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Corporate M&A

Puerto Rico

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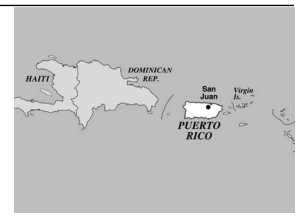
Law and Practice



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1. Trends

1.1 M&A Market

The 2020 M&A market, when compared to the 2019 market, should see increased activity as both local investors and investors relocating to Puerto Rico under Act 60 of 2019 (formally under Act 22 of 2012, known as the Act to Promote the Relocation of Individual Investors to Puerto Rico, as now codified in Act 60-2019, known as the Puerto Rico Rico's Tax Incentives Code), take advantage of the tax incentives offered to private equity funds organised pursuant to Act 60 of 2019 (formally under Act 185 of 2014, known as the Private Equity Funds Act, as now codified in Act 60-2019).

1.2 Key Trends

As with growing economies, the distress associated with contracting economies yields significant M&A activity. Although there is no publicly available data regarding M&A activity in Puerto Rico, the recession continues to trigger the sale in bulk by local financial institutions of distressed property loan portfolios, repossessed developments and residential and commercial properties. Also, as stated in **1.1 M&A Market**, the creation of private equity funds under Act 60 of 2019 should increase the pool of investable capital ready to be deployed for the acquisition of Puerto Rico businesses.

1.3 Key Industries

The main industries that could potentially continue to witness significant M&A activity in Puerto Rico are property, construction, pharmaceutical and healthcare, tourism, agriculture and the financial industry.

2. Overview of Regulatory Field

2.1 Acquiring a Company

It is important to note that the vast majority of companies located in Puerto Rico are privately held. Thus, the overwhelming majority of M&A transactions in Puerto Rico involve the purchase and sale or consolidation of privately held companies.

The main acquisition mechanisms available are:

- a stock or ownership interest purchase;
- an asset purchase; or
- a merger or consolidation.

In a stock purchase, the purchaser acquires the target corporation's outstanding equity interest from its shareholders by means of a stock purchase agreement to be executed by and between the purchaser and the target corporation's shareholders. A stock purchase requires the consent of the target corporation's individual shareholders and the purchaser's board of directors. In spite of the above, in the event that the purchaser holds at least 90% of the target corporation's shares, it may undertake a "short form merger". In such a merger, the parent company is able to merge the target into the parent without the approval of the target corporation's board of directors, of the parent corporation's shareholders or of the target's minority shareholders.

In an asset purchase, the purchaser generally acquires the target corporation's assets and, in some cases, it may also assume certain liabilities of the target company as part of the consideration. This transaction structure allows the parties to pick and choose the particular assets (and corresponding liabilities) that will be acquired (or assumed) by the purchaser. In the event that the target corporation is selling all or almost all of its assets, both the board of directors and the majority stakeholders must approve the transaction. It is advisable that, to limit the risks that may be associated with the acquired assets and liabilities, the purchaser organise a subsidiary to acquire the assets and assume any liabilities being transferred.

In a triangular merger, the target corporation is merged into a new corporation (organised solely for purposes of the underlying transaction) resulting in the survival of the new corporation as a subsidiary of the purchaser. Nevertheless, under certain circumstances the target corporation could be the surviving entity. The alternative structure is often referred to as a "reverse triangular merger" and it is commonly used when the target corporation has contracts, permits, licences or tax attributes that cannot be transferred to a third party.

2.2 Primary Regulators

Puerto Rico, as an unincorporated territory of the USA, enjoys US constitutional, legal, financial and regulatory protection. Thus, almost all federal laws and regulations, including federal securities laws, apply to Puerto Rico.

The Puerto Rico General Corporations Act of 2009, as amended (the General Corporations Act), provides the substantive corporate law. It is the principal and most comprehensive statute in connection with the constitution, governance and dissolution of corporate entities and limited liability companies in Puerto Rico. The General Corporations Act is modelled on the Delaware General Corporations Act and the Puerto Rico Supreme Court has determined that the decisions of Delaware courts in connection with the interpretation of the Delaware General Corporations Act are to be followed in Puerto Rico courts.

When an M&A transaction involves financial institutions, the Commissioner of Financial Institutions of Puerto Rico has to evaluate and approve the mergers or consolidations. If the trans-

action involves banks, the appropriate federal regulators will also have to evaluate and approve any merger.

Similarly, the Puerto Rico Insurance Commissioner must evaluate and approve the merger or consolidation of insurance companies organised under the Puerto Rico Insurance Code. The Puerto Rico Insurance Code further provides that insurance companies may only merge or consolidate with other insurance companies of the same classification.

2.3 Restrictions on Foreign Investments

As an unincorporated territory of the USA, Puerto Rico enjoys US constitutional, legal, financial and regulatory protection. Thus, the Foreign Investment and National Security Act 2007 and the Exon-Florio Amendment to the Omnibus Trade and Competitiveness Act 1988 both apply to Puerto Rico. These statutes grant the Committee on Foreign Investment in the USA the authority to investigate and block transactions that may threaten the national security of the USA.

2.4 Antitrust Regulations

The Puerto Rico Monopoly Act (the Monopoly Act) governs, from a state law perspective, the antitrust considerations that could arise in connection with the purchase or sale of an ongoing concern, expressly prohibiting business combinations that result in an unreasonable restraint of trade or commerce in Puerto Rico. The Monopoly Act does not require that the parties to a transaction obtain the prior approval of the Office of Monopoly Affairs of the Puerto Rico Department of Justice but it may issue advisory opinions if voluntarily requested by the parties. While a negative advisory opinion does not prohibit the execution of the proposed transaction, a positive advisory opinion provides a certain degree of immunity if the transaction is closed under the terms and conditions previously disclosed to the Office.

The Clayton Act, as amended by the Hart-Scott-Rodino Antitrust Improvements Act 1976 (the HSR Act), also applies to Puerto Rico. This HRS Act prohibits M&A transactions that may substantially lessen competition or tend to create a monopoly. The HSR Act grants to the Federal Trade Commission and the federal Department of Justice the power to review and object to certain transactions that, given the size of the transaction and/or the size of the parties involved, may have antitrust implications.

As of February 2020, if one of the parties involved in the transaction has USD188,000 million in annual net sales or total assets and the other party has USD18,800 million in net annual sales or total assets, then the "size-of-person" test is met under the HSR Act. If, as a result of the transaction, the purchaser acquires or holds voting securities or assets of the seller that are valued in excess of USD94,000 million but not in excess of USD376,000 million, the "size-of-transaction test" is met. Additionally, if the transaction value exceeds USD376,000 million, a filing can be required even if the size-of-person test is not met. If both size threshold tests are met, the parties are required to notify the Federal Trade Commission and the federal Department of Justice prior to the consummation of the transaction.

2.5 Labour Law Regulations

The most significant legislation with regard to labour matters in connection with M&A transactions in Puerto Rico is Act 80 of 1976, as amended (Act 80). Act 80 provides that employees who are discharged without just cause have a right to severance pay based on the duration of their employment. Thus, within the context of the purchase of an ongoing concern, if the purchaser does not retain all or some of the employees of the target corporation, the purchaser is required to retain from the purchase price an amount sufficient to satisfy severance payments to the employees who are not hired by the purchaser.

Act 80 also provides that if the employer hires all or some of the employees of the target entity, the new employer must recognise the seniority of their employment with the target corporation and, in the event of any termination without cause after the closing, the new employer will be responsible for providing any benefits accrued while employed with the target corporation, including severance.

In addition, the Puerto Rico Supreme Court has adopted the successor employer doctrine, which provides that if the purchaser of assets retains some or all of the target company's employees and, subject to certain factors, is deemed a successor employer, the purchaser:

- could be responsible for any damages caused by the termination without cause of an employee by the target corporation;
- must comply with prior collective bargaining agreements; and
- could be liable for illicit practices undertaken by the prior employer.

In addition, purchasers must also comply with the provisions of the Employee Retirement Income Security Act, which governs private industry employee pension and health plans.

2.6 National Security Review

Puerto Rico is an unincorporated territory of the USA and enjoys US constitutional, legal, financial and regulatory protection, and as such, the Foreign Investment and National Security Act of 2007 and the Exon-Florio Amendment to the Omnibus Trade and Competitiveness Act of 1988 both apply. These statutes grant the Committee on Foreign Investment in the USA

the authority to investigate and block transactions that may threaten the national security of the USA.

3. Recent Legal Developments

3.1 Significant Court Decisions or Legal Developments

The most significant legal development impacting on the local M&A market is the enactment of Act 60 of 2019 (formally under Act 185 of 2014, known as the Private Equity Funds Act, as now codified in Act 60-2019), which establishes the framework for the creation and taxation benefits of two types of private equity funds in Puerto Rico. Among other things, private equity funds must invest at least 80% of their paid-in capital in Puerto Rico private businesses.

Although quite new to the Puerto Rico market, the Act is expected to generate more M&A activity as well as other corporate transactions. Furthermore, another significant aspect of Act 60 of 2019 (formally under Act 22 of 2012, known as the Act to Promote the Relocation of Individual Investors to Puerto Rico, as now codified in Act 60-2019) which has provided, and should continue to provide, a new influx of investors and capital to Puerto Rico.

3.2 Significant Changes to Takeover Law

In recent years there have been no other significant changes to local laws that may have a direct impact on M&A activity in Puerto Rico, nor is there, at the time of writing, any pending legislation that could impact on such activity in the coming 12 months.

4. Stakebuilding

4.1 Principal Stakebuilding Strategies

Given the private nature of most businesses in Puerto Rico, it is very difficult, if not impossible, to acquire a stake in a target corporation or limited liability company prior to launching an offer to acquire it. The general practice is to approach the owners, make an offer and hopefully generate sufficient interest to commence negotiations for the acquisition of the target. Nonetheless, if the target is one of the six Puerto Rico-based companies that currently trade on US stock exchanges, a stake could be acquired prior to launching an offer via the acquisition of its publicly traded stock.

4.2 Material Shareholding Disclosure Threshold

Unless the target is a publicly traded corporation based in Puerto Rico, which would be subject to the disclosure requirements under the federal securities laws, there is no material shareholding threshold disclosure requirement under Puerto Rico laws. When the target is a publicly traded corporation, any person who acquires a beneficial ownership of more than 5% of the outstanding shares with equity voting rights is required by the federal securities laws to comply with Section 13-d of the Securities Exchange Act 1934 by filing Form-13D with the SEC. Note that beside the outright ownership of the shares, beneficial ownership is attributed to persons who have the right to acquire these shares within a period of 60 days via other types of securities, such as call options.

4.3 Hurdles to Stakebuilding

There are no statutory requirements Puerto Rico concerning ownership thresholds for privately held companies. Thus, Puerto Rico companies do not engage in the practice of introducing different reporting thresholds in the articles of incorporation, bylaws or elsewhere other than those applicable to publicly traded companies under federal securities laws.

4.4 Dealings in Derivatives

Under federal and Puerto Rico securities laws, dealing in derivatives is allowed. Notwithstanding this, the use of derivative securities or instruments is not common among Puerto Rico privately held companies and their use is very limited and confined to sophisticated parties.

4.5 Filing/Reporting Obligations

As mentioned in **4.2 Material Shareholding Disclosure Threshold**, under Section 13-d of the Securities Exchange Act 1934, beneficial ownership of voting stock for triggering the 5% disclosure requirement includes the right to own such shares via derivatives. Additionally, depending on the size of the transaction, disclosure to the Federal Trade Commission and the federal Department of Justice under the HSR Act may be required.

4.6 Transparency

Generally, in Puerto Rico shareholders do not have to publicly disclose the purpose of the proposed acquisition or their intention regarding the control of a private corporation. Nevertheless, if the target is a banking institution or an insurance company, the purchaser will be required to disclose additional information concerning the transaction to the Office of the Commissioner of Financial Institutions or to the Office of the Commissioner of Insurance.

5. Negotiation Phase

5.1 Requirement to Disclose a Deal

There are no statutory disclosure triggers applicable to privately held companies in Puerto Rico. However, as discussed in **4.6 Transparency**, insurance companies contemplating a transac-

tion must disclose their plans and obtain the approval of the Commissioner of Insurance and financial institutions must also disclose their plans and obtain the approval of the Commissioner of Financial Institutions prior to closing. As a general rule, these entities should disclose the transaction following the execution of a non-binding letter of intent. With regard to Puerto Rico's publicly traded companies, there are no statutory requirements regarding deal disclosures other than the requirements under federal securities laws and regulations.

5.2 Market Practice on Timing

There are no statutory disclosure triggers applicable to privately held companies in Puerto Rico.

5.3 Scope of Due Diligence

The scope of the due diligence review will depend on the complexity of the transaction and the target company's corporate structure and operations. A comprehensive due diligence review will include an investigation and analysis of the target company's business operations, financials, accounting practices, corporate governance, labour or litigation disputes, tax filings and compliance, environmental and permitting, liabilities and intellectual property.

As indicated earlier, the vast majority of M&A transactions in Puerto Rico involve privately held companies. A comprehensive due diligence review of the target company is required for the purchaser to validate his or her valuation of the business and its structure for the transaction, to assess particular risks and to ascertain the viability of the proposed deal.

5.4 Standstills or Exclusivity

Given the limited number of publicly traded companies in Puerto Rico standstill agreements are not seen in local M&A transactions.

However, exclusivity provisions are fairly common in local M&A transactions. The purpose of these provisions is to prevent a target company from seeking additional purchasers after it has entered into a non-binding letter of intent or has agreed to be acquired by the purchaser. A typical exclusivity provision prohibits a target company from engaging in the solicitation of other acquisition offers, providing information or engaging in discussions with other potential purchasers during the due diligence process and up until the acquisition closes or negotiations are terminated.

5.5 Definitive Agreements

Tender offers are issued in the context of publicly traded companies and thus are not usually seen in Puerto Rico.

6. Structuring

6.1 Length of Process for Acquisition/Sale

The due diligence review is generally a transaction's most time-consuming phase. The investigation and assessment of areas such as taxation and labour require an in-depth review of company records, given Puerto Rico's complex tax and labour laws and regulations. Although each transaction is inherently different, purchasers and vendors can typically expect the whole process from initial term sheet to closing to take anywhere from two to eight months. In larger, complex and multiparty transactions, the process may exceed the eight-month mark.

6.2 Mandatory Offer Threshold

There are no mandatory offer thresholds under Puerto Rico law. However, as with most US jurisdictions, shareholders do have statutory appraisal rights that they may enforce in local courts when they are "squeezed-out" as part of a merger. In the event that certain statutory requirements are met, a court of competent jurisdiction will determine whether the price per share received by a dissenting shareholder is fair in light of the circumstances.

6.3 Consideration

Cash is the most typical form of consideration, followed by equity, given that most of the transactions in Puerto Rico involve privately held companies with valuations below USD50 million.

6.4 Common Conditions for a Takeover Offer

Due to the private nature of companies in Puerto Rico, local transactions are typically negotiated and not hostile in nature. Hostile acquisitions are only possible in the context of publicly traded companies and, as stated in **2.1 Acquiring a Company**, Puerto Rico has only six publicly traded companies. As discussed, there are no local regulations addressing takeovers of privately held companies other than the appraisal rights that dissenting shareholders may have.

6.5 Minimum Acceptance Conditions

Given that tender offers are made in the context of publicly traded companies, they are not usually used in Puerto Rico.

6.6 Requirement to Obtain Financing

There is no impediment to making business combinations conditional on the bidder obtaining financing.

6.7 Types of Deal Security Measures

Typically, when purchasers wish to lock down a potential transaction they may execute a term sheet or letter of intent that is partially binding on the parties. Typical binding provisions may include:

- exclusivity provisions whereby sellers may not look elsewhere within a certain period of time;
- break-up fees and expense reimbursement if sellers fail to close;
- non-solicitation provisions;
- non-disclosure provisions; or
- non-solicitation provisions to avoid the purchaser hiring talent from the target company if the transaction fails to close.

6.8 Additional Governance Rights

Purchasers who acquire less than total ownership in a target company typically require the following rights:

- drag-along rights whereby all shareholders are forced to sell their holdings in the target company with a predetermined vote threshold and/or valuation;
- restrictions on transfers of equity, which can be absolute or subject to a right of first refusal;
- reserved board of directors' seats to be filled only by persons appointed by the purchaser;
- reserved approval rights for material decisions – eg, amendments to charter documents, asset sales, dividends or future offerings of securities, etc;
- pre-emptive rights of subscription for any future securities offerings by the target company; and
- non-compete and non-solicitation provisions.

6.9 Voting by Proxy

Shareholders may vote by proxy in Puerto Rico, but the term of such proxies is limited to three years unless the proxy expressly provides for a longer term.

6.10 Squeeze-Out Mechanisms

Local statutes permit a company in a merger to pay any particular shareholder or shareholders in cash in lieu of stock and therefore be effectively squeezed out of the surviving entity. If the purchaser holds at least 90% of the shares with voting rights, it may perform a short form merger, which only requires the approval of the purchaser's board of directors and avoids the requirement of shareholder approval.

6.11 Irrevocable Commitments

It is not common to obtain irrevocable commitments from principal shareholders. Usually, the parties enter into a non-binding letter of intent, which does not impose the obligation to close the transaction upon principal shareholders. However, it would include no-shop provisions and/or break-up fees that could be triggered if the seller were to terminate negotiations due to receiving a better offer.

7. Disclosure

7.1 Making a Bid Public

Under Puerto Rico law, there are no statutory requirements for privately held companies to publicly disclose a bid for the acquisition of another privately held company or to publicly produce and disclose financial statements (generally prepared pursuant to generally accepted accounting principles – GAAP) for a M&A transaction. Notwithstanding, for a transaction to be effective, the merger or acquisition agreement or a certificate of merger must be filed with the Puerto Rico Department of State.

7.2 Type of Disclosure Required

Similarly, there is no statutory requirement to publicly disclose the issue of shares in a business combination. Nevertheless, according to the General Corporations Act, if an acquiring corporation issues common shares exceeding 20% of the amount of common shares outstanding before the effective date of the acquisition or merger, this acquisition or merger will require the approval of the shareholders of the surviving company.

7.3 Producing Financial Statements

Given the fact that most M&A transactions are executed among private companies, there are no applicable statutory requirements for the bidders to produce or disclose financial statements to the general public. Financial statements, when prepared, are generally prepared pursuant to GAAP.

7.4 Transaction Documents

The General Corporations Act requires that the parties involved in a transaction file the corresponding merger or acquisition agreement with the Puerto Rico Department of State. The parties may, however, elect to file a certificate containing the following information instead:

- whether the transaction is a merger or a consolidation;
- the names, jurisdictions of incorporation or organisation, and the registry numbers of the constituent companies;
- certification that the constituent companies have adopted a merger or consolidation agreement pursuant to the General Corporations Act;
- the name of the surviving or resulting company;
- a description of the changes or amendments to the articles of incorporation;
- the address of the surviving company where the merger or acquisition agreement is available; and
- an assurance that the surviving entity will provide, free of charge, a copy of the agreement to the shareholders.

8. Duties of Directors

8.1 Principal Directors' Duties

The General Corporations Act is based on the Delaware General Corporations Act and, substantially, all theories of corporate doctrine adopted by Delaware courts have been adopted or are considered in Puerto Rico. This includes the fiduciary duties of care and loyalty owed by directors and officers to the corporation and to its shareholders.

Note that the duties of care and loyalty have been expressly included in the General Corporations Act and that they also apply to managing members, managers and other officers of limited liability companies. The General Corporations Act also states that besides directors and officers, the duty of loyalty applies to majority shareholders, thus providing an additional layer of protection to minority shareholders.

In general terms, the duty of care requires that directors and officers exercise their duties in a prudent and diligent manner, and with the same degree of attention and care as a competent and responsible director or officer under similar circumstances. In a merger or acquisition transaction, directors need to be well informed of all the material terms of the transaction and, if they are not familiar with them, they have the duty to make the necessary enquiries and become informed prior to making a decision. A corporation may limit or eliminate, via its certificate of incorporation, the responsibility of directors or managers for duty of care violations.

However, under the General Corporations Act the duty of loyalty requires that directors, officers and majority shareholders act in the best interest of the corporation and its shareholders and that they should not promote their own personal interest at the expense of the corporation's interests. Complying with the duty of loyalty requires that directors act in good faith and in an honest and reasonable manner. Contrary to the duty of care, liability for a violation of the duty of loyalty cannot be limited or eliminated via the certificate of incorporation or an operating agreement.

8.2 Special or Ad Hoc Committees

Although special committees are not generally constituted to evaluate a potential transaction, there are certain circumstances in which they might be advisable. Special committees are formed when a director or a majority shareholder is on both sides of the proposed transaction or has other personal interests in the transaction that could cause a conflict of interest and possibly an enhanced standard of judicial scrutiny of the transaction if it is challenged in court.

8.3 Business Judgement Rule

The business judgement rule establishes a rebuttable presumption that when a board of directors makes a decision, it makes it in good faith, on an informed basis and with the honest belief that the decision was in the best interest of the corporation and its shareholders. The business judgement rule doctrine states that if there is any reasonable commercial basis for a decision, directors will not be held liable for mere judgement errors even if those errors cause unfavourable results to the corporation. The rule does not apply to, and does not protect, directors or officers for illegal acts, ultra vires acts, fraudulent acts or acts that involve gross negligence or a clear conflict of interest.

Delaware jurisprudence, which is highly persuasive in Puerto Rico, has established the following criteria to determine whether the business judgement rule is preserved:

- the director or officer has no personal interest in the subject matter he or she is deciding;
- the director or officer is sufficiently informed regarding the matter he or she is deciding; and
- the decision was made in good faith and rationally, and it was taken for the benefit of the corporation.

When a director or officer has a conflict of interest, courts will use an "entire fairness" standard of review pursuant to which the directors and/or officers must prove that the decision was taken with the "utmost good faith" and that the decision is "inherently fair" to the shareholders. Under this standard of review, the directors and/or officers must show that the transaction was the result of "fair dealing" and that a "fair price" was obtained.

Although Delaware courts have developed another standard of review called the "intermediate standard of review", which is applied when a board of directors uses defence mechanisms such as a "poison pill" to prevent a hostile acquisition, this review has not yet been adopted by Puerto Rico courts. Under the intermediate standard, courts evaluate the actions taken by the board of directors and the process for taking those actions. The directors must show that the decisions taken by them are reasonable and not merely rational under the business judgement rule.

8.4 Independent Outside Advice

Generally, companies that are considering a M&A transaction engage outside counsel and financial advisers. Depending on a company's particular industry, hiring other specialised consultants may be advisable.

Independent counsel for the purchaser is generally responsible for the preparation of the transaction documents and completion of the legal due diligence review. Financial advice is nor-

mally provided by certified public accountants, since investment bankers do not often participate in Puerto Rico M&A transactions, unless it is complex.

8.5 Conflicts of Interest

Given that the number of M&A transactions is a fraction of the number of transactions that occur in Delaware and in other parts of the USA, the quantity of conflict of interest suits due to a M&A transaction is very limited. Nonetheless, there have been judicial claims involving directors', officers' and majority shareholders' conflicts of interest. Plaintiffs bear the burden of proof to show that the a decision was taken by the directors who had a personal interest in the transaction, who were not informed regarding important facts relevant to the decision before them and who took a decision absent of good faith.

9. Defensive Measures

9.1 Hostile Tender Offers

Although the General Corporations Act does not prohibit hostile tender offers, they are virtually non-existent given the private nature of businesses in Puerto Rico and the fact that transactions are always voluntarily negotiated transactions.

9.2 Directors' Use of Defensive Measures

As discussed in **8.1 Principal Directors' Duties**, the directors owe a duty of care and a duty of loyalty to the corporation and to its shareholders and they must always act for the benefit of the corporation, be it in negotiating the price for the acquisition of a target company, the sale of the corporation or implementing a defensive measure to prevent an acquisition.

9.3 Common Defensive Measures

In Puerto Rico, the most common defensive measures are:

- super-majority (ie, two-thirds of votes) voting requirements for extraordinary transactions;
- right of first refusal provisions that entitle other shareholders and/or to the corporation to acquire the shares of a selling shareholder before that shareholder has the opportunity to sell them to a third party; and
- the creation of a staggered board of directors.

Additionally, directors could use poison pills as a defensive measure. However, this type of defensive measure is rare in Puerto Rico.

9.4 Directors' Duties

Directors owe a duty of care and a duty of loyalty to the corporation and to its shareholders. As previously mentioned, currently there is no local case law interpreting the applicability of the intermediate judicial scrutiny applicable to defensive measures executed by directors, as adopted by Delaware courts.

9.5 Directors' Ability to "Just Say No"

Under the General Corporations Act, the merger or acquisition agreement may provide that, at any moment before the certificate filed in the Puerto Rico Department of State becomes effective or before the closing of an asset purchase, the board of directors of any of the corporations involved in the transaction may terminate the agreement. This is so even if it has been approved by the shareholders of all or some of the corporations involved in the transaction.

10. Litigation

10.1 Frequency of Litigation

Given the private nature of companies in Puerto Rico, local M&A transactions are friendly in nature. Hostile takeovers or acquisitions are only possible in the context of publicly traded companies and, as already explained, Puerto Rico only has a handful of publicly traded companies. As a result, litigation in the context of M&A transactions in Puerto Rico is very limited, particularly with regard to disputes between the purchaser and the target company. This contrasts significantly with the pattern witnessed in mainland USA, where M&A litigation is much more common.

Notwithstanding, given the complexity of Puerto Rico labour laws applicable to the sale of an ongoing concern, it is more common for litigation to arise in connection with severance payments, holiday pay and sick leave owed to retained and/or laid-off employees. To avoid potential litigation between the parties to a merger or acquisition transaction, each party's responsibilities in connection with labour matters are generally subject to extensive negotiation and are carefully addressed in the agreements.

10.2 Stage of Deal

In the event that labour litigation does arise, it generally occurs following the execution of the merger or acquisition agreement.

11. Activism

11.1 Shareholder Activism

For the most part, Puerto Rico companies are closely held, wherein the shareholders are actively engaged in the day-to-day management of the business. As a result, shareholder activism in the traditional sense is not commonplace, particularly as an investment strategy. Thus, shareholder activism is mostly non-existent in Puerto Rico.

11.2 Aims of Activists

Activists are not common in Puerto Rico M&A transactions due to the private nature of most business organisations.

11.3 Interference with Completion

Since most local businesses in Puerto Rico are private in nature, activist investor presence is rare. Notwithstanding this, minority shareholders who are not actively involved in the management of the corporation may attempt to interfere with a proposed M&A transaction based on alleged breaches of fiduciary duties and claims of dissenting rights, although such interference is also extremely rare.

Ferraiuoli LLC houses an M&A practice group that represents buyer and seller clients including Puerto Rico's premier venture capital, private equity and industry-specific investment companies in both local and cross-border M&A transactions. Skilled in developing complementary tax and regulatory strategies, the team regularly handles sophisticated transaction structures, with experience in LBOs, recapitalisations, complex and extensive due diligence initiatives, local and cross-border mergers, asset sales and business unit divestitures, stock sales and capitalisations, as well as restructurings. The firm's services include the drafting and negotiation of letters of intent, confidentiality agreements, offering term sheets and memoranda, and acquisition and other definitive agreements, and its activity spans all business segments, including finance, manufacturing, technology, health, oil and gas, software, services, distribution, advertising, gaming, transportation, food, retail, education, and the equipment leasing and telecommunications industries. Firm practitioners benefit from being able to draw on the experience of their colleagues in tax, employee benefits, intellectual property, bankruptcy, litigation, commercial real estate, environmental and labour to address any issues that arise in structuring, negotiating and closing complex business combination transactions.

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