

Main practices areas of Barbosa, Müssnich & Aragão

Administrative Law and Concessions

Environmental Law

Competition and International Trade

Litigation and Conflict Resolution

Corporate Ethics and Compliance

Real Estate

Finance and Capital Markets

Intellectual Property

Recovery of Distressed Businesses

Corporate

Employment, Labor and Pension Law

Tax

**01**

Mergers and acquisitions: Evaluating the risks associated with anti-corruption legislation

**02**

The limits on ANVISA's involvement in the grant of pharmaceutical patents

**03**

CADE's new members shouldn't wait for new legislation before rolling up their sleeves

**04**

The Brazilian Corporations Law and reverse share splits

New rules on debentures and the New Fixed Income Securities Market

**05**

ICMS Protocol 21 and tax sharing between Brazilian states

**06**

Reflections on the Review of BM&Fbovespa's Corporate Governance Segments

Antenor Madruga | [ant@bmalaw.com.br](mailto:ant@bmalaw.com.br)

## MERGERS AND ACQUISITIONS: EVALUATING THE RISKS ASSOCIATED WITH ANTI-CORRUPTION LEGISLATION

A bill that would impose administrative and civil liability on legal entities for acts committed against the public administration is now before the Brazilian Congress. Broadening the front of the fight against corruption to include the private sector is not an initiative that is confined to Brazil alone, nor a mere future possibility. To the contrary, putting private sector businesses in the sights of anticorruption arms is the result of an international movement. And even without any change to the current legislation, businesses that become involved in corruption-related situations already face more serious consequences than they once did.

The risk of criminal proceedings against executives and employees, searches and seizures, loss of property, forfeiture of profits, fines in the millions, bans from government contracting, and damage to a company's image are just some of the effects that the intensifying fight against corruption can – and does – have in the corporate world.

The attitude of law enforcement authorities, which have turned their attention to those who offer bribes as well on those who receive them, using new techniques for investigating fact and producing evidence, and the advances in international legal cooperation are some of the changes that are reflected in the increased risk of serious consequences for businesses that engage in corrupt practices. Another important development can be attributed to legislation that punishes corruption of foreign government officials and the efforts some countries have made to apply their legislation to acts committed outside their territories. The most striking example of this development is the application of the Foreign Corrupt Practices Act – FCPA by the American authorities.

The US has used the FCPA to reach not only American companies, but also foreign companies whose shares trade on US exchanges or that use the American market. For example, the US authorities consider that they have jurisdiction over foreign companies that make transactions in dollars, since these transactions are necessarily cleared through banks located in the US. Almost one half of all the companies prosecuted on the basis of the FCPA in 2010 are foreign, and some of those companies are Brazilian.

Involvement in corruption-related problems represents a significant risk to a business's operational capacity and financial health, and this risk is not always identified in non-specialized due diligence investigations and audits. The risk is even greater in companies that do not have effective compliance programs and control mechanisms.

Evaluating the risks associated with anti-corruption legislation in the context of mergers and acquisitions is no longer a merely ethical duty: it has become a business imperative.



Antenor Madruga, partner, Litigation and Corporate Ethics & Compliance

## THE LIMITS ON ANVISA'S INVOLVEMENT IN THE GRANT OF PHARMACEUTICAL PATENTS

In 2001, a new provision, article 229-C, was introduced into Brazil's Industrial Property Law (Law 9279/1996 – the "IPL") to include ANVISA, Brazil's drug and health products regulator, in the process for granting patents for pharmaceutical products and processes. Since then, Brazil's intellectual property authority, the National Industrial Property Institute (INPI), drug companies and ANVISA have been on a collision course over the limits of ANVISA's powers with respect to the protection of pharmaceutical technologies in Brazil.

While ANVISA took the new provision to be an extension of its jurisdiction, the INPI found its decisions being overturned by the agency, and sector businesses were faced with contradictory decisions and legal uncertainty over the scope and meaning of article 229-C.

The controversy over the limits of ANVISA's authority in patent applications quickly came before the courts, and the Office of the Federal Attorney-General (Advocacia Geral da União – AGU) has now issued an opinion on the correct interpretation of article 229-C of the IPL, suggesting that the debate may close to an end.

Article 229-C provides that where the INPI proposes to grant a pharmaceutical patent application, the application will be submitted to ANVISA for its consent to the grant of exclusivity under the patent. This procedure would be entirely in accordance with the legislation, except for the fact that ANVISA has interpreted the provision as giving it additional powers.

Based on this interpretation, ANVISA began to deny its consent to the grant of patents on the grounds that the requirements for patentability had not been met, an issue that falls squarely within the INPI's exclusive jurisdiction and that the INPI had already examined. ANVISA's jurisdiction, according to article 6 of the Law that created the agency (Law 9782/1999), is limited to "protecting the health of the population, through the control and inspection of the production and sale of products and services subject to health standards control...".

Companies whose patent applications were denied by ANVISA turned to the courts to have the legality of the agency's decision reviewed. Two actions are now before the appeal courts, one in the 1st Region Federal Appeal Court and the other in the 2nd Region Federal Appeal Court.

Due to the conflicting positions taken by ANVISA's and the INPI's legal departments, the AGU was called upon to issue a brief on the matter. The AGU concluded that ANVISA's attempt to review patentability requirements was illegal, and that article 229-C of the IPL does not expand the scope of ANVISA's jurisdiction.

Based on the AGU's brief, the 1st Regional Federal Appeal Court granted a preliminary injunction ordering ANVISA to review the application again, this time considering only questions related to public health.

In January of this year, ANVISA submitted a request for reconsideration to the AGU, but the AGU reaffirmed its position that ANVISA's actions had been contrary to the law. This suggests that the debate is now closed, since the AGU's opinion was endorsed by the Federal Attorney-General: according to Complementary Law 73, 1993, a opinion endorsed by the Federal Attorney-General is binding on all federal agencies.

There have been reports in the press that ANVISA will try to convince the Federal Attorney-General to change his position, and NGOs have protested in front of the United Nations against "a step backward for public health" and "a victory for the drug companies".

The AGU is not partisan, and its opinion simply sets out the best interpretation of the law, while noting that the two federal agencies can and should work together, each with the limits of its jurisdiction. The opinion also states that ANVISA can assist the INPI in its review of patent applications by providing support on the technical aspects involved in the process.

To adopt ANVISA's interpretation of article 229-C of the IPL, which would give it powers to reexamine the INPI's decision on patentability, would represent yet another obstacle and more delay for users of the system. The solution adopted by the AGU reduces the number of steps and the time involved in obtaining patent protection for pharmaceutical products. Clearer and less bureaucratic procedures contribute to the growth of the pharmaceutical industry and of the Brazilian economy as whole.

At the same time, the delimitation of ANVISA's authority does not mean that the health of the Brazilian population has been given a back seat. Within the scope of its jurisdiction, ANVISA can deny licences to sell any medication that it believes to be harmful to public health.

## CADE'S NEW MEMBERS SHOULDN'T WAIT FOR NEW LEGISLATION BEFORE ROLLING UP THEIR

Between the end of March and the beginning of May of this year, the Minister of Justice invested in office three councilors and the new chairman of Brazil's antitrust authority, CADE (Councilors Alessandro Octaviani, Marcos Veríssimo and Elvino Mendonça and Chairman Fernando Furlan), along with Vinícius Carvalho as the new head of the Secretariat of Economic Law (Secretaria de Direito Econômico – SDE). With the news that the head of Treasury's Economic Monitoring Secretariat (Secretaria de Acompanhamento Econômico – SEAE) will remain unchanged, the composition of Brazil's competition authorities under President Dilma's government has been set.

The new officials' résumés show that they were chosen on the basis of their qualifications in competition matters, following the trend established by the previous two governments. Two of the new councilors are professors of law and one is an economics professor, and they join other PhDs on the Council. It is a recipe that has worked well in the past, as evidenced by the international recognition that CADE has conquered in recent years. In fact, the federal government's attitude is praiseworthy, especially in view of the various complex mergers and acquisitions – some with a high degree of media appeal – now before CADE, and important investigations that will depend on the position that the Council adopts.

What remains to be seen is whether the undoubtedly qualified Councilors and Secretary will be able to maintain the reputation CADE and the SDE have achieved over the last eight years. The recognition CADE has obtained should mark the end of the passage from the rocky adolescence of Brazil's antitrust system to its adulthood, and a corresponding increase its responsibilities. The challenges faced by the new officials are perhaps not so different from those that arose in the past, but they may have dimensions that are still unknown.

The expected growth of the Brazilian economy indicates that society's demands on the competition authorities will intensify on various fronts: increased numbers of M&A transactions submitted to CADE, the need for rapid decision-making that is compatible with economic opportunities and the international competitiveness of companies doing business in Brazil, the importance of the cases, and the need for increasingly sophisticated and precise economic analysis of transactions.

The SDE, the SEAE and CADE will have to reconcile these demands with the apparently insurmountable difficulties resulting from their overlapping jurisdictions and the confusing procedure established

by the governing legislation, on one hand, and, on the other, with the traditional problems of Brazilian bureaucracy, brought about by insufficient personnel and infrastructure, and the lack of a merit-based system that rewards the best staff.

Some say – and CADE's former Chairman went so far as to stress the point in an appeal to the legislature – that these challenges can only be overcome if Senate Bill 6/2009 is made into law. The Bill proposes a complete reformulation of the antitrust system, and its approval has been expected for at least five months.

There may be a good portion of truth in the argument, but anxiously awaiting the enactment of the new legislation can have a counter-productive effect. The Bill is a welcome initiative, without question, despite the controversial changes it will introduce. However, the expectation generated by the Bill seems exaggerated and has led the authorities to neglect their current powers, adopting a waiting stance that is completely incompatible with the dynamism required of competition authorities.

For example, under the Bill, prior approval by CADE will be required before mergers and acquisitions can be implemented, and the Council will have one month to issue its response. The requirement for prior approval imposes a burden on companies that they do not now have, and directly ties the companies' interest in a quick response from CADE to providing, in advance of the transaction, extensive information and certain undertakings. The current legislation, however, does not establish the same system, and at times it seems that the competition authorities are attempting to implement the prior approval system before it becomes law, with the result that companies are being unfairly labelled as intransigent. There is still much room for improvement within the current system for review of mergers and acquisitions, and no shortage of mechanisms for the authorities to make those improvements, starting with the urgent need for a clear and consistent position on routine issues.

In this context, it is clear that the members of CADE and the Secretaries of the SDE and the SEAE have a role to play right now that is just as important as preparing for the transition to the new system that will be introduced when and if the Bill becomes law: ensuring that the powers and duties established under the current Law 8884/1994 are exercised as effectively as possible. The Law, and the Brazilian economy, depends on it.

## THE BRAZILIAN CORPORATIONS LAW AND REVERSE SHARE SPLITS

Brazil's Corporations Law (the Lei das Sociedades Anônimas or LSA) has a number of topics that are largely unexplored by corporate law scholars. One of those topics is the reverse share split, which reduces the number of shares in a company without a corresponding reduction in capital. Reverse share splits are most commonly used to simplify a company's corporate structure or to increase the trading price of shares.

The LSA makes only a general reference to reverse share splits in article 12, without going into detail. As there is little if any scholarly commentary on the subject, companies are left to apply the LSA's provisions on share splits by analogy to deal with practical questions such as the treatment of fractional shares and the risk of litigation if the transaction results in the exclusion of shareholders.

When dealing with fractional shares, publicly-traded companies have applied the provisions of article 169 of the LSA to fix a period of at least 30 days for shareholders to transfer their fractions to make up entire shares before the company sells the shares on the market. The product of the sale is kept available for three years.

The CVM takes the position that a reverse share split which has the effect of excluding shareholders will constitute an abuse of control unless the controlling shareholder provides mechanisms for shareholders to retain their interest in the company. Likewise, BM&FBovespa, recommends that companies listed in the Novo Mercado segment establish mechanisms to ensure that shareholders can remain in the company after a reverse share split.

These measures, however, do not completely resolve the issue. Does the LSA effectively confer the right to remain as a shareholder of a company? Can the controlling shareholder be compelled to ensure that a reverse share split does not exclude shareholders? What happens if there is no controlling shareholder? Some would argue that the abusive exclusion of shareholders should be prevented by other means.

Nevertheless, companies have followed the guidelines established by the CVM and BM&FBovespa, since they serve as a parameter for implementation of reverse share splits, reducing the risk of challenges. Still, there is much room for further study on reverse share splits, including the question of how they should be dealt with under the LSA.

## NEW RULES ON DEBENTURES AND THE NEW FIXED INCOME SECURITIES MARKET

In December of last year, Provisional Measure 517 was passed to encourage the growth of a more profitable and dynamic secondary market in fixed-income securities. PM 517/2010 made a number of significant changes to the provisions on debentures under the Brazilian Corporations Law: it is now easier for issuers to repurchase debentures; boards of directors have powers to issue convertible debentures; companies can make overlapping issues of debentures; the limit on unsecured debentures was removed; and companies can now engage the same trustee for more than one debenture issue. As an incentive to investment, the Provisional Measure also reduces the tax burden on earnings from debentures issued by special purpose companies (SPCs) created for infrastructure projects.

However, given the complexity of the subject and the possible impact on the market, Brazil's securities regulator, the CVM, has presented suggested changes to PM 517 and is still studying the adjustments to be made to current regulations.

In a related initiative, ANBIMA, the association that represents agents in the Brazilian capital and financial markets, released in April the general outline of a new listing segment for fixed income securities, the Novo Mercado de Renda Fixa (NMRF). The proposed NMRF establishes minimum rules on standardization and liquidity for fixed-income securities, such as yields tied to a pre-fixed rate, price index or the Brazilian Libor, a maturity of more than four years, minimum levels of market dispersion, and rules applicable to market makers.

The objective of the NMRF is to create, through self-regulation mechanisms, conditions that will allow the development of the primary and secondary markets for private debt securities, with a view to sustainable growth of the Brazilian economy.

The biggest challenge faced by the project is the lack of liquidity of private fixed income securities, and to address this problem the project includes a proposal for a liquidity support fund (LSF) composed of public and private funds that will act as a market maker, generating liquidity for the secondary market, and a proposal for a liquidity guarantee fund (LGF) to provide a market for intermediaries in non-liquid situations. In short, the NMRF project promises to stimulate the growth of an active market for long-term financing in Brazil.

## ICMS PROTOCOL 21 AND TAX SHARING BETWEEN BRAZILIAN STATES

On April 1, 2011, the Conselho Nacional de Política Fazendária – CONFAZ (the National Tax Policy Council) issued ICMS Protocol 21, which was signed by 18 Brazilian states and the Federal District. The Protocol provides for the sharing of ICMS (the state VAT) attaching to sales of goods to final consumers when the purchaser does not take delivery of the merchandise at the seller's establishment (internet and telemarketing sales and sales made at showroom).

Under the Protocol, the state where the merchandise will be delivered can demand a share of the ICMS attaching to the sale, regardless of whether the state from which the merchandise is sent is a signatory to the Protocol.

According to ICMS Protocol 21, the state of destination is entitled to demand ICMS corresponding to its internal ICMS tax rate (which is usually 17% or 18%), minus (i) 7% for merchandise originating from the South and Southeast regions, with the exception of the state of Espírito Santo, and (ii) 12% for merchandise originating from the North, Northeast, or Midwest regions or from Espírito Santo. The state of origin is required to tax the sale at the interstate rate (7% or 12%, depending on the state to which the merchandise is sent).

The states that signed the Protocol argue that the growth of electronic commerce has reduced the need for businesses to create establishments in their states to serve local clientele, and as a result tax revenues that would once be generated in the state are being transferred to other states.

The difficulty is that ICMS Protocol 21 contradicts the provisions under the Federal Constitution concerning the application of ICMS to interstate sales to final consumers. Article 155 §2 (VII) and (VIII) of the Constitution establish that (i) the tax attaches at the internal rate of the state of origin when the recipient of the merchandise is not an ICMS taxpayer, and (ii) the tax attaches at the interstate rate when the recipient is an ICMS taxpayer, in which case the state of destination is entitled to the difference between the internal rate and the interstate rate.

In other words, for sales in which goods are sent to final consumers (who are not ICMS taxpayers) located outside the state of sale, the Federal Constitution provides that the full ICMS tax rate applicable to internal sales in the state of origin applies, and there is nothing in the Constitution to authorize a claim by the state of destination to part of the tax on the sale.

By establishing a rule contrary to the Federal Constitution, ICMS Protocol 21/2011 harms the interests of both companies and final consumers. The problem arises when consumers located in signatory states acquire goods from non-signatory states. In these situations, ICMS is payable to the state of origin at the internal rate, and the state of destination will demand collection of the additional amount provided for under the Protocol. For example, merchandise acquired by a consumer located in a signatory state, which has a 17% internal ICMS rate, from a supplier in a non-signatory state with an internal ICMS rate of 18%, will be subject to taxation at a total rate of 28%: 18% owed to the state of origin and 10% (17% - 7%) to the state of destination.

In addition, the Protocol authorizes signatory states to require presentation of proof, to the state border tax agents, that the ICMS supposedly owed to the state of destination has been collected, or, alternatively, to require that the establishment that remitted the goods register as an ICMS taxpayer in the state. These requirements delay the delivery of merchandise and result in double taxation, imposing losses on purchasers and sellers.

ICMS Protocol 21/2011 was signed by the states of Acre, Alagoas, Amapá, Bahia, Ceará, Espírito Santo, Goiás, Maranhão, Mato Grosso, Mato Grosso do Sul, Pará, Paraíba, Pernambuco, Piauí, Rio Grande do Norte, Roraima, Rondônia and Sergipe and the Federal District.

Among the states that did not sign the Protocol are Minas Gerais, Rio de Janeiro and São Paulo – which are where the largest e-commerce distributors are located – since they rightly believe that they have no obligation to share tax revenues generated by their tax payers.

## REFLECTIONS ON THE REVIEW OF BM&FBOVESPA'S CORPORATE GOVERNANCE SEGMENTS

Following the end of the last revision of the Listing Rules for the Nivel 1, Nivel 2 and Novo Mercado segments, listed companies submitted new suggestions for changes, imposing the need for a new – though brief – revision. Almost immediately, new companies launched shares and achieved wide market dispersion, and as a result, a controlling shareholder is no longer a regular feature of Brazilian companies. Then poison pill mechanisms began to be tested in the wake of the financial crisis of 2008. Faced with an increased dispersion of capital and questions as to the effectiveness of the corporate governance rules in effect at the time, proposed revisions to the Novo Mercado, Nivel 2 and Nivel 1 Listing Rules were presented in October 2008.

Recently, the new versions of the Listing Rules for the three segments came into effect. Not only do the revised rules address the issues that first set the revision process in motion, they also seek to deal with more recent changes to Brazilian equity market regulations, such as CVM Instruction 480, which establishes higher standards of transparency for publicly-traded companies, and the adoption of the IFRS as the accounting standard in Brazil.

Although many listed companies have already implemented some of the proposed suggestions, the amendments approved for all three segments provide for (i) the inclusion of certain minimum provisions in the bylaws of listed companies, (ii) the mandatory adoption and disclosure by listed companies of their securities trading policy and code of conduct, and (iii) a prohibition against the same person holding the positions of Chairman of the Board of Directors and Chief Executive Officer in listed companies (in August 2010, when the revision began, 78% of companies listed on the Novo Mercado, 72% of Nivel 2 companies, and 93% of Nivel 1 companies had already adopted this rule).

In addition, the three sets of Listing Rules incorporate the Monetary Penalties Regulations, a compilation of provisions that previously were spread out over the Listing Rules for each segment and the original Penalties Regulations, which was attached as a schedule to the listing agreement. The new Monetary Penalties Regulations apply to the company, the members of its management and its shareholders, and the penalties vary according to the nature and seriousness of the offense, the damage to the market, the advantage gained by the offender, and repeat offenses. Any application of penalties under the Regulations is preceded by notice to the offender, establishing a period of time to remedy the offense, and giving the offender the opportunity to present a defense. If responsibility for an offense is attributed to more than one person, each will be jointly liable for the fine.

Companies currently listed on the Novo Mercado, Nivel 2 and Nivel 1 segments will have three years to bring their corporate practices and documents into compliance with the revised rules, while new entrants will be required to comply prior to listing.

The revised Listing Rules are another sign of the Brazilian equity market's growing maturity. If the objectives of the revised rules are achieved, they will not only preserve market value, but reinforce BM&FBOVESPA's commitment to the highest international standards of corporate governance.

### PROJECT TEAM

#### EDITORIAL COMMITTEE

Paulo Cezar Aragão,  
Francisco Antunes Maciel Müssnich,  
Plínio Simões Barbosa.

#### PRODUCTION

Lígia Batista

#### GRAPHIC DESIGN AND LAYOUT

Soter Design

This publication may not be reproduced in whole or in part without prior authorization by BM&A - Barbosa, Müssnich & Aragão.

BM&A Review ® is published for informational purposes only and should not be relied on as legal advice for specific transactions or operations

#### BM&A ADVOGADOS

##### Belo Horizonte

Tel. (+55) (31) 3326 9200  
Fax. (+55) (31) 3326 9250

##### Brasília

Tel. (+55) (61) 3218 0300  
Fax. (+55) (61) 3218 0318

##### Rio de Janeiro

Tel. (+55) (21) 3824 5800  
Fax. (+55) (21) 2262 5536

##### São Paulo

Tel. (+55) (11) 2179 4600  
Fax. (+55) (11) 2179 4597

#### BM&A PROPRIEDADE INTELECTUAL

##### Rio de Janeiro

Tel. (+55) (21) 3824 5757  
Fax. (+55) (21) 3824 5740

#### BM&A CONSULTORIA TRIBUTÁRIA

##### São Paulo

Tel. (+55) (11) 2179 5300  
Fax. (+55) (11) 2179 5211

##### Rio de Janeiro

Tel. (+55) (21) 2114 7601  
Fax. (+55) (21) 2114 7602

BM&A Review content is produced by members of Barbosa, Müssnich & Aragão Advogados, BM&A Consultoria Tributária and BM&A Propriedade Intelectual.

