transactions are carried by private sale and purchase agreements, involving either the acquisition of assets or of equity.

Even though most of the transactions do not involve a competitive process, auction sales are becoming increasingly common, as they, despite being more time consuming, tend to result in seller friendlier outcomes.

Courts do not usually participate in acquisition transactions, unless it involves:

- the acquisition of equity/assets owned by minors or that comprise an instate estate;
- parties that are under judicial reorganisation; or
- the acquisition of assets of the bankrupt estate.

In the second and third cases, the acquisition must follow the specific procedures set forth in the Brazilian Bankruptcy Law (Law No 11,101/2005).

Finally, whenever the target company is a public company, the acquisition may be carried either by means of a privately negotiated agreement negotiated with controlling shareholders or a public tender offer (see **7.1 Public-to-Privates**).

5.2 Structure of the Buyer

Private equity buyers are typically structured as *Fundos de Investimento em Participações* – FIPs, which are local funds regulated by the Brazilian Securities and Exchange Commission (CVM). FIPs are pools of assets, organised as non-personified condominiums.

The choice for the FIP structure is mostly based on its friendly tax regime (eg, FIPs are exempt from taxation over the gains and income from its portfolio, as a rule, such taxation is deferred to the time that the resources are distributed to the FIP quotaholders).

FIPs either invest in target companies directly or through a holding company. Note, however, that leveraged buyouts are usually carried out through holding companies, as FIPs have restrictions to debt financing.

5.3 Funding Structure of Private Equity Transactions

Most of the Brazilian private equity transactions are equity financed. However, due to the recent lower interest rates trend in Brazil, it is likely that leveraged buyout transactions become more common (in most of these cases, the acquisition will be expected to be carried out through a holding company, as Brazilian private equity funds' debt financing is limited to 30% of its assets). It is also not unusual for private equity buyers, in a mixed debt/equity financing structure, to raise debt overseas, and remit funds down to Brazil as capital for funding the acquisition.

Private equity buyers are usually reluctant to offer equity commitment letters or other types of comfort to sellers. Nevertheless, whenever such letters are offered, the shareholders of the private equity acquisition vehicle commit to fund the vehicle through equity subscription or loans.

Lastly, it is common for private equity funds to hold either controlling or minority stakes in their portfolio companies. Regardless of the structure, private equity funds usually negotiate strong shareholders' agreements, as FIPs in general must effectively participate in the management and the decision-making process of their portfolio companies.

5.4 Multiple Investors

Deals involving a consortium of private equity sponsors are still rare in Brazil, since private equity sponsors, when investing in Brazil, are usually well capitalised and reluctant to reduce their equity ticket. Nevertheless, they are becoming more frequent in growth equity investments (ie, investments to back growing companies with proven business models) in the tech industry, which are usually led by foreign private equity investors.

Co-investments are also not so usual in Brazilian private equity transactions. However, whenever they occur, such co-investors may be either legal entities in the up streamline of the private equity sponsor or external co-investors. Whether such co-investor holds a passive or a more active stake in the invested company, depends on the terms and conditions agreed between the parties.

6. Terms of Acquisition Documentation

6.1 Types of Consideration Mechanisms

Frequently Used Transactions

The purchase price mechanism in most private equity transactions involves the parties agreeing to a base purchase price, jointly with a post-closing adjustment, considering the variation between the target company's estimated closing accounts (eg, working capital, cash, indebtedness), and the actual closing accounts.

Locked box consideration mechanisms are also frequently used, especially in acquisitions involving companies whose accounts suffer great variations thorough the year. In most of the cases where parties opt for locked box mechanisms, leakages to sellers and their related parties (except for permitted leakage) will be considered as purchase price reductions, and contributions by sellers and related parties (except if in the ordinary course of business) will be considered as purchase price increases.

Other Transactions

Private equity transactions with fixed price mechanisms are rare. However, when used, it usually is in transactions with simultaneous signing and closing.

Deferred purchase price payments upon the achievement of heavily negotiated milestones (ie, earn-out structures) are most common in transactions with private equity buyers where sellers remain in the invested company as part of its management team (usually in a C-level position) and, thus, are responsible for the achievement of such milestones.

It is usual for private equity buyers to holdback or hold in escrow part of the purchase price, in order to secure sellers' payment obligations related not only to purchase price adjustments (either closing accounts adjustments or leakage adjustments) but also to indemnities. As for private equity sellers, they typically accept an escrow account structure, which provides for cleaner investment exists, since sellers are less likely to accept payment obligations that could delay the liquidation of the private equity investment vehicle.

6.2 Locked-Box Consideration Structures

Locked box structures are common in Brazilian private equity transactions, seconded to more usual closing accounts mechanism. Usually, interest is charged on the purchase price as from the date of the locked box accounts until the actual payment of the purchase price, but no interest is charged on leakage.

6.3 Dispute Resolution for Consideration Structures

Upon the parties' failure to amicably resolve any disputes regarding the closing accounts or leakage/contribution amounts within the timeframe set forth in the agreement, such disputes are usually submitted to an independent third-party, usually an audit firm, whose decision is binding on the parties.

6.4 Conditionality in Acquisition Documentation

Conditions precedent to the closing of private equity transactions vary according to the specific characteristics of the target company and the transaction itself. Nevertheless, common conditions precedent are the following:

- approval of the transaction by the Brazilian Antitrust Agency (CADE), where applicable;
- approval of the transaction or notice in this regard to regulatory agencies, where applicable;
- absence of law or governmental order that prohibits, makes illegal or otherwise restricts the closing of the transaction;
- representations and warranties of the target company, seller and buyer are true and correct at closing;
- pre-closing covenants and obligations have been complied with;
- specific third-party consents and/or waivers and/or delivery of specific third-party notices; and
- absence of outstanding material adverse changes (whose definition is usually heavily negotiated).

6.5 "Hell or High Water" Undertakings

Private equity-backed buyers are reluctant to accept "hell or high water" undertakings regarding the obtainment of regulatory approvals or of the Brazilian Antitrust Agency's clearance. Whenever such undertakings are accepted, private equity buyers usually succeed in negotiating limits to the effects thereof (eg, restricting divestment obligations to a certain threshold).

6.6 Break Fees

Break-up fees may be negotiated in specific scenarios, but they are not common market practice.

6.7 Termination Rights in Acquisition Documentation

In addition to the possibility of terminating the purchase agreement upon the parties' mutual agreement, private equity sellers and buyers also have termination rights in the event:

- closing has not occurred by the long-stop date (provided closing has not occurred due to the terminating party's fault or because the terminating party has failed to fulfil the precedent conditions under its responsibility); or
- the other party has materially breached its obligations under the purchase agreement.

It is also common for purchase agreements to provide for termination rights, prior to the long-stop date, whenever it is clear that conditions precedent, which cannot be waived, will not be fulfilled by the longstop date (eg, occurrence of an irreversible material adverse change).

6.8 Allocation of Risk

Brazilian M&As, including those involving private equity investors, normally follow the "your watch/our watch" principle. Therefore, seller is often responsible for liabilities arising in connection with pre-closing triggering events, whereas buyer is responsible for liabilities arising in connection with post-closing triggering events. On the same note, and differently from many other jurisdictions, anti-sandbagging provisions are not market in Brazilian transactions and, thus, seller is usually responsible for indemnifying pre-closing liabilities, whether they are or not within buyer's knowledge.

In view of the above, parties typically allocate risk by means of seller's indemnity obligations. Private equity buyers will usually seek maximum legal protection, pushing for uncapped indemnification obligations and a broad definition of indemnifiable losses; whereas private equity sellers will seek to limit their indemnification obligations, pushing for caps, some of the main limitation on seller's indemnification are the following:

- time limitation for bringing claims;
- financial limitations, such as caps, deductible or tipping baskets and de minimis;
- narrow definitions of loss, excluding lost profits, indirect, incidental and consequential damages, moral damages, among others; and
- restricting seller's indemnification events (eg, seller will be responsible for indemnifying for losses arising in connection with pre-closing triggering events, provided such triggering events relate to breach of agreements or violation of applicable laws).

6.9 Warranty Protection

The scope and extent of the representations and warranties to be provided by private equity sellers depend on the private equity sellers' involvement in the management of the target and the size of its equity stake. If the private equity seller is a passive minority shareholder, it will seek to limit its representations and warranties to basic representations and warranties. However, if seller is a controlling shareholder or otherwise have a significant level of influence over the target company, it will most likely provide a more robust set of representations and warranties as any other controlling shareholder and, then, seek to limit its indemnification obligations.

Usually sellers' representations and warranties are carefully reviewed by sellers jointly with their legal counsel and the target company management team, in order to include the necessary carve-outs and materiality and knowledge qualifiers to guarantee that no misrepresentations are being made. The foregoing carve-outs are, many times, made through disclosure schedules, since a general disclosure against the data room is not usually accepted.

Despite participating in the review of the representations and warranties, the management team (except for sellers that are management shareholders) does not have any contractual liability in connection with the violation of such representation and warranties, which is fully allocated to sellers. Sellers, on the other hand, usually have the obligation to indemnify for the violation or breach of the representations and warranties given in the purchase agreement. However, as mentioned above, sellers will seek to limit such indemnification obligations.

6.10 Other Protections in Acquisition Documentation

Warranty and indemnity insurances are still a novelty in the Brazilian market and, as such, sellers continue to be the sole responsible for indemnifying buyer in most of the Brazilian private equity transactions.

Due to the incipient adoption of warranty and indemnity insurances, buyers usually resort to other types of protection to secure sellers' indemnification obligations, such as escrow accounts and holdbacks, parent company guarantees, bank guarantees, pledge over target company shares that are still held by sellers, among others.

6.11 Commonly Litigated Provisions

Litigation is generally rare and confidential in private equity transactions, as Brazilian parties to an investment agreement or stock purchase agreement tend to choose settling disputes through arbitration. Nevertheless, post-closing disputes usually revolve around purchase price adjustments, earn-out payments and indemnification for third party claims.

7. Takeovers

7.1 Public-to-Privates

Public-to-private transactions, especially private equity transactions, are not common in Brazil. Whenever such a transaction takes place, the rules of the Brazilian Securities and Exchange Commission (CVM) must apply.

7.2 Material Shareholding Thresholds

Material shareholding disclosures are applicable to public companies. Shareholding disclosure thresholds as well as filing requirements are set forth in the rules of the Brazilian Securities and Exchange Commission (CVM), which provide as follows:

- any shareholder or group of shareholders, acting jointly or representing the same interests, must notify the company of any transaction or group of transactions by means of which the shareholding held by such shareholder or group of shareholders surpasses or falls below 5%, 10%, 15% and so on of a same type or class of shares of the company;
- during a mandatory tender offer for acquisition of control, any shareholder or group of shareholders, representing the same interests, that hold more than 2.5% of a type or class of shares shall disclose any 1% variation to the holding of its shares; and
- in order to acquire shares of a Brazilian company via a public takeover, bidder must launch its public tender offer by publishing the tender offer notice and instrument in the mass circulation newspaper usually used by the public com-

pany and in the Official Gazette. Such notice and instrument will also be sent to the public company's investor relations executive officer, so that they may immediately disclose the notice to the market.

7.3 Mandatory Offer Thresholds

MTOs apply to public companies only. According to the Brazilian Corporations Law (Law No 6,404/1976) and the Brazilian Securities and Exchange Commission (CVM) rules, the obligation to launch a mandatory offer is triggered whenever:

- the controlling shareholders or a person related to them acquire shares representing more than one third of all outstanding shares of each type and class of shares; and
- there is a sale of the public company's control.

7.4 Consideration

Cash is more commonly used as consideration. However, other securities or a combination of cash and other securities are also used as consideration in sparse cases.

7.5 Conditions in Takeovers

Brazilian tender offers are subject to the Normative Rule No 361/2002 of the Brazilian Securities and Exchange Commission (CVM), among other terms and conditions, such Normative Rule establishes that the tender offer must:

- be directed indistinctly to all shareholders of the same type and class of shares that are the object of the tender offers;
- guarantee the equal treatment of its recipients;
- furnish the recipients of sufficient information about the company and the bidder so the recipients have sufficient information for their decision making; and
- be intermediated by a brokerage firm, securities dealer, or a financial institution with a portfolio investment.

The tender offer may also be subject to condition established by the bidder on the tender offer notice and instrument, provided the fulfilment of such condition does not depend, directly or indirectly, on action to be carried out by the bidder or any of its related parties.

In the event a competing tender offer is launched, the initial bidder as well as the competing bidder are entitled to raise the price of their offers by any amounts and as many times they deem necessary, provided the required formalities are observed.

7.6 Acquiring Less Than 100%

If a bidder does not seek or obtain 100% ownership of the company following the completion of its tender offer, it may still have significant control over the target company depending on the shareholding percentage it holds. For example, the Brazilian Corporations Law (Law No 6,404/1976) provides that: (i) the general quorum for approval of resolution in general shareholders' meetings is the majority of the voting capital stock present at the meeting (please note that the company's by-laws may establish higher approval quorums, as well as there are specific provision with higher approval quorums established by law); and (ii) if the multiple voting system for the election of members of the Board of Directors (ie, each share will hold as many votes as Board members positions, and the shareholders will be able to distribute their votes among the Board candidates as they deem fit) is required by shareholders representing 10% of the company's voting capital stock, the shareholder or groups of shareholders bound by a voting agreement, holding more than 50% of the company's voting capital stock, will be able to elect equal number of Board members elected by the other shareholders plus one Board member.

Additionally, if following the completion of a delisting tender offer, less than 5% of the company's shares remain outstanding, the company shareholders' meeting may approve the redemption of such outstanding shares (squeeze out), based on the same price per share paid in the tender offer.

7.7 Irrevocable Commitments

Because dispersed ownership companies are still unusual in Brazil, it is more common for a bidder to first negotiate a private purchase agreement with the company's controlling shareholders or relevant shareholders and, following such acquisition, launch a public tender offer for the acquisition of the shares of the remaining shareholders, in which it must guarantee to such remaining shareholders a purchase price per share of 80% or 100% of the purchase price per share paid to the controlling shareholder, depending on the listing level of the public company with the Brazilian stock exchange.

7.8 Hostile Takeover Offers

Hostile takeovers, although permitted, are still rare in Brazil. Despite that, a few Brazilian public companies have implemented defences against hostile takeovers, such as poison pills. The "Brazilian poison pills" provided in the by-laws of the certain public companies provide that the acquisition of a certain percentage of shares triggers the acquirer's obligation to launch a mandatory tender offer, which makes the hostile takeover more expensive.

8. Management Incentives

8.1 Equity Incentivisation and Ownership

Equity incentivisation of the management team is a common feature in Brazilian private equity transaction, especially when founding shareholders remain in the management of the target company.

The level of equity ownership held by management varies from transaction to transaction, depending on the private equity fund's philosophy and on how essential are certain members of the management team.

8.2 Management Participation

Whenever sellers remain in the target company as part of its management team, it is common for such sellers to continue holding equity directly in the target company or have such equity rolled over to a holding company. The nature of such equity may either be the same as or different from the equity of the private equity shareholder. In any case, management team members holding equity in the target company and the private equity shareholder will execute a shareholders' agreement regulating governance rights, if management team holds a relevant stake in the company, and share transfer rights.

In the event the members of the management team do not already hold equity in the target company prior to the transaction, management incentive plans may also be structured as stock option plans or phantom stock plans.

8.3 Vesting/Leaver Provisions

Vesting of management equity depends on the type of equity. The equity the management shareholders already hold in the company as well as rollover equity and cash investments are vested upon issuance. Stock option plans, on the other hand, usually have vesting provisions that are part time-based and part returned-based.

Leaver provisions are usually a given in stock option plans, but more negotiated in shareholders' agreements as such negotiations are usually tied to the negotiations of the purchase/investment agreement regulating the entry of the new shareholder into the target company. It is common for such leaver provisions provide for the repurchase of the equity management at market value or less than market value, depending on whether it is a "good" or "bad" leaver situation.

8.4 Restrictions on Manager Shareholders

Customary restrictive covenants assumed by management shareholders are confidentiality, non-disparagement, non-solicitation and non-compete obligations. In order to non-compete obligations be enforceable, they must observe a few requirements:

- proper compensation is paid for the leaving shareholder (ie, a portion of the purchase price);
- the geographical limitation thereto cannot be greater than the entire country; and
- the term does not exceed five years.

8.5 Minority Protection for Manager Shareholders

Management shareholders usually hold a minority stake in the company and, thus, may enjoy tag rights (see **10.3 Tag Rights**) and the minority rights provided by law, such as:

- pre-emption rights for the subscription of shares in future capital increases;
- withdrawal rights, in the event the shareholder does not agree with the approval of certain provisions, such as amalgamation or merger of the company or its shares, split up of the company, change of the corporate purpose of the company, among other matters;
- right to minimum mandatory dividends (which consist of 25% of the net profits of the company, in case the by-laws do not set forth a specific percentage);
- veto on the transformation of the company's corporate type; and
- certain information rights.

Management shareholders' control will typically be restricted to the actions within the competence and threshold limits of the positions they hold in the management of the company (usually C-level positions). However, depending of the percentage of the equity stake held by them, management shareholders may be able to indicate members to the company's Board of Directors and prevent the approval of resolutions that require higher approval quorums.

Usually management shareholders' have little or no influence over the private equity investor's exit. Nevertheless, management shareholders may be involved in the discussions regarding the exit and the shareholders' agreement of the company may include the management shareholders' obligation to cooperate with the private equity investor's exit.

9. Portfolio Company Oversight

9.1 Shareholder Control

Brazilian Securities and Exchange Commission (CVM) rules regarding Brazilian investment funds establish that Brazilian funds must, as a rule, participate in the decision-making process of their portfolio companies, with effective influence over the definition of their strategic policies and management. Exception to such rule are if:

- the Brazilian fund's investment in the company is reduced to less than half of its original percentage and represents less than 15% of the portfolio company's capital stock;
- the book value of the Brazilian fund's investment is reduced to zero, subject to the approval of the Brazilian fund's general quotaholders' meeting; and
- the investment is in public companies listed in a special listing segment, whose governance standards are higher than those required by law, provided such investment corresponds to up to 35% of the Brazilian fund's subscribed capital.

In view of the above, Brazilian funds usually negotiate strong shareholders' agreements with corporate governance rules, which provide for:

- right to appoint Board members;
- right to appoint executive officers;
- information rights; and
- veto rights over certain reserved matters (eg, capital increase and issuance of convertible securities; changes to by-laws/articles of association; corporate restructurings; acquisition and divestures; formation of joint ventures; approval of the business plan and annual budget; capex investments; incurrence of new indebtedness; execution of related-parties transactions); among other matters.

9.2 Shareholder Liability

As a rule, shareholders are not liable for the contingencies of their invested companies. A few exceptions to this rule are the following:

- certain cases of violation of law (eg, fraud to harm third parties, commingling of assets), in which there is the piercing of the company's corporate veil;
- labour liabilities, since the member of the same economic group are jointly liable for any amounts due to the employees of other companies belonging to the same economic group;
- corruption liabilities, since the Brazilian Anti-Corruption Law (Law No 12,846/2013) provides for the joint liability of controlled and controlling companies, affiliates and members of a consortium; and
- if the legal entity is an obstacle for the redressing or compensation of environmental damages.

9.3 Shareholder Compliance Policy

Because the adoption of compliance programs may assist companies in mitigating risks and lowering fines they might face regarding breaches of compliance obligations (provided the compliance program was already in force at the time of the wrongdoing); it has become common for private equity fund shareholders to push their Brazilian portfolio companies into adopting compliance programs, which not necessarily are the same ones as of the private equity fund itself.

10. Exits

10.1 Types of Exit

Private equity investors typically hold their investments for five to ten years. It is rare for private equity funds to reinvest upon exit, as in many cases the exit date will be close to the end of the private equity fund's life itself and, thus, the private equity fund would not have enough time to liquidate the reinvestment prior to its wound-up.

Despite the increasing number of Brazilian companies' IPOs in the past years (including 2020), private sales to strategic buyers or other private equity funds continue to the most common way of exiting private equity investments in Brazil. It is not unusual for the exit to be conducted as a "dual track" process, since it offers the private equity fund the opportunity to better assess which route (ie, private sale or IPO) is more advantageous and, thus, mitigate the risks of an aborted IPO.

10.2 Drag Rights

Private equity investors usually are entitled to drag along rights in the event of the sale of the company's corporate control. Drag rights are usually applicable to management shareholders and institutional co-investors alike.

Drag rights are rarely used by private equity investors as they represent a more aggressive approach whereby one shareholder obliges the other shareholders to sell their shares at a pre-agreed price to a third party. Negotiated amicable exits are more common in the Brazilian market.

10.3 Tag Rights

It is common for all shareholders of an invested company to be entitled to tag along rights. The tag threshold is usually the sale of the invested company's corporate control, and the tag right may comprise all the shares of the other shareholders. However, it is not unusual for shareholders' agreements to provide for lower tag thresholds, where other shareholder may exercise only a pro rata tag right.

10.4 IPO

The lock-up period for controlling shareholders and management in Brazilian IPOs is of 180 days counted as from the IPO date, followed by an additional 180 day-period in which controlling shareholders and management cannot sell more than 40% of the shares they held immediately after the completion of the IPO. Relationship agreements are not a common in Brazilian IPOs.

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Machado Meyer Advogados has been building its history for more than 48 years, inspired by sound ethical principles, the technical skills of its professionals, and a close relationship with its clients. The firm is ranked as one of the major law firms in Brazil, with over 700 professionals. Machado Meyer provides innovative legal solutions, anticipates scenarios and makes business possible. Combining expertise in various areas of law, broad knowledge of legislation and a thorough understanding of the matter, the firm's professionals go beyond simple problem-solving to create and preserve value for companies. Because of the significant flow of today's existing investment, the firm has organised professionals specialised in advising clients abroad, creating multidisciplinary groups, especially in Germany, Latin America, Iberia, and Asia, which have special desks.

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Laura Dabronzo provides specialised legal advice in connection with the structuring, negotiation and implementation of merger and acquisition transactions, as well as corporate advice to national and international clients with or intending to engage in activities in Brazil. She has previous experience in several areas of knowledge, such as tech, energy, healthcare, pharmaceutical, real estate, services and retail.

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