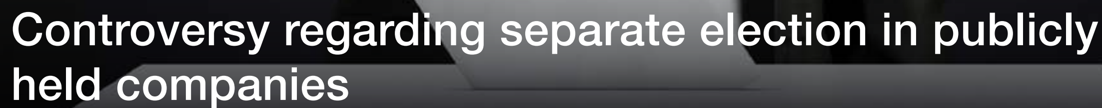

Controversy regarding separate election in publicly held companies

The season for ordinary shareholders' meetings is approaching and several companies, in addition to approving the management accounts and the financial statements, must deliberate on the election or reelection of directors for a new term. Considering the several modalities of elections that can be adopted, a matter that usually leads to different interpretations is the applicability of the separate election in publicly-held companies.

The separate election of a member of the board of directors, contemplated in paragraph 4 of article 141 of the Brazilian Corporation Law, is a mechanism to protect minority shareholders and aims to ensure their representation on the board of directors. This structure is applicable only to publicly held companies and exclusively to minority shareholders that provide evidence of uninterrupted ownership of their shares in the company during the three months immediately prior to the shareholders' meeting in question. For the separate election to be applicable, the uninterrupted ownership of shares must be of 15% of the voting capital or 10% of the capital stock, nevertheless, the Brazilian Securities and Exchange Commission ("CVM") understands that, for companies that only issue voting shares (common shares), the percentage of 10% applies.

Diverse interpretative currents

The controversy regarding the applicability of the separate election arises at the moment that shareholders of corporations without a controlling shareholder or defined block of control, consider electing separately a member of the board of directors, exercising this right guaranteed by the Brazilian Corporation Law. CVM has not yet expressly stated its position on the matter, and, therefore, two interpretative currents may be identified.

Although this issue is rarely addressed in a specific and public manner by legal experts, who end up discussing the matter in individual opinions and consultations with clients, many believe that the adoption of the mechanism of separate election presumes the existence of a controlling shareholder or a defined block of control. For many of them, as a mechanism to protect minority shareholders from abuses by controlling shareholders, it would be contradictory that the separate election could be adopted in a company without a defined controlling shareholder, since there would be no shareholder to be prevented from participating in such separate election. In other words, in this case, if there is no controlling shareholder, all shareholders could qualify as "minority" in the separate election.

Nevertheless, some legal experts argue that the adoption or not of the separate election mechanism in companies that do not have a controlling shareholder, or a defined block of control should be analyzed on a case-by-case basis, taking into consideration the company's capital structure and the behavior of the shareholders with greater preeminence in management over time. The defenders of this position argue that the adoption of separate election would make sense in case the relevant minority shareholder has participation exceeding the legal quorums (of 10% and 15%) and the power to elect alone the majority of the members of the board of directors in a certain meeting (or all of them, in the case of election of a short list).

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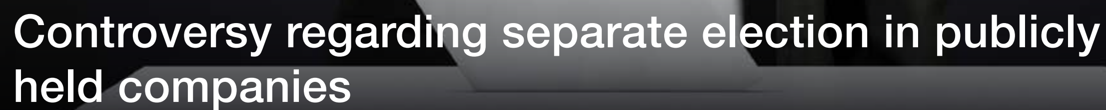

Controversy regarding separate election in publicly held companies

Despite the discussion, in practice there are publicly held companies that do not even provide the questions related to the separate election in the remote voting bulletin, as is the case of B3. And according to public information, none of them have been questioned about this practice so far.

CVM has already expressed its position on the topic indirectly in the analysis report of the public hearing on the amendment of CVM Instruction No. 481, released on December 20, 2017. At the time, the Commission acknowledged that the distance voting bulletin items regarding the separate election may not be applicable to all companies, but did not expressly agree that such a mechanism could not be adopted generally by corporations without a controlling shareholder.

Until CVM is provoked to specifically address the issue more clearly, the discussion is likely to continue.

The text above was published in Portuguese in the Legislação & Mercado section of Capital Aberto on March 15, 2022, and can be accessed through the link below:

https://tinyurl.com/3zfcs55j

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Former partner's liability for debts of a limited liability company

The liability of a partner after selling its quotas in a limited liability company or the dissolution of the company is often discussed.

The Brazilian Civil Code establishes that the assigning partner is jointly liable with the assignee, before the company and third parties, for the obligations it had as a partner, up to two years after the amendment to the articles of association regarding its withdrawal from the company.

It is important to emphasize that this legal provision does not constitute an unlimited, unrestricted, joint and several liability of the assignor partner for any debts of the company. It constitutes, however, the liability of the assignor for the obligations it had as a partner, and the obligations of the partner are not to be confused with the obligations of the company itself.

As a rule, the liability of each partner is limited to the value of their quotas and all are jointly and severally liable for the payment of the capital stock. In other words, as a general rule, partners and former partners are not liable for the debts of a limited liability company.

As stated in the Brazilian Civil Code, "the patrimonial autonomy of legal entities is a legal instrument of risk allocation and segregation, established by law with the purpose of stimulating undertakings, for the generation of jobs, taxes, income, and innovation for the benefit of all".

However, in certain specific cases, limited liability company's creditors may resort to the assets of the partners (and former partners) to settle debts, among which we highlight the piercing of the corporate veil.

Recently, the Superior Court of Justice (STJ) decided that in the case of former partner liability arising from the piercing of the corporate veil, the former partner is not accountable for the company's debts incurred after its formal withdrawal, even if the debts refer to the period of two years after its withdrawal. In this case, it was understood that the two-year period provided for in the Brazilian Civil Code is the time limit for collection from the partner for obligations assumed prior to its exit.

Although this STJ decision is not binding, it is extremely relevant, because in several decisions from different courts, including the STJ itself, the liability of withdrawing partners has often not been restricted to the period in which they still held ownership.

In another STJ judgment, which discussed the possibility of holding the partners and their personal assets liable for the remaining debt owned by a company that was regularly terminated, the court considered that in limited liability companies, after paying-in the capital stock, the partners are not liable with their personal assets for the debts owed by the company, so that the succession depends intrinsically on proof of the existence of positive net equity and its effective distribution among the partners.

Therefore, there is no increase in the former partner's liabilities at the time the partner withdraws from the limited liability company, there is only a time limitation on the collection for applicable obligations related to the time of their participation in the company.

The text above was published in Portuguese in the Legislação & Mercado section of Capital Aberto on April 20, 2022, and can be accessed through the link below:

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Brazilian Securities and Exchange Commission sanctions managers of a publicly held company for irregularities in a Shareholders' Meeting

On April 26, 2022, the Brazilian Securities and Exchange Commission ("CVM") judged the Administrative Sanctioning Proceeding ("PAS") CVM SEI No. 19957.003922/2020-50, filed by the Superintendence of Company Relations ("SEP") to ascertain supposedly abuses of officers during a shareholders' meeting.

At the time, the controlling shareholders, who were also the chief executive officer and vice president of the company, voted and approved their own accounts as managers, indirectly through other companies controlled by them, aside from an abusive compensation for themselves, in non-compliance with Law No. 6.404/1976 ("Brazilian Corporation Law").

The defendants argued that the legal prohibitions for approving the accounts would affect only the person of the manager and not companies of which they were shareholders and questioned the conclusion of the technical area regarding the allegation of abusive compensation, declaring that the values approved were in in line with market practices and with the competence and experience of the managers.

In her vote, Reporting Officer Flávia Sant'Anna Perlingeiro, in line with CVM precedents, reinforced that the prohibition imposed on managers for the approval of their own accounts, provided for in articles 115, §1 and 134, §1 of the Brazilian Corporation Law, should affect the legal entities controlled by them in cases where it is not possible to dissociate the will of a particular shareholder, legal entity, from the influence of the shareholder-manager, who is prevented from deliberating on his own accounts, as it was confirmed in the present case.

Regarding the approval of abusive compensation for their own benefit, the Reporting Officer stated that in cases where the compensation of managers is discussed, the commission must interpret article 152 of the Corporation Law, which provides that the compensation of managers must be fixed considering their responsibilities, the time dedicated to their functions, competence and professional reputation and the value of the services in the market, as a beacon. Since it will be from these criteria that the values of the global or individual compensation will be formulated and justified, concluding that, the performance of the controlling shareholder who approves the compensation in disagreement with such guidelines may constitute an abuse of the power of control in the light of article 116 , §1 of the Corporation Law.

In the case under analysis, it was found that the defendants received high compensations when compared to the company's revenue, and during two fiscal years the remuneration exceeded the company's revenue, which, according to the Reporting Officer, given the absence of consistent justification in meeting the social interest, reveals a clear disproportionality, even more so considering the company was facing financial difficulties, in a scenario of negative net equity and the impossibility of distributing dividends.

Nevertheless, the Reporting Officer's acknowledged that the company's revenue will not always be an adequate criterion for determining the existence of abuse in setting the managers' compensation, given that the circumstances of each case are relevant to elucidate the fundamentals of compensation and whether they adhere to the social interest.

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Brazilian Securities and Exchange Commission sanctions managers of a publicly held company for irregularities in a Shareholders' Meeting

Finally, CVM's Board unanimously decided to sentence each of the company's managers to pay R$210,000.00 (two hundred and ten thousand reais) for the approval of their own accounts and R$ 425,000.00 (four hundred and twenty-five thousand reais) regarding the approval of abusive compensation.

The full text of PAS CVM SEI 19957.003922/2020-50 can be accessed in Portuguese through the following link:

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