Brazil

The Role of Institutional Investors in Promoting Good Corporate Governance Practices in Latin America: The Case of Brazil

In 2007, the OECD asked the **Capital Markets' Investors Association (AMEC) to produce a report** which was used as input to the discussion paper entitled ***the Institutional Investors and Corporate Governance in Latin America: Challenges, Promising Practices and Recommendations*** presented at the 2007 Roundtable meeting in Medellin, Colombia.

In 2008, IBGC was invited to update the document and add new topics, such as the role of insurance companies and private equity as institutional investors.

Brazil's report was elaborated by a task force integrated by representatives of the **Capital Markets' Investors Association (AMEC)**, the **National Association of Investment Banks (ANBID)** and the **Brazilian Institute of Corporate Governance (IBGC).**

For ease of understanding, the section in grey boxes corresponds to the original country report. For any comments or questions regarding the original country report please contact Edison Garcia at edisongarcia@amecbrasil.org.br

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GOVERNANCE
PRACTICES ON ASSET MANAGEMENT
IN BRAZIL

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ANBID - National Association of Investment Banks
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1. Introduction

1.1. Participating Entities

This report was prepared with the cooperation of three of the most important associations involved in the protection of minority shareholder rights, good governance practice and self-regulation of the investment funds market in Brazil.

AMEC - Capital Markets' Investors Association is the convergence of several independent portfolio managers and those linked to financial institutions, that joined forces driven by the conviction that the current stage of development in the Brazilian capital markets required the existence, and provided the necessary conditions for the creation of an independent entity to represent the interests of fund investors as minority shareholders.

AMEC was conceived with the purpose of endowing capital markets with the opportunity for coordination, discussion and execution of initiatives aimed at defending investors' interests, above all fund investors in their relations with Brazilian publicly held companies.

Its members are convinced that strengthening capital markets, which have been consolidated into a modern instrument for financing the new cycle of self-sustainable development of the Brazilian economy, involves the respect and broadening of minority shareholder rights.

Within the scope of this work, AMEC was responsible for obtaining and compiling information with respect to the relationship between the portfolio managers and listed companies.

ANBID - National Association of Investment Banks is the leading representative of the institutions that operate in the Brazilian capital markets, its objective is to seek the market's consolidation as an instrument for fostering the country's development.

Acting in an innovative manner, ANBID is the only class entity, which, besides representing the interests of its members, self-regulates their activities with the adoption of standards that are generally stricter than those established by legislation. ANBID is also the principal source of information for the capital markets as well as promoting broad-based initiatives directed towards the education of investors and market professionals.

Its members are not only investment banks but also other institutions – financial (multiple banks, brokers, dealers..) and non-financial (typically the so-called independent asset managers and capital markets' consultants, incorporated as non-financial companies) – with varied profiles, having as their common denominator activities involving asset management, public offerings of securities, mergers and acquisitions, private banking, depository services and qualified services for the capital markets.

ANBID's operations are the responsibility of about 90 professionals, with roughly another 720 executives, who represent member institutions divided among the 50 different bodies of the entity. On average some 50 meetings are held to discuss topics of critical importance to ANBID's members, the market and the country every month.

ANBID's contribution to this report consisted in the systematisation of information on good governance practice adopted internally by the investment funds and their relationship with their quota holders as well as information on the new standards of conduct that must be implemented by the funds as a result of ANBID's Self-Regulation Code, currently under discussion.

IBGC - Brazilian Corporate Governance Institute, a non-profit organisation founded in 1995, is the first organisation to be created in Brazil specifically focused on Corporate Governance. Among its initiatives and endeavour in this field is the preparation and revision of the Brazilian Code of Best Corporate Governance Practice.

The Institute is considered nationally and internationally as one of the principal entities responsible for the introduction of the concept of Corporate Governance in Brazil, and also recognised for the dissemination of the importance of good practice in the country, leading to the growing interest of Brazilian companies in consolidating their position in the market through the adoption of such practice.

IBGC today has more than 1,200 members and has been actively participating in the development of the principles of corporate governance in Brazil in partnership with the Brazilian Securities and Exchange Commission - CVM, the São Paulo Stock Exchange - Bovespa and other market entities.

In 2007, IBGC was responsible for gathering the information on pension funds and the adoption of good governance practice. In 2008, IBGC lead the report update.

1.2. Economic Context

Over the past few years, the Brazilian economy has been notable on the international scene for its vigour and strength. This can be attributed to various reasons among which key are: international market liquidity, the decline in the basic rate of interest, control of inflation and the consolidation of capital markets.

Set against this background, the sophistication and improvement in capital markets' instruments stand out in particular, indicative of their importance for economic development and growth.

The Brazilian equity market has been developing at a fast pace. Domestic companies are alert to this fact, and are now using this medium as one of the principal sources for financing their investments.

Up to September 1st 2008, BOVESPA[1] had reported the listing of 4 new companies, against 64 companies in 2007, 26 companies for 2006, 9 in 2005 and 7 in 2004. By value, the total volume of issues jumped from R$ 5 billion in 2005 to R$ 15 billion in 2006, by the end of 2007 reaching the sum of R$ 56 billion[2] and R$7.5 billion in the 9M08.[3]

The development of the capital markets has brought greater investor security following improvements in self-regulation, changes in corporate law, adoption by companies of good corporate governance practices and the consolidation of institutional investors.

Investor confidence in publicly held companies has been evolving, especially in those companies whose level of corporate governance ensures greater management transparency and better information flows. At the same time, these same investors have been astonished at the ample range of opportunities for acquiring equities in companies covering broad slices of Brazilian economic activity.

[1] Information available in www.bovespa.com.br/Principal.asp
[2] Information available in www.cvm.gov.br/
[3] The information from the past was changed here to keep the consistency with current data.

At this time of changes, the market has also witnessed a dispersal of shareholding control as well as hostile take-over bids, events previously only the subject of academic discussions but today a reality in Brazilian corporate operations.

Among the principal drivers behind the recent development in the capital markets, are the amendments to Law 6,404 of 1976 and Law 6,385 of 1976, which regulate, respectively, joint stock companies, determining the rights of the shareholders, and the principles and basic rules of corporate governance. Reforms at the Brazilian Securities and Exchange Commission - CVM, the capital markets regulatory watchdog, responsible for overseeing a prosperous and secure business environment, have also been key factors, not to mention the creation of a special listing segment on the BOVESPA, the “Novo Mercado” (New Market).

The two laws above were updated by Law 10,303 of 2001, which introduced material changes, such as: (i) the practice of buy back resulting in a low percentage of shares tradable on market; (ii) the mandatory requirement to make a public offering prior to delisting; (iii) the reduction in the limit for the issue of preferred shares: (iv)the pre-emptive rights of preferred shares; (v) the possibility of litigation among shareholders being settled through an Arbitration Panel; (vi) the provision on shareholders’ conflict of interests; (vii) the provision for shareholder responsibility for abusing voting rights; (viii) the self-executable nature of shareholders agreements; (ix) the convening of the General Meeting in specific cases, by the fiscal council and by the shareholders; (x) the interruption and extension of the period between the convening of the Meeting and its realisation; (xi) the right of withdrawal in the event of a spin-off, if this implies a change in the corporate purpose (xii) the right of minority shareholders with 15% of the shares with voting rights or 10% of the capital stock in preferred shares to elect, in a separate vote, a member to the Board of Directors; (xiii) the duty of confidentiality of all stakeholders with respect to insider information; (xiv) the manifestation of transparency through the disclosure of market information; (xv) the expanded powers of the fiscal council; and (xvi) the restitution of legal tag along rights to the holders of common shares at 80% of the value paid for the control of the company.

The change in the legal environment was complemented by a far-reaching revision of the regulations issued by the Brazilian Securities and Exchange Commission. Based on some of the new legal initiatives or simply in the modernisation of existing provisions, the capital markets regulator has upgraded all aspects of its procedures. Of particular note are the amendments to the rules on public offerings (CVM Instruction 361), material facts and significant holdings (CVM Instruction 358), as well as investment funds (CVM Instructions 409 and 450).

Another point in the direction of the consolidation of a robust equities market is the size that investment funds have been reaching in Brazil and consequently the activism these have been exercising. The net assets of the domestic investment funds industry have already exceeded the R$ 1.1 trillion[4] mark, being one of the largest in the world.

1.3. Economic Context – Update

The IBOVESPA index peaked in May 2008, after which the effects of the global financial sector crisis spread throughout Brazilian capital markets and the index suffered from strong foreign capital outflow.

[4] Source: Anbid, database date: October 7th (www.anbid.com.br)

Stock prices are reaching historical lows as future interest rates are climbing, although the government has announced a series of measures to calm investors and stanch the cash leakage.

Despite the impact on equity and fixed income markets, the effect on the real economy has still not been felt. It is believed, however, that some time in the near future there will be some degree of weakening in production and consumer demand, and that Brazilian GDP growth will slow down.

Key Economic Indicators	**2008**	**2007**	**2006**	**2005**
Population (million)	192*	190	187	182
GDP (US$ billion)	1,518*	1,151	903	768
Real GDP growth	4.83%*	5.40%	2.86%	2.28%
GDP *per capita* (US$)	7,900*	6,070	4,820	4,214
Inflation rate (retail)	6.57%*	4.46%	3.14%	5.69%
Unemployment rate	14.60%*	15.50%	16.80%	17.90%
Stock market capitalisation (US$ billion)	1,382**	1,398	723	482
Number of Companies	398**	404	350	343
Saving deposits (US$ billion)	155.36*	105.71	77.06	67.67
Time deposits (US$ billion)	311.21*	151.69	133.66	93.32
Trade Balance (US$ billion)	22.60*	40.04	46.08	44.71
Total International Reserves (US$ billion)	200.83* (Jun/08)	147.10 (Jun/07)	62.67 (Jun/06)	59.88 (Jun/05)
Exchange Rate (R$/US$)	1.5919 (Jun/08)	1.9254 (Jun/07)	2.1635 (Jun/06)	2.3504 (Jun/05)
Net Public Sector Debt (as % of GDP)	40.65* (Jun/08)	42.80 (Jun/07)	49.97 (Jun/06)	51.65 (Jun/05)

** Forecasts for close of 2008. Source: Central Bank's FOCUS report or economists of principal financial market institutions.*

***Source: BM&FBOVESPA – June 2008 / Data Provided by ANBID*

1.4. Relevant Developments in Corporate Governance Rules

- **Adjustment of Accounting Rules to International Standards (IFRS)**

Law 11,638, approved towards the end of 2007, introduced changes to Law 6,404, Brazilian Corporate Law, as regards to accounting practices. The purpose of the Law was to adapt Brazilian accounting rules to international accounting norms and with this give Brazilian companies greater access to international capital.

Another provision of Law 11,638 was to extend to large corporate entities (annual sales in excess of R$300 million) the obligation to prepare their financial statements in conformity with Brazilian Corporate Law, as well as submitting them to an external audit, which they were not obliged to do previously. The original bill included the obligation to publish these financial statements, although this ended up not being included in the Law as finally approved. The simple existence, however, of financial statements prepared in conformity with such norms is already an improvement in corporate transparency in those cases where they are voluntarily disclosed for the information of stakeholders such as suppliers, the authorities, clients, employees, banks and share or quota holders[5].

Finally, another important decision in terms of corporate governance was to give the Accounting Standards Committee-CPC, a Brazilian entity roughly equivalent to the IASB or FASB, the authority to revise and update accounting standards, making it easier and quicker to introduce or amend accounting rules where necessary.

The Law was finally approved at the end of 2007 and requires 2008 financial statements to be prepared and published in accordance with the changes therein. By the year 2010, Brazilian consolidated financial statements will need to be published in accordance with IFRS accounting standards. During 2009 the CVM and the CPC will issue the new norms required for conformity.

- **A Break in the Rotation of Auditors**

The rule in Brazil for listed companies is that external auditors need to be rotated every five years. CVM Ruling 549 allows companies to defer the rotation of their external auditors during the period in which companies must adapt to international accounting standards. This avoids having to undertake two transitions at the same time: the transition to a new auditing firm and the transition to the new accounting standards. While still convinced of the need to rotate external auditors, in order to avoid eventual conflicts, the CVM is concerned with ensuring the continuity and stability needed by companies to successfully adapt to the new accounting norms without any loss in transparency.

- **CVM's Rules on Shareholder's Meeting**

CVM accepted the proposal of several market players active in Corporate Governance with respect to the following points:

1. Powers of attorney granted by shareholders using electronic signatures with digital certification, where accepted by the company. Brazilian Corporate Law determines that shareholders should either attend in person or be represented by another shareholder, member of company management or a lawyer authorised by a power of attorney granted not more than one year ago. In the same way, quota holders in equity funds should be represented by the fund manager, who, in turn, may delegate his powers to other authorised representatives. One common requirement has always been that the signatures on the documents required by the company for the shareholders' meetings need to be notarised. The CVM, however, concluded that this practice is not a legal requirement but a condition established by companies themselves and that companies should be free to waive it should they so decide. In practice, a consulting firm will offer its services to companies that prefer to receive their powers of attorney by means of a website called On-line Shareholders' Meetings (Assembléias On-line). The website will register shareholders and their digital signatures in conformity with whatever security parameters the company stipulates, and allow it to be duly audited, and shareholders will be represented in person in the shareholders' meeting by a representative defined by the company. Votes will be accepted up to one hour prior to the meeting. Foreign shareholders will benefit, since it will be easier and quicker to establish powers of attorney in favour of local representatives, investment funds and individual shareholders will also benefit, since it will become easier for them to be represented from

[5] Listed companies are already obliged to publish financial statements, so quota holders refer only to unlisted companies.

afar. Given the expected increase in the number of participants in the shareholders' meetings, the website will also help with the preparations for the shareholders' meetings;

2. Internet forums or blogs, where shareholders can post their comments regarding the agenda. These blogs may even remain open during the meetings, with the supervision of company management. The purpose of these blogs would be to enable shareholders to discuss among themselves issues on the agenda, organise themselves to vote on controversial issues, and even on issues such as the selection of the minority shareholders' representatives on the board of directors and on the fiscal council;

3. Allow companies to use the On-line Shareholders' Meetings register to update shareholder information when it is outdated on their internal shareholder registers. The objective behind this request is to enable companies to reach the greatest possible number of shareholders, especially at the time of shareholders' meetings of companies with a broad shareholder base and that need a quorum for certain situations as established under Brazil's corporate law;

4. Live transmission of shareholders' meetings on the internet for the general public, including non-shareholders. The CVM allows this, provided the company considers it to be in its interest. The advantage is that it gives all shareholders and members of the general public access to information regarding the issues discussed during the meeting, allows them to monitor the participation of their representative as well as broadening their knowledge regarding the treatment given shareholders at the shareholders' meetings.

As yet none of these measures for providing greater access to shareholders' meetings as approved by the CVM in June 2008 has actually been put to the test, this is hardly surprising given the small number of shareholder meetings held since then. The acceptance by companies and investors of these procedures will become clearer during the next shareholder meeting season, which will be between March and April of next year. According to MZ Consult, an Investor Relations Services Company involved in the proposal, about four companies have already shown interest in adopting these measures during their shareholders' meetings[6].

- **Changes in the Criteria for Elections to the Fiscal Council**

The fiscal council is a supervisory body that does not exist outside Brazilian legislation. It is composed of 3 to 5 members, of which 1-2 are representatives of minority shareholders and 2 to 5 are representatives of the controlling shareholders. Members of the fiscal council are independent and, since they are elected by the shareholders, they cannot be removed during their one year period of office. Given the inequality between majority and minority shareholders that still exists in Brazilian corporate control structures, the role of the fiscal council is to bring minority shareholders into closer contact with the supervision of the company, since they have a greater chance of being elected to the fiscal council than to the board of directors. In a recent decision, the CVM ruled that minority shareholders with common shares have the right to elect a representative to the fiscal council whenever such minority shareholders represent at least 10% of the free float. Previously, in order to be able to elect a representative to the fiscal council, the shareholders present at the meeting needed to control 10% of the company's voting capital. Easier access of minority shareholders to the fiscal council is an

[6] The OECD submitted a follow up question on this point: "Will shareholders push for this? **Answer**: we still don't know, but probably yes, mainly because of self-regulation of anbid forcing funds to participate on shareholders meetings and consequently funds incentivising companies to adopt this on-line meeting"

advance in Brazilian corporate governance, since it will subject companies to closer supervision by their minority shareholders.

- **Protection of Minority Shareholders in the Event of an Incorporation of Subsidiaries (Guideline 35)**

CVM's Guidelines are a form of regulation, without, however, the force of the law. They reflect CVM's interpretation and understanding of the law. With these Guidelines, the CVM sought to reduce the scope for conflicts of interest in the approval of such incorporations, suggesting that "company management observe certain procedures during the negotiation of mergers, incorporations or incorporations of shares involving the controlling shareholder and its subsidiaries or other companies under common control". The importance of these Guidelines is that it makes it clear to the market how the CVM interprets the law and provides advance notice about how the CVM is likely to judge cases of incorporation of subsidiaries where due care is not taken to ensure that such incorporations are executed in an entirely objective manner, in conditions of equality between the incorporating entity and the minority shareholders of the entity being incorporated. Among the CVM's suggestions are the recommendations that the transaction be made conditional upon the approval of a majority of the non-controlling shareholders, including non-voting shareholders, that the negotiations and decisions regarding the incorporation be documented, that any external advisors that are retained be unrelated to and independent of the controlling shareholder and that all the documents on which management's decision are based be placed at the disposal of shareholders[7].

- **Greater Flexibility in Secondary Issues**

CVM's Instruction 471 establishes a simplified procedure for the registration of secondary public offerings.

This instruction speeds the process up, mainly by providing for the possibility of CVM establishing agreements with self-regulating entities[8], resulting in more time for the CVM to dedicate to those aspects of each transaction that require greater attention. This has simplified access to the market.

On the other hand, it is worth noting that the Instruction in fact increased CVM's supervisory powers, since it will now be responsible for also supervising the self-regulating entity (responsible for the acts of its managers and representatives), which is obliged to act in a diligent manner and to reimburse the CVM for any losses caused in the course of the respective agreement with the CVM.

- **Transparency in Derivatives Transactions**

CVM Decision 550 deals with the disclosure of information regarding financial derivatives transactions in the notes to the financial statements.

[7] The OECD submitted a follow up question: "How is, if at all, pressure applied to follow guidelines?" **Answer:** so far there was no situation where the application of this guideline could be tested, but this guideline shows how CVM will judge these cases, meaning that any company that disregard the guideline can guess will suffer sanctions from CVM.

[8] The OECD submitted a follow up question: "Concretely what does this mean?" **Answer**: If a listed company wants to make a secondary offer, it is possible to do it with anbid (only anbid is a candidate so far). Before only CVM would allow this issue, and due to a large number of offerings the process was lengthy. With other entities, such as anbid, it is expected that the time will be reduced.

The principal characteristic of this decision is precisely its insistence upon one of the pillars of governance: total transparency in the disclosure of information. With such Decision CVM shows its concerns with the continuous evolution of the regulatory system.

The Decision applies to all quarterly interim statements (ITRs) for quarters ending after September 30 2008 (inclusive). It was an answer to the losses recently announced by Aracruz and Sadia in the third quarter of 2008, caused by investments in foreign exchange derivatives transactions in a quarter when the exchange rate depreciated far more than the market expected[9]. Prior to the current legislation, the applicable legislation had required that firms disclose their exposures to financial transactions at market value, but had never required that firms disclose their specific exposures to derivatives, mainly due to the difficulty of valuing them. Experience, however, has shown that companies need to better monitor risks just as much as investors need to be able to see and understand them.

2. Main Institutional Investors in Brazil (II)

This chapter highlights the main institutional investors in Brazil, the distribution of their assets, pertinent legislation, the corporate governance rules to which they are subject and how these institutional investors affect corporate governance of invested companies. In the report, it is possible to observe the existence of three groups of IIs based on their impact on the spread of good governance practices in the market: 1) IIs that are big shareholders in invested companies, and, as a consequence, have a higher possibility of promoting good practices of governance in them; closed pension funds and investment funds are among these; 2) IIs that have a small percentage of companies' shares, and, as a result, do not influence directly the promotion of good governance practices, but they use their influence in the market to provide incentives so that companies seek better practices; and 3) IIs that do not work with publicly owned companies, such as Private equity funds, but help to promote good practices looking for higher margins in the future.

2.1 Closed pension funds

Closed pension funds are the second largest group of institutional investors in Brazil, following on the heels of the investment funds. They manage a larger volume of resources than open pension funds, which are regulated by SUSEP and will be better explained in the section 2.3 on insurance.

Closed pension funds managed R$84 billion in stocks in June 08, representing about 19% of total assets and 35% if investments in variable income funds are included. Previ (Caixa de Previdência dos Funcionários do Banco do Brasil) is the most important pension fund in Brazil, accounting for 30% of total assets, followed by Petros, with 9% and Funcef, with 7%. Almost half of Previ's assets were variable income securities at the end of 2007, compared with 30% of Petros' assets and 36% for Funcef. As this report will show, investment in equities is more important for this industry than for average asset distribution of institutional investors in Brazil.

[9] In one month - August to September – the Real to Dollar exchange rate increase from R$ 1.63 to R$ 1.90 for 1 USD.

Closed Pension Funds Portfolio of Investments

in R$ million	2007	Jun/08	Breakdown Jun/08
Fixed Income (bonds and funds)	248.302	263.353	58,4%
Stocks	90.451	84.005	18,6%
Investment funds in equity	69.563	74.085	16,4%
Others	27.454	29.523	6,5%
Total	435.770	450.966	100,0%

Source: ABRAPP

Pension funds hold mostly minority stakes in listed companies, generally acquired in the market. In some cases, the larger pension funds, such as Previ and Petros, hold controlling stakes, but always with the intention of exiting as soon as the investment matures. Private equity investments as well as infra-structure investments are also growing as a percentage of their portfolios.

The main governance rules of pension funds imposed by current legislation are:

- The organisational structure of a public sector company closed pension fund should include an Advisory Committee, a Fiscal Council and an Executive Board;
- The Fiscal Council should evaluate the conformity of the fund's asset management to current legislation and the fund's own investment policy;
- Pension funds are obliged to be audited by independent auditors;
- Each different type of pension plan managed by the pension funds should be managed according to its own specific investment policy, which should be reviewed annually;
- Basically, self-regulation does not exist in the pension fund industry, but recent legislation has been focusing on improving the corporate governance of companies in which the pension funds invest. Bacen (Brazilian Central Bank) Resolution 3456 establishes certain rules about how pension funds should invest the resources under their management:
- Pension funds may distribute resources between fixed income securities, variable income securities, real estate or loan instruments;
- Asset limits:

Main assets	Portfolio share
Fixed income – low risk	up to 100% of portfolio
Fixed income – low risk credit	up to 80% of portfolio
Fixed Income	up to 50% of portfolio
– stocks in BOVESPA’s Nivel 2 and Novo Mercado segments	up to 50% of portfolio
– stocks in BOVESPA’s Nivel 1 segment	up to 45% of portfolio
– stocks in Bovespa Mais segment	up to 40% of portfolio
– other shares and	up to 35% of portfolio
- private equity funds*	up to 20% of portfolio
	Maximum share
Fixed income	25% of issuer’s equity in low credit risk companies
Fixed income - credit	15% of issuer’s equity in other cases
Fixed income - stocks	20% of voting shares
Fixed income - stocks	20% of total shares
Fixed income - stocks	5% of total assets under management (AuM)
Fixed income - stocks	10% of total AuM, if the asset represents more than 2% of any stock exchange index
Fixed income – participation and funds	25% of project or fund equity
Fixed income - participation and funds	40% of project or fund equity when pension fund or sponsor are in the project
Fixed income - stocks	Not allowed to invest in stocks outside a governance level in BOVESPA if the stocks have been in the market from 2007 onwards (from 2007 and before, there is no prohibition)
Derivatives	Position that generates up to 100% of pension fund’s assets
	Short selling is forbidden

** In the equity participation portfolios, where there is no stock exchange listing, the bylaws should provide, among other things, of:*

- *a two-year term of office for the board of directors;*
- *disclosure of any contractual obligations with related parties, shareholders’ agreements, or stock options;*
- *acceptance of the arbitration panel’s decision to resolve disputes between shareholders;*
- *annual audit of financial statements by external auditors.*

The bulk of the pension funds’ work to improve governance in invested companies is done on a voluntary basis. Except from the above-mentioned regulation, there is no organised movement for self-regulation of investments in this field. However, pension funds individually encourage companies to improve their governance.

The activist approach of Brazil’s principal pension funds has played an important role in changing the relevant legislation, especially at the CVM level and has contributed to a perception in the market of pension funds as important players in the effort to improve Corporate Governance practices. In this context, Previ published in 2004 a Corporate Governance Guide for use by invested companies (Petros also published one in 2002), containing the following topics (Please find the Previ’s code in the annex to this document):

1) Transparency, Disclosure and Accountability;

2) Shareholder's Rights;

3) Equitable Treatment;

4) Corporate Ethics;

5) Board of Directors;

6) Executive Office;

7) Fiscal Council;

8) Committees;

9) Independent Audit.

Other initiatives by Previ have been the ongoing training of board members with incentives to attend educational courses, frequent web forums and attend an annual seminar to discuss board and corporate governance issues, as well as guidelines for Board members and Fiscal Council members sitting on boards. In addition, Previ uses proprietary corporate governance ratings for investment decisions.

Pension funds consider companies' corporate governance practices before investing, and once invested, exercise their shareholder activism through voting, one-on-one meetings, and nomination of directors to the board and to the fiscal council. Obstacles to stronger activism on the part of smaller pension funds, as pointed out by the pension funds themselves, include the lack of proxy advisory services and the fact that exit of small stakes is more effective than trying to improve governance.

Please refer to the topic on Pension fund-related evaluations at the end of this document.

2.2 The Funds Industry in Brazil

Size and equity investments.

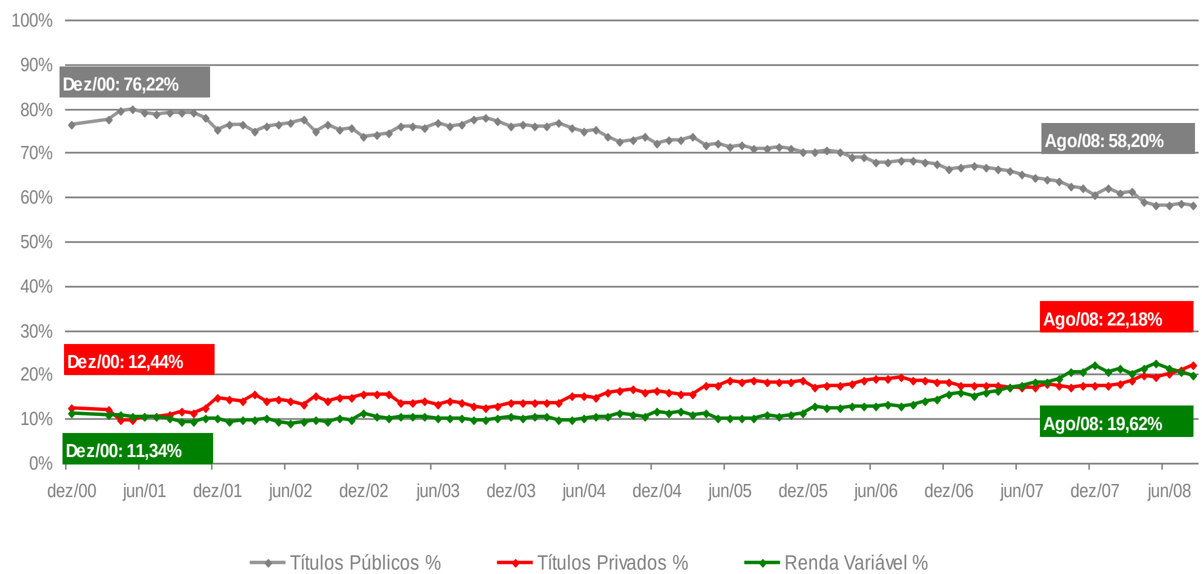
Mutual Funds Industry - Assets under Management

As of Aug/08	**R$ million**	**Breakdown**
Fixed income	996.703	80,4%
Equity	243.344	19,6%
- Stocks – Total	239.581	19,3%
- Sustainability/Governance	1.683	0,1%
- Others – stocks	237.898	19,2%
- Other variable	3.763	0,3%
Total	1.240.047	100,0%

Source: ANBID

Private sector trends in the composition of the portfolios

Over the past few years, the funds sector has been undergoing a significant transformation in terms of investment profile. While it is still possible to see a strong bias towards government bonds, structural changes are becoming evident. The following graph indicates the trend in these alterations: in December 2000, government bonds accounted for 76.22% of the portfolios while by August 2008, this share had fallen to 58.2%. On the other hand, the share of private sector credit – fixed income, typically represented by CDs and debentures – had risen from 9.65% to 22.18%. An impressive advance was seen in the participation of equities, a rise from 7.44% to 19.62%.



- *Government bonds*

- *Private sector bonds*
- *Equities*

Source: ANBID

These figures are still only modest by world standards. Typically, in those countries that have already reached economic stability, low rates of interest and investment grade status, the investment mix has advanced to a combination of between 40% and 50% in equities and the remainder in fixed income products.

It appears that the Brazilian market is already moving in this same direction, albeit, this tendency – still limited – is not easily perceptible, since the growth in variable investments has not been so intense through equities funds, but rather through significant growth in multi-market funds, known as "the Brazilian hedge funds".

These funds have seen a strong intake of new money, and are increasingly using equity strategies. An important example of this progress was the appearance over the past few years of funds specialised in long and short strategies. This movement has triggered the creation in 2006 of a specific category of funds which focus on this investment policy. This class began with 30 funds, and assets of R$ 5 billion (US$ 2.2 billion), and now after just a year, totals R$ 8 billion (US$ 4.1 billion) and 60 funds. However, due to the financial crisis, these funds have suffered and lost a high percentage of their assets. In September 2008, the total AuM of these funds was about R$ 3 billion (R$ 1.4 billion).

However, the industry as a whole is performing well. The total Assets Under Management (AUM) in June 2008 amounted to US$ 741.2 billion, equivalent to an increase of 31.66% compared with the same month in 2007, when AUM stood at US$ 556.6 billion. In addition, the funding raised in the period from June 2007 to June 2008 was US$ 2.4 billion. Leading fund raising vehicles were: (i) FIDCs (ABS funds) with US$ 13.9 billion; (ii) Private Equity with US$ 9.6 billion; (iii) Retirement Funds, US$ 4.6 billion and (iv) Money Market: US$ 6.9 billion. Net redemptions were largely concentrated in the following categories: (i) Fixed Income: US$ 28.1 billion and (ii) “Multimercado”: US$ 4.6 billion.

Change in equity funds profile

In addition to advances in the participation of variable income strategies, the equities funds’ segment has also undergone a significant change in profile. Typical funds, merely with the purpose of tracking the traditional BOVESPA index, are no longer a major attraction for the investor, and the tendency has been towards the segmentation of strategies, the highlight being the success of funds focused on dividend yield, small caps, sectors, social and corporate governance.

This transformation in the make-up of the portfolios (“FIXED INCOME”: Public Bonds → CREDIT: Private Sector bonds → “VARIABLE INCOME”: Equities and Multimarkets) as well as in the strategies of the equities funds (IBOVESPA → FOCUSED STRATEGY), is also a reflection of the evolution in the economic scenario of the country. For many years, the investment funds sector was an efficient generator of products either indexed to high inflation rates or to high interest rates. This “economic function of the sector” implied a short-term horizon, and a tendency to a low participation of equities funds.

Since the market is now moving towards a low interest rate one, it is only natural to expect a movement of: (i) fixed income funds investing in the long term, (ii) an expanded participation of private sector securities and (iii) a change in the focus of equities funds, where passive equity portfolios are no longer enough to satisfy investor demand and requiring diversified strategies with a horizon of specific equity market and corporate values: be they in the form of dividends, strategic sector, potential company growth, social policies and added value as a reflection of corporate governance - and no longer funds that simply “track the market index (Ibovespa)”.

Investment funds are regulated by the CVM, namely CVM Instructions 409 and 450. In addition, ANBID is editing a large number of self-regulation documents, which focus both on fund governance as well as the corporate governance that funds should require of their invested companies.
Regarding regulatory developments in the last 12 months, Anbid highlights two, listed below:

- **Advances in regulation with the internationalisation of the market –** The CVM has published Instruction 465/08. This has introduced changes to fund regulation, the most important are: (i) modifications in operational aspects for overseas investments involving the custodian and the guarantee of the existence of assets held by the fund in these markets; (ii) authorisation for allocation of up to 100% in overseas markets for those funds which require minimum investments of

R$ 1,000,000.00 per investor; (iii) these funds are exempted from complying with limits of concentration per asset and issuer, mandatory for remaining funds; and (iv) the marking to market of equity is now to be based on closing as opposed to average prices before;

- **Additional rules for politically exposed persons – CVM Instruction 463/08** has introduced new procedures for tracking operations undertaken by politically exposed persons. It represents an effort on the part of the domestic regulator to improve the regulation for combating money laundering and illicit practices.

In addition, main self-regulatory developments were as follows:

- **New classification of equity funds – Revised classification is based on the concept of strategies and on** international standards and no longer on eligible assets for investment. The following types of classification were created: (i) Dividends; (ii) Small Caps, (iii) Sustainability/Governance, (iv) Sectorial and (v) Private Equity Funds;

- **New code for self-regulation processes approved –** This code disciplines the procedures adopted in the event of evidence of failure to adhere to the norms established for all ANBID's codes. Previously, such practices were individually defined for each code. A specific code has now been introduced for standardizing procedural processes for the various self-regulatory segments: investment funds, corporate finance, custody and private banking;

- **Structured Funds Commission –** At the beginning of 2008, the Structured Funds Commission was created with three subcommittees: ABS Funds, Private Equity Funds and Real Estate Funds. These types of funds are becoming increasingly popular in Brazil and, therefore, a focused forum for the players in these markets was organised. Self-regulation initiatives are their hot topic;

- **STI ANBID –** A project started in late 2007, ANBID's Information Exchange System ("STI") consists of a new service that will enable the exchange of standardised files and messages related to investment funds and managed portfolios between industry players – portfolio managers, custodians, brokers, distributors etc. The system should go live by mid-2009;

- **New Guidelines for the Self- Regulation Code for Investment Funds**[10]

Proxy Voting – New chapter in the funds self-regulation code requiring that each manager has a policy for proxy voting allowing for mandatory voting under certain very specific situations in meetings involving companies, funds and debentures in which the fund under management has a participation;

[10] It is important to note, as mentioned later in this report, that the Proxy Voting chapter in ANBID's self-regulation code was a joint action between ANBID and AMEC.

Suitability – Suitability practices are defined[11]. Under the new rules, fund dealing institutions should adopt suitability methodologies for all investor profiles, including private and retail segments;

Division of the responsibilities by service provider – Previously all responsibility was concentrated on the fund manager itself even for those activities of the funds undertaken by service providers. With the introduction of the new Code, each service provider is accountable for its own sphere of operations;

Mandatory contracting only of service providers which have signed up to the self-regulation codes – Complementary to the division of the responsibilities was the requirement from fund managers to engage only service providers that have signed up to the Codes or which are members of ANBID. This thus obviates exposure of investors to service providers outside the scope of the self-regulation code and jurisdiction;

New criteria for membership/adhesion – Criteria for the admission of new members or those adhering to the ANBID codes, establishing a series of minimum requirements, and a more rigorous process of due diligence than the current one;

Minimum criteria for ranking – Minimum prerequisites were defined for use of rankings and awards in fund advertising;

- **Advances in supervision procedures of fund self-regulation**

Supervision based on risk – Implementation of self-regulation supervision based on risk, initially focused on the analysis of the fund prospectus. Under the new methodology, the prospectus will be analysed on a sample basis. Eventual errors identified will be classified according to their potential risk for the market. Cases that involve more serious risks shall be given greater priority, and will be brought to the attention of the investment funds monitoring commission (ANBID's self-regulation body which analyses cases and decides on the eventual opening of proceedings), which shall decide the most appropriate course of action;

Methodology of fund supervision routine filters revised and improved as well as the definition of new thematic filters – The old filters were perfected, and a new method defined, incorporating non-parametric techniques for the selection of funds subject to analysis by the technical area. Analysis is designed to verify adherence of the funds to their mandates as defined in the Investment Policy. New 'thematic filters' were also instituted for analyzing the consistency of funds where there is a concentration on certain classes of assets. In this case, funds with a major concentration on private issues were selected;

- **Self-regulation statistics –** The following statistical chart tabulates the penalties imposed under the investment funds self-regulation criteria in the period - divided by the principle topics covered by the Funds Self-Regulation Code. The statistics below show the number of penalties imposed in the period of Jun-07 to Jun-08. It is important to note that there is a hierarchy between letter, fines[12] and self-regulatory process as one is imposed after the other.

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[11] Suitability is assessed by setting the profile of clients, through a questionnaire, and identifying their risk profile and then offering them the best product.

[12] The OECD submitted a follow up question: "What is this? How large are the fines? What are the fines used for (ANBID administration)?" **Answer**: the fines are used in the educational area of ANBID; and they can reach up to

Enforcement	Prospectus	MTM	Advertising	ABS funds	Mandate	Fail On database delevery	Total
Letter	11	0	17	27	3	n.a	58
Fines	66	n.a	8	21	n.a	111	206
Self regulatory process	0	0	2	0	2	n.a	4

Obs: MTM = market to market, ABD Funds = FDIC

2. 3. Insurance Companies

General overview

The insurance industry in Brazil has experienced a steady growth since 2003. With annual expansion reaching 18.2% per year, the market (excluding health insurance) has more than doubled its size during this period. The main driver for this expansion is the inclusion of a product called VGBL in the life insurance segment. VGBL is considered a life insurance product, although it is more similar to a pension fund plan (in fact, it can be compared to unit-linked products). Because VGBL is a product with distinctive features, it became the main selling product for many insurance companies, including the market leaders. As of August 2008, life insurance accounted for around 50% of the market, with an annual growth of 22.8%. VGBL alone represents 32% of the industry; with an annual growth of 33%. It is clear that this insurance product brought major development for the whole industry.

Additionally, this market is dominated by what is called "bancassurance", where the main leaders are either owned or a part of big banks' groups. This makes the Brazilian market a unique case in the world, as insurance products are generally a secondary product that is sold in a bank branch. Considering the top 10 companies ranked by Gross Written Premium (GWP), these groups account for more than 85% of market share, with 8 players. Also, this segment in Brazil is highly regulated, overseen by SUSEP, the official governmental agency.

Investment capacity

However, insurance companies generally lack resources to investment. SUSEP and CMN (National Monetary Council) stipulate that a very high percentage of premiums sold must be converted into compulsory provision[13]. Although it means that the insurance segment becomes safer, it also reduces the ability of insurance companies to remain healthy in the long term. Because of the lack of resources to invest, insurance companies tend to be very conservative. Fixed income funds are preferred, although direct investments in governmental bonds also have a great share of this portfolio. On the other hand, stocks are not popular, as they do not provide the safety that insurance companies need.

In VGBL's case, the situation is slightly different. Because this product has many characteristics of open pension funds, there is a higher margin for investments in equity segments. Most companies offer VGBL in different formats, some with a higher percentage of total resources directed to the capital market.

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100 times the current monthly payment ANBID receives from its associates – currently R$21,485/US$9,341 per month.

[13] The OECD submitted a follow up question: "Fixed income funds and bonds?" **Answer**: Mainly fixed income and bonds

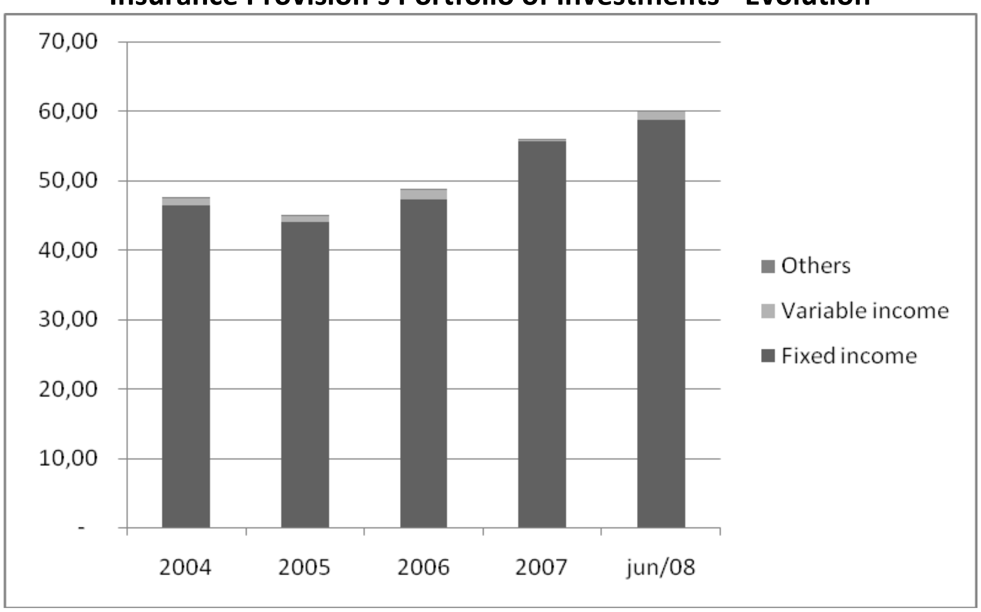
In the last 3 years, with the economic stability and the maturity of the Brazilian Capital Market, insurance companies have started to think about raising the amount of resources directed to variable income, as stocks are considered to be long-term investments. However, most of them are still conservative about this decision, and not many changes will be seen in the near future. The investment strategy that companies must follow, due to regulatory forces, is conservative, prioritizing fixed income assets and government bonds, in place of private companies' debt or the stock market.

Insurance provision's portfolio of investment at Jun/08

in R$ million	**Jun/08**	**Breakdown Jun/08**
Fixed income	58.745	97,7%
Equity	1.295	2,2%
- Stocks traded in the traditional segment	120	0,2%
- Stocks trades at "Nível 1"	574	1,0%
- Stocks trades at "Nível 2"	20	0,0%
- Stocks trades at "Novo Mercado"	152	0,3%
- Other stocks and investment funds	429	0,7%
Other	110	0,2%
Total	60.150	100,0%

Source: Susep

Insurance Provision's Portfolio of Investments - Evolution



Source: SUSEP

Demands for governance

Insurance companies have an important role as promoters of good governance practices in companies. This statement is true in most countries, but in Brazil it has gained a new meaning since 2007, when reinsurance companies started to actively operate in the market. The reinsurers act as sentinels to prevent high risks involved in some transactions. In Brazil, before 2007, the only reinsurer that operated was the state-owned IRB. The new rules that were established for reinsurance market allowed many companies to operate in the market, and the risks that were accepted by IRB alone, at a given price, now can be distributed among many other companies, and it stimulates companies to improve their governance practices in order to reduce insurance expenses.

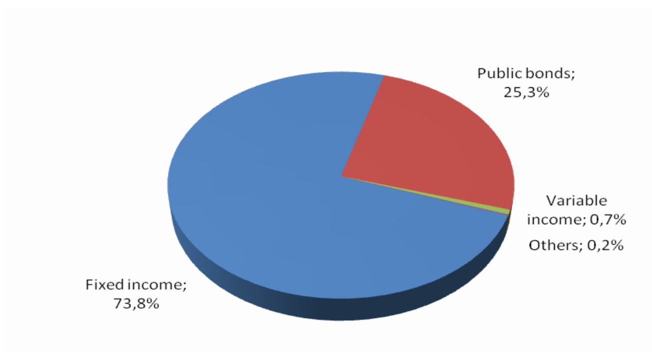
Big companies, like Petrobras, for instance, sign only one insurance deal, but involving many insurers and reinsurers at the same time. The reinsurers are the main players in this scenario, as they create incentives for companies to pursue better governance practices so there is room to reduce the price.

Open pension funds

In Brazil, the open pension funds industry experienced good growth since the participation of PGBL in the market. PGBL is a pension product providing some tax incentives to investors, in order to popularise the product and the habit of saving among the population. This strategy has worked well, as in 2004 open pension funds reached R$ 66 billion; in December 2007 the total amount of resources under management was R$ 127 billion.

However, although it has experienced a steady growth since 2003, open pension funds represent only 1.4% of total insurance provisions. In addition, PGBL managers are even more conservative investors than insurance companies. The share dedicated to variable income is much lower, due to the risks associated with the respective markets, such as capital markets or the foreign exchange market.

Open pension funds' provision portfolio of investments



Source: SUSEP

Conclusion

The insurance segment in Brazil is not a main player to promote good governance practices in invested companies. Due to the regulatory framework, as well as the composition and profile of the market, with the main players being the same for mutual funds and open pension funds industries, it seems that most companies are not willing to take a more active approach in this issue in the near future.

The main developments in this area are the changes in the rules for reinsurers, which is believed to benefit the market as whole, from its own operations to the incentive for companies to reduce their risks in order to obtain financial gains in insurance contracts. It is believed that, from a corporate governance point of view, companies will tend to be more transparent and responsible.

The open pension funds' portfolio of investment, as well, although higher than that of insurance, has a very small portion of available resources directed to variable income. Pension funds in Brazil are conservative, as companies are reluctant to expose themselves to a higher degree of risk. There is a long-term trend, however, towards a higher share of variable income making it an increasingly important investment for this segment as well.

2.4 Private Equity Funds

General overview

Private equity funds are quite recent in the Brazilian financial market. The demand for this product has been rising since 2006, when the Brazilian capital market experienced a huge leap. New products, called FIPs (which are investment funds in private companies), started to amass as more and more investors began to accept a higher risk in exchange for higher expected gains. Many foreign funds started to operate in the Brazilian market, and in December 2004, the total volume of committed capital was US$ 5.58 billion, while in July 2007 this volume was US$ 16.7 billion, in 89 fund managers and 153 funds investing in 404 portfolio companies. In addition, many companies started to look for different options to finance their activities, and the private equity funds appeared as a feasible alternative for many of them.

ABVCAP is the association that represents the private equity and venture capital funds. There are movements in the direction of the promotion of self-regulation of the market, but a self-regulatory document is yet to be published.

CVM is the governmental organisation that regulates the operation of FIPs. There are three main codes about this topic: Instruction 209, which is the first that regulates these funds in Brazil, and provides a few limitations to its administration and management; Instruction 391, which is the main law regulating the market; and Instruction 409, which is a general regulation for funds in Brazil (mostly mutual funds).

Promotion of corporate governance

There are few but conclusive studies that indicate that private equity (PE) funds have a positive impact in promoting good governance practices. In most cases, PE companies tend to demand modifications in governance, in order to better control the risks that are involved in companies' activities and add more value to the business.

The results of this professional approach can be better observed when PE funds sell their participations in invested companies. Some studies show that companies that went public through IPOs show better results in their first 12 months when they had PE funds investments previously to the public offer (GIOIELLI, Sabrina, 2008). This is more visible when we observe that manipulation of accounting information is less detected in these cases. It means that governance practices are being used, providing the new minority shareholders with higher degree of transparency.

In addition, in PE-backed companies the Board of Directors tends to be more professional and independent. It has a direct influence on the quality of the executive boards, as they are appointed based on qualities and experiences necessary for each role.

Risk managements and conflicts

Using their network and leveraging the investments made, PE funds tend to act as main driver of companies' improvements in management, but not always in governance practices. In addition, there may exist conflicts between PE funds and the company itself, as their relationship has limited duration. In Brazil, though, the role of these investors has been positive, as it has helped many companies to grow and then go public, adding value to them and the market as a whole. PE funds have provided good examples of how Corporate Governance can be used to generate wealth in the market.

3. Good Governance Practice

3.1. Current Panorama

Number of issues	**Total**				
units	**2004**	**2005**	**2006**	**2007**	**9M08**
Novo Mercado	7	10	29	52	6
Nível 2	3	4	7	7	1
Nível 1	5	3	4	10	3
Traditional Market	-	2	-	1	-
Bovespa Mais	-	-	-	-	1
BDR	-	-	2	6	1
Total	15	19	42	76	12

Volume of issues	**Total**				
R$ million	**2004**	**2005**	**2006**	**2007**	**9M08**
Novo Mercado	4.084	7.114	18.779	53.588	9.520
Nível 2	1.645	2.412	5.717	4.159	508
Nível 1	3.076	2.989	4.384	7.622	23.840
Traditional Market	-	1.422	-	2.069	-
Bovespa Mais	-	-	-	-	21
BDR	-	-	1.556	2.675	367
Total	8.805	13.936	30.436	70.113	34.255

In recent years and up to the 1st half 2008, in addition to economic changes in Brazil as a whole with an impact on investor behavior, and on the funds sector profile, the equity market has already gone through an important transformation as illustrated in the graphs. The first graph shows the volume in Reais of issues since 2003 by level of corporate governance while the second shows the number of operations. In practice, share issues in the so-called traditional market without minimum governance requirements are virtually no longer an option open to companies.

As of July 2008, with the drop in international markets and a decrease in international flows to Brazilian markets, there was a contraction in the market and issues completely stopped,

3.2 Recent Past: Investment Funds and Proxy Voting

In an investment funds market that traditionally tracked Fixed Income benchmarks, and in an environment of stock exchange trading in which governance was not a priority, it would be natural that a discussion of Proxy voting would not have been seen as relevant.

Even with the small percentage of equity funds that existed in the past, investments in companies on many occasions were seen as an instrument for achieving short and medium term returns. Thus, within the confines of this "investment philosophy" disagreements between minorities and controlling shareholders were merely viewed as information for pricing the security. It was therefore acceptable practice to adopt one of the known versions of the "Wall Street Rules"- "on investments: sell a stock rather than try to change the company's policies", or "selling the shares of a company whose performance is unsatisfactory".

In the same way, the Brazilian norm always dealt with the question of political activism in vested companies as an option for the portfolio manager. It was obligatory[14] to describe in the investment fund prospectus the "policy relative to the exercise of voting rights of the fund by the portfolio manager or by its legally appointed representatives, in general meetings of the companies in which the fund held shares", there being no restrictions should the policy be specifically not to exercise voting rights – the most common stance taken over the last years.

With the maturity of the variable income market and investors taking a longer term view, this investment philosophy no longer holds, and the adoption of good governance by both funds and companies, as well as the policy of exercising voting rights have become an important variable.

The market itself has perceived that these practices need to advance further and the policy of "not exercising voting rights under any circumstances" is no longer an option aligned with the direction in which the investment funds industry has moved: namely, a focus on the long term and with increasingly more specific strategies. Thus, the trajectories are divergent, leaving little scope for "non proxy voting policies".

Beside the funds political activism question, some qualified investors began to question the independence of portfolio managers linked to large financial institutions, especially when these funds also invest in listed companies that are clients.

Responding to these concerns the large Brazilian financial institutions, inspired by foreign examples, split the activities of commercial banking and portfolio managing, "building" Chinese walls and implanting rough ethics codes concerning how they deal with partners.

[14]The OECD submitted a follow up question: "By regulation?" **Answer**: Yes, CVM required even before ANBID's self-regulation

3.3 The Protection of Minority Shareholders Rights in Brazilian Capital Markets- Investment Fund Activism [15]

Recent Brazilian capital markets history has brought to light several examples of cases where portfolio managers have mobilised in defense of minority shareholder rights.

Among the principal actions of the investment funds, some brief accounts of higher profile cases in the securities' market will be given through the following summaries.

TELEMAR OPERATION – The company's controllers moved in October 2006 to promote a corporate restructuring through the incorporation of a holding company and various subsidiary companies under the umbrella of Telemar Participações S/A. The controllers suggested that the group's existing corporate structure was restricting its ability to access capital markets and that restructuring would inject greater liquidity into the company's securities.

In the light of the company's proposal, the market concluded that the exchange ratio for shares under the new structure was unduly onerous to the minorities holding the preferred shares, notably the amount to be paid for the controlling stake[16]. The operation as proposed would unjustifiably dilute the participation of the preferred shareholders.

In addition to the question of the control premium and the dilution of the minority shareholders, the Telemar operation further provoked issues involving conflict of interests, which were submitted to the regulator (the CVM) and the Law Courts[17].

This corporate restructuring story resonated widely in the press and resulted in an unusually high shareholder presence at the General Meeting, which rejected the proposed operation[18].

ARCELOR OPERATION – This 2007 operation involved the change in indirect control of Arcelor Brasil, parallel to Mittal's hostile bid for the controlling shareholder of the Brazilian steel company, Arcelor Europe.

The issue revolved around the obligation or otherwise on the part of Mittal - that acquired the indirect control of Arcelor Brasil - to hold a public offering to acquire the company's minority shareholders.

Various portfolio managers took the view that the public offering was necessary from the legislative point of view and principally on the grounds of the company's bylaws. At first Mittal rejected the idea of a public offering. However, in the face of an investor outcry and a ruling from the Brazilian Securities and Exchange Commission, Mittal yielded and held a public offering for buying out the Brazilian shareholders.

However, the conditions of the public offering initially proposed were for a value below that offered to European investors. As a result, portfolio managers and minority shareholders filed a complaint with the

[15] AMEC´s contribution (original report)
[16] The OECD submitted a follow up question: "Was it too low?" **Answer**: The premium for ordinary voting shares was too high.
[17] The OECD submitted a follow up question: "Are they still pending or have they now been resolved?" **Answer**: Resolved because CVM judged no conflict of interests could be determined ex-ante (i.e., before the transaction was completed and conflicts were proven by decisions)
[18] The OECD submitted a follow up question: How could they reject it if controlling shareholders voted in favour?" **Answer**: Only preferred non-voting shareholders voted and the controlling shareholder did not have the majority of shares.

regulator, arguing that the offer to Brazilian shareholders was unfair, as it was less than had been offered to European investors.

The technical area of the Brazilian Securities and Exchange Commission ruled against the Mittal offer and set a price of R$ 51.27 per share, well above the approximately R$ 33,00 initially proposed, indicative that this subsequent victory was only possible thanks to direct minority shareholder pressure.

IPIRANGA CASE – This operation consisted of a share purchase agreement announced in March of 2007, through which the controllers of the companies of the Ipiranga Group sold their shares representing the shareholding control and the control of its subsidiaries to Ultrapar, in the role of direct purchaser and commission agent for Petrobras and Braskem.

The minority shareholders of the Ipiranga companies identified in the restructuring the possibility of an infringement of their rights and a negative impact on their assets, particularly in relation to the exchange ratio set for minority shareholders in the incorporation of the shares of the Ipiranga Group companies by Ultrapar.

Another element that caused some unease in the market related to the absence of any prior or concomitant appraisal report of the companies involved in the operation for assessing a fair exchange value.

The premature disclosure of the exchange ratio caused some turbulence in the price of the securities involved, although with the publication of the material fact the market adjusted prices using as a parameter the exchange value and the market price of the companies involved.

Even after the disclosure of the appraisal report of the companies involved in the restructuring, some questions continued unanswered following a direct analysis of the information provided in the document. In light of this, AMEC forwarded correspondence to the chairmen of the boards of directors and the respective investor relations officers of all the publicly held companies involved as well as to the investment bank responsible for the appraisal report, requesting information and documents on the restructuring operation.

At the same time, a suggestion was put to management as to the possibility of setting up a meeting so that any clarifications deemed necessary could be provided in order to contribute to the transparency considered appropriate in the equities' market as well as for its healthy development.

TRAFO CASE – this operation involved Weg S.A.'s acquisition of Trafo and the subsequent delisting of the acquired company.

In this case, the minority shareholders were alerted to (i) the absence of a control premium paid on the common shares of the former controller, which also had preferred shares; and, (ii) the inconsistencies in the appraisal report prepared by the companies for Trafo's delisting. Among these inconsistencies, particularly notable were (a) the zero perpetuity growth rate attributed to Trafo (b) the absence of any justification for the forecasted increase in raw material costs of the acquired company; and (c) the Brazil country risk rate used to calculate Trafo's discounted cash flow rate.

In terms of the absence of the control premium, Weg paid the same price for both common and preferred shares of the former controller. However, in Brazil the tag along feature is a guaranteed right in law for holders of common shares only. Hence if the acquiring company pays the same price for the two classes of share, the minority common shareholders understand this to be tantamount to an infringement of their rights.

In addition, the acquiring shareholder proposed to delist Trafo's capital paying the preferred shareholders a lower amount than had been paid to the former controllers.

Given this scenario, the portfolio managers, represented by AMEC, requested information and documents from the board directors and investor relations officers of the companies involved in addition to those responsible for preparing the appraisal report.

NEW HYPOTHESIS FOR A MATERIAL FACT – another example of portfolio activism supported by AMEC relates to an actual case in which the minority shareholders believed their rights had been infringed, alleging insufficient transparency on the part of the vested company in light of the latter being judicially ordered to pay a significant amount in cash relative to the net assets or company sales.

Besides the absence of any disclosure of the judicial decision, the company was also found wanting in its obligation to transparency in not disclosing to the market that it had also been required to cancel the resolution of the general shareholders' meeting, which approved the increase in capital, thereby triggering a change in the company's shareholding structure.

In Brazil, there are rules both of a legislative as well as a regulatory nature requiring a company to disclose material facts which may have an impact on the price of its shares quoted on the stock exchange, influencing the investor's decision to buy, sell or hold the securities or further, the decision to exercise any rights inherent in the condition of title owner to the securities.

Such rules serve as examples, and do not expressly require that key judicial decisions be disclosed with immediate notice to the market. Thus, with the purpose of contributing to the juridical, legislative and regulatory framework, AMEC published Resolution AMEC 02 on the need for publicly held companies to disclose information and publish as an announcement of a material fact judicial decisions or arbitration awards that contemplate material facts.

In addition to the isolated attitudes adopted in the specific cases and the regulation proposal presented, in another study, Brazilian portfolio managers are also working to get from the vested companies the adoption of good governance practices, materializing these efforts by the indication/election of board of directors' members, especially members to the fiscal council.

The preference by the election of members to the fiscal council is justified by the legal rights given to the minority shareholders, who can demand the creation of the council in companies where they are not permanent, by the vote of 10% of the shares with voting rights or 5% of the capital stock in preferred shares.

Beyond the creation of the fiscal council, Brazilian corporate law has another right to the minority shareholders that allows the election, in a separate vote, of members to the fiscal council by the shareholders that owns the capital stock in preferred shares. The same right is granted to the shareholders that own at least 10% of the shares with voting rights.

The above cases illustrate that while the Brazilian equities market is showing clear signs of maturity, much remains to be done before consolidation is complete. On this point, the activism of minority shareholders, investment funds and their portfolio managers as well as firm action on the part of entities linked to good governance practice and protection of investor interests are of crucial importance to the improvement of regulatory and/or legislative rules for strengthening the capital markets. This will ensure that the investment environment can be made more transparent, more symmetrical in relation to company information and engender greater investor security.

3.4 Updates since the First Report was Edited[19]

COSAN CASE: The Cosan case was closely followed by AMEC and ended up forcing it into action. Cosan S/A, whose shares trade on Bovespa's Novo Mercado, created another company – Cosan Limited – in an off-shore location where minority shareholders receive less favorable treatment.

The restructuring of the Cosan group, first proposed in June 2007, was to be executed in three stages. First, a global offering was made by Cosan Limited, headquartered in the Bermudas. This was followed by a corporate reorganisation which actually did not alter the shareholding control structure. Finally, an offer was made to the minority shareholders of Cosan S/A, listed on the Novo Mercado, to migrate to Cosan Limited.

As far as the global offer was concerned, the question that gave rise to the greatest questioning and mistrust on the part of minority shareholders had to do with the proposed capital structure of Cosan Limited. The company was to have two classes of common shares: "A" and "B" shares. The "A" class shares to be represented by Brazilian Depositary Receipts (BDRs) and offered to Brazilian investors. The "B" class shares to be subscribed by the controlling shareholder of Cosan S/A. The difference between one class of shares and the other lies in their respective voting rights. The "B" class shares have the right to 10 votes, whereas the "A" class shares have the right to just one vote.

The market had little doubt that the rules and principles of corporate governance were seriously threatened by this proposal. One of the foundations of good corporate conduct, endorsed by all corporate governance manuals and by capital markets themselves, is that of equitable treatment for all shareholders, including foreign ones. AMEC considers the principle of one share/one vote is absolutely fundamental, one of the most heavily defended rules of good corporate governance.

The proposal, communicated in the same announcement to the market as Cosan's corporate restructuring, was poorly received. As the result of pressure from AMEC, minority shareholders and the Bovespa, Cosan's controlling shareholder eventually reconsidered the proposal. The decision was that, as part of the public offer of a voluntary exchange of shares in Cosan S/A for shares in Cosan Limited, the company would grant shareholders in Cosan S/A the right to exchange, of their own free will, their common shares in Cosan S/A for Class "A" shares issued by Cosan Limited, for BDRs representing Class "A" shares issued by Cosan Limited or for class "B" shares of a second series to be issued by Cosan Limited.

This was a clear case of the pressure exerted by corporate governance entities preventing the rights of minority shareholders from being ridden roughshod over.

THE CASE OF M&G POLIÉSTER – PREVIOUSLY RHODIA: In July 2007, M&G Poliester informed the market that it had entered into a contract with M&G Polímeros, both companies being controlled by the same Italian parent company Mossi & Ghisolfi S.p.A.. The contract was described as an Instrument for the Proposal and Justification of an Incorporation of Shares (Instrumento de Protocolo e Justificativa de Incorporação de Ações). This document established the conditions under which shares issued by Polímeros would be incorporated into the balance sheet of Poliéster, resulting in the conversion of the first into a wholly-owned subsidiary of the second.

[19] AMEC's contribution to 2008 update

The contract also provided for the conversion, once the incorporation was completed, of the company's preferred shares into common shares, in the proportion of one common share per preferred share. Shareholders of Poliéster would also be given tag along rights equivalent to 100% of the price paid for the shares owned by the controlling shareholder.

As part of this transaction, the controlling shareholder of Poliéster had created another firm, Polímeros, which had commenced operations in March of that year. The operations of Polímeros were to be exactly the same as those of Poliéster. Thus the controlling shareholder was the owner of two companies, both of which competed in the business of producing and selling PET resin.

AMEC, however, concluded that there were signs of possible abuse of power on the part of the controlling shareholder. One of these had to do with the criterion used to calculate the share exchange ratio in the incorporation transaction, which, it felt, was excessively beneficial to the controlling shareholder and to the detriment of the minority shareholder. AMEC also pointed out the disrespect of the principle of loyalty on the part of the controlling shareholder, and the unjustified dilution of existing shareholders, something that is not permitted under the existing legislation.

An objective analysis of the proposed transaction made it possible to detect signs of inconsistencies, such as the fact that the perpetuity growth rate used to calculate the projected cash flows of Polímeros was significantly higher than that used in the calculations for Poliéster, despite the two companies operating in exactly the same line of business.

Faced with this situation, AMEC felt that the proposed date for convening the Extraordinary General Shareholders' Meeting of Poliéster should be postponed, given its suspicions of abuse of shareholder control and conflicts of interest. CVM, when it was called upon to opine on the matter, suggested that postponing the Shareholders' Meeting might not be the ideal reaction in this case, given that the above suspicions of shareholder abuse and conflict of interest could only be analysed by CVM after the decision was taken at the Shareholders' Meeting[20].

AGRENCO: The information published in the papers in July 2008 and thereafter about Agrenco Ltd., its management and controlling shareholders ensured that this case was included in AMEC's agenda of things to discuss. Agrenco Ltd. Was accused of fraud, tax evasion and misuse of funds amongst others. Its Technical Commission analysed the details that would later become public knowledge and have had a significant influence on the pricing of the company's Brazilian Depositary Receipts (BDRs). As to the crimes and other irregularities that the controlling shareholders are alleged to have committed, AMEC's position was that these are being investigated by the appropriate authorities (Federal Police and the CVM), and that the best thing would be to wait for the result of those investigations before commenting on them.

Nevertheless, the matter remains high on the agenda of the Technical Commission, due to its enormous relevance for Brazilian capital markets and investor perceptions of BDRs. The objective of the discussions is to contribute to improving the regulation and self-regulation inherent in BDRs, in the companies that issue them and the players in the markets that deal in them. This is typical of the sort of proactive conduct we have come to expect from AMEC.

[20] The OECD submitted a follow up question: "So what happened? Did the meeting go ahead and is CVM's review pending?" **Answer**: CVM did not postpone the meeting because the suspicion of shareholder abuse and conflict of interest could only be analysed after the decision was taken at the GSM and the Exchange concurred although minorities were against it. AMEC's role in the issue stopped in this moment.

The AMEC Technical Commission investigated issues relating to the protection of minority shareholders, the responsibility of the managers and coordinators of public offers, the responsibility of auditors regarding the quality of financial analysis and other aspects of corporate governance.

TOTVS / DATASUL: The merger between the above two software companies, announced in July 2008, has been the topic of much debate in AMEC's Technical Commission. The transaction, structured so as to take place over time, consists in the incorporation of Datasul by Makira, an unlisted company owned by Totvs. Only after Datasul has been incorporated by Makira will the incorporation by Totvs take place. The way the transaction is structured has led to the debate concerning the mechanisms used and the implications for company law.

Albeit in this specific case no potential loss has been detected for the shareholders of either company, it is AMEC's opinion that the model of the incorporation of shares by an unlisted company could be copied in other situations and opens up the possibility of losses for shareholders outside the controlling shareholder group.

One of AMEC's main concerns as regards company law is the fear that this episode could lead to minority shareholders being deprived on other occasions of the right to vote on proposals involving the incorporation of other companies.

Another detail that caught the eye was the disclosure of the values and exchange ratios prior to the appraisal being terminated.

For these reasons, the transaction is on the Technical Commission's agenda for further discussion.

VCP/ARACRUZ: In August of 2008, VCP – Votorantim Celulose e Papel announced the acquisition of 28% of the voting stock of Aracruz (previously in the possession of Arapar), equivalent to 12.4% of the company's total capital. The acquisition, in the amount of R$2.71 billion, was to be accompanied by a corporate reorganisation of the two companies involved, terminating in a merger.

At the time the acquisition was announced, minority common shareholders, with the support of AMEC, questioned the way that VCP was intending to gain control of Aracruz, which deprived them of the right to include their shares in the sale (tag along rights).

In the same month of August, international investors, led by F&C, also questioned, in a letter addressed to the CVM, the way in which the transaction was being structured, and which, in their opinion, would end up negatively affecting the attractiveness of the Brazilian market.

At that time AMEC received a copy of that letter and took it upon itself also to manifest its opinion to the CVM, underscoring certain particularly sensitive points, such as the disclosure of the share exchange ratio before the valuation reports were ready, as well as the possibility of control being transferred in stages.

As it turned out, the parties involved decided to postpone the transaction in order to adjust the numbers to the new economic situation, due to changing international economic conditions, the appreciation of the US dollar against the Brazilian real and the announcement by Aracruz of major losses from foreign exchange transactions, to the tune of R$1.95 billion. On October 17, the suspension of the merger between the two companies was announced.

Considering the losses to which the management of Aracruz has had to admit, AMEC is supporting the initiative planned by the minority shareholders, who intend to use the legal instruments at their disposal to demand greater transparency on the part of the company as regards disclosure of exposures to derivative financial instruments.

TENDA/GAFISA[21]: On September 1 2008 TENDA made an announcement to the market concerning a merger between TENDA and Fit Residencial Empreendimentos Imobiliários Ltda. ("FIT"), a company controlled by Gafisa S.A. ("GAFISA").

The transaction was to take place by means of an incorporation of FIT by TENDA. TENDA would therefore continue to exist and be listed on Bovespa's Novo Mercado, whereas FIT would be extinguished.

With the incorporation, GAFISA became owner of 60% of TENDA's shares, after an exchange of GAFISA's share in FIT for TENDA shares.

What attracted AMEC's attention to this transaction, leaving aside the values attributed to FIT and TENDA, was the fact that the transaction was approved without any consultation with GAFISA's shareholders, on the argument that it was a transaction entered into with one of GAFISA's own subsidiaries.

The two main questions concerning this transaction have to do with the possibility that a legal maneuver may have been used to avoid characterizing it as a sale of controlling stake, and the consequent triggering of tag along rights for other shareholders. The second concerns the existence of an unjustifiable dilution of minority shareholders.

In the end, however, seeing that the original controlling shareholder and the minority shareholders received identical treatment, these doubts were eventually dispelled.

SADIA[22]: Sadia invested in foreign exchange derivatives in the hope of profiting from the continued strength of the real against the dollar. This scenario, however, with the deepening of the financial crisis in the USA, failed to materialise.

As the company's exposures under these derivatives began to exceed the limits established by its risk policies, Sadia was forced to start closing out these contracts in order to get back within policy limits, and consequently to book losses in the region of R$760 million.

It was later disclosed that Sadia's exposures under these derivatives contracts had reached twice the level that had been authorised by the board of directors. Instead of restricting itself to the maximum 6 month tenor authorised by the board, Sadia's finance department had entered into 12 month contracts. And instead of hedging the equivalent of 6 months exports, the company's exposure was twice that.

[21] Note (IBGC): the transactions involving Totvs/Datasul and Tenda/Gafisa merited a pronouncement from the CVM (Memo SRE/Nº 214/2008) on the topic of the non-applicability of tag along rights. In CVM's view, the incorporation consisted of an original acquisition of shares, a situation in which shareholding control is acquired, but not sold, since the acquiring entity is already part of the controlling block of shares. Besides conforming to current legislation, such transactions permit minority and majority shareholders to migrate on an even basis. They are, however, frustrating for those minority shareholders who were expecting a premium for poison pill clauses in the company's bylaws, which were not triggered because such clauses are not applicable when the chosen vehicle is incorporation.

[22] Note (IBGC): The Aracruz and Sadia cases were responsible for the editing of CVM Instruction 550 (disclosure of derivative exposures) discussed here, as well as a Note by AMEC, with the support of IBGC and APIMEC Nacional.

At the request of the PREVI pension fund, one of Sadia's shareholders, the new chairman of Sadia's board of directors convened an Extraordinary General Meeting for November 3 2008, to provide shareholders with information and explanations. Among the items on the agenda for that Meeting is PREVI's request for a "Vote regarding the filing of a civil liability suit, as provided for in article 159 of Law 6,404/76 and a demand for indemnification for the losses suffered".

AMEC supports PREVI's initiative and, on October 23, approved a motion calling upon minority shareholders to attend the Extraordinary Meeting and demand of the company greater transparency in its disclosure of financial information.

3.5 Main Issues under Discussion by Portfolio Managers[23]

Portfolio managers have been debating various points considered of critical importance for guaranteeing minority shareholder rights as well as the conduct that must be adopted in the relationship between the portfolio managers themselves and the vested companies. Among the points are the following:

- The dissemination of mechanisms of proxy voting as a means of stimulating activism and participation of the funds at shareholder meetings of the vested companies, and with this the reduced chances of conflicts of interest arising between portfolio managers and quota holders in the exercise of voting rights;

- Raising awareness among the portfolio managers that exercising voting rights is part of their fiduciary duty to investors. There already exist CVM decisions confirming these understandings, such as CVM process 2001/1857, in which it was decided that "For this reason, such funds normally carry the portfolio management brand in its denomination (as occurs in the case in hand): it is the name of the portfolio manager that is at stake, and, thus, its capacity of achieving success in the investments, continuing to do so in the future and progress in its activity. The entity/person that contracts this portfolio manager has no desire to manage, normally considering itself/herself/himself unsuitable for doing so or as having no vocation for such management. Indeed, this characteristic of participative investment funds would be completely distorted if quota holders could change key decisions on investments such as for example sign or no, a shareholders' agreement.";

- Definition and disclosure of voting policies on the part of funds and portfolio managers, the vote being exercised by the portfolio managers, their in-house legal departments or lawyers hired for this purpose;

- Making a convincing case that a passive posture with respect to fund management does not comply with the fiduciary duties of the portfolio manager towards its quota holders, as well as the vested company at the meetings of which the fund manager must exercise its voting rights in the best interests of the corporation;

- The understanding that the rules of transparency, including good governance practices, are fully applicable to the portfolio managers which, in order to legitimately require the implementation of Corporate Governance in the vested companies, should adopt this same posture in relation to their investors. Based on this understanding, there should be no confusion between the principle of

[23] AMEC´s contribution (original report)

transparency and the disclosure of strategies, which in the case of portfolio managers represents the composition of the investment portfolios. The option to disclose this composition is at the discretion of the managers and explained in the fund regulations. In any case, and especially in view of the lengthening of the investment profile, the view is that the delay of three months before disclosure is very short and that such a term should be increased;

- The lack of need to install “boards of directors” of the funds, an entity currently absent in the configuration of Brazilian funds that adopt the juridical format of condominiums, where investors have the power of decision through their participation in quota holder meetings. At such meetings, quota holders can also pass resolutions to remove the portfolio manager. It is the belief of the portfolio managers that this legal format allows greater quota holder autonomy, thus mitigating the risks of limited independence, a characteristic of the US corporate model;

- The understanding that the implementation of investment committees pursuant to CVM Instruction 409 is seen more as a tool to be offered to exclusive funds, which in some cases carries the risk of reducing the clarity of the fiduciary duties of the manager, bearing in mind the functions of the investment committee;

- The discussion on ways to reduce absenteeism and increase the participation of quota holders in the meetings of the funds themselves. Among the possible solutions of particular importance is the earlier dispatch of more comprehensive material for examination by quota holders, detailed notices, and the transmission of quota holder meetings via webcast and the possibility of disseminating the employment of electronic voting as a useful and necessary tool for encouraging activism;

- The understanding that there is no need to audit the portfolio managers, since their products, namely the funds offered to third parties are, and should continue to be, audited. Here it is appropriate to mention that there is room for improvement in procedures for auditing funds.

3.6 Other Initiatives Taken by AMEC in the Interest of Easier Access for Minority Shareholders to General Meetings and Improvements in the Quality of Market Disclosure [24]

The importance being given to the presence of shareholders at company meetings is increasing all the time, particularly in those companies with a broad shareholder base and that need a more active attitude on the part of shareholders

This being so, and bearing in mind the obstacles encountered by shareholders, Brazilian or foreign, to exercising their voting rights, AMEC has sought to maintain a fluid dialog with the entities responsible for regulation and self-regulation in Brazilian capital markets.

Such labors have yielded, so far, the following fruit:

Compulsory Voting for Fund Managers

AMEC, together with ANBID, fostered the rules that oblige fund managers to exerce their voting rights in shareholder’s meetings.

[24] AMEC’s contribution to update

General rules were determined, allowing the portfolio manager to build their specific rules as a manner of differentiation. (note: for more details see topic 4.2)

Easier Access to Statements of Shares Held in Custody

One of the greatest obstacles faced by minority shareholders to enforcing their voting rights at company general meetings has always been the ability to obtain from CBLC – custodial agent for the BM&F/BOVESPA - statements proving their ownership of their shares.

In order to accelerate the process of issuing statements proving share ownership, AMEC has held discussions with CBLC and obtained a firm commitment on their part to implement new and innovative technology that will permit statements to be issued and duly authenticated by authorised third parties, thus removing the present operational bottleneck.

Proxy Voting and Electronic Voting

Because of general debates, in which AMEC was an important player to foster, Director Marcos Barbosa Pinto, of CVM, publicly declared the understanding that Brazilian law allows electronic power of attorney documents.

The electronic vote, however, is still under observation, especially regarding the minimum quorum for the shareholder meeting, which may require specific legislation. AMEC technical commission is analyzing this issue (please refer to topic “CVM rules on shareholders meetings”).

Draft Bill on Portfolio Manager’s Votes

AMEC’s technical department is drafting a bill to permit fund managers/equity portfolio managers to exercise, directly and in person, the voting rights associated with the shares belonging to the funds/portfolios managed by them.

This measure is intended to make it easier for voting rights to be exercised by those who have effective knowledge of the company in whose shares the funds have been invested - the fund/portfolio manager – thus contributing to a healthy activism on the part of minority shareholders.

Possible Changes to Market Announcement Rules

AMEC, as a member of CODIM – Committee for the Market Disclosure of Material Information, dedicated to improving the standards of market disclosure, presented its recommendations concerning the disclosure of material events or facts.

The Committee accepted the proposal that “Any judicial decision, injunction, restraining order or form of prior relief proffered in whatever instance or any arbitration award condemning a company to make material payments” should be considered a material fact and, thus, be the object of an announcement to the market.

This proposal will be opened to public hearing in the next few days and if approved will be the guideline henceforth, even though without the force of law, as the procedures to be followed by those companies concerned with good corporate governance.

3.7 Pension Fund-Related Evaluations[25]

The Brazilian pension funds have contributed to this report by providing their analysis as to the current stage of development of the Brazilian pension funds industry.

Among the items in the analysis, the following are worth mentioning:

- The current scenario of declining returns from fixed income applications should increase the participation of the pension funds in the variable income and real estate markets;
- Various smaller sized funds have opted to outsource their equities' portfolios also offering differentiated profiles to their members. In parallel to this tendency, a growing activism has been detected combined with the interests of minority shareholders concerned with the results of inspection;
- Recent increased flexibility on the part of the National Monetary Council on the rules applicable to pension funds has permitted an increase in the limit for applications in variable income instruments through the maintenance of a reserve surplus higher than the exceeded value, thus maintaining a perfectly controlled risk profile;
- Both the inspection processes as well as the audit procedures have proved to be appropriate to the Brazilian reality, perhaps there even being rather too much detail and costs for account of the pension funds.

4. ANBID Proposal[26]

4.1 Improvements to the Self-Regulation Code for Investment Funds

ANBID, a self-regulation entity for the investment funds industry – the self-regulation, it should be noted, is exercised without any powers of legal enforcement, but on the voluntary initiative of its participants - has decided to deal with the question of improvements on the basis of self-regulation. During 2007, ANBID has been progressing positively in these discussions. As from 2008, "ANBID's Self-Regulation Code for Investment Funds" will already be incorporating minimum practices with respect to the matter, eliminating the possibility of not exercising voting rights under any circumstances.

Despite being the subject of discussion of its members, self-regulation will also begin covering Proxy voting at General Meetings of Publicly Held Companies, but not only restricted to these assets – the policy will cover any asset class in the fund where there are voting rights, including debentures, fund quotas and other assets. Such policies should be adopted by the investment funds in the following manner:

- The rules on Proxy voting shall be compulsory to Funds which have as their investment policy the application in financial assets such as, but not limited to: (i) rights, share participations and stock splits; (ii) investment fund quotas; (iii) debentures, commercial papers, promissory notes, contracts, certificates and private bonds in general and (iv) other securities, should these assets be eligible for discussion in shareholders' meetings;
- In these cases, it is obligatory to define a "Policy for Representation of Fund Investments in Meetings", covering the principles and procedures to be adopted by this representation, aligned with

[25] IBGC´s contribution (original report)
[26] ANBID´s contribution (original report)

the “Guidelines for a representation policy of funds in meetings”, issued by the Anbid Funds Self-Regulation Committee;

- The regulations and prospectuses must obligatorily describe the “Policy of Representation of the Funds in Meetings”, either in its unabridged or simplified version, in the latter case making reference to the website where the investor can find the complete version of this policy. The unabridged version will also be registered at ANBID;

- The “Guidelines for a representation policy of funds in meetings” should be divided into four chapters: (i) the Purpose of the Policy; (ii) General Principles; (iii) Best Practice and (iv) Minimum Structure, which lists the requirements and the minimum structure for the “Policy of Representation of the Investment Funds in Meetings”.

- In the Chapter “Purpose of the Policy”, the guidelines should (i) describe the applicability of the policy; (ii) explain what occurs in relation to any financial asset of the fund which generates a voting right with respect to a matter of critical investor interest and (ii) establish that the same had already defined general parameters and which are guidelines for exercising voting rights in alignment with the investment fund policy.

- In the Chapter “General Principles” the policy should meet the following requisites: (i) that a decision to allocate a financial asset is not an “isolated act”, given that its possession makes the allocation decision over time a “ continuous act”, that should provoke the process of judgment, decision and the manifestation as representative of those investors in matters which can affect their interests, and, consequently the value of the financial asset; (ii) that the vote is the manifestation of an opinion given in the name of the investors – in the cases in which the manager believes that such a manifestation is relevant – the decision being integral to the management of the investment fund – and as such, should be taken in a diligent manner, free of conflicts of interest, its purpose being in the best economic interests of the investors; (iii) that it is not obligatory to exercise voting rights in all the meetings but only in items defined by the Policy and (iv) that the policy should cover the decision-making standards and process that results in the decision to vote or otherwise, and, in the cases where the voting is applicable, what principles should guide this vote and how it should be formalised;

- The “Best Practices”, Chapter must obligatorily make clear that: (i) the representation is a function of the portfolio manager, since the decision is integral to the investment policy; (ii) establish a strategic vision of how to act in relation to aspects of governance with respect to financial assets held by the funds; (iii) have a broad vision of understanding of the other stakeholders on the matters on the agenda; (iv) maintain prior contact with the company whenever there are doubts on matters to be voted on; and (v) monitor the execution of the decisions taken by the companies;

- Finally in the Chapter “Minimum Structure”, it will be obligatory to clearly define a priori: (i) general principles guiding the voting policy; (ii) quantitative themes and parameters where the exercise of voting rights is obligatory; (iii) prior minimum periods for analyzing items on the agenda; (iv) a description of the decision-making process and the way in which decisions are registered and formalised; (v) who is responsible for the control and execution of the policy; (vi) procedures in the event of conflicts of interest; and (vii) policy for disclosing votes tendered on behalf of the investors.

The matter is at an advanced stage of discussion in the various bodies of ANBID. The current phase involves the conclusion and approval of these assumptions, subsequently passing on to the basis and juridical structure of the final text of the code, also considering the alignment of these provisions to the best IOSCO practices and to CVM rulings. This second technical phase having been concluded, the theme is to be submitted to a public hearing, this final phase entailing a discussion of the text in an open manner among all the members of ANBID, and also with the regulator.

At the end of this process, the text will be formally incorporated in ANBID's Self-Regulation Code for Investment Funds through a general meeting of members. Besides approving the text, the meeting will also decide upon the period that the new practices will come into operation. The forecast is for this process to be concluded by the end of 2007. In other words, the probability is that as from January 2008, investment funds in Brazil will be operating under policies specific to Proxy voting, thus contributing significantly to the improvement in the country's corporate governance practice.

4.2 Investments Funds and Proxy Voting- Evolution 2007-2008[27]

When this document was first written, the topic mentioned above was still a project. As of January 2008 it became effective, and the final version and ANBID' s report on its application is described below.

After lengthy discussions during 2007, the general meeting approved, in December of that year, the final alterations to the Investment Funds Self-Regulation Code, with the document "Guidelines for Exercising Voting Rights in Shareholder Meetings", in other words the rules for investment fund managers regarding their proxy voting obligations. The policy defines the rules for exercising voting rights at shareholder meetings for fund management companies, investment funds or even debenture holders.

Once approval was given, the following obligations were incorporated into the previously mentioned self-regulation code, with specific guidelines:

CHAPTER VIII – POLICY FOR EXERCISING VOTING RIGHTS IN MEETINGS

Article 21 - This Chapter applies to the Investment Funds, the investment policy of which permits the allocation in financial assets that contemplate voting rights in shareholder meetings. First Paragraph - The following are excluded from this discipline:

I. Exclusive or restricted Investment Funds, if approved, in a meeting, the inclusion of a clause in the regulations specifically noting that the portfolio manager does not adopt the Voting Policy for this Fund;
II. financial assets of an issuer outside Brazil; and
III. Brazilian Depository Receipts - BDRs.

Second Paragraph - The Investment Fund's Prospectus or the Regulations, should there be no Prospectus, shall notify that the portfolio manager adopts a Voting Policy, make reference to the website where the Policy can be found in its complete version and shall describe in summarised form the purpose of the Voting Policy, with the printing of the following notice or similar with the same content:

THE PORTFOLIO MANAGER OF THIS FUND ADOPTS A POLICY OF EXERCISING VOTING RIGHTS IN MEETINGS. THIS POLICY DISCIPLINES THE GENERAL PRINCIPLES, THE DECISIONMAKING PROCESS AND DEFINES THE RELEVANT OBLIGATORY MATERIALS FOR EXERCISING VOTING RIGHTS. THIS POLICY GUIDES

[27] ANBID's contribution to update

THE DECISIONS OF THE PORTFOLIO MANAGER IN SHAREHOLDERS' MEETINGS WHICH GRANT VOTING RIGHTS TO THE HOLDERS OF SECURITIES.

Third Paragraph - It is incumbent on the fund management company, conditional on the request of the portfolio manager, to grant legal representation for the exercising of voting rights in meetings relative to the financial assets held by the Investment Fund, pursuant to the Voting Policy adopted by the portfolio manager, and according to the minimum requirements under this Code and the guidelines established by the Self-Regulation Board.

Article 22 - The exercising of voting rights in meetings is a function of the Participating Institution responsible for the portfolio management of the Investment Funds as set forth in Article 21, being an integral part of the investment fund policy, and shall be exercised in a diligent manner in accordance with good corporate governance.

First Paragraph - The Participating Institution responsible for the portfolio management of Investment Funds included in the concept of Article 21 shall adopt a Voting Policy in accordance with the guidelines prepared by the Self-Regulation Board.

Second Paragraph - The Voting Policy shall be set forth in a specific document and registered with ANBID by the Participating Institution as portfolio manager, always in its complete and updated version, being available for public consultation.

Article 23 - Prior to the registration of ANBID's Voting Policy, the portfolio manager shall agree with the fund management company of the Investment Fund the operating conditions for implementing the Policy. It is then incumbent on the fund management company to provide the conditions for exercising the Voting Policy in the manner specified by it.

GUIDELINES FOR EXERCISING VOTING RIGHTS IN MEETINGS
(PROXY VOTING)
Article 1 - The purpose of this rule is to discipline the minimum requirements necessary for meeting the Policy for Exercising Voting Rights in Meetings ("Voting Policy"), applicable to the cases described in ANBID's Investment Funds Self-Regulation Code with the definitions dopted therein.

Article 2 - The exercising of the Voting Policy is mandatory in relation to Obligatory Relevant Matters, definition of which is contained in these Guidelines, except in the following cases, in which the exercising of the Voting Policy shall be at the exclusive discretion of the portfolio manager, if:

I. the Meeting takes place in any city which is not the capital city of the state and absentee voting is impossible;
II. the related cost for exercising the vote is incompatible with the participation of the financial asset in the Investment Fund; and
III. the total participation of the Investment Funds under management, subject to Voting Policy, is equivalent to less than 5% (five percent) and no Investment Fund has more than 10% (ten per cent) of its net worth invested in the asset in question.

Sole Paragraph - Voting in a meeting on a material fact is optional, in the event that there is a conflict of interest, or if the information provided by the company is insufficient for making a decision, in spite of requests for additional data and clarifications.

Article 3 - Obligatory Material Matters in which the exercising of the Voting Policy is mandatory, constitute:
I. in the case of shares, their rights and subsequent events:
a) election of minority representatives to the Board of Directors, if applicable;
b) approval of stock option plans for remunerating company management if including the purchase of call options "in the money" (the strike price of the option is less than the underlying share, taking into account the meeting's convening date);
c) acquisition, merger, incorporation, spin-off, alterations in control, corporate reorganisations, alterations or conversion of shares and other changes in the bylaws, which in the understanding of the portfolio manager, can have a material impact on the value of the asset held by the Investment Fund; and
d) other matters that imply differentiated treatment;

II. in the case of fixed or mixed income financial assets: changes in term or payment term conditions, guarantees, anticipated expiry date, early redemption, repurchase and/or remuneration originally agreed for the operation;

III. in the case of the quotas of Investment Funds:
a) changes in investment policy which alters the CVM class or ANBID type of the Investment Fund;
b) change in fund management company or portfolio manager, not between members of their financial conglomerate or group;
c) increase in administration fee or establishment of entry and/or exit fees;
d) alteration in the conditions of redemption which result in an increase in the exit period;
e) merger, incorporation or spin-off that leads to an alteration in the conditions listed in the preceding items;
f) winding up of the Investment Fund; and
g) quota holder meeting in cases pursuant to Article 16 of CVM Instruction 409/04.

Article 4 - The Policy must define:

I. its purpose;
II. the general principles that shall guide the portfolio manager, specifically in the examination of the Obligatory Relevant Matters;
III. the procedures that must be adopted in situations of potential conflicts of interest;
IV. the decision-making process for voting and how this is formalised, obligatorily describing:

a) the responsible person responsible for controlling and implementing the Voting Policy;
b) the procedures for decision-making, registration and formalisation;

c) the rules for the functioning of Advisory Councils qne, Technical or Investment Committee involved, where applicable.

Article 5 - The votes declared by the portfolio managers shall be disclosed to the quota holder of the Investment Funds in the manner set forth in the Voting Policy.

The above-cited code went into effect in January 2008, giving members until June 2008 to adapt to its contents. This was the deadline for institutions to register their proxy voting policies with ANBID and commence implementing these.

By the end of September ANBID had received and registered 130 voting policies, with another 100 applications still awaiting registration. These referred to institutions joined ANBID after the June 2008 deadline and thus received special terms and conditions.

ANBID's main concern regarding proxy voting will now be to establish mechanisms to control the applicability and the monitoring of these practices by the market, as is ANBID's normal practice. In other words, for each new obligation established by the self-regulation code, a corresponding enforcement mechanism has to be introduced.

5. Corporate Governance Rating Agencies

In Brazil, some rating agencies have just started to develop models to analyse the governance level of companies. Both national and international agencies are introducing worldwide changes that have been developed since the Enron scandal in 2001. However, the main targets for the agencies have been companies with publicly traded shares, because of the availability of information to include in the analysis.

This enforces the idea that one of the main problems in Brazil is lack of material to make accurate analysis of a company's governance. In this case, the approach that the agencies must take is "no news, bad news", as the lack of information is generally associated with poor governance practices on the part of the company. However, it is in the interest of companies operating in capital markets to provide the information necessary in order to receive good ratings. They can improve the market's perception of value, and help the stock price appreciate.

The methodology that agencies use to analyse and rate companies is very similar to that used worldwide, focusing on: transparency, sustainability, environmentally friendly attitudes, minority shareholders' representation, independence of the board of directors and other good governance practices.

The tendency is for these rating agencies to start giving increasingly more weight to governance and sustainability ratings. Society demands that companies become more responsible for their actions; and investors demand more transparency and accuracy from the players involved, in order to quantify their risks accordingly.

The only Brazilian rating company that operates in Brazil so far is Austin Rating. It does not offer consulting services, as it believes this conflicts with its corporate governance rating activities.

Glossary

BMF-Bovespa's Levels of Corporate Governance:

New Market (Novo Mercado):	Higher requirement of CG standards - only voting shares
Level 2 (Nível 2):	Intermediate level of CG - allow PN shares, but with tag along rights
Level 1 (Nível 1):	Basic level of CG - requirements related to disclosure

Bovespa Mais: segment of BOVESPA Organised OTC Market where only those publicly traded companies duly registered with CVM can be listed.

Exchange Rate R$: US$

	2003	2004	2005	2006	2007	2008	June/08	July/08	Aug/08	Sep/08
End of period	2,90	2,66	2,33	2,14	1,77	-	1,61	1,57	1,63	1,90
Average	3,12	2,93	2,43	2,18	1,72	1,73	1,62	1,60	1,61	1,79

Source:
Oanda.com