

Colombia

Chamber of commerce:

Cámara de Comercio de Bogotá
Avenida El Dorado 68D-35
Bogotá
Colombia
Tel: +57 1 383 0300
Web: camara.ccb.org.co

Professional body:

Colegio de abogados de Bogotá
Av. 19 No. 109-40
Bogotá
Colombia
Tel: +57 1 620 3100
+57 1 213 52 77
Fax: +57 1 215 7355

Proposed amendments to the financial system

Carlos Fradique-Méndez and Mauricio Cuesta
Brigard & Urrutia
Bogotá

The Colombian financial sector has recently experienced an enormous transformation as a result of a significant increase in the size of the securities market: an important number of infrastructure finance opportunities, the consolidation of compensation and settlement systems, a deep transformation of the financial industry due to mergers, acquisitions and the presence of new players in the market and the creation of the Financial Superintendence of Colombia, resulting from the merger of the former Superintendence of Banks and the Superintendence of Securities.

This transformation has been accompanied by a regulatory evolution based on a specialised holding and subsidiaries model, arranged around a number of milestone regulations:

- Law 35 of 1993, which set the framework for government intervention in the financial system;
- Law 510 of 1999, which introduced international standards of supervision;
- Law 546 of 1999, which set a new regulatory framework for household credit and finance; and
- Law 795 of 2003, which amended the disciplinary regime and conflict of interest rules.

In spite of these important regulatory efforts, the government was mindful of the fact that development in the banking and capital markets and the increasing size and depth of the financial sector required further adjustments to the financial system model. As a result, the Ministry of Finance recently introduced a bill with the purpose of reorganising and modernising the regulatory and institutional framework to address strategic aspects for an adequate performance and supervision of the financial market. The bill was approved in the first debate by the third commissions of the Senate and the Low Chamber, respectively.

The bill introduces the following main changes to allow a greater development in the financial markets.

Consumer protection regime

The bill: (i) establishes a regime for the protection of the consumer of financial services that sets the principles, rights and obligations applicable to relations between the financial entities and their clients; (ii) provides for the financial entities to implement a client service system that sets the policies, procedures and controls required to protect the financial customer and that guarantees complete and opportune flow of information to the client, including the fee structure applicable to financial services; and (iii) as an additional protective measure, it requires certain financial entities to appoint a financial customer advocate with a degree of autonomy and independence to address complaints filed by the client.

Structure of the financial system

The changes include: (i) the broadening of the authorisation of services rendered by banks, allowing them to provide operative and financial leases, and to finance the acquisition of industrial or commercial companies; (ii) the transformation of financial corporations into financial service corporations that may continue to finance investment in industrial or commercial companies, but exclusively with their own funds or with funds raised in the capital markets; and (iii) the migration of the administration of the pooled funds into specialised vehicles to comply with international recommendations, avoid regulatory arbitrage, reduce conflict of interest issues and provide transparency in terms of transactional costs.

Interest rate regime

The bill: (i) provides that the limits to the interest rates are applicable as of the execution of the credit agreement only; (ii) reiterates that the maximum limits for the interest rate and default interest rate are one and a half times and two times, respectively, the interest charged by local banks, as determined by the Financial Superintendence of Colombia; and

(iii) clarifies that the sanction for charging interest in excess of legal limits is losing the excess amount over the maximum default interest rate.

Mandatory pension funds regime

A pension fund may currently administer one portfolio only, so the fund administrators have been compelled to design common strategies with no option to consider differences in ages or expectations of investors. The bill: (i) provides for a multi-fund regime allowing private pension managers to offer different types of portfolios to satisfy the risk return appetite of investors; and (ii) sets for the new regime (a) a minimum guaranteed return by the pension funds to be set by the government and (b) a mixed fee system calculated in terms of return and the mandatory contributions by users of the pension system.

Structure of financial services

If the free trade agreement with the US is approved and ratified (the treaty was recently approved by the Colombian congress and the Constitutional Court), Colombia would acquire certain commitments in the area of financial services that are already reflected in the bill. The bill: (i) reiterates that international insurance contracts may only be executed with insurance entities authorised by the government, with the exception of insurance for international commerce associated with sea transportation and commercial aviation; (ii) allows Colombian residents to freely buy insurance abroad except in the case of (a) insurance in connection with the social security system, (b) mandatory insurance policies and (c) insurance taken by public entities; and (iii) includes a regulation for branches of foreign financial entities.

In an effort to clarify the scope of supervisory activities of the Financial Superintendence of Colombia, the bill also provides for authority on antitrust and unfair competition activities incurred by financial institutions. Accordingly, the bill provides that the Financial Superintendence of Colombia may object not only to mergers and

acquisitions but also to conversions, spin-offs, split-offs, asset purchases and other integration schemes involving financial institutions. Also, the bill incorporates general rules for anticompetitive agreements and activities performed by the abuse of a dominant position in the market, as well as general anti-trust rules. The bill clarifies that the Superintendence will approve and oversee the publicity for financial services and that all other activities considered unfair competition would be overseen and decided by the Superintendence of Industry and Commerce.

Financial and corporate

Recommended firms

Tier 1

Baker & McKenzie
Brigard & Urrutia
Gómez-Pinzón Zuleta

Tier 2

Cárdenas & Cárdenas
Posse Herrera & Ruiz
Prieto & Carrizosa

Tier 3

José Lloreda Camacho & Co
Parra Rodríguez & Caveller

The growth of the capital markets is energising the Colombian legal community. Lawyers are beginning to advise their clients on the advantages of using the markets to raise capital rather than simply turning to the banks. Finance lawyers accustomed to plain-vanilla transactions are now observing complex products in the markets - subordinated structures, derivatives, asset securitisations - from international banks like Citibank and HSBC.

Securitisations are on the rise because Colombia's institutional investors, such as private pension funds, need long-term products to invest the \$500 million that flow in every month. There have traditionally been few options in the local market, so banks are looking to address those needs. The government has recently passed legislation allowing institutional investors to invest in private-equity funds for the first time.

The pull of the capital markets is helped by the push in other areas of finance: in June 2007, the government imposed a mandatory deposit scheme. To counteract the appreciation of the peso against the dollar, Colombian borrowers must now deposit 40% of any foreign currency received. While this has succeeded in strengthening the peso, it also means that bank lending from international

institutions has slowed. This is another factor in the rise in interest in the capital markets.

While some larger Colombian companies have looked to the international markets to make issuances, there has been particular interest in local placements. The recent \$3 billion IPO of Ecopetrol tells the story: initially floated on the Colombian market, the company had planned an international placement once the local markets were tapped. But the offerings were oversubscribed in Colombia, with 400,000 new retail shareholders grabbing up the shares. "This has proved clearly that going to the capital markets is a viable alternative," says a local lawyer, "and the transaction has set the tone for what you will see in Colombia in the future".

Colombia has more medium-sized law firms than many other Latin American countries. This suggests an opportunity for consolidation, particularly as firms look to grow organically and by other means. The May 2008 merger of Gómez Pinzón Linares Samper Suárez Villamil and Zuleta & Partners could prove to be the watershed moment for such deals within the Colombian legal community.

Baker & McKenzie

The lawyers at Baker & McKenzie receive high praise clients. Says one: "Baker & McKenzie exhibits common sense, and everything else that you would want in local counsel. Also, because they have a US affiliation, they are good for US institutions that want counsel that understands where you are coming from." Rivals acknowledge that the firm had a successful 2007, and its deal list confirms this.

Baker & McKenzie's banking and finance practice has been particularly strong in the past year. The firm advised Standard Bank and the Interamerican Investment Corporation when the financiers granted \$77 million in new financing and refinanced the existing loans of Biofilm. The deal highlighted the firm's ability to draw on its global affiliates for cross-border mandates. During the transaction, Colombia's foreign-exchange control regulations changed, meaning the lenders received different collateral in Colombia, Mexico, and New York. The operations had to be timed depending on separate negotiations with each bank.

Baker & McKenzie was also involved in the \$2.8 billion IPO of Ecopetrol, which issued shares equal to 10% of its capital to Colombian investors. The firm advised on the joint venture between Citibank and Merrill Lynch, which undertook an alternate valuation of Ecopetrol.

In July 2007, Jaime Trujillo led an M&A team that advised JP Morgan in its acquisition of a portion of Almacenes Éxito and then sold it via an issuance of ADRs for \$392 million. The firm prepared the offering memorandum and ancillary documentation, and provided regulatory advice. This was the first primary offering of securities by a Colombian company outside its home market in more than a decade.

Leading lawyers

Jorge Lara
Jaime Trujillo

Brigard & Urrutia

"Brigard & Urrutia offers the full scheme of support," says one satisfied client. This sentiment is matched by rivals, who note that the firm does not have any weak practice areas.

Brigard & Urrutia has handled a number of acquisitions on behalf of mostly foreign clients over the last year. The firm, led by partner Carlos Umaña, represented Chilean industrial gas group Indura Industria y Comercio in its purchase of 99.5% of the capital stock of its Colombian rival, Cryogas. The sale of stock was a condition imposed by the Colombian antitrust authority in response to the acquisition by Cryogas's parent company of BOC Group in 2006.

The firm also advised French supermarket retailer Groupe Casino in its acquisition of a minority stake in Colombian retail chain Almacenes Éxito through structured GDRs. This stock purchase, valued at \$380 million, raised Casino's interest in Almacenes Éxito to 75%, paving the way for its eventual takeover of the company. Sergio Michelsen and Carlos Fradique led the capital markets team that advised on the company's \$392 million issuance of GDRs.

The banking team also advised JP Morgan and UBS Investment Bank as joint bookrunning managers in the issuance of \$400 million subordinated notes for Colombian bank Bancolombia. Carlos Urrutia led the team that conducted the due diligence, and advised the bank on banking, securities and tax matters related to the transaction.

Leading lawyers

Carlos Fradique-Mendez
Sergio Michelsen
Carlos Umaña Trujillo
Carlos Urrutia

Gómez-Pinzón Zuleta

Gómez-Pinzón is the youngest of the three top-tier firms, but has been making great strides in establishing itself. The firm made

headlines earlier this year with its takeover of Zuleta & Partners, a boutique with a strong reputation for litigation and arbitration. “Gómez-Pinzón has established a strategy of growth and is expanding aggressively,” noted one rival before the merger was announced. The tie-up was viewed generally as an unsurprising but smart strategic move.

The firm regularly advises international and local banks in a variety of corporate and financial transactions. In May 2007, José Luis Suárez Parra led the team that advised Bancolombia in its issuance of \$400 million senior secured notes.

Gómez-Pinzón was involved in the public offering of Ecopetrol shares, representing JP Morgan, Credit Suisse, and Banca de Inversion Bancolombia as structuring agents. In November 2007, the firm also advised Lehman Brothers as the arrangers in the issuance of \$69 million notes from Termovalle Investment.

Gómez-Pinzón has also been involved in a number of important M&A deals in Colombia over the past year. The firm counselled retailer Carulla Viveroon on its sale to Almacenes Éxito for \$700 million. This created the country’s largest retailer which will operate more than 260 retail outlets and will have a combined revenue of more than \$2.4 billion.

In March 2008, AIG reached an agreement to purchase consumer-finance lender Inversora Pichincha from Banco Pichincha and other minority shareholders. Alejandro Linares Cantillo led the team that represented the buyer, AIG. At the time of writing, this transaction was still subject to regulatory approval.

Leading lawyers

Alejandro Linares Cantillo
José Luis Suárez Parra

Posse Herrera & Ruiz

“Posse Herrera & Ruiz is an up-and-coming firm that was involved in some very high-profile deals last year,” says a competitor. The firm has been involved in a growing number of capital markets transactions, and has garnered respect for its work in the financial sector.

Posse Herrera was the advisor to Cencosud in negotiations with Grupo Toro. This was a proposed \$300 million stock-purchase agreement for Almacenes Éxito shares. Cencosud was eventually blocked in this effort when rival supermarket conglomerate Groupe Casino exercised its right of first refusal to buy the shares. The deal, which was complicated because Groupe Casino is a majority shareholder in Almacenes Éxito, tested the firm’s

capabilities in advising on complex deals in the capital markets.

In September 2007, the firm advised ABN Amro in the initial purchase of \$750 million 10-year notes offered through a Rule 144A/Regulation S issuance by natural-gas pipeline operator Transportadora de Gas del Interior. This was the biggest bond sale by a Colombian company, and ABN Amro was sole bookrunner and joint lead manager in the issuance, as well as the initial purchaser.

Leading lawyers

Daniel Posse
Mariana Posse

Prieto & Carrizosa

Prieto & Carrizosa is raising its profile by building a large roster of Colombian clients and working on some of the most prominent deals in the country. “They have model lawyers at Prieto & Carrizosa, and the firm has a good critical size, with access to groups of specialised lawyers in different practice areas like tax and labour,” says a client. Rivals concur. One says: “The lawyers at Prieto are very driven and focused.”

In the last year, many of the firm’s significant financing deals derived from its solid corporate relationships. A team comprising Juan Fernando Gaviria, Lucas Saffon, Santiago Arango and José Oliveros advised concessionaire Opain on a bridge loan obtained from BNP Paribas and Bancolombia to build the new El Dorado airport in Bogotá. The financing closed September 2007.

The firm also participated in some of the most important M&A deals of 2008. Martin Acero represented investment group Valorem and other investors in the sale of Propilco. State oil company Ecopetrol paid \$690 million for a controlling interest in the petrochemicals group.

In October 2007, Acero acted for PVC manufacturer Mexichem. The Mexican company paid \$600 million for Amanco Holdings. Prieto y Carrizosa advised on the Colombian aspects of the multijurisdictional deal.

Leading lawyers

Martin Acero
Juan Fernando Gaviria
Juan Carlos Rocha