

Trends and Developments

Contributed by:

Enrique Tello Hadad, Daniel Domenech Varga, Claudiney Machado and Marcus Luan Silva
Loeser e Hadad Advogados

Loeser e Hadad Advogados was founded in 1989, and the firm now has offices in São Paulo, Campinas, Rio de Janeiro and Brasília. It focuses on business law, particularly corporate, M&A, corporate governance, regulatory, compliance, privacy and data protection, and tax matters. The corporate department, which includes four partners and 16 associates, provides the full gamut of business law advice covering issues such as business implementation, corporate governance, compliance, restructuring, IPO-related matters, divestments, and M&A, including legal due diligence and post-closing advice.

Clients include both buyers and sellers from a wide range of sectors, both regulated and non-regulated, private and publicly held, including banking, private equity, food and beverage, retail, automotive, medical devices, life sciences, energy and real estate. The firm also applies digital up-skilling programmes to all its professionals, from law clerks to partners, and uses cutting-edge technology, including AI tools, to bring the utmost digital experience to its clients and allow more efficient deliverables and attractive costs.

Authors



Enrique Tello Hadad is the managing partner of Loeser e Hadad Advogados and co-ordinates the international transactions practice group, including the corporate and M&A areas. He has extensive corporate law expertise and is highly experienced in the full range of corporate issues, such as restructuring transactions, governance and compliance matters, in addition to M&A legal support. With a strong track record of successful M&A and corporate transactions and recognition from clients for strategic and practical legal advice, Enrique has been a leading partner in corporate transactions in a wide array of business sectors including in the oil and gas and chemicals sectors.



Daniel Domenech Varga has 15 years of experience in corporate law. He has received attention and recognition for his competence, dedication and success in the projects in which he has been involved. He has managed, national and international mergers and acquisitions in the chemicals, health, food, and beverage industries.

BRAZIL TRENDS AND DEVELOPMENTS

Contributed by: Enrique Tello Hadad, Daniel Domenech Varga, Claudiney Machado and Marcus Luan Silva, Loeser e Hadad Advogados



Claudiney Machado is a senior associate at Loeser e Hadad Advogados with a background in the firm's corporate practice and over five years of post-qualification experience. He has

experience in corporate law and investment funds, with emphasis on the structuring and incorporation of liquid and illiquid investment funds. He also possesses expertise in corporate structuring and restructuring and general business law.



Marcus Luan Silva is a junior associate at Loeser e Hadad Advogados with over a year of post-qualification experience. His works has included

experience with M&A, corporate law and contracts. He works on matters related to corporate restructuring and general business law.

Loeser e Hadad Advogados

Torre Milano - Av. Francisco Matarazzo
1400 - 15º andar - Água Branca
São Paulo - SP, 05001-903
Brazil

Tel: +55 11 98178 7997
Email: enrique.hadad@lhlaw.com.br
Web: www.lhlaw.com.br



LOESER
HADAD
ADVOGADOS

BRAZIL TRENDS AND DEVELOPMENTS

Contributed by: Enrique Tello Hadad, Daniel Domenech Varga, Claudiney Machado and Marcus Luan Silva, Loeser e Hadad Advogados

Over the last few years, Brazil has experienced noticeable growth in shareholders' awareness of, and active involvement in, corporate governance matters, reflecting a broader global surge in shareholder activism. This article provides:

- an examination of Brazil's evolving shareholders' rights and activism landscape;
- an analysis of the legal framework governing shareholder rights;
- an inventory of the tools available to shareholders; and
- a breakdown of the defensive strategies adopted by companies to address these developments.

Furthermore, it delves into the complexities of the Brazilian regulatory environment, shedding light on how companies and investors are navigating and adapting to these evolving regulatory changes.

The Legal Framework for Shareholders' Rights in Brazil

The rights of shareholders in Brazil are primarily regulated by two key pieces of legislation: the Brazilian Civil Code (Law No 10,406 of 2002) and the Brazilian Corporation Law (Law No 6,404 of 1976). These laws collectively provide a comprehensive framework that governs the operations of both public and private companies in Brazil. They outline a wide range of rights and obligations for shareholders, including voting rights, dividend entitlements and protection against unfair treatment. Additionally, these laws emphasise the importance of transparency and fairness in corporate governance, aiming to foster a robust and ethical business environment.

Under this legal framework, shareholders are granted a range of fundamental rights essential for their participation in the company's govern-

ance. Among these are the rights to vote at general meetings, receive dividends, and oversee management actions. The right to vote is particularly significant, as it allows shareholders to influence critical corporate decisions, such as the election of board members, the approval of financial statements, and decisions regarding mergers and acquisitions. By exercising their voting rights, shareholders can play a crucial role in shaping the company's strategic direction and safeguarding their financial interests.

In Brazil, the protection of minority shareholders' rights is crucial due to the prevalence of concentrated ownership structures in many Brazilian companies. This ownership dynamic often places minority shareholders at a disadvantage compared to controlling shareholders. In response to this challenge, Brazilian legislation has established specific mechanisms aimed at safeguarding the interests of minority shareholders. One prominent mechanism is the "tag along" right, which grants minority shareholders of publicly traded corporations the right to sell their shares, at a minimum price of at least 80% of the price paid to the exiting majority shareholder, in the event of a change in company control.

In addition to the tag along right, minority shareholders in Brazil can initiate legal actions to defend their individual or collective rights. For instance, shareholders can file liability actions against directors who act in a manner detrimental to the company's interests. This legal recourse provides an essential avenue for minority shareholders to hold management accountable and protect the value of their investments.

The Rise of Shareholder Activism in Brazil

Although shareholder activism is still in its early stages in Brazil compared to more mature markets such as the United States, it has gained sig-

BRAZIL TRENDS AND DEVELOPMENTS

Contributed by: Enrique Tello Hadad, Daniel Domenech Varga, Claudiney Machado and Marcus Luan Silva, Loeser e Hadad Advogados

nificant traction in recent years. This increase in activism is also driven by a growing awareness of environmental, social, and governance (ESG) issues, which have become increasingly important to investors worldwide. In Brazil, shareholders use their influence to pressure companies to adopt more sustainable and transparent practices. Through engagement with companies and voting on shareholder resolutions, they are contributing to a broader movement towards responsible corporate governance. This trend reflects a shift in investor priorities and a recognition of the importance of sustainable and ethical business practices.

Characteristics of Shareholder Activism in Brazil

In Brazil, shareholder activism takes various forms, such as participating in general meetings and organising public campaigns to influence company management. Activist shareholders often aim to bring about strategic changes within the company, such as replacing board members, re-evaluating executive compensation policies, or adopting more rigorous corporate social responsibility practices.

A recent example of shareholder activism in Brazil is the pressure exerted by institutional investors on large companies to adopt more transparent policies regarding their carbon emissions and other environmental impacts. This type of activism, often led by investment funds with a clear sustainability agenda, has significantly changed how Brazilian companies approach their ESG responsibilities. In many cases, these changes have been implemented in response to direct shareholder pressure, highlighting the growing influence of activism on the Brazilian corporate landscape.

Comparative Analysis: Brazil vs Other Markets

While shareholder activism is increasing in Brazil, it still faces significant challenges, especially when compared to more developed markets such as the United States. In the USA, shareholder activism is a well-established practice, with major hedge funds and other institutional investors frequently spearheading campaigns to influence company management. These efforts often succeed in bringing about changes in corporate strategy, governance and operations.

In contrast, the corporate culture in Brazil remains relatively conservative, characterised by traditional business practices and decision-making processes. Shareholders, particularly those holding minority stakes, encounter substantial hurdles when attempting to exert significant influence within companies. This is primarily due to the prevalent concentrated ownership structure, where a small number of large controlling blocks hold substantial sway over corporate decision-making. As a result, minority shareholders often find it challenging to form alliances and coalitions, impeding their ability to effectively launch activist campaigns and drive meaningful change within the companies in which they have invested.

Despite these challenges, there are signs that shareholder activism in Brazil is on the rise. The increasing importance of ESG practices, coupled with pressure from international investors, is driving a shift in the Brazilian corporate landscape. As more companies recognise the value of engaging with their shareholders and addressing their concerns, shareholder activism will likely become a more prominent feature of the Brazilian market.

BRAZIL TRENDS AND DEVELOPMENTS

Contributed by: Enrique Tello Hadad, Daniel Domenech Varga, Claudiney Machado and Marcus Luan Silva, Loeser e Hadad Advogados

Tools and Strategies for Shareholder Activism

In order for shareholders to effectively engage in activism, it is crucial for them to have a comprehensive understanding of the legal tools and strategies available to them in Brazil. The country's corporate governance framework offers a range of mechanisms that empower shareholders to influence corporate decisions. These mechanisms include, but are not limited to, voting rights, shareholder resolutions, and engagement with company management. However, it is important to note that the effectiveness of these tools can be influenced by factors such as the extent of shareholding, the level of support from other investors, and the regulatory environment. Therefore, shareholders must carefully assess these factors when considering their activist initiatives in the Brazilian market.

Suggesting actions at general meetings

One of the key methods employed by shareholders in Brazil to advocate for their interests is to suggest actions or resolutions during general meetings. This avenue is open to any shareholder, provided they adhere to the deadlines and requirements outlined by the law and the company's by-laws. This mechanism proves to be especially beneficial for minority shareholders who aim to highlight concerns that may not be prioritised by the management.

For instance, shareholders who are focused on enhancing corporate governance may introduce resolutions aimed at implementing more stringent transparency policies or re-evaluating executive compensation practices. Even if these proposals do not receive approval, they can exert pressure on the management and bring crucial issues to the attention of fellow shareholders. This form of activism can be particularly potent in its ability to shed light on governance

issues and to compel companies to re-evaluate their practices.

Calling extraordinary general meetings

Shareholders who own at least 5% of a company's share capital are entitled to exercise their right to request the convening of an extraordinary general meeting (EGM). This meeting allows them to address specific issues that they believe require urgent attention or are not being adequately handled by the company's management. The EGM serves as a powerful tool for shareholders to voice their concerns and take action when they feel that the company's best interests are at stake.

One common scenario where this right is exercised is when activist shareholders use the EGM to advocate for the replacement of certain board members or to vote on a merger proposal that they deem unfavourable. By leveraging the EGM mechanism, shareholders can exert significant pressure on the management and influence decision-making in a manner that aligns with their interests, ultimately bringing about changes they believe are necessary for the company's welfare.

Proxy voting

Recent legislative changes and regulatory developments that may encourage shareholder activism include proxy voting. The Brazilian Securities and Exchange Commission (*Comissão de Valores Mobiliários*, or CVM) has implemented regulations facilitating proxy voting, making it easier for shareholders who cannot attend in-person meetings to participate and vote.

Regulatory Challenges and the Need for Reform

Despite the escalating prevalence of shareholder activism in Brazil, activists encounter substantial

BRAZIL TRENDS AND DEVELOPMENTS

Contributed by: Enrique Tello Hadad, Daniel Domenech Varga, Claudiney Machado and Marcus Luan Silva, Loeser e Hadad Advogados

regulatory challenges. While Brazilian legislation has made significant advances in some areas, it still imposes barriers that impede the full exercise of shareholder rights, particularly for minority shareholders.

Costs and complexity of activist campaigns

One of the main challenges faced by activist shareholders in Brazil relates to the high cost and intricate nature of organising impactful campaigns. The country's legislation imposes a series of formal requirements for proposing actions and convening meetings, which can be overwhelming for small investors or groups with limited resources. Additionally, navigating the intricate web of legislation and corporate mechanisms demands a profound level of understanding, presenting a significant barrier, particularly in a country where financial education and investor participation culture are still developing.

Furthermore, many shareholders, especially minority ones, may find themselves lacking access to the necessary resources or knowledge to effectively mobilise campaigns. This restriction significantly diminishes the potential for activism in Brazil, as shareholders might be deterred from pursuing their objectives due to the perceived difficulty and expense associated with initiating a campaign.

Concentrated ownership structure

The structure of concentrated ownership in Brazil, characterised by the prevalence of large controlling blocks, poses a significant obstacle to shareholder activism. Within many Brazilian companies, controlling shareholders possess a substantial stake that affords them significant sway in corporate decision-making, thereby creating barriers for minority shareholders seeking to exercise influence. Consequently, the concentrated power held by controlling shareholders

can curtail the efficacy of activist campaigns, as they have the ability to dismiss proposals and resolutions put forth by minority shareholders.

However, in instances where the interests of controlling shareholders align with those of activists, or when there is substantial pressure from institutional or international investors, shareholder activism can wield greater influence. For example, if controlling shareholders acknowledge the long-term advantages of embracing ESG practices, they may demonstrate a greater willingness to entertain activist demands, ultimately leading to positive changes within the company.

Need for legal reforms

To overcome these challenges, it is essential that Brazil continues to promote legal reforms that facilitate shareholder activism and strengthen the protection of minority shareholders, such as the potential reduction of the shareholding thresholds required to propose meetings or measures. This adjustment would effectively empower minority shareholders, making it more feasible to exercise their rights and influence corporate decisions. By lowering these thresholds, a broader spectrum of shareholders would be empowered to actively participate in corporate governance, ultimately bolstering management oversight.

Another example of a significant reform entails streamlining the processes for obtaining corporate information. Implementing measures that enable shareholders to access necessary information swiftly and easily will allow these reforms to facilitate more informed decision-making and increase shareholder activism. Moreover, advocating for greater transparency in corporate operations and governance would break down barriers to active shareholder participation, ensuring that every shareholder, irrespec-

BRAZIL TRENDS AND DEVELOPMENTS

Contributed by: Enrique Tello Hadad, Daniel Domenech Varga, Claudiney Machado and Marcus Luan Silva, Loeser e Hadad Advogados

tive of their stake, has the opportunity to contribute meaningfully to the company's strategic direction. This commitment to transparency and open communication bolsters shareholder trust and engagement, fostering a more inclusive and accountable corporate environment.

Corporate Defence Mechanisms

As shareholder activism becomes more prevalent in Brazil, companies are developing strategies to protect themselves against activist campaigns. These strategies range from preventive measures to reactive responses, depending on the nature of the activist campaign and the interests at stake.

Governance shielding

One of the frequently employed corporate strategies is referred to as "governance shielding" and encompasses the inclusion of specific clauses in the company's by-laws. These clauses are intended to restrict the voting power of shareholders and establish additional conditions for the approval of certain measures. By doing so, companies seek to prevent minority shareholders from exerting influence without majority shareholder support.

Despite its widespread use, governance shielding has been subject to criticism. Many argue that it can perpetuate poor governance practices and serve as a safeguard for existing management against legitimate challenges. Therefore, it is important for companies to navigate a delicate balance, ensuring protection against activist interference while upholding transparent and responsive corporate governance principles. It is incumbent upon companies to carefully monitor governance shielding to avoid its potential misuse as a means of increasing management authority to the detriment of shareholder rights.

Active dialogue with shareholders

Another fundamental strategy for companies is maintaining an active and ongoing dialogue with their shareholders. This involves responding to shareholders' concerns during general meetings and proactively engaging throughout the year, seeking to understand investors' expectations, and adjusting corporate practices as necessary.

By maintaining open lines of communication with shareholders, companies can anticipate and mitigate potential activist movements before they become public. This proactive engagement can reduce the risk of confrontations damaging the company's reputation and value. Moreover, by building trust with their shareholders, companies can secure their support during times of crisis, ensuring that they have the backing of their investors when faced with challenging decisions.

Reactive responses to activist campaigns

When an activist campaign is already underway, companies need to be able to respond effectively. This may involve a variety of strategies, from direct negotiation with the activists to mobilising support among other shareholders to defeat activist proposals.

In some cases, it may be prudent for the company to consider embracing some of the demands put forth by the activists, particularly if these demands are poised to yield long-term benefits for the company. For example, if activists advocate for enhanced transparency or better ESG practices, aligning with these requests can strengthen the company's corporate reputation and appeal to a broader investor base.

In other cases, companies may need to adopt a more defensive stance, using all available legal tools to resist the proposed changes. This could

BRAZIL TRENDS AND DEVELOPMENTS

Contributed by: Enrique Tello Hadad, Daniel Domenech Varga, Claudiney Machado and Marcus Luan Silva, Loeser e Hadad Advogados

involve challenging the legality of the activists' proposals or rallying support from other shareholders to oppose the activists' agenda. Ultimately, the effectiveness of the company's response will depend on its ability to navigate the complex dynamics of shareholder activism and align its strategy with the long-term interests of all shareholders.

Conclusion

Shareholder activism in Brazil has experienced notable growth, which aligns with the global trend of increased investor participation in corporate governance. Although the country still faces regulatory and cultural hurdles, the legal frameworks currently in place and a dynamic governance environment suggest a promising future for advancing shareholders' rights in Brazil. This trend reflects a broader movement towards greater shareholder empowerment and influence on corporate decision-making processes.

In light of the rapidly changing business landscape, companies must adjust to this new reality by implementing defensive strategies and actively engaging with shareholders. The ability to navigate this increasingly dynamic and competitive environment will ensure their resilience and success. Moreover, as shareholder activism advances, the future of corporate governance in Brazil will hinge on the collaborative efforts of shareholders and companies in establishing sustainable value. This will necessitate a delicate balance between all parties' short- and long-term interests.

This collaborative approach, supported by ongoing legal reforms and a commitment to transparency, will be key to fostering a robust and vibrant corporate governance landscape in Brazil. The continued growth of shareholder activism, coupled with these legal reforms, will not only enhance the accountability of companies but also contribute to the broader development of the Brazilian capital market.