

## Cross-Border M&A in Latin America During Pandemic Times

By Paulo Rage<sup>1</sup>

As in many areas of the world economy, COVID-19 dramatically disrupted the otherwise steady growth of Latin American cross-border M&A activity. As the market slowly begins to return, participants should consider the potential challenges that will likely emerge in the new environment, which are further discussed in this article.

### Introduction

Since 2015, Latin America evidenced a growth of regional cross-border transactions, with specialized studies<sup>2</sup> showing that M&A activity rose up to USD 152 billion by the end of the decade. According to such specialized studies,<sup>3</sup> the majority of M&A activity in Latin America was intra-regional both in terms of value and volume, with Brazil, France and the United States being the top investing countries, while Brazil, Chile and Mexico were the top destination countries. Several large multinational and regional companies expanded their operations to other neighboring countries in the region. Such expansions took the form of (i) new greenfield projects or (ii) mergers & acquisitions (“M&A”) and joint ventures (“JV”), through which regional companies acquired or joined forces with existing national players of each country.

While this growth process accelerated through 2019, the COVID-19 pandemic started in 2020 and impacted the region. The pandemic did not stop this cross-border expansion movement, which tends to continue as the business consolidation model will continue to be a trend in a globalized world. But the pandemic had a negative impact on 2020 figures<sup>4</sup> and certainly posed several business and legal challenges that need to be mitigated or overcome when performing a cross-border M&A transaction. Thus, the object of this article is to analyze the potential challenges and impact resulting from the pandemic in the process of cross-border M&A transactions in the Latin American region.

### Overview

Initially, an M&A process could follow (i) a free negotiation between the parties or (ii) a competitive tender, whose stages are defined in a proper tender notice. A competitive tender normally sets forth its own process and outlines the main milestones and required legal documents. The former, which we will focus on this article, does not follow a strict process (and may vary from deal to deal), but there are some commonly followed steps and documents in international deals that we will address here.

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In brief, the free negotiation process starts with the commercial negotiation phase between the parties. In many cases, this initial step does not involve legal documents or advisers until a certain point where the parties may wish to formalize in writing the potential transaction. In order to formalize the transaction in writing and assure basic commitments among the parties (such as confidentiality or exclusivity), the parties may execute several documents (from simpler Letters of Intent (“LOI”) to more complex sales and purchase agreement (“SPA”) as the negotiations progress. When the main document that will actually formalize the main rights involved (i.e., assets or shares being sold, parties being merged or third parties being incorporated) is signed, we have the “Signing”. Although the deal is signed, it will be effective only after several obligations and conditions precedent are achieved, and it is at that time when the “Closing” of the deal occurs. At this point the deal can be considered completed, but in many cases, the parties will still hold mutual postClosing obligations for the upcoming years. Through all these steps, the pandemic may result in challenges for the parties and their legal advisers.

## Negotiations

Initially, even before moving forward with the legal documents and involving the legal advisers, the current travel restrictions in the Latin American region (and globally) forced all parties to get used to virtual negotiations via new technologies. It certainly provided more speed and represented less costs for this initial stage, but on the other hand it changed several long-term negotiation tactics “at the table”.

In this initial stage of negotiations, besides the oral meetings and informal talks, the parties will eventually start to formalize their intentions in writing. Normally, the initial documents they exchange are LOIs, which are basic documents declaring the preliminary commitment of one party to do business with another. Some LOIs also summarize core business intentions and very basic and fundamental aspects of a potential deal (e.g., price, terms and conditions, deal structure, parties involved, preliminary obligations, process to be followed, timelines, requirements). LOIs could either be preceded, include or be followed by non-disclosure agreements (“NDA”) and no-solicitation provisions, in

order to guarantee the confidentiality of the process. Depending on the complexity of the deal, additional documents could be negotiated and signed by the parties to summarize and reach agreements on fundamental aspects of the deal, before moving forward with the negotiation of the main agreements. Such documents could take the forms of a: (i) term sheet: which consists in an agreement that outlines the basic terms and conditions of a transactional document; (ii) heads of agreement: which is an initial document that establishes the basic framework for a partnership or transaction; or (iii) memorandum of understanding: which is an agreement that expresses a convergence of will between the parties thereto and indicates an intended line of action.

Such initial documents are normally of a non-binding nature, outlining the preliminary understandings between two or more parties, which they intend to later formalize in a legally binding agreement. However, it is important to note that certain Latin American and other international jurisdictions may have a different treatment of their binding or non-binding nature, while in some it can be stated by law, but in others it is not. It is thus always advisable, especially considering that legal counsel is often not involved in the negotiation or drafting of such documents, that such nature and the governing law are expressly established therein.

Before the pandemic, parties used to think more carefully about provisions addressing unforeseen major circumstances, such as *force majeure* (“FM”), when drafting the more complex and main agreements. However, since the pandemic, such provisions must be carefully analyzed and drafted since the initial stages of the deal. One example is clauses addressing any material adverse change (“MAC”) for the deal and the events that would be considered FM events, as well as their respective impacts on the deal. Also it is important to note that Latin American legislations may differ from other international jurisdictions regarding statutory versus contractual provisions related to such events.

If the negotiations progress successfully, a due diligence will be performed by the buyer (or by both parties depending on the nature of the deal). In this stage, an investigation, audit or review of all parties’ documents and information will be performed to confirm facts or

details of the transaction under analysis. During the pandemic, many local authorities of multiple Latin American jurisdictions have their activities reduced to issue only necessary documents, which has been causing frequent delays in due diligence. Before the due diligence, a party may often issue a non-binding offer, which could be confirmed via a further binding offer, after the due diligence is completed.

## Signing

The next stage is that the parties will negotiate the main agreement of the transaction. Its execution by the parties, contractually agreeing with the terms and conditions of the transaction, is considered the "Signing." The type of the main agreement involved will depend on the structure of the deal (purchase of assets, purchase of shares, acquisition, merger, incorporated or unincorporated JV formation, etc.). In practice, most of the M&A deals are actually purchases of assets or shares by party A from party B, rather than technical acquisitions (party A incorporates B) or mergers (parties A and B merge to form C). Thus, sales and purchase agreements (SPAs) are the most common type of main agreement to be signed. Such Signing is normally not yet the completion of the deal, since its effectivity may still be subject to conditions precedent, which are conditions or events that must be achieved in order to bring the agreement into effect.

## Between Signing and Closing

During the stage between Signing and Closing the parties work together in a mutual effort to achieve all the conditions precedent. Some of the conditions precedent depend on (i) unilateral acts of each of the parties; (ii) reaching further agreements by the parties; and/or (iii) third parties, either private (such as contractual consents) or governmental authorities (such as antitrust and regulatory approvals). Thus, this stage deserves special attention during pandemic times, since many of involved governmental authorities in Latin America may have significantly reduced their activities during these times and the respective approval processes may take even longer. When such conditions precedent are achieved, their formal acknowledgment by the parties is considered the

"Closing" and at this point the transaction is considered completed and the eventual transfer of ownership takes place.

## After Closing

When the Closing happens, the deal can generally be considered completed. However, in many cases, the parties will still hold unilateral or mutual post-Closing obligations for the upcoming years. Examples of such pending obligations are, the holding of a certain percentage of the deal price in escrow accounts to guarantee the fulfillment of all obligations and/or to compensate potential breaches and future liabilities (either mapped or not mapped yet in the due diligence). Such outstanding obligations could be not properly or totally not fulfilled as a direct or indirect result of the pandemic. For example, additional payment obligations or unexpected liabilities could be the result of economic effects caused by the pandemic. In such cases, the provisions defined since the beginning of the negotiations, such as MAC and FM could be invoked or challenged by the parties for possible disputes. In such cases, additionally to dealing with the possible different interpretation of such clauses by Latin America courts (e.g., different interpretations in each country in a multi-jurisdiction deal) the parties should be prepared for additional delays from local Latin America courts to resolve the matters or to enforce arbitration decisions.

## Conclusion

The pandemic momentarily reduced the cross-border M&A transactions expansion movement from the last decade, but as soon as the regional Latin American economies begin to recover, it is likely to continue to grow. The pandemic caused several business and legal challenges to cross-border M&A processes, which need to be mitigated or overcome when drafting, negotiating and executing the transactions. In this sense, special attention should be given to MAC- and FM-related clauses. Additionally, it is advisable to clearly define the process to be followed and the establishment of the effects and responsibilities in the deal, in case such hardship circumstances materialize with an eventual

prolongation or worsening of the pandemic. The choice of the governing law of the agreements and the analysis of how such law will interplay with obligations under local laws of the countries where

the targets are located is also crucial to anticipate and predict the legal effects of MAC and FM events in multiple countries of Latin America.

## Endnotes

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- <sup>2</sup> "M&A in Latin America," Deloitte, 2019 – available at: <https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Finance/m-and-a-in-latin-america-14-edition-oct-2019.pdf>
- <sup>3</sup> "Deal Trends in Latin America," S&P Global, 2019 – available at: <https://www.spglobal.com/marketintelligence/en/documents/deal-trends-latin-america-september-2019.pdf>
- <sup>4</sup> "The COVID-19 impact on Latin America's FDI," BNA, 2021 – available at: <https://app.bnamericas.com/article/section/all/content/xmchykveu-spotlight-the-status-of-fdi-across-latin-america-amid-pandemic>

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