Legal Bulletin
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New rules on infractions in capital markets

Provisional Measure ("MP") No. 784 broadened enforcement powers of the Central Bank and the Securities Commission (CVM)[1] effective June 8, 2017.

With respect to the CVM – which is the scope of this article – MP No. 784/2017 creates a leniency program, increased penalties and adopted new punitive procedures.

Leniency agreement

The leniency program is inspired by the antitrust leniency program existing since 2000.

Articles 30 to 33, and 35, of MP No. 784/2017 grant CVM powers to enter into leniency agreements under which individuals and corporations, in return for their cooperation in prosecuting a case, are excused from administrative penalties. The cooperation needs to result in the identification of other members taking part in the violation and in the obtaining of documents that evidence such violation.

All of the following must be met: (i) the applicant is the first to come forward and confesses its participation in the relevant violation (this requirement is waived for individual applicants); (ii) the applicant ceases all involvement in the violation; (iii) CVM lacks sufficient information on the illegal activity to otherwise ensure punishment; and (iv) the applicant agrees to provide full, continuing and complete cooperation throughout the investigation. If all above requirements but (i) are met by a corporate applicant, leniency might be granted in the form of reduction of applicable penalties by one third.

MP No. 784/2017 does not provide for the participation of the Prosecutors' Office in the execution of leniency agreements. As only the Prosecutors' Office may bring and settle criminal cases, if it does not take part in a leniency agreement it will only be effective to set aside administrative penalties. News indicate that the Federal Government might consider amending MP No. 784/2017, providing for the joint action of the Prosecutors' Office and CVM (or Brazilian Central Bank in case of offenses committed by agents of the financial system)[2]. Cooperation between criminal and administrative authorities in leniency program will in any scenario lead to much more effective results than their independent actions.

Rules on settlement ("*termo de compromisso*") remain untouched. A settlement does not require indication of unlawful conduct of third parties, but merely the obligation to cease a given practice and pay for damages, in exchange for suspension of the CVM sanctions procedure. Proceeds from settlements will be directed to a fund ("*Fundo de Desenvolvimento do Mercado de Valores Mobiliários*") to be managed by CVM with the purpose of promoting securities market development and financial education through CVM projects.

Increased administrative penalties

By amending Article 11 of Law No. 6,385, of December 7, 1976, MP No. 784/2017 altered the regime of sanctions that can be sought by CVM through administrative proceedings. The sanctions include censures, fines, suspension of authorizations or registrations to hold specified offices and temporary bars from engaging in certain activities related to the securities industry.

1. According to CVM, MP No. 784/2017 aims to ensure "(i) greater effectiveness of CVM's proceedings, fine-tuning enforcement as an effective instrument to provide guidance to securities market participants; (ii) a larger pool of possible sanctions and regulatory tools to properly and proportionally deal with a number of different irregularities verified within the ambit of securities market; and (iii) conditions to support faster and more effective supervision actions, strengthening CVM's role in discouraging malpractices." www.cvm.gov.br/noticias/arquivos/2017/20170608-1-1.html.

2. See www.valor.com.br/international/news/5002079/government-wants-give-power-bc-participate-leniency-deals

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The new cap for fines is the highest of (i) BRL 500 million; (ii) twice the amount of the issuance of irregular transaction; (iii) three times the economic benefit resulting from the infraction; and (iv) if the wrongdoer is a company, 20% of its gross revenues (individually or considering its economic group) in the fiscal year before the fiscal year when the administrative procedure starts. Fines imposed in case of non-compliance with orders issued by CVM may reach BRL 100,000 per day.

CVM was also granted powers to forbid the company from (i) entering into agreements with public financial institutions up to five years and (ii) participating in public bids held by public administration for acquisitions, sales, rendering services and concessions of public services. MP No. 784/2017 does not set out a term for sanction. This issue needs to be clarified as it is not reasonable that the company faces an unlimited time punishment.

The new wording of Article 11 of Law No. 6,385/1976 makes clear that the penalties above may be imposed by CVM cumulatively.

New procedural rules

The administrative procedure for seeking sanctions has been reshaped by MP No. 784/2017.

It sets forth as a general rule that execution of judgment will not be stayed by appeal (Article 29). The defendant may only request a stay of execution to the same authority that issued the judgment and shall submit to such authority's decision. Exception is made for sanctions of censure or fine, in which case the appellate body may grant stay of execution.

A provision in Article 27 to the effect that the defendant has the burden of proof raises due process concerns related to shifting burden of proof. The best interpretation, however, is that it merely states that the defendants have to prove new facts alleged as defense, which is the general rule of administrative procedures.

Articles 23 and 24 of MP No. 784/2017 enable CVM to notify defendants by electronic means.

Retroactivity versus prospectivity

Increased penalties laid down by MP No. 784/2017 are to be applied only to future conducts.

On the other hand, leniency agreements may cover violations occurred prior to the issuance of MP No. 784/2017. Differently from new heavier penalties, which under a Constitutional principle cannot apply past violations, new procedural rules apply immediately.

Final remarks

There is much room and need for CVM to detail the norms of MP No. 784/2017. CVM officers announced that the Commission will hold public discussions with market participants on the application of the new rules.

MP No. 784/2017 must be converted into law by the Brazilian Congress within 60 days from the date of its publication, extendable for an additional 60 days.

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