Global Private M&A Guide - Limited External Content - Brazil

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*This content was last reviewed around October 2023. Note: Given the significance of an indirect tax reform introduced via an amendment to the Brazilian Constitution on 16 December 2023, a brief summary of that reform has been included.*

# Quick reference guide

## Due diligence, pricing and closing

**Typical due diligence issues**

In Brazil, it is customary to finalize the due diligence before the execution of the acquisition agreement. Nevertheless, in some cases, the parties may agree that further confirmatory due diligence regarding certain aspects of the target company will be a condition precedent to closing (e.g., completion of phase two environmental due diligence).

The main areas of concern in the due diligence process vary from project to project. Compliance, environmental, regulatory, labor and tax issues are always in the spotlight of any legal due diligence work. In Brazil, due diligence does not trigger obligations to report any issues found to regulators, except for certain environmental aspects.

Based on the due diligence findings, the parties may negotiate special closing conditions. An escrow account to deposit part of the purchase price to guarantee the seller's indemnification obligations may be opened, or the purchase price may be reduced.

**Pricing and payment**

In a share deal, it is not legally required to have an independent appraisal report to support the valuation of the target company. However, if the buyer intends to benefit from the tax amortization of the goodwill paid in the transaction, the buyer will need an appraisal to support the purchase price, and certain other conditions must be observed. In this context, "goodwill" means the difference between the acquisition price and the book value of the shares acquired in the target company. As an example, to benefit from the tax amortization of the goodwill paid in the transaction, the acquisition must be made through a company organized in Brazil, and a subsequent reorganization of the acquisition vehicle/buyer and the target company must occur via a downstream or upstream merger.

In the case of an asset deal, there is no need to have an independent appraisal to support the valuation of the assets.

If the seller is Brazilian, the purchase price payment must be made in Brazil, even if the buyer is not Brazilian. The purchase price can be remitted in foreign currency to the seller's bank account in Brazil, and the seller will be responsible for converting it into Brazilian currency. A financial tax (Imposto sobre Operações Financeiras - IOF) at the rate of 0.38% will be due upon the conversion. Every time there is a foreign party involved in a share deal as either the buyer or seller and the transaction involves an amount equal to USD 100,000 or more (or the equivalent in other currencies), the Brazilian target will need to register the transaction with the Central Bank of Brazil (BACEN), as described in detail below.

**Signing/closing**

*Share sale*

Apart from a merger control filing (as described below) and for approvals related to specific regulated industries (e.g., energy or telecom companies, financial institutions and insurance companies), government approval is not required as a condition to closing, and a simultaneous signing and closing is possible.

Closing conditions will also depend on the issues raised during the due diligence exercise and on the commercial conditions agreed between the parties to complete the transaction (e.g., repayment of intercompany loans, and obtaining approval from suppliers or creditors).

*Asset sale*

Unless the foreign buyer already has an existing entity with the requisite business scope and licenses in Brazil to acquire and operate the assets, there will normally be a gap between signing and closing.

If an existing Brazilian subsidiary of the foreign buyer acts as the asset buyer, it is necessary to ensure that its business scope is broad enough to cover the acquired business post-closing and that it has the required licenses and registrations. An amendment to the business scope may be implemented through an amendment to the articles of association or a shareholders' meeting approving an amendment to the bylaws. Both the amendment to the articles and the bylaws must be registered with the competent state commercial registry. The buyer may also need to establish additional branches to operate the business if the acquired business is in a different location from where the subsidiary is registered.

If the foreign buyer does not have an existing subsidiary or affiliate located in Brazil, the buyer will need to take all the measures required to organize a company in Brazil by obtaining the licenses and registrations needed to receive the business/assets to be acquired and, afterward, transfer the assets under the asset sale. Establishing an entity may take approximately one month to complete. This timeline may be extended to several months where specific licenses are required, as is the case for manufacturing.

In multijurisdictional transactions, a local asset sale/transfer agreement is needed to comply with local requirements, especially to allocate the purchase price among the assets being transferred in Brazil.

## Approvals/registrations

**Foreign investment restrictions**

There is no national foreign investment review (FIR) law in place in Brazil.

However, there are sectoral foreign investment licensing regimes that apply to certain investments relating to nuclear power, the aerospace industry, telecommunications, financial institutions, healthcare, insurance, media, mail and telegraph services, mineral resource prospecting and mining in border areas, the acquisition or rental of rural property, and the exploitation of Brazil's border areas. In addition, foreign direct investment and external credit operations are required to be registered with the Central Bank of Brazil.

**Antitrust/merger control**

Brazil has a mandatory pre-merger and suspensory merger control regime, which means that transactions that meet the relevant turnover thresholds are met need to be notified to the competition authority and cleared before they can be completed. A change of control is not a requirement for a transaction to be considered subject to the mandatory merger control process. The thresholds for mandatory filing are: (i) the transaction must generate at least potential effects in Brazil; and (ii) the parties' economic group must meet the revenue criteria. Nonetheless, the Brazilian Administrative Council for Economic Defense (CADE) can request the notification of any transaction that does not meet the thresholds for up to one year after closing, with powers to order divestitures. For further information, see the more detailed section on "Antitrust/merger control".

**Other regulatory or government approvals**

*Foreign exchange controls*

Since the unification of the free rate and the floating rate exchange markets in March 2005, the Brazilian government, through the Brazilian Monetary Council (CMN) and BACEN, has introduced rules to make the currency exchange market simpler and the controls over the market more flexible. Notwithstanding that simplification, Brazilian foreign exchange control rules require that foreign investments in Brazilian companies are registered with BACEN to enable the following:

The remittance of profits and/or interest on equity (juros sobre capital próprio) to foreign investors

The repatriation of foreign capital invested in Brazil

The reinvestment of profit and/or interest on equity. For this purpose, both the foreign investor and the Brazilian company are required to register with BACEN.

On 31 December 2022, the BACEN issued a new regulation (Resolution 278) establishing a minimum amount for transactions to be registered, establishing that investments equal to USD 100,000 or more (or its equivalent in other currencies) are required to be registered with the BACEN. It is no longer mandatory to register foreign investments below that threshold. However, it is still advisable to voluntarily register investments below USD 100,000 for corporate tracking records.

It is the responsibility of the Brazilian company in which the foreign investment is made (the target company) to register the foreign investment with the declaratory system of BACEN within 30 days from the date that the investment is made. The target company may be subject to fines for late registration, or failing to register.

## Tax

There is no stamp duty in Brazil.

For Brazilian corporate sellers, capital gains form part of their taxable income. They will be subject to corporate income taxes (CIT) — Imposto de Renda sobre Pessoa Jurídica (IRPJ)  and Contribuição Social sobre o Lucro Líquido (CSLL) at a combined rate of 34%. Higher combined rates apply to financial institutions.

For Brazilian individuals, capital gains will be subject to income tax at progressive rates ranging from 15% to 22.5%, depending on the gains.

For foreign sellers of shares (both individuals and entities), capital gains will also be subject to income tax at the progressive 15% to 22.5% rates, unless the foreign seller is domiciled in a jurisdiction defined by Brazilian tax rules as a low-tax jurisdiction, in which case a 25% flat rate will apply.

For cross-border remittances of the purchase price, a 0.38% financial tax (Imposto sobre Operações Financeiras) will apply on the exchange transaction performed to remit or receive the purchase price to or from abroad.

**OECD's Two Pillar Solution**

The OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting has put forward a so-called Two-Pillar Solution to address the tax challenges arising from the digitalization of the economy. Pillar Two is intended to introduce a global minimum effective rate of tax of 15% for large businesses in each jurisdiction where they operate and will lead to fundamental changes in the international tax system. It is currently being implemented in a large number of jurisdictions.

Groups will need to consider how the Pillar Two rules could impact on the life cycle of M&A transactions from the pre-acquisition phase (including transaction planning (such as the choice of acquisition structure and financing) and due diligence of the target group), the acquisition phase (such as contractual risk allocation around Pillar Two) to the post-acquisition phase and the impact of Pillar Two on any post-acquisition integration.

## Post-acquisition integration

For information on post-acquisition integration matters, please see our [Post-acquisition Integration Handbook](https://www.bakermckenzie.com/en/insight/publications/resources/post-acquisition-integration-2023).

# Common deal structures

## What are the key private M&A deal structures?

The acquisition of a business may be achieved by purchasing the shares of the company that operates the business or the assets and liabilities of the business. Share acquisitions are more common than asset acquisitions in Brazil, as they are less burdensome from a bureaucratic point of view and, depending on the circumstances, may be more tax-efficient. Each type of acquisition has its advantages and disadvantages. The choice of structure will largely depend on the circumstances of the transaction and, in particular, the parties' tax considerations.

The acquisition of a company or business in Brazil does not require government consent, except for merger control approval if the parties' gross annual turnover is above antitrust thresholds or where the transactions involve regulated activities controlled by the government. Nevertheless, the transaction may trigger the application of various laws and rules to protect the rights of parties or persons.

Auction processes in Brazil are quite common, usually preceded by bid process letters. Usually, the negotiations start with a letter of intent and bids are issued as nonbinding offers. However, bid letters may be binding depending on the process, particularly in the final offer stage of the process.

Scheme of arrangement procedures are not addressed in the Brazilian legal framework.

In Brazil, the following types of mergers are available: (i) horizontal; (ii) vertical; (iii) market extension; (iv)product extension; and (v) conglomeration. In general, the most common types of mergers in Brazil are vertical mergers in which two or more companies operating in the same supply chain merge.

## Which entity is likely to be the target company (on a share sale) or the seller (on an asset sale)?

A Sociedade Limitada (Ltda) is generally considered a more flexible form of a limited liability company. A Sociedade Anônima (SA) is another common form of private company.

## What are the different types of limited liability companies?

The two most common types of limited liability companies are the following:

SA, a limited liability corporation

Ltda, a more flexible form of a limited liability company

These types of companies are the most popular with nonresident investors in Brazil. A new rule was recently enacted authorizing Ltdas to have only one owner.

In an SA, shareholders' liability is limited to the amount of capital invested by each shareholder. This type of corporation may be closely held (capital fechado) or publicly held (capital aberto).

An SA must have at least two shareholders, except in a few situations in which it can be wholly owned. The shareholders may be entities or individuals.

There are no residency or nationality requirements for the owners of Ltdas and SAs; however, if they are not a Brazilian resident, they must appoint an attorney-in-fact resident in Brazil vested with powers to receive court summons on its behalf.

At least 10% of the stated capital of the SA must be paid up in cash at the time of the SA's incorporation. No minimum capital is required except to carry out certain regulated activities, e.g., banking, insurance and trading companies. The capital of the SA is divided into shares. According to the rights attributed to their holders, the shares may also be qualified as ordinary or preferred.

Organizing a Ltda may be more flexible since: (i) it involves lower costs, in both organization and management; (ii) its articles of organization may be amended by a simple document executed by the company's partners or their attorneys-in-fact, and the publication of the amendment in the official gazette and newspaper is not required; (iii) no stock certificates or corporate book, such as share registration, share transfer book, shareholders' and board meeting's minute books, are required; and (iv) Ltdas are now allowed to have a single quota holder. In a Ltda, all corporate information is addressed in its articles of organization. For this reason, the Ltda's structure is often used to incorporate wholly owned subsidiaries (including purchase vehicles for local acquisitions) in Brazil. The liability of quota holders is also limited to the amount of the capital invested by each quota holder, but if the capital is not fully paid in, quota holders are liable for the payment of the full amount of the company's capital.

## Is there a restriction on shareholder numbers?

Ltdas in Brazil can only have one owner. An SA must have at least two shareholders (except in a few situations it can be wholly owned).

## What are the key features of a share sale and purchase?

From a transactional point of view, a share (or quota) transaction is much simpler and involves less documentation than an asset transaction. No individual transfers of title to the company's assets and inventory are required, and no cumbersome formalities need to be observed. Normally, public licenses and permits are not affected by a change in the control of the target company. Generally, unless a contract or agreement expressly requires prior consent before the transfer of control (common in contracts with the public sector, but not necessarily an obstacle), the company's rights and obligations under its contracts and agreements are not affected. A share acquisition also offers more flexibility in terms of tax planning.

## What are the key features of an asset sale and purchase?

Asset acquisitions tend to be much more complicated than share acquisitions, as each asset and liability to be included in the sale has to be identified and transferred, individually or by legal category (e.g., each equipment and inventory item must be described, valued and quantified in the transfer invoices to be delivered by the seller to buyer). In some cases, the issuance of these transfer invoices may trigger transfer taxes. The title to real properties is transferred through the registration of deeds that trigger the payment of tax and notarial fees.

The parties do not need to transfer the whole business and are generally free to select the assets and liabilities they wish to transfer. The buyer is generally liable only for obligations acquired, which the buyer assumes expressly in the purchase agreement. There are, however, certain exceptions where the buyer assumes certain liabilities of the seller by operation of law, e.g., tax, labor and environmental liabilities. This risk of inheriting hidden liabilities and the time-consuming procedural requirements tends to dissuade some buyers from electing asset deals as an acquisition vehicle in Brazil.

Some public licenses and governmental permits may not be transferred along with the business, in which case the buyer must apply for a new one. Buyers should therefore obtain all of the necessary governmental licenses before the completion of an asset deal to avoid any interruption to business and the risk of incurring penalties.

# Preliminary documents

## Is it customary to prepare a letter of intent or term sheet and, if so, to what extent are they binding on both parties?

Parties in a negotiation typically start with a letter of intent or term sheet. Although in many cases, buyers may proceed in negotiations with sellers using such letters of intent (stipulating only a few provisions that are intended to be legally binding like confidentiality and exclusivity), under Brazilian law, these pre-contractual letters will not necessarily have a legal effect because whether or not a letter will create legal obligations depends on the substance of what is said and not on its format. If the letter of intent has the same basic elements of the definitive agreement, such as the target company and the price, there is a risk that the letter of intent may be deemed to be binding.

## Does a term sheet, in this context, customarily include provisions on exclusivity, break fee or confidentiality?

**Exclusivity:** Where letters of intent and term sheets have been prepared, it is fairly common to include binding provisions on exclusivity.

**Break fee:** Break fees are rarely used.

**Confidentiality:** Where letters of intent and term sheets have been prepared, it is common to include binding provisions on confidentiality.

## Are exclusivity, break fee and confidentiality provisions supplemented with separately negotiated agreements?

It is very common to negotiate separate confidentiality agreements or non-disclosure agreements. It is less common to negotiate separate exclusivity agreements because exclusivity provisions are more often included in letters of intent or term sheets.

## Is there a duty or obligation to negotiate in good faith?

Under Brazilian law, the parties are deemed to act in good faith. Therefore, if the letter of intent has the same basic elements of the definitive agreements, such as the target company and the price, there is a risk that the letter of intent is deemed to be binding. In this event, if one of the parties walks away from the deal, the other party can claim damages. The best way to address that is to expressly set forth in the letter of intent whether or not the parties are bound to close the deal or if it is just an initial step for further negotiations. In these situations, it is common to address this concern by including break-up fees as part of the terms of the letter of intent, with those break-up fees prevailing over any damages claim.

# Agreeing to the acquisition agreement → Purchase price

## Is a purchase price adjustment common?

Frequency/market practice: Purchase price adjustments are common and may even be negotiated when signing and closing are simultaneous, because of the length of time that may elapse from the date of the base balance sheet for valuation purposes and the actual closing.

## What type of purchase price adjustment is common (e.g., debt-free, cash-free)?

Frequency/market practice: Different price adjustments are seen, including cash-free debt-free, working capital and net asset value adjustments.

## Is there a collar on the purchase price adjustment?

Frequency/market practice: Rarely; collars are not common, but not unheard of either.

## Who usually prepares the closing balance sheet (where applicable)?

Frequency/market practice: This is usually prepared shortly after the transaction closing by the buyer or an independent appraiser appointed by the buyer.

## Is the balance sheet audited (where applicable)?

Frequency/market practice: Rarely; except for listed companies, large-scale companies (entities or a group of entities under common control with assets higher than BRL 240 million in the latest fiscal year or annual gross earnings higher than BRL 300 million), multinational subsidiaries or entities involved in activities regulated by the government, most Brazilian companies are not audited.

## Is an earn-out common?

Frequency/market practice: Earn-outs are fairly common, especially in transactions:

Where the sellers continue to manage the target company after closing

In private equity transactions

If a future renewal of a relevant license or a concession is not certain

If there is a future commercial operation date

If the target needs to achieve a certain financial goal in the future.

## Is a deposit common?

Frequency/market practice: Rarely

## Is an escrow common?

Frequency/market practice: Escrows are very common. The escrow account is the most common guarantee in private M&A transactions involving a Brazilian target business, even if an escrow account can only be maintained with financial institutions that charge fees for their services. In Brazil, it is quite common to have escrow funds applied in interest-bearing financial applications.

## Is a break fee common?

Frequency/market practice: Rarely

# Agreeing to the acquisition agreement → Conditions precedent

## Express Material Adverse Event (MAE) closing condition?

Frequency/market practice: Fairly common; however, it is also common to have transactions where signing and closing are simultaneous without condition.

## Is the MAE general or specific?

Frequency/market practice: Both are seen. Sellers usually demand it to be specific.

## Is the MAE quantified?

Frequency/market practice: Common regarding the financial impact.

# Agreeing to the acquisition agreement → Covenants

## Is a noncompete common?

Frequency/market practice: It is common for a maximum term of five years with a clear definition of the applicable territory. Noncompetes are also foreseen by law. For enforceability, it must be expressly provided that the party bound by the noncompete receives compensation.

## Is it common to use waterfall or blue pencil methods to interpret contractual provisions?

Frequency/market practice: Waterfall and blue pencil provisions are not common.

## Are nonsolicitation provisions (of employees) common?

Frequency/market practice: Fairly common.

## Are nonsolicitation provisions (of customers) common?

Frequency/market practice: Fairly common; combined with noncompete.

## Are seller restrictions usually imposed on the target business between signing the purchase agreement and closing?

Frequency/market practice: Fairly common.

## Is there broad access to books, records and management between signing and closing?

Frequency/market practice: Fairly common.

## Is it common to update warranty disclosure or notify of possible breach?

Frequency/market practice: Fairly common; updating schedules is common, as is the insertion of a clause requesting the seller to notify the buyer of a possible breach. This may trigger termination or price adjustment.

# Agreeing to the acquisition agreement → Representations and warranties

## Materiality in representations — how is it quantified (e.g., by a USD amount)?

Frequency/market practice: Materiality qualifiers are common, but are often not quantified (other than specific warranties, e.g., contract value).

## How is knowledge qualified (e.g., specific people, actual/constructive knowledge)?

Frequency/market practice: Knowledge qualifiers are increasingly common, usually including actual knowledge or matters that should have been known upon due inquiry. Listing individuals and corporate positions is not common.

## Is a warranty that there is no materially misleading/omitted information common?

Frequency/market practice: Fairly common.

## Is disclosure of the data room common?

Frequency/market practice: Usually, disclosure of the data room is not accepted as a liability limitation.

# Agreeing to the acquisition agreement → Repetition of representations and warranties

## Is it common to repeat warranties at closing?

Frequency/market practice: Fairly common; in some cases, the parties execute a closing memorandum or similar document addressing any amendments in the warranties and confirming those that have not suffered any changes.

## Is it common to repeat warranties at all times between signing and closing?

Frequency/market practice: It is common to have a statement in the R&W section saying that the warranties are true for signing and will continue to be for closing.

## Is a bring-down certificate at closing common?

Frequency/market practice: Fairly common.

## What is the applicable repetition standard, e.g., true in all material respects or Material Adverse Effect?

Frequency/market practice: Both are seen separately but usually true and accurate in all material aspects.

## Is double materiality common (a materiality qualification in bring-down at closing and in representation(s))?

Frequency/market practice: Rarely; double materiality is usually avoided.

# Agreeing to the acquisition agreement → Limitations on liability

## What is the common cap amount (as a percentage of purchase price)?

Frequency/market practice: The buyer often starts negotiations by asking for a cap of 100% of the purchase price, but the seller tends to negotiate to decrease the percentage and a common ground is generally reached (taking account of the due diligence findings and potential exposure provided by the auditors). Some obligations, such as noncompete, may have a higher cap, depending on the size of the deal. Lower caps may be negotiated. In infrastructure projects, the cap is usually between 10-20% of the purchase price.

## Does the cap (and other liability limitations) apply to the whole agreement or just warranties (or particular terms)?

Frequency/market practice: Usually, the cap applies to all obligations of the agreement, except for certain obligations that may be excluded, depending on the amount of the deal, e.g., noncompete or confidentiality obligations.

## What are the common exceptions to the cap?

Frequency/market practice: This depends on the size of the deal and noncompete/non-disclosure provisions, breach of fundamental reps and warranties, and breach of compliance law.

## Is a deductible or basket common?

Frequency/market practice: Both are common; it varies from case to case.

## Is a de minimis common?

Frequency/market practice: Fairly common; it varies from case to case.

## How long does seller liability survive?

Frequency/market practice: It usually survives for five years, in line with the statute of limitation for tax (which is usually increased to six years) and labor liabilities. However, a reduced period is sometimes seen.

## Are there any common carve-outs from limitation on seller liability (e.g., fraud, tax, key warranties)?

Frequency/market practice: Yes, all those carve-outs apply.

## Is warranty insurance common?

Frequency/market practice: This is fairly uncommon, as it is still an expensive tool only recently introduced in the Brazilian market.

# Agreeing to the acquisition agreement → Set-offs against claims

## Is a set-off against claims for tax benefits common?

Frequency/market practice: Rarely.

## Is a set-off against claims for insurance proceeds common?

Frequency/market practice: Common.

## Is a set-off against claims for third-party recoveries common?

Frequency/market practice: Rarely.

# Agreeing to the acquisition agreement → Damages, knowledge

## Is there an obligation to mitigate damages?

Frequency/market practice: Rarely, except that sellers will generally ask buyers to commit to refraining from self-denouncing certain non-materialized pre-closing liabilities identified during the due diligence to the authorities after closing.

## Is there an exclusion of consequential damages?

Frequency/market practice: Fairly common; by operation of law, consequential damages are excluded.

## Are provisions that there is no liability if the buyer has knowledge common, or does buyer knowledge have no effect?

Frequency/market practice: Fairly common; this is usually claimed by the seller but often successfully resisted by buyers.

# Agreeing to the acquisition agreement → Dispute resolution

## Does local law allow for a choice of governing law?

Frequency/market practice: Brazilian law only allows for a choice of governing law where arbitration is the conflict resolution option in the contract. If litigation is chosen, it is not possible to choose governing law. Under Brazilian law, the jurisdiction where the contract was entered into will determine the governing law. When it is not possible to determine the place of the contract, Brazilian law presumes that the contract was perfected in the place of business of the party who makes the binding offer; the proponent of the deal.

## What is the common governing law?

Frequency/market practice: Brazilian law.

## Is litigation or arbitration more common? If arbitration, where?

Frequency/market practice: Arbitration is more common. The location varies from case to case.

# Agreeing to the acquisition agreement → Stamp duty and tax

## If stamp duty is payable, is it normally shared?

Frequency/market practice: None.

## Is a separate tax covenant/indemnity or tax deed common?

Frequency/market practice: It is fairly common to have a specific tax indemnity included in the purchase agreement.

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