

1 February 2002

# Latin America Strategy

## Brazil: Upcoming Tender Offer Regulation

The Brazilian Securities Exchange Commission, or CVM for its Portuguese acronym, drafted a new tender offer regulation that will replace regulations 229, 299 and 345. The new tender offer regulation is available for public consultation and the CVM will accept suggestions until 18 February 2002. We expect the CVM to approve a new tender offer regulation 60 days after all suggestions have been accepted. Below we highlight some of the key elements of the proposed regulation, which has four main topics:

1. Tender offers
2. Requirements for delisting a company
3. Increase of controlling group's participation in the company
4. Sale of control of a company

Some of the key changes worth highlighting include:

- **Fair Price:** The controlling group has to disclose a valuation report by the broker-dealer in charge of carrying out the tender offer estimating fair price. It must disclose 3 price estimates, based on: shareholders' equity, average share price over the past year, and economic value.
- **Broker-Dealer Disclosure:** The broker-dealer evaluating the company must certify that there are no conflicts of interest between the two parties. It must decide which valuation criteria it deems the fairest and must disclose to the CVM all compensation received from the company, or the party making the offer, over the previous 12 months.
- **Minimum Liquidity:** A controlling group that acquires shares, leading the free-float of those shares to fall below 25%, must tender for the remaining shares.
- **No Price Ceiling For Tender Offers:** Tender offers will be made through auctions where the tendering group can make an unlimited number of offers, as long as the price keeps rising. All shares receive equal price.
- **Shareholder Disclosure:** Companies would be required to disclose its list of shareholders during a tender offer process. With a known list of shareholders, minority investors would have an easier task organizing themselves around a certain issue.
- **Delisting Approval:** In order for a stock to be delisted, more than 2/3 of the entire free-float would need to agree with the delisting.

# Main Aspects of Proposed Regulation

This proposed new regulation deals with four main topics:

1. Tender offers
2. Requirements for delisting a company
3. Increase of controlling group's participation in the company
4. Sale of control of a company

In the sections below we highlight some of the key points of the four main topics of this new tender offer regulation.

## 1. Tender Offers

***The price paid must be uniform to all shareholders of the same share class***

**Mechanics:** All shareholders must be treated equally in tender offers. This means that the price paid must be uniform to all shareholders of the same share class. The tender offer must be intermediated by a broker-dealer. It is forbidden to charge the costs associated with the execution of a tender offer to the company. All tender offer auctions have to be conducted between 30 and 45 days following the publication of the offering memorandum ("edital"). The price paid for tender offers can be raised during the auction, but has to be offered equally to all shareholders that are tendering.

***The broker-dealer doing the tender offer becomes jointly liable with those offering the tender offer for any problem***

**Broker-Dealer:** The broker-dealer doing the tender offer becomes jointly liable with those offering the tender offer for any problems. The broker-dealer must be independent from the company and must, among other things, provide the following information on the company who is subject of the tender offer:

Analyze the fundamentals of the company object of the tender offer, showing at a minimum, the following information:

- Average stock price for past 12-months
- Value of company's shareholders' equity
- Economic value of the company, calculated using either a DCF model or equity valuation multiples, depending on the industry
- Fair value of the company

***Economic value is one of the criterias for assessing fair value***

Disclose to the CVM all income received from the company, or party making the tender offer, over the past 12-months.

**Shareholder Protection:** The new regulation would require the group making the tender offer to be liable for a period of one year to pay the difference in price to the shareholders who sold their stock in the tender offer under the following conditions:

- If within a year an important event occurs leading to a forced tender offer, or



- If the company engages in an activity that leads minority shareholders to be able to sell their shares back to the company (“direito de recesso”).

***Tender offers for over 1/3 of outstanding shares must remain open for 3 months***

**Tendering For More than 1/3 of Shares:** The new regulation requires that all tender offers designed to acquire over 1/3 of the outstanding shares of a single share class, must be extended to all shareholders of that share class for a period of 3 months following the day of the original tender offer auction. The idea is to provide protection to minority shareholders that believe that they should not tender. It can be argued that these shareholders could be forced to tender if they fear that liquidity will dry up following the tender offer. Thus, by providing them with an additional 3 months, they can evaluate the impact of the tender offer to the stock liquidity and make a decision.

**Competing Tender Offers:** The CVM allows for two or more parties to tender for the same shares as long as they are both properly registered with the CVM. The competing offer must be made with a minimum price that is at least 5% higher than the previous tender offer.

#### Prohibitions:

***A second tender offer can only be offered after 1 year of the first tender***

**Restricting Subsequent Tender Offers:** The same person or associated group cannot make a second tender offer at a higher price for the same shares for which they tendered during the previous 12-months, unless the same price is offered to all shareholders who tendered in the first tender offer.

**Tender Offers Acceptance Limitations:** In any tender offer where more than 1/3 and less of 2/3 of outstanding shares are tendered, the group making the tender offer can either:

- a. Acquire only up to 1/3 of outstanding shares on a pro-rated basis, or
- b. Cancel the tender offer.

## 2. Requirements for delisting a company,

***Approval from at least 2/3 of the free-floating shares is needed for delisting***

A company can only cancel its registration when shareholders representing at least 2/3 of the free-floating shares agree either through tendering their shares or in an expressed manner. It would be understood by the CVM that shareholder who do not tender or do not express their desire that the company be delisted, that they are indeed against the delisting.

A special assembly of shareholders must approve the price of the tender offer for the company delisting. This special shareholders’ meeting must be called within 15 days following the publishing of the value of the tender offer price.

### 3. Increase of controlling group's participation in the company

***If liquidity falls below 25%, due to corporate action by the controlling group, it must tender for all shares***

The controlling group and persons related to it must proceed to a full tender offer if they acquire shares that lead to:

- a. ownership of 75% or more of the outstanding share class, or
- b. Their newly acquired shares (including from the time the new tender offer regulation is in place) exceed 1/3 of the total free-float of the share class.

Note that the proposed regulation includes not only shares that are acquired from the market but also share subscriptions.

The controlling group can request the CVM not to do a tender offer if it sells sufficient shares within a period of 3 months in order not to violate the previous conditions.

### 4. Tender Offer Due To Sale of Company Control

In accordance with the new corporate law, the group acquiring control of the company has the option of either tendering shares and paying 80% tag along rights to minority shareholders or paying the difference between the stock price and the price paid to the controlling group selling control. Note that minorities in the former case would remain as minority investors in the company after control is transferred. It is understood by the CVM that all shareholders that do not tender are implicitly accepting to remain a shareholder and the acquiring group must pay them the price difference for their shares.

### Information Disclosure

***Companies involved in a tender offer must disclose its shareholder structure***

Under the new regulation a company who is involved a tender offer must disclose its shareholder structure, including the nominal distribution of shares among voting and non-voting shareholders. Special attention is given to the information pertaining to the controlling group and persons affiliated to it.

The company must also disclose financial indicators for the 2 previous years and the most recent quarter.

The average trading price for the stock, together with its economic value and shareholder equity, according to the most recent evaluation made by the broker-dealer who will be carrying the tender offer.

The company must also disclose the number of shares that will be tendered, the price and payment conditions and all information pertaining to the auction.



## Issues Pending Clarification

Some of the main points where the CVM would like to hear the opinion of investors include:

1. Tender offers:
  - a. The time frames proposed by CVM
  - b. Whether to restrict trading on the stock of the parties making the tender offer during the tender offer.
2. Delisting requirements:
  - a. The understanding by the CVM that investors who do not participate in a tender offer designed to close capital did so because they are in disagreement with the delisting or price offered.
  - b. The need for regulations on stock loans in case of a tender offer.
  - c. The procedure to review the price to be paid in a tender offer.
3. Is there a need to regulated tender offers for selling indirect control?

## Additional Information Available upon Request

**Disclosure Checklist**

| <b>Company</b>              | <b>Disclosure</b> | <b>Company</b>           | <b>Disclosure</b> |
|-----------------------------|-------------------|--------------------------|-------------------|
| Alfa                        |                   | Distribucion y Servicio  |                   |
| Ambev                       |                   | Elektra                  |                   |
| América Móvil               | 10                | Femsa                    | 10                |
| Apasco                      |                   | Eletrobras PNB           | 10                |
| Aracruz Celulose            | 10                | Embratel                 | 10                |
| Argos                       |                   | Endesa Chile             |                   |
| Asur                        |                   | Enersis                  |                   |
| Banacci                     | 2                 | GF Galicia               | 7,2               |
| Banco do Brasil (Not Rated) |                   | Gigante                  |                   |
| Banco Edwards               | 2                 | Globo Cabo               |                   |
| Banco Frances               | 2                 | Gruma                    |                   |
| Banco Hipotecario           | 2                 | Itaubanco                | 2                 |
| Banco Santander Chile       | 2                 | Iusacell                 |                   |
| Banco Santiago              | 2                 | Kimberly-Clark de México |                   |
| Bancomer                    | 2                 | Light ON                 |                   |
| Bansud                      | 2                 | Maseca                   |                   |
| Bimbo                       |                   | Metrogas                 | 10                |
| Bradesco                    | 6,2               | Metropolitana PN         |                   |
| Brasil Telecom              | 10, 11            | Modelo                   |                   |
| Capex                       | 10                | Panamco                  | 10                |
| Carso                       |                   | Pepsi-Gemex              |                   |
| CBD                         | 11                | Perez Companc            | 10                |
| CCU                         |                   | Petrobras                | 1,10              |
| Celesc PNB                  |                   | Quilmes                  |                   |
| Cemex                       | 1,2,7,10,11       | Sabesp ON                | 7                 |
| Cemig PN                    | 10                | Sanluis                  |                   |
| Central Puerto              |                   | Soriana                  |                   |
| Chilectra                   |                   | Tele Celular Sul         |                   |
| CIE                         |                   | Telemar                  | 10                |
| Coca-Cola Femsa             | 10                | Telemig Celular          |                   |
| Coelce PNA                  |                   | Telesp Celular           | 10                |
| Comercial Mexicana          |                   | Televisa                 |                   |
| Consorcio ARA               |                   | Telmex                   | 10,11             |
| Contal                      |                   | TGS                      | 10                |
| Copel PNB                   |                   | TVAzteca                 |                   |
| Corporación GEO             |                   | Unibanco                 | 2,10              |
| Costanera                   |                   | Vitro                    | 10                |
| CVRD                        |                   | Votorantim Celulose      | 10                |
| Desc                        | 10                | Walmart de Mexico        |                   |

Source: Deutsche Banc Alex. Brown estimates and company information

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