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Mergers and Acquisitions in the legislation of Guatemala.

Introduction.

The rules relating for mergers and acquisitions in the Guatemalan legislation are contained in the Code of Commerce (*Código de Comercio*) Articles 256 to 262, although in certain cases the legal form in order to effectuate a merger or an acquisition may be different, for instance, through the creation of a third corporation, typically a holding company.

Given the size of the Guatemalan economy and the fact that the securities market is mostly composed of corporate bonds, State securities, and Central Bank securities issues, there have been relatively few mergers and acquisitions that could be considered genuine, as opposed to, for example, the restructuring of corporate groups, where the entities involved are related corporations that belong, directly or indirectly, to the same shareholders. Often times this kind of mergers and acquisitions take place as a result of changes in the tax or labor legislation, this is, in order to adjust to new or different taxing structures or similar circumstances.

However, in recent years and due to new regulations in the banking area, as well as in view of changing financial market conditions, there have been a few mergers of banks, in order to strengthen their capital base and, as a consequence thereof, to enhance their ability to extend credit facilities. Additionally, the globalization process has prompted a few acquisitions of local businesses and/or joint ventures between local and foreign companies that are setting the pace for a more active M&A environment.

The purpose of this article is to lay down the basic rules for mergers and acquisitions proper, rather than other forms used to achieve similar objectives in Guatemala. Although it is risky to refer to any established practices, for the reasons mentioned above, there are a few aspects that shall be discussed within the context of these general rules.

The regulation of mergers and acquisitions.

According with Article 256 of the Code of Commerce various corporations (*sociedades*) may merge either: (1) by the creation of a new corporation and the dissolution of all the previously existing ones, that become integrated in the new corporation; or (2) when one corporation “absorbs” other corporations that become dissolved. For the purposes of this article we call the former a “merger”, and the latter, an “acquisition”.

In both cases the new corporation or the surviving one, acquire the rights and obligations of the corporations that become dissolved. The transfer or assignment of the obligations and the rights, respectively, are thus a natural effect of the merger or the acquisition.

The Code of Commerce regulates various corporate structures, as is the case in most jurisdictions. Some of these structures entail that the partners (*socios*) are personally liable

for the obligations of the corporation when the corporation's assets do not suffice; other structures limit the liability of the shareholders (*accionistas*) to the share of capital each one of them may have subscribed. In any case it is possible to merge corporations of kinds different from the one that becomes organized as a result of the merger. In this case, according with Article 257 of the Code of Commerce, the new corporation shall be subject to the regulations applicable to its specific corporate form and its articles of incorporation and bylaws shall be prepared accordingly.

If any of the corporations that merge entail personal liability of the *socios*, as mentioned above, their personal liability does not cease to exist as a result of the merger or the acquisition regarding the obligations derived from transactions of a date prior to the merger.

The basic steps for M&A.

The initial agreement.

Obviously the Code of Commerce does not refer but to the formal corporate actions and procedures that produce the legal consequences of a merger or an acquisition. Prior to these steps it is necessary, however, that the parties have conducted the customary *due diligence* procedures and that the basic agreement have been executed. It is important to note, however, that the initial or basic agreement to merge or acquire two or more corporations does not, in and of itself, produce the ultimate effects of the merger or the acquisition. These later require a number of certain corporate actions, on behalf of the competent corporate bodies, plus the execution of a merger or acquisition deed (*escritura pública de fusión*) before a notary public.

By far the most used corporate structure in Guatemala is the *sociedad anónima* (the stock company or corporation by stocks) and according with Article 135 of the Code of Commerce, the amendment of the corporation's bylaws (*estatutos o escritura social*) which would of course be required for a merger or an acquisition, has to be approved in an "extraordinary shareholders meeting". This requires a minimum sixty percent of the issued and outstanding shares quorum and a minimum of fifty percent of the issued and outstanding shares for a valid and binding resolution of the shareholders. Thus, depending on many different circumstances, such as the number of shareholders and/or the existence of a controlling interest of fifty percent or more, it may well be that corporate officers must seek a preliminary approval to carry out merger negotiations and to execute the merger agreement, or that this latter be executed subject, among other things, to a further approval of the shareholders in an extraordinary meeting. Whatever the case, the merger or acquisition agreement shall be considered –as is usually the case in other jurisdictions—an agreement to merge or to acquire, this is more precisely, an agreement to take the necessary corporate, contractual, and legal steps in order to effectuate the merger subject to the specified terms and conditions.

Corporate actions and registration.

The basic steps, according with Article 259 of the Code of Commerce, in order to effectuate the merger or the acquisition, are, first, the corporate resolution deciding the

merger or the acquisition that, as indicated above, is often one of the consequences of the merger or acquisition agreement. The resolution must be passed, of course, by each one of the merging corporations competent bodies (typically the extraordinary shareholders meeting) and must be recorded in the minutes books and certified by means of a deed before a notary public (*acta notarial*). The *acta notarial* that transcribes and certifies each one of the resolutions must be filed and recorded with the Mercantile Registry (*Registro Mercantil*).

Once the corporate resolutions (for each and every entity involved) have been filed and recorded at the *Registro Mercantil*, this latter issues edicts that must be published in the Official Gazette (*Diario de Centroamérica*) and in a major newspaper, three times during a term of fifteen days. The balance sheets of each one of the merging corporations or those involved in the acquisition, as the case may be, must be published together with the corporate resolutions.

The merger or acquisition deed.

The actual merger or acquisition is perfected by means of a deed before a notary public (*escritura pública de fusión*). It is this instrument that shall contain, henceforth, the bylaws of the new corporation or the amendments to the bylaws of the surviving corporation, in case of an acquisition. Additionally, the *escritura pública de fusión* shall provide for the issuing and/or exchange of shares as may be required, the removal and/or the appointment of new officers or the procedure to do it, and whatever other particulars of the same nature.

Third party oppositions.

The *escritura pública de fusión*, however, may not be executed prior to a two months term, during which the creditors of the corporations involved may file their opposition to the merger with a civil judge of first instance, to the extent that their credits may become unfavorably affected thereby. Obviously previous planning of the merger process takes notice and care, to the extent possible, of these circumstances and the Code of Commerce (Article 260) provides for the possibility that creditors give their consent, by writing, to the merger, or that the sums of their credits be deposited in a bank, in their name and favor. In this latter case term credits shall be considered to have expired, due and payable.

If any opposition to the merger or the acquisition were to be filed, the process becomes stayed, although it is possible to request the court to allow the merger process to continue, provided adequate security is given in any legal form.

According with Article 261 of the Code of Commerce, the shareholders who vote against the merger resolution have the right to become “separated” from the corporation. In this case, according with Article 236 of the Code of Commerce, the respective shares shall be liquidated and paid to the interested parties. Article 231 of the Code of Commerce grants the corporation the right, for a term of six months, to place the shares of the shareholders that wish to become separated and voted against the merger. If this were not possible, the capital of the corporation shall be reduced in as much as was paid to the separated shareholders.

Once the two months term has expired and no opposition has been filed or in case adequate security has been fixed by the court and provided, the *escritura pública de fusión* may then be executed and its certified copy shall be registered at the *Registro Mercantil*,

whence the merger or the acquisition becomes perfected *erga omnes*. Obviously, upon the registration with the *Registro Mercantil*, the new or the surviving corporation shall notify the tax authorities, the Social Security Institute, and any other governmental agency that may exercise jurisdiction over the corporation, of the merger or the acquisition.

Special rules for financial institutions.

As indicated above, Executive Decree 696-93 provides for certain specific rules that apply to the merger or acquisition of banks, in addition to what is provided for in the Code of Commerce. Fundamentally this decree mandates that the interested parties shall file their application for the merger or the acquisition with the *Superintendencia de Bancos* (the authority in charge of the supervision of financial institutions), together with their financial statements and the draft bylaws of the new financial institution that would be created, or with the draft amendments to the bylaws of the would be surviving entity, as the case may be. The *Superintendencia de Bancos* shall determine whether the financial situation that would result of the merger or the acquisition fulfills the capital and reserve requirements prescribed by the banking laws and regulations and shall report to the Monetary Board (*la Junta Monetaria*) its findings, so that this latter authority may grant its approval for the merger or the acquisition.

Banks are exclusive corporate object institutions and thus may not merge with non-financial institutions.

New legislation.

The Guatemalan M&A activity is following the trend of other emerging markets in the Latin American region and as a natural consequence of this process there is legislation pending before the Congress of the Republic, in the areas of both competition law and securities law that will partly apply to these transactions. On the other hand, the Central American countries have been involved over the last approximately four decades in a process of economic integration that, now that the region has been politically stable for some years, has seen the first cross border mergers that will, most probably, be followed by yet others in view of more integrated, interdependent, and freer markets.

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