REDUCING THE RISK OF LABOR LIABILITY FOR SHAREHOLDERS

The over protection of Brazilian labor law and Labor Courts towards workers is well known, and potential exposure to labor contingencies has always worried foreign and local investors. Encouragingly, however, new laws and Court precedents have been subtly reducing labor liability risks.

The so-called Labor Reform, that became effective at the end of 2017, enhanced legal certainty for former shareholders. The new law has limited the extent of the liability of a former shareholder for labor obligations to a period of two years as from the date the shareholder ceases to hold shares.

In addition, it established that former shareholders are liable on a secondary manner ("*responsabilidade subsidiária*"), i.e., they can only be held liable should the company and current shareholders not have assets to guarantee and/or pay the labor debts. Until then, case law held that former shareholders were liable for obligations stemming from labor relations in effect during the period in which they held interest in the company, regardless of the time elapsed after their departure and without discussing any priorities in terms of liability.

Another improvement brought by the Labor Reform is the fact that the disregard of the legal entity requires specific procedure prior to the Court decision, giving opportunity for shareholders and/or managers to present defense; previous case law authorized the disregarding of the legal entity without specific request and opportunity for shareholders and/or managers' defense.

Pursuant to Brazilian Corporate Law, in general, shareholders' liability for the company's debts is limited to the value of their fully paid-up shares. The corporate veil may be lifted only if specific conditions are met.

Labor Courts generally apply the broad rule of disregard of the legal entity on the grounds of the vulnerability of the creditor, as prescribed in the Consumer Defense Code. Courts hold that the mere lack of assets to pay up labor obligations is sufficient to lift the corporate veil and hold shareholders (even minority shareholders) and managers liable for labor obligations.

Conversely, the Civil Code reasonably provides for the disregard of a legal entity on the grounds of abuse of the corporate personality, in which the company is used by shareholders and/or managers to obtain personal advantages and damage third parties. Abuse is deemed to have occurred solely in cases of misuse of the corporate purpose ("*desvio de finalidade*") and when

there is no segregation between the company's and shareholders' assets ("*confusão patrimonial*").

The Law on Economic Freedom, yet to be enacted, aims at the simplification of business activities, and sets out that shareholders shall only be held liable when they benefit directly or indirectly from the abuse of the corporate personality. This provision protects minority shareholders having no managerial power. The rationale underlying it is the limitation on the use of the lifting of the corporate veil by Courts. Even considering that this provision is not binding upon labor relationships, it may inspire Labor Courts and future labor law reforms.

Some sparse decisions of the Labor Courts seem to be based on similar rationale. In 2018, the Labor Court of Appeals in Rio de Janeiro decided that minority shareholders with no power to manage are not personally liable for labor obligations of the company. This decision supports the idea that shareholders shall be personally liable once they have benefitted from the abuse of the corporate personality. It is still soon to predict, but hopefully similar decisions will become more frequent following the recent legal changes.

Several labor-related laws and regulations have been discussed in Congress, and a new labor reform is also currently being considered. The trend is to provide more flexibility to labor rules, more freedom for employee and employer to establish the terms and conditions of their relationship, aiming at generating less hurdles to companies and more jobs.

The Brazilian labor markets are still entangled in red tape and complexity, as labor judges understand that the risk of the economic activity cannot be shared between employers and employees. However, recent changes in relation to the use of lifting of the corporate veil may be considered a stride towards a more modern and market-oriented interpretation of the law. Some improvement in relation to shareholders' exposure to labor obligations has already been attained and more can be expected.

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