CtW Investment Group

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REQUEST FOR INVESTIGATION

Change to Win ("CtW") Investment Group requests that the Securities and Exchange Commission investigate Arcos Dorados Holdings Inc. ("Arcos") based on substantial evidence of its misrepresentations concerning its related-party transactions with a distributor and its potentially material omissions concerning its relationship with a private equity firm.

Arcos' Chairman, former CEO and controlling shareholder Woods Staton dominates the company through his substantial voting power and his long-standing personal relationships with other directors. Publicly-available information suggests that Staton has used his dominance to engage in related party transactions that benefit him at the expense of other shareholders. Disclosure regarding those transactions has been misleading or non-existent. Last year, Staff of the Division of Corporation Finance asked Arcos about its disclosures regarding transactions with Axionlog, a distributor owned by Staton with which Arcos claims it has negotiated at arm's length. Arcos's incomplete, inconsistent and implausible responses suggest that Arcos is continuing to mislead the Staff and shareholders about its relationship with Axionlog. In addition to these misrepresentations, we believe Arcos may have failed to disclose material information regarding related party transactions with Pegasus Group, a private equity investment group that appears to have been founded by Woods Staton and director Michael Chu. As a result, and whatever the Staff's determination may have been as to that filing on the basis of the information the company provided, we believe that a more in-depth investigation is warranted on the basis of the information set out below..

On February 26, 2016, CtW Investment Group requested inspection of the company's books and records relating to its policies and procedures for approving related party transactions, as well as documents relating to transactions with Axionlog and Pegasus Group. In its request, CtW Investment Group expressed concern that Arcos may be engaging in transactions that are beneficial to Staton and detrimental to shareholders and that its disclosures about its relationship with Axionlog and Pegasus Group were misleading and inadequate. On March 21, 2016, Arcos responded that it would only grant inspection of a very limited set of documents − the memorandum and articles of association, the register of members, the register of directors, meeting minutes, and shareholder resolutions−to which CtW Investment Group is entitled under B.V.I. law. Despite CtW Investment Group's reasonable inquiries into the company's questionable relationships, the company has refused to provide any of the requested information about related party transactions.

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Given the company's intransigence in addressing a minority shareholder's valid concerns about inadequate disclosure of related party transactions, and public shareholders' inability to influence Arcos' governance, CtW Investment Group believes that an SEC investigation is the only means by which to hold Arcos to account for its obfuscation and misrepresentations to shareholders.

Change to Win Investment Group

The CtW Investment Group works with pension funds sponsored by affiliates of Change to Win, a federation of unions representing over five million members, to enhance long-term shareholder value through active ownership. These funds invest over $250 billion in the global capital markets and are investors in Arcos. In April 2015, CtW Investment Group wrote to three independent directors of Arcos expressing its agreement with Institutional Shareholder Services' recommendation to withhold support from Arcos' Chairman and then-CEO Woods Staton due to the board's failure to establish a majority independent board and due to Staton's serving on the compensation committee. The letter also expressed concern about a number of other governance issues, including the company's insider-dominated board and insufficient oversight of related party transactions with Staton.

Background on Arcos Dorados

Arcos, the world's largest franchisee of McDonald's restaurants, was founded in 2007 as a result of its acquisition of McDonald's business in Latin America. The company, which is incorporated in the British Virgin Islands and headquartered in Argentina, went public in 2011. It currently operates or subfranchises approximately 2,100 restaurants in twenty countries in Central and South America and the Caribbean, and represented over five percent of McDonald's global sales in 2014.

Woods Staton, Arcos' Chairman and former CEO, is the controlling shareholder through his substantial ownership of both classes of Arcos' stock. Class B stock is not publicly traded and has five votes per share. All of the Class B common stock is held by Los Laureles Ltd., an entity solely owned by Staton. Through Los Laureles Ltd, Staton controls 75 percent of Arcos' voting power and 38 percent of the outstanding shares of common stock.[1] Los Laureles Ltd. established the Los Laureles voting trust to exercise the voting rights of the Class B shares. The trust vests voting authority in a committee consisting of Staton and whomever else he wishes to appoint. The trust also allows its committee members to be monetarily interested in any transaction to which Arcos is also a party and indemnifies committee members for all actions arising out of their duties, unless such actions constitute fraud.[2] Staton also owns 7.6 million shares of Arcos' Class A stock, which is traded on the NYSE and has one share per vote. Almost seven million of these shares, which represent 5.8% of all Class A shares, are held through Chablais Investment S.A., an entity incorporated in the British Virgin Islands that lists Staton as its controlling shareholder.[3] Taken together, Staton's Class A and Class B shares represent 41.5% of Arcos' equity and 76.8% of its voting power.[4]

I. Misrepresentations and Material Omissions about Related Party Transactions

Foreign private issuers are required to disclose, in their annual Form 20-F filing, certain information about transactions with related parties, including "[t]he nature and extent of any transactions .

[1] Arcos Form 20-F, Apr. 29, 2015, at 94.

[2] Los Laureles Voting Trust, Ex. 9.1 to the Company's Registration Statement on Form F-1, Mar. 25, 2011, Sections 8.1(a), 8.6, 8.7.

[3] Arcos Form SC 13D, Mar. 11, 2016, at 3-4.

[4] *Id.* at 4.

. .which are material to the company or the related party, or any transactions that are unusual in their nature or conditions, involving goods, services, or tangible or intangible assets, to which the company or any of its parent or subsidiaries was a party . . ." As discussed in detail below, we believe that Arcos has misrepresented the nature of its relationship with related party Axionlog and has failed to disclose a material relationship with related party Pegasus Group.

A. <u>Axionlog</u>

Axionlog, a company that has provided distribution services to Arcos' McDonald's restaurants in Central and South American countries since Arcos' inception, was a subsidiary of Arcos until 2011, when Staton purchased Axionlog and became its sole shareholder. Following the split off just prior to Arcos' initial public offering in 2011, Arcos entered into a master commercial agreement with Axionlog pursuant to which Axionlog continues to provide distribution services. Axionlog currently provides logistics and distribution services for Arcos restaurants in seven countries: Argentina, Chile, Colombia, Mexico, Peru, Uruguay and Venezuela.

In its SEC filings, Arcos has consistently characterized its relationship with Axionlog as arm's length.[5] This means that, although Arcos and Axionlog are related parties, the prices and other terms agreed to with Axionlog should be very similar to those that would have been negotiated with an unrelated party. U.S. accounting principles, which Arcos uses, provide that disclosures about related party transactions "shall not imply that the . . . transactions were consummated on terms equivalent to those that prevail in arm's-length transactions unless such representations can be substantiated."[6] Yet substantial evidence suggests that this is not the case.

Aspects of the Arcos/Axionlog relationship suggest that Axionlog has benefited from special treatment that would not have been extended to an unrelated vendor. In February 2014, one month before Arcos re-measured its operations in Venezuela using a less favorable exchange rate, Arcos and Axionlog agreed to change the currency in which a $13.7 million receivable from Axionlog was denominated from US dollars to Venezuelan bolivares. This had the effect of reducing the receivable's value from $13.7 million to $1.7 million, cutting by over 80% the amount Axionlog owed Arcos.[7] The change in currency is especially unusual given that Arcos conducts much of its business, including financial reporting to shareholders and payment of royalties to McDonald's, in US dollars.

Similarly, in November 2011, Arcos entered into a revolving loan agreement with Axionlog B.V., a holding company for the Axionlog business, in which Arcos agreed to lend Axionlog $12 million at an interest rate of LIBOR plus 6 percent, which was below the rate that Arcos was paying at the time on its own debt.[8] In its Form 20-F filed in 2012, Arcos disclosed that it guaranteed deposits on Axionlog's behalf that served as collateral for Axionlog's obligations to its suppliers. Arcos did not charge Axionlog

[5] Arcos Form 20-F, Apr. 29, 2015, at 31. According to section 7.7 of the master franchise agreement between Arcos and McDonald's Corporation, "Except as expressly permitted by this Agreement, Master Franchisee shall not, and shall not permit any of its Subsidiaries to, directly or indirectly, enter into or permit to exist any transaction (including any purchase, sale, lease or exchange of any property or the rendering of any service) with any Related Party of Master Franchisee otherwise than on an arm's-length basis." Amended and Restated Master Franchise Agreement, Ex. 10.1 to Registration Statement filed on March 25, 2011.

[6] FASB Accounting Standard 850.50-5.

[7] Arcos Form 6-F, Nov. 4, 2014, at F-30, F-32.

[8] Arcos Form 20-F, Apr. 18, 2012, at 31.

any fees or interest for the funds used as a guarantee.[9] And, in 2012, Arcos assumed and settled $1.6 million in Axionlog's obligations to suppliers and collected no fees or interest for doing so.[10] One would not expect to see the accommodations Arcos has granted Axionlog in a relationship between unrelated parties.

Arcos' statements to Commission Staff last summer strongly suggest that it has never analyzed whether its master commercial agreement with Axionlog is on arm's length terms. As detailed below, Arcos refused to answer basic inquiries about the master commercial agreement and instead replied with inconsistent or implausible claims about how its payment to Axionlog is calculated and about the materiality of the contract, which further suggest that Arcos is attempting to obfuscate the terms of the agreement because it has mischaracterized it to shareholders.

1. <u>Arcos' Correspondence with Commission Staff about Axionlog</u>

In a July 2, 2015 letter to Arcos, Commission Staff requested that Arcos provide an analysis as to how it determined that the master commercial agreement with Axionlog was entered into on arm's length terms. The Staff also requested that Arcos discuss the material terms of the master commercial agreement and file the agreement as an exhibit to its Form 20-F.

In its response on July 17, 2015, Arcos stated that it believed that the agreement was on arm's length terms because the fees paid to Axionlog are derived from a formula that is standard for distribution services in the industry and because a very similar formula is used throughout Arcos' territories with other distribution service providers. This formula, according to Arcos, "is based on a projection of merchandise volume to be transported from one location to another and reflects the services provider's projected costs plus a margin of approximately 5%, which is standard for the industry." Arcos also noted that, under its master franchise agreement with McDonald's Corporation, all business with related parties must be conducted on an arm's length basis, and that any noncompliance with this requirement would constitute a breach of its agreement with McDonald's.

Arcos also refused to file the master commercial agreement as an exhibit, arguing that the filing was not required because the agreement is not material to its operations. In support of this argument, Arcos stated that Axionlog only provides distribution services for six of the company's 20 territories[11] and accounts for only 3.6% of Arcos' food and paper costs. Arcos also stated that it routinely contracts with other logistics service providers in the rest of its territories and is not substantially dependent on Axionlog's services for its operations.

In a follow-up letter to Arcos on August 6, 2015, the Staff sought additional information on how Arcos determined its payment to Axionlog, including "the variable components of the pricing formula", as well as a comparison of "the variable components of the Axionlog agreement with those of your other distribution service providers." The Staff also asked that Arcos "[c]ompare the fee paid to Axionlog as a percentage of products acquired from Axionlog with the same percentage for similar agreements throughout your other territories." Finally, the Staff requested the basis for Arcos' conclusion that it is not substantially dependent on Axionlog in light of the total value of the contract, which, the Staff noted, appeared to be much higher than the 3.6% cited by Arcos.

In its response to the Staff on August 28, 2015, Arcos explained that it establishes an annual budget with each distribution provider that is reviewed quarterly. The budget is calculated using a standard pricing formula, which contains certain fixed costs and certain variable components, most of

[9] *Id.*

[10] *Id.* at 96.

[11] At the time of the letter, Arcos did not have a contract with Axionlog in Peru.

which are market-specific. Arcos also refused to compare the fee paid to Axionlog as a percentage of the total costs of products acquired through Axionlog because, according to Arcos, this measure is not representative of how the industry measures distribution costs. A better measure, Arcos asserted, is a comparison of distribution costs as a percentage of food and paper costs. Finally, in support of its argument that it is not substantially dependent on its contract with Axionlog, Arcos stated that the contract is standard for a company operating in the food services industry and that, in 2014, Arcos paid Axionlog $45.1 million in distribution fees, which accounted for only 3.6% of the company's total food and paper costs of $1.2 billion. The rest of the payment made to Axionlog represented pass-through costs for products purchased on behalf of Arcos.

On September 14, 2015, the Staff responded that it had completed its review of Arcos' filing.

2. Inconsistencies and Inaccuracies in Arcos' Statements to Commission Staff about Axionlog

Publicly-available information about Arcos' relationship with Axionlog, as well as Arcos' own statements about the relationship, suggest that the agreement was not negotiated at arm's length, as Arcos claims. As an initial matter, Arcos disclosed in its Form 20-F that, because it has long-standing and strong relationships with its suppliers, it has oral agreements with the vast majority of them.[12] Arcos' informal relationships with its suppliers suggest that it is not conducting a rigorous analysis of whether the terms and prices offered by its vendors, including Axionlog, are competitive with the market.

Several statements made to the Staff last summer cast doubt on Arcos' assertion that the agreement was negotiated at arm's length. Arcos stated that it has used the same formula to calculate Axionlog's fee both before and after the Axionlog split-off.[13] This suggests that Arcos has not revisited the formula to ensure that it results in an arm's length arrangement despite the new level of Staton's control on both sides of the business relationship following his acquisition of Axionlog. Arcos also made inconsistent statements about how each distribution service provider's payment was calculated. It claimed in its first letter to the Staff that payment is based on a formula that is used with Arcos' other distribution providers throughout its territories that is standard in the industry. In its second letter, however, it stated that the formula varies by market because of market-specific differences and that payment is based on an annual budget proposed by each distribution provider that is reviewed quarterly by the company.

Arcos' description of the formula used to calculate Axionlog's payment also calls into question the claim that the agreement is at arm's length. In its correspondence with the Staff last summer, Arcos described the formula used to calculate Axionlog's fee as reflecting Axionlog's "projected [fixed and variable] costs plus a margin of approximately 5%, which is standard for the industry."[14] But that general description falls far short of showing the arrangement is on arm's length terms.

[12] Arcos' 2015 Form 20-F states: "Our 25 largest suppliers account for approximately 80% of our purchases. Very few of our suppliers have entered into written contracts with us as we only have oral agreements with a vast majority of them. Our supplier approval process is thorough and lengthy in order to ensure compliance with McDonald's high quality standards. We therefore tend to develop strong relationships with approved suppliers and, given our importance to them, have found that oral agreements with them are generally sufficient to ensure a reliable supply of quality products." Arcos Form 20-F, Apr. 29, 2015, at 17.

[13] In a July 17, 2015 letter to the SEC, Arcos disclosed that "[t]he formula utilized to calculate the fee paid to Axionlog prior to the split-off is the same formula which is now contained in the MCA [Master Commercial Agreement] . . ."

[14] July 15, 2015 letter to the SEC, at 2.

The fact that the same formula is used in other distributorship arrangements says nothing about the competitiveness of the actual costs themselves, which determine the contract price. It seems unlikely that all distributors that serve, or could serve, a territory would project the same costs. Differences in labor rates, the cost of warehouse space and other distributor-specific factors[15] would be expected to produce variation in projected costs. As well, in negotiating a cost-plus contract, a purchaser generally must ensure that overhead charged to the contract is appropriate. Finally, terms not related to the contract amount, such as payment terms, might vary substantially from those an unrelated party could obtain; if Arcos pays Axionlog within 10 days of being invoiced, for example, while other vendors wait 90 or 120 days, the arrangement looks less like an arm's length transaction. Such terms have not been disclosed by Arcos and were not mentioned in Arcos' responses to the Staff's inquiries.

It is reasonable to assume that if Arcos had analyzed Axionlog's direct or indirect costs, or the other terms of their arrangement, and substantiated that the terms are arm's length, Arcos would have documented those analyses to the Staff. The inadequacy of Arcos' responses is particularly concerning in light of the other accommodations Arcos has extended to Axionlog, none of which would be expected in an arm's length relationship. As a result, there is a strong basis to believe that Arcos cannot substantiate its assertion that its arrangement with Axionlog is on arm's length terms.

Arcos' assertions that it is not substantially dependent on the Axionlog contract and that the contract is not material to its operations are also dubious. It is likely that Axionlog is the exclusive distributor for Arcos restaurants in the seven countries in which Axionlog operates.[16] Three of these countries−Argentina, Mexico and Venezuela−are top-five markets for Arcos and contributed more than a quarter of Arcos' revenue in 2014.[17] In addition, food and paper costs were the single largest expense in 2014, amounting to $1.24 billion last year.[18]

[15] Arcos' response to the Staff emphasized the impact of market-specific factors on costs, but did not acknowledge that even within a market, vendors may have different costs.

[16] It appears that Arcos operates through exclusive supplier contracts in each country. According to its July 17, 2015 letter to the Staff, Arcos has exclusive supplier contracts with Martin Brower in four territories: Brazil, Puerto Rico, Costa Rica, and Panama. In the same letter, Arcos stated that it "routinely contracts with other logistics service providers [other than Axionlog] *in the rest of its territories*." (emphasis added). This suggests that Axionlog is the exclusive logistics service providers in the seven countries in which it has a contract with Arcos.

[17] As of December 31, 2014, we had more than 100 restaurants in operation in each of Argentina, Brazil, Mexico, Puerto Rico, and Venezuela. No other Territory had more than 85 restaurants in operation." Arcos Form 20-F, Apr. 29, 2015, at 114. "In 2014, 80.3% of our total revenues were derived from our restaurants in Argentina, Brazil, Mexico, Puerto Rico and Venezuela." *Id*. at 5. We estimate that the seven markets served by Axionlog represent approximately 45% of Arcos' revenue, up from 38% in 2014. These figures were estimated by multiplying the revenues for each regional segment by the proportion of stores each country represents in each segment. For example, Argentina has approximately 58% of the stores in Arcos' South Latin America division ("SLAD"), and SLAD revenues in 2015 were $925.2 million. Therefore if Argentina also contributes 58% of revenues to the segment, its revenues are estimated as $534.9 million.

[18] Arcos Form 20-F, Apr. 29, 2015, at F-47. Arcos recently disclosed its food and paper costs for 2015. Although total food and paper costs decreased to $1.04 billion for the year, the $164.9 million in fees paid to Axionlog still represented 16 percent of total food and paper costs. Arcos Form 6-K, Mar. 16, 2016, at F-4, F-45-46.

In its correspondence with the Staff, Arcos argued that the master commercial agreement is not material because only $45.1 million was paid to Axionlog for its distribution services in 2014 and the remaining $154.7 million represented pass-through costs to suppliers contracted through Axionlog.[19] This argument is not persuasive. In two of Arcos' largest markets, Mexico and Argentina, Arcos disclosed that, in 2014, Axionlog's distribution fees represented 10.5% and 9.3%, respectively, of Arcos' food and paper expenses in these countries.[20] Using a revenue-weighted average of these figures, Axionlog's fees are estimated to comprise 9.6% of Arcos' food and paper expenses across territories served by Axionlog. By dividing Axionlog's distribution service fees of $45.1 million by 9.6 percent, the total value of food and paper distributed in Axionlog markets can be estimated as $469.8 million. If that figure is divided by Arcos' 2014 reported total food and paper expenses across all territories of $1,243.9 million,[21] an estimated 37.8% of total food and paper cost is distributed through Axionlog, a percentage that is certainly material to Arcos' operations.

Since it corresponded with the Staff, Arcos disclosed the amounts it paid to Axionlog in 2015. It paid Axionlog $164.8 million in 2015, of which $44.2 million was for distribution fees and $120.7 million was for supplies purchased and managed through Axionlog.[22] Using the same methodology and assumptions as above, this implies that, in 2015, the $44.2 million in logistics service fees that Axionlog collected from Arcos corresponds to an estimated $460.1 million in total food and paper distributed in these territories, or 44.3% of Arcos' total food and paper expense,[23] a significant increase from 2014.

The publicly-available information about the relationship between Arcos and Axionlog suggests that Arcos has misled shareholders and Commission Staff about the nature and materiality of the master commercial agreement. That information supports a conclusion that, notwithstanding Arcos' statements to the contrary, the master commercial agreement is a material part of Arcos' operations and has been negotiated on terms that are unreasonably beneficial to Axionlog and detrimental to Arcos' minority shareholders.

B. **Pegasus Group**

Arcos' current and prior Form 20-Fs disclose that independent director Michael Chu is a founding partner of Pegasus Group and continues to serve as a senior advisor.[24] Pegasus Group is a real estate and private equity investment firm founded in 2000 that has offices in Argentina and Colombia.[25] Although not disclosed in Arcos' filings, according to other publicly-available information, Woods Staton co-founded Pegasus Group with Michael Chu and one other individual.[26] An SEC filing from 2009 regarding

[19] August 28, 2015 letter to the SEC. Arco's food and paper expenses in 2014 were $199.8 million. *See* Arcos Form 20-F, Apr. 29, 2015, at F-47.

[20] August 28, 2015 letter to the SEC.

[21] Arcos Form 20-F, Apr. 29, 2015, at 2.

[22] Arcos Form 6-K, Mar. 16, 2016, at F-45-46.

[23] Arcos' total food and paper expense in 2015 was $1.037 billion. *Id.* at F-4.

[24] Arcos Form 20-F, Apr. 29, 2015, at 87.

[25] Grupo Pegasus website, *available at*: http://www.pegasusvc.com/grupo_pegasus.php?w=1600&h=900.

[26] Javier Blanco, *El Banco Galicia Apuesta al Consumo: Compró Efective Sí*, LA NACION, June 3, 2009; Executive profile of Woods Staton, BLOOMBERG BUSINESS, *available at:* http://www.bloomberg.com/research/stocks/private/person.asp?personId=11275776&privcapId=129040994.

the acquisition of a financial services company by Pegasus Group indicates that Staton owned one-third of its equity at that time.[27] Given the longstanding business relationship between Chu and Staton, Staton's affiliation with Pegasus Group should have been disclosed so that investors could adequately assess whether Chu is truly an independent director of Arcos.

In addition to the undisclosed relationship between Chu and Staton, it appears that Pegasus Group has engaged in undisclosed related-party transactions with Arcos. We believe that investee companies of Pegasus Group have entered into real estate transactions with Arcos. Pegasus Group is the controlling shareholder of Argentinian real estate developer Rukán,[28] which owns the Tortugas Open Mall in Argentina, in which Arcos currently operates two restaurants.[29] Rukán also developed Urbana Centro Empresarial where, as of 2010, both Arcos and Axionlog maintained offices.[30] In addition, in 2011, Pegasus Group formed a partnership with Ospinas & Cía to create an investment platform to purchase, develop and manage real estate assets in Colombia.[31] The real estate firm's website lists several commercial malls in Colombia where McDonald's restaurants operate.[32] Without disclosure of the related-party transactions with Pegasus Group, it is impossible for Arcos shareholders to understand the nature of these transactions and assess whether they were conducted on arm's length terms.

II. Staton's Domination of Arcos

CtW Investment Group believes that Arcos' misrepresentations and material omissions concerning related party transactions are intended to conceal transactions that benefit Woods Staton at the expense of other shareholders. We also believe that these poorly-managed related party transactions are a direct result of Arcos' corporate governance, which blunts accountability to public shareholders through a dual-class capital structure and an insufficiently independent board.

Along with controlling a majority of Arcos' voting and economic interests, Staton dominates Arcos' board of directors. Arcos' board consists of nine directors, only four of whom are considered independent. Even more troubling, at least one putatively independent board member has a long-standing personal relationship with Staton. As discussed above, independent director Michael Chu has an undisclosed relationship with Staton through their co-founding of Pegasus Group, a private equity firm that appears to be engaging in transactions with Arcos.

Two non-independent directors−Annette Franqui and Carlos Hernández-Artigas−also have several connections to Staton, only some of which are disclosed to shareholders. According to Arcos' Form 20-F filings, immediately before founding Forrestal Capital in 2003, they served in senior management positions at Panamerican Beverages during the same time that Staton was CEO and Chairman of that company. Arcos' filings also disclose that that they serve as directors of Axionlog Cold Solutions[33] and are founding partners and current managers of Forrestal Capital. What is not disclosed is that Forrestal Capital is a private investment office devoted solely to managing the Staton family's

[27] Grupo Financiero Galicia SA Form 20-F, Exhibit 4.7, Stock Purchase Agreement, June 1, 2009, Ex. D, Schedule 1.

[28] Grupo Pegasus website, *available at*: http://www.pegasusvc.com/grupo_pegasus.php?w=1600&h=900.

[29] *See* Rukan website, *available at*: http://www.rukan.com.ar/proyecto/tortugas-open-mall/.

[30] Adriana B. Anzillotti, *Oficinas Premium Bien Cerca Del Verde*, LA NACION, Aug. 30, 2010.

[31] Grupo Pegasus website, *available at*: http://www.pegasusvc.com/grupo_pegasus.php?w=1600&h=900.

[32] Ospinas website, *available at*: http://ospinas.com.co/en/.

[33] Axionlog and Axionlog Cold Solutions appear to be the same company, according to a review of Axionlog Cold Solutions' website. *See* www.axionlog.com.

wealth. Publicly-available information suggests that Forrestal Capital's initial assets included some or all of the $127 million paid to Woods Staton when Panamerican Beverages, a company founded by his grandfather, was sold to Coca-Cola in 2002.[34]

Some of Arcos' operations appear to be intertwined with those of Forrestal Capital even though they are distinct entities. As recently as 2014, correspondence between McDonald's Latin America LLC, a wholly owned subsidiary of McDonald's Corporation, and Arcos about Arcos' compliance with the terms of the master franchise agreement was directed to Forrestal Capital in Miami.[35] Moreover, although neither Franqui nor Hernández-Artigas are employed by Arcos, corporate documents have identified Hernández-Artigas at Forrestal Capital's Miami office as the official contact for Arcos and its affiliated companies.[36]

Franqui and Hernández-Artigas are connected to Staton and his Arcos investments in other ways as well. According to the Los Laureles trust, they are designated to become members of the trust's voting committee−which decides how to vote all of Staton's Class B shares−upon Staton's death or incapacitation. Franqui is also one of two directors of Chablais Investment S.A, the entity that holds most of Staton's Class A shares; the other listed director of Chablais is Staton's son Francisco Staton.[37]

The fact that at least three directors—one of whom is alleged to be independent—have deep and long-standing relationships with the controlling shareholder suggest that the board is incapable of monitoring related-party transactions and ensuring adequate disclosure of these transactions to shareholders, reinforcing the need for a Commission investigation.

Investigation into Potential Disclosure Violations

CtW Investment Group believes that Arcos has made misrepresentations and material omissions concerning related-party transactions with two entities in order to conceal that the company is being managed in a way that puts the controlling shareholder's interests ahead of the company's. Arcos has represented that its master commercial agreement with related-party Axionlog is on arm's length terms, a statement that has been seriously called into doubt by Arcos' other disclosures to the SEC and other publicly-available information. CtW Investment Group also believes Arcos has failed to disclose information regarding material related party transactions with Pegasus Group, a private equity investment group that appears to have been founded by Woods Staton and director Michael Chu.

CtW Investment Group believes that Arcos' inadequate disclosures about these related party transactions are a direct result of a board of directors that lacks independence and, as a result, provides virtually no checks on Staton's control. The company's weak governance has made it vulnerable to improperly managed related party transactions and inadequate disclosures about those transactions.

Since April of last year, CtW Investment Group has attempted to engage the company about these related-party transactions to no avail. Because minority shareholders have no meaningful ability to

[34] In an interview, Franqui said that Forrestal Capital "was founded in 2003, after the sale of Panamerican Beverages, at the time the largest Coca Cola bottler outside the US, and the principal asset of the family." Annette Franqui interview, *available at*: http://lavca.org/2015/01/28/lp-profile-annette-franqui-co-founding-partner-forrestal-capital/. *See also* Kerry A. Dolan, *Arcos Dorados IPO Creates First McDonald's Billionaire*, FORBES, Apr. 28, 2011.

[35] Arcos Form 20-F, Apr. 29, 2015, Ex. 4.4.

[36] *See, e.g.,* Amended and Restated Master Franchise Agreement, Exhibit 10.1 to Registration Statement filed on Mar. 25, 2011, at 80.

[37] Arcos Form SC 13D Ex. 7.1., Joint Filing Statement, Mar. 11, 2018.

persuade the company to address these concerns, an SEC investigation is necessary to ensure that shareholders are given complete information about the company's related party transactions. CtW Investment Group respectfully requests that the SEC reopen its inquiry into the company and require the company to disclose all material aspects of its relationship with Axionlog and Pegasus Group in advance of the company's annual meeting. CtW Investment Group also requests that the SEC conduct its own investigation of these relationships to ensure that all company disclosures are complete and accurate.

Sincerely,

Dieter Waizenegger
Executive Director, CtW Investment Group