
OFFICER AND DIRECTORS LIABILITIES IN BRAZILIAN COMPANIES

The Brazilian Law 10.406, of January 10, 2002 (the New Civil Code), in its Article 1.061, has created the possibility, previously inexistent, for the quotaholders to appoint a non-quotaholder as an officer of the Limited Liability Company (*Sociedade Limitada*). According to the former Civil Code and Decree 3.708, the administration of the Limited Liability Company was restricted to the partners designated as quotaholder-managers and, if not explicitly designated to the contrary, executed by all quotaholders. In such previous context, the appointment of the administration and representation of the company by third parties was only allowed if expressly permitted in the company's Articles of Incorporation and, when allowed, the representation by third parties would lead to the personal liability of the quotaholder for the acts performed by such indicated third party, the delegated. Quotaholders-managers were therefore jointly and unlimitedly liable for excessive mandate and for acts in breach of the articles of association or the law, and it was not possible to hold the liability to a non-quotaholder.

The Brazilian New Civil Code revived the discussions on the responsibilities of the officers of the Brazilian companies, for acts executed beyond, in violation or excess of their powers granted by the articles of association (for the limited liability companies) or by laws (for the corporations – “sociedades anônimas”).

The provisions created by the new Brazilian law aim to impute the subjective responsibility of the officer, for acts performed with negligence or misconduct. In this sense, the officers should not be held responsible while undertaking ordinary obligations assumed on behalf of the company or in virtue of acts of regular management, provided, of course, that such acts are practiced in accordance with the powers granted.

It is the officers duty to take all care and diligence that any ordinary man should employ in managing its own business (Article 1.011, of the Civil Code and Articles 153 to 155, of the Corporations Law), being personally responsible for negligence or misconduct in the performance of its acts, before the company and any third party (article 1.016, of the Civil Code and article 158 of the Corporations Law).

As a consequence of the personal civil responsibility of the officer, its private assets may be used for the redress of any irregular act; act that violates the law, articles of association or by laws; and acts which harms the company or third parties.

On the other hand, the officer or director will not be liable for illegal acts performed by other officers, except when the officer or director by negligence or connivance, did not investigate nor tried to stop any illegal act performed by other officers. In this situation, in order to be excused for

any responsibility, the officers shall inform such fact and/or express its disagreement to the shareholders or quotaholders, and include information in a minute of shareholders' meeting (article 158, paragraph 1, Corporations Law).

The officers will assume joint liability for the damages caused by the non compliance of the legal duty to ensure the regular course of business of the company (article 158, paragraph 2, Corporation Law). Such joint liability will not be applied to the officers of publicly-held companies, being the responsibility, in this case, restricted to those officers identified in the by laws with specific responsibilities to do so (article 158, paragraph 3, Corporation Law), except when the officer knows the obligation non-accomplished by the last officer, or by the competent officer and do not communicate it to the General Shareholders' Meeting, in this case, the officer will be jointly liable (article 158, paragraph 4, Corporation Law).

In view of the above, please find bellow some of the events where the officers shall be responsible for its management:

(i) Conflict of interests

It is prohibited to the officer to participate of any transaction or deliberation with interests contrary to the companies' interests. The non-compliance to such obligation will result in the personal responsibility of the officer.

(ii) Misuse of the corporate name

It is the officer or director duty to refund or pay the equivalent of goods or credits invested for his own interest or for third parties interest, and also for the damages caused without written notice of the shareholders or quotaholders.

(iii) Deviation of purpose and assets' confusion

In the situation where the deviation of purpose the legal personality of the company can be ignored, which can result in the extension of the effects of certain obligations to the personal goods of the shareholders / quotaholders or officers.

(iv) Malicious and fault acts

The officer will be liable for the damages caused by its fault, before the company or third parties.

The fault is characterized by the imprudence, malpractice or negligence in the officers' acts. Maliciously is characterized by the intention of the officer to execute the malicious act or to assume the risk of producing it.

(v) Distribution of illegal or non existing profits

The officer is personally responsible before the company for the distribution of illegal or non existing profit, being obligated to refund the profit and the damages caused to the company (article 1.009, Civil Code and article 201, paragraph 1 and 2). The quotaholders with knowledge of the irregularity are liable for the refund of the dividends received. The bad-faith shall be presumed when the profits are distributed without drawn up the balance sheet or in disagreement of the results.

For the officer to be exempt of culpability by decisions taken with good-faith, it shall prove diligence appraisal of the liabilities and assets of the company, observing the legal criteria and the methods adopted by Governmental agencies and professional associations.

(vi) Delay on the approval on the instrument of appointment

The officer appointed in an instrument other than the articles of association shall be responsible for the registration of such act, within 10 (ten) days, before the Commercial Registry (article 1.062, Civil Code).

In case of delay on such registration, the officer is jointly liable with the company for the acts carried out before the registration of the instrument of its appointment.

The statute of limitation for compensation for damages of the company is of 03 (three) years, starting with the presentation to the quotaholders or shareholders of the balance sheet regarding the corporate year when the violation has occurred, or in the General Meeting where the fact was taken into knowledge (article 206, paragraph 3, VII, 'b', Civil Code). The statute of limitation for the compensation for damages caused to third parties prescribes is of 10 (ten) years.

The officer's term of office ends with its resignation, dismissal or upon the expiration of the term, if it is not reelected. In order to be effective against third parties, the corporate act related to the end of the officer's term of office shall be registered before the Commercial Registry within 10 (ten) days. The officer's resignation is effective before the company as of the receipt of the resignation letter.

Finally, the responsibility for regular management acts carried out in the company's ordinary course of business only ends with the approval of the officer's accounts by the General Meeting, in accordance with the article 1.071, I of the Civil Code.

Professional Civil Responsibility Insurance

In Brazil, there are professional civil responsibility insurances to several activities, including specific insurances to officers, the so called D&O ("Directors & Officers") Insurances.

D&O insurances provide an "armor" to the assets of the top members of companies' management (officers, board members, managers) against lawsuits filed by shareholders and/or by third parties against such officers.

The change of the legislation, as mentioned above, and the effective application of the law, which resulted in the increase on number of lawsuits filed against companies for acts of mismanagement of their officers has impacted in the D&O insurance market in Brazil. Indeed, in accordance with information provided by the Private Insurance Superintendent – SUSEP, the D&O insurance has grown 12,3% in the year of 2005.

In order to allow the insurance company to analyze whether the insurance is viable and the value of the insurance premium, it is necessary to fulfill a form for the analysis of the risk. However, it is possible to evaluate an insurance premium of 1 to 3% of the value of the insurance.