

## Approved new law on administrative proceedings in financial system

Law No. 13,506, dated November 13, 2017, amended the rules applicable to punitive procedures conducted by the Central Bank of Brazil (BCB) and the Brazilian Securities Commission (CVM).

With respect to BCB, which is the scope of this article, the new law affects all entities under the surveillance of BCB, such as banks and members of the Payment and Consortium Systems. It also impacts individuals and corporations developing activities under the surveillance of BCB, rendering certain audit services to such entities or holding management positions therein.

### Infractions

When compared to Law No. 4,595, dated December 31, 1964 (which governs the National Financial System – “SFN”), the new law broadened the list of administrative infractions to which individuals and companies are subject. The new list is long and includes the failure to provide information required by law or regulation to BCB (such as the declaration of Brazilian assets abroad), the performance of transactions prohibited or not aligned with BCB’s authorization and the exercise of management positions in financial or similar institutions without BCB’s approval.

Prohibited transactions include: (i) issuance of debentures; and (ii) acquisition of real estate properties not intended for use of the acquiring entity, except those received as payment of non-performing loans or when expressly authorized by BCB, in compliance with rules to be issued by the National Monetary Council (CMN).

The restriction on the issuance of debentures is not new. The rules on acquisition of distressed assets, on the other hand, were amended by the new law.

Under the previous system, distressed assets needed to be sold within one year, extendable two times at BCB’s discretion. Those assets were usually sold at a very low percentage of the par value, since the banks were forced to get rid of them within the legal term in any circumstances. As of the publication of the new law, CMN is allowed to provide for more flexible sales criteria, taking into account urgent matters, as crisis in the real estate market.

### Penalties

Law No. 13,506/17 provides for the following penalties, separately or cumulatively: (i) public admonition (which is the disclosure of the sentence, including the name of the convicted party and the description of the infraction incurred); (ii) fines; (iii) prohibition to engage in certain activities or transactions for a maximum period of 20 years; (iv) suspension of permission to hold positions which depend on the authorization from BCB for a maximum period of 20 years; and (v) cancelation of authorization to operate. Penalties indicated in “iii” to “v” only apply to “serious offenses” (as defined in the new law).

Law No. 13,506/17 increased fines from BRL 250 thousand (or 300% of the transaction value in case of foreign exchange related infractions) to the highest of BRL 2 billion or 0.5% of the services and financial products revenue in the year preceding the infraction. Fines above BRL 50 million must be reviewed by a BCB collegiate body<sup>1</sup>. In case of bankruptcy, extrajudicial liquidation or other insolvency proceedings against the defendant, the credits emerging from the imposition of fines by BCB are subordinated to other creditors’ rights.

BCB may also impose daily fines in case of non-compliance with coercive and pre-emptive orders issued by such authority, which fines may reach the highest of BRL 100 thousand and one thousandth of the services and financial products revenue of the entity in the year preceding the infraction.

<sup>1</sup> Criteria to stipulate the fines and other penalties in concrete cases were defined by Circular BCB No. 3,857, issued on the same day as the publication of Law No. 13,506/17. The same circular also regulated agreements with the Central Bank under Law 13,506/17.

### São Paulo

Av. Brig. Faria Lima, 2601  
12th floor - 01452-924  
São Paulo, SP - Brazil  
Phone. +55 11 3555 5000

### Rio de Janeiro

Praia de Botafogo, 440  
15th floor - 22250-908  
Rio de Janeiro, RJ - Brazil  
Phone. + 55 21 3503 2000

### Brasília

SBN Q 1, Bl B, n. 14, Ed. CNC  
2nd floor - 70714-900  
Brasília, DF - Brazil  
Phone. + 55 61 2109 6070

contato@levysalomao.com.br

Increased penalties laid down by Law No. 13,506/17 are to be applied only to conducts occurred after November 14, 2017 (the law's effective date) due to a Constitutional principle that prevents the application of penalties to past violations.

### Settlement and Leniency Agreement with BCB

Law No. 13,506/17 creates leniency and settlement programs with BCB to prevent negative consequences arising from investigations and to reduce or extinguish penalties.

If there is no serious offense, individuals and corporations may enter into a settlement (*termo do compromisso*) with BCB in order to prevent the commencement of an administrative proceeding or suspend the procedure initiated. The signatory of the settlement undertakes to: (i) cease the practice under investigation or its effects; (ii) correct the irregularities pointed out and indemnify losses; (iii) pay the fine imposed and comply with any other conditions as may be agreed in a particular case.

Law No. 13,506/17 also provides for the "administrative agreement in supervision proceeding", which is the designation of the leniency agreement under the new law. BCB is allowed to sign such an agreement with individuals or corporations who confess administrative offenses (classified as serious or not) under the authority of the BCB. The signatory of the agreement may be entitled to a waiver from the administrative penalties or reduction by one-third to two-thirds.

The administrative agreement and settlement may cover violations occurred prior to the issuance of Law No. 13,506/17, because new procedural norms apply immediately to ongoing proceedings and because more favorable rules to regulated persons can apply to past violations.

Agreements with BCB have however the set back of not extending to criminal matters, being limited to the administrative level.

Based on provisions from the Bank Secrecy Act (Complementary Law No. 105, dated January 10, 2001), Law No. 13,506/17 requires BC to notify Prosecutors' Office and the competent public agencies of possible crimes detected by BCB as soon as the proposal for an administrative agreement is received. Thus, if a given conduct constitutes an administrative infraction and a crime at the same time, the applicant will be forced to negotiate with the Prosecutors' Office alongside with BCB. Otherwise, chances of criminal charges precisely because of the cooperation with the regulatory authority will be increased.

BCB's notification to the Prosecutors' Office has the advantage of preventing crimes from remaining unnoticed. However, negotiations with the Prosecutors' Office are not always available to the regulated persons, since plea bargain agreements are restricted to criminal organizations and other more extreme cases (such as drug dealing). For conducts practiced by only one agent, without any criminal organization (as usually occurs in the financial industry), the applicant who reveals information to BCB will be unprotected in regard to criminal liability even if it does not conclude the administrative agreement.

The new law should have extended the benefits arising from the agreements concluded to criminal matters, instead of only providing for the participation of the Prosecutors' Office in the negotiations. This solution would stimulate the interaction between the regulatory and the criminal bodies and provide additional safety to the applicant.

### Procedural rules

As of Law No. 13,506/17, the BCB can decide at its own discretion to initiate or not administrative proceedings related to conducts which do not result in substantial damages. Such discretion allows BCB to focus efforts and public resources on proceedings with higher impacts on markets and society.

The new law provides that the enforcement of a BCB's judgment can be stayed by appeal (suspensive effect). However, in case severer penalties are applied (bars from engaging in certain activities or transactions, suspension of permission to hold positions and cancelation

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### Brasília

SBN Q 1, Bl B, n. 14, Ed. CNC  
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Phone. + 55 61 2109 6070

contato@levysalomao.com.br

of authorization to operate), the appeal will not suspend the enforcement of the judgment, except if this is requested by the defendant to the same authority that issued the judgment. This clearly affects negatively the probability of achieving such an effect. Thus, BCB must be extremely careful, since the authority's decisions may jeopardize the survival of the companies.

#### Other topics

**Private credit netting:** Law No. 13,506/17 also changed different rules applicable to the financial system, as those regarding "private credit netting" (*compensação privada de créditos*), which is the discharge of credits and debts between persons domiciled abroad and persons domiciled in Brazil not formalized through foreign exchange agreements.

The private credit netting is not permitted under Brazilian law, which increases transaction costs, especially to exporters. There is no reason to keep such a prohibition nowadays. Instead, BCB could demand the record of such transactions in order to control foreign exchange transactions. However, Law No. 13,506/17 maintained the ban on private credit netting as a rule and permitted such operations to occur only in exceptional cases, to be expressly provided for in the regulation to be issued by the monetary authority.

The netting operation which fails to comply with the regulation to be issued will be punished with the penalties provided for in Law No. 13,506/17.

**Penalties standardization:** Law 13,506/17 sought to standardize the sanctions applicable to persons and activities regulated by BCB. Several conducts will now be subject to the penalties provided under the new rule, such as: (i) failure to provide BCB with information on assets held abroad by Brazilian-resident individuals or Brazilian legal entities, as required under law or regulation; (ii) violation of rules governing the register of foreign capital with BCB; (iii) violation of laws and regulation governing the Consortium System; and (iv) failure to apply minimum required amounts of funds in rural credit transactions.

**Credit operations involving related parties:** Law No. 13,506/17 amended the laws regulating loans and advances to related parties at administrative and criminal levels.

An important development was that Law No. 13,506/17 provides for exceptions to the general prohibition against credit operations between related parties. Certain transactions, as those carried out under market conditions and those authorized by CMN are accepted from now on. This may relieve from penalties entities and individuals connected to them now under prosecution, since the more favorable rule apply to these cases immediately upon being issued.

Other credit operations" between "related parties" remain banned, but as per the new text: i) "credit operations" definition will be given by the regulation issued by CMN; and ii) the term "related party" no longer includes "sister" companies. Even so, transactions between sister entities may be forbidden in certain circumstances, for instance when there is a common officer or member of the board of directors to them.

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Phone. + 55 21 3503 2000

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2nd floor - 70714-900  
Brasília, DF - Brazil  
Phone. + 55 61 2109 6070

contato@levysalomao.com.br

Fabio Kupfermann Rodarte  
[frrodarte@levysalomao.com.br](mailto:frrodarte@levysalomao.com.br)