Brazil

Financial Assistance

IBA Corporate and M&A Law Committee 2022

Contact

Paulo Coelho da Rocha

Demarest Advogados, São Paulo

procha@demarest.com.br

Contents

INTRODUCTION

According to Brazilian law, there are no laws or regulations dealing directly with the concept of financial assistance. More specifically, there are no general prohibitions on direct or indirect advancement of funds by a target company to a third party, for the purpose of the third party acquiring quotas or shares issued by the target company (or quotas or shares issued by any other company in the group to which the target company belongs).[1]

Notwithstanding the above, this guide sets out an overview of certain aspects of Brazilian law that should be considered in the framework of an acquisition transaction as above. Depending on the relationship between the target company and the third party receiving the advancement of funds, or the nature of the involved parties, certain prohibitions and/or restrictions may apply – particularly since the two involved entities become related parties once the acquisition transaction is consummated.

This guide does not consider the concepts of disguised distribution of profits (*distribuição disfarçada de lucros* or DDL) and thin capitalisation, which may need to be considered depending on the case.

RELEVANT MATTERS

The following aspects of Brazilian law should be considered whenever an acquisition transaction comprises a prior direct or indirect advancement of funds by the target company to a third party, for the purpose that the third party acquires quotas or shares issued by the target company (or by any other company in the group to which the target company belongs).

Restrictions on security for the advancement of funds
In accordance with Article 30, paragraph 3 of Brazilian Law No. 6,404, of 15 December 1976 (the Corporations Law), applicable primarily to closely held and public corporations (*sociedades por ações*), and of subsidiary application to limited liability companies (*sociedades limitadas*), a company shall not receive its own shares as security, except for the specific purpose of securing the tenure of the members of its management bodies.

Advancement transaction at arm's length, with no abuse of power by controlling shareholder and no breach of management duties
The concept of arm's length is provided in the Corporations Law and must be observed by a company, especially in transactions with its controlling shareholder, related parties and members of its management bodies.

The abuse of controlling power by the controlling shareholder when dealing with the company is prohibited by Articles 117 and 246 of the Corporations Law, as well as by Regulation No. 323 of the Brazilian Securities and Exchange Commission (*Comissão de Valores Mobiliários* or CVM). This is applicable to listed corporations.

[1] For advances provided by non-financial institutions, interest rates (if any) should be limited to 12 per cent per year.

Pursuant to Article 154, second paragraph, section (b) of the Corporations Law, members of the company's management shall not use the assets, services or credits of the company in the benefit of third parties without first obtaining the authorisation of the general shareholders meeting or of the board of directors.

Management duties are also established by the Corporations Law. Article 155 provides for the duty of loyalty of the members of the management, which must also be observed in transactions between these members and the company. Article 156 prevents the managers from dealing with the company in case of conflict of interests, or in conditions under which are not deemed to be arm's length. Hence, the transaction supporting the advancement of funds must necessarily be at arm's length. Finally, according to Article 245, the management may not favour an associated, controlling or controlled company to the detriment of the company, and shall ensure that transactions are equitable or compensated by adequate payment.

As set forth in these articles of the Corporations Law, the concept of arm's length must be taken into consideration when the target company advances funds for acquisition of its own shares.

Financial institutions – restrictions on credit transactions
Financial institutions may not perform credit transactions (including loans and guarantees) with their related parties,[2] except:

1. if the relevant transaction is conducted at arm's length basis; and
2. the outstanding amount of all transactions entered with:
    a. all related parties do not exceed 10 per cent of the financial institution's adjusted shareholders' equity;
    b. one single related-party individual does not exceed 1 per cent of the financial institution's adjusted shareholders' equity; and
    c. one single related party legal entity does not exceed 5 per cent of the financial institution's adjusted shareholders' equity.

Currently, there are also certain restrictions imposed on financial institutions that limit lending to public sector entities, such as public or government-controlled companies and governmental agencies. Public sector entities are also subject to certain limits on indebtedness.

Financial institutions – restrictions on risk concentration
Brazilian law provides that a financial institution may not extend credit to any person, group of persons or company in an aggregate amount equal to 25 per cent or more of the financial institution's adjusted shareholders' equity.[3] This limitation applies to all transactions involving the extension of credit, including those involving loans and advances, guarantees and the underwriting, purchase, and renegotiation of securities.

Consequences of providing financial assistance
The violation of the above restrictions may expose the individual and/or the company to a range of consequences. These range from administrative penalties to prosecution for civil and criminal liabilities.

[2] Namely: (1) Controlling shareholders; (2) executive officers, members of statutory bodies (and their respective spouses or relatives to the second degree); (3) individuals or legal entities holding more than 15 per cent of a financial institution's capital stock; and (4) legal entities: (a) in which a financial institution holds more than 15 per cent of the capital stock; (b) in whicha financial institution holds the operational controlling or prevalence in corporate approvals; and/or (c) which have executive officers or directors in common with financial institutions.
[3] Restrictions on risk concentration applicable to non-related parties. For those applicable to related parties, please refer to item above.