Articles

How Universal Is the Corporate Form? Reflections on the Dwindling of Corporate Attributes in Brazil

MARIANA PARGENDLER*

The business corporation, a central pillar of modern capitalism, is deemed to have a set of defining features that are universal across different jurisdictions and ever more widely available. However, a close examination of legal developments in Brazil, one of the world's largest economies, shows a surprisingly different picture. In the past decades, Brazil has significantly watered down the canonical elements of the corporate form, including limited liability and capital lock-in. After describing this phenomenon, the Article analyzes it in view of efficiency and distributional considerations. It puts forward the possibility that the blurring of the corporate attributes may be an adaptive response to a weak institutional environment, which, among other things, fails to protect minority investors and curb externalities through regulation. The Article concludes by examining how the erosion of the corporate attributes in Brazil subverts our conventional understanding about the evolution of corporate law and the immutability of the corporate form.

* Professor of Law, Fundação Getulio Vargas Law School in São Paulo (FGV Direito SP); Stephen and Barbara Friedman Visiting Professor of Law, Columbia Law School; Global Professor of Law, New York University School of Law. I am grateful to Stephen Bainbridge, Donald Clarke, Martin Gelter, George Georgiev, Zohar Goshen, Henry Hansmann, Klaus Hopt, Yu-Hsin Lin, Curtis Milhaupt, John Morley, Juliana Pela, Bruno Salama, and participants in workshops at Columbia, FGV, and Penn law schools and in the IV Annual Meeting of the Ibero-American Institute for Law and Finance in São Paulo for their very helpful comments. All errors are my own.

INTRODUCTION 2
I. EVOLUTION (OR INVOLUTION) OF CORPORATE ELEMENTS IN BRAZIL 9
A. Legal Personality and Lock-In 9
B. Limited Liability 19
C. Delegated Management Under a Board Structure 30
D. Transferable Shares 34
E. Investor Ownership 37
II. EVALUATING THE DWINDLING OF CORPORATE ATTRIBUTES IN BRAZIL 38
A. Efficiency 39
1. Limited Liability 40
2. Lock-In 45
3. Delegated Management 47
4. Transferable Shares 48
5. Investor Ownership 49
B. Distribution 50
C. The Significance of Decorporatization 51
III. BEYOND BRAZIL 53
IV. CONCLUSION 56

INTRODUCTION

The business corporation is a central institution of modern capitalism. Since its inception several centuries ago, the reported history of the corporate form is one of continued proliferation and diffusion to different contexts, including developing and formerly communist economies. Remarkably, most large-scale business firms adopt the corporate form, which displays the same core characteristics around the world. These are (i) legal personality (including lock-in), (ii) limited liability, (iii) delegated management, (iv) transferable shares, and (v) investor ownership.[1] These characteristics, in turn,

1. These core features are widely recognized in the literature. *See, e.g.*, John Armour, Henry Hansmann, Reinier Kraakman & Mariana Pargendler, *What Is Corporate Law?*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 1 (John Armour et al. eds., 3rd ed. 2017) [hereinafter ANATOMY OF CORPORATE LAW]; Curtis J.

generate three types of agency problems: between managers and shareholders, controlling shareholders and non-controlling shareholders, and shareholders and creditors. Most of corporate law is devoted to mitigating these agency problems.[2]

The booming field of comparative corporate governance has documented significant variation in the contours and effectiveness of the legal mechanisms used in different jurisdictions to alleviate agency problems and protect outside investors.[3] In fact, scholars have suggested that such variation is highly predictive of levels of capital market development and, possibly, economic growth.[4] Other works have posited that the considerable differences in the protection of investors and workers are linked to fundamental aspects of national history, political economy, and economic structure.[5] A recurring theme in the corporate law scholarship of the last few decades is the divergence (and, more recently, partial convergence) in the ownership structures of business corporations around the globe. The traditional view is that only Anglo-Saxon jurisdictions boast significant levels of dispersed ownership, while controlling shareholders remain the norm elsewhere in the world.[6]

These efforts have painted a clear picture: the corporate form itself is universal, but ownership structures and the legal strategies used to protect investors and other constituencies are not. This Arti-

---

Milhaupt, *Chinese Corporate Capitalism in Comparative Context*, *in* THE BEIJING CONSENSUS? 275, 291–93 (Weitseng Chen ed., 2017) (citing these elements as "the universal attributes of the corporate form"); GREGOR BACHMANN ET AL., REGULATING THE CLOSED CORPORATION 25 (2014); ROBERT CHARLES CLARK, CORPORATE LAW 2 (1986).

2. Some countries (most notably Germany) have also deployed corporate law to protect workers, and different countries have increasingly, if controversially, used corporate governance mechanisms to promote a variety of broader external objectives, from reducing systemic risk and inequality to protecting human rights and the environment. *See* Luca Enriques, Henry Hansmann, Reinier Kraakman & Mariana Pargendler, *The Basic Governance Structure: Minority Shareholders and Non-Shareholder Constituencies*, *in* ANATOMY OF CORPORATE LAW, *supra* note 1, at 90–91.

3. *See, e.g.*, Alexander Dyck & Luigi Zingales, *Private Benefits of Control: An International Comparison*, 59 J. FIN. 537, 551 (2004); CORPORATE GOVERNANCE IN CONTEXT (Klaus J. Hopt et al. eds., 2005).

4. *See*, *e.g.*, Rafael La Porta et al., *Law and Finance*, 106 J. POL. ECON. 1113 (1998); Simeon Djankov et al., *The Law and Economics of Self-Dealing*, 88 J. FIN. ECON. 430 (2008).

5. *See*, *e.g.*, MARK J. ROE, Political Determinants of Corporate Governance (2003); Raghuram Rajan & Luigi Zingales, *The Great Reversals: The Politics of Financial Development in the Twentieth Century*, 69 J. FIN. ECON. 5 (2003).

6. Armour, Hansmann, Kraakman & Pargendler, *supra* note 1, at 26.

cle seeks to complicate this understanding. It draws attention to considerable, but largely overlooked, divergences with respect to the scope and strength of the core defining elements of the corporate form in Brazil—the largest emerging economy of the West.[7] This means that, beyond important differences in the content of corporate law and the protection it affords to investors, the existing divide can be more profound.

The Brazilian version of the business corporation (the *sociedade anônima* or S.A.) is, in its current form, not as "corporatized" as conventional understandings suggest. Whereas most analyses view the glass as half full in asserting the universality of the business corporation,[8] here I view the glass as half empty. While the five canonical elements of the business corporation are formally present in the Brazilian S.A., they take on a watered-down form, with potentially important practical implications.

Significantly, Brazilian law has eroded the most fundamental elements of the corporate form—namely, "capital lock-in" (or "entity shielding") and limited liability—with the effect that there is no longer a strong separation between the assets of Brazilian business corporations and their shareholders. Despite the initial absence of statutory authorization, Brazilian courts have granted minority shareholders in closely held corporations the right to withdraw at will by seeking a partial dissolution of the corporation, which is effectively forced to buy back their shares. And through a combination of statutory and case law, Brazil has greatly mitigated, if not eliminated, limited liability in a variety of contexts, ranging from labor and environmental law to consumer protection and the failure of financial institutions.

Beyond the clear deterioration of lock-in and limited liability, the remaining attributes of the corporate form are also weaker in Brazil relative to the international norm. The element of delegated management to a board of directors is frail from a comparative perspective since Brazilian shareholders enjoy an unusual amount of power. Share transferability has also suffered through a combination of specific statutory rules, practical constraints, and the erosion of limited

7. As of 2018, Brazil was the ninth largest economy in the world, following the United States, China, Japan, Germany, the United Kingdom, France, Italy, and India. *GDP (Current US$)*, WORLD BANK: DATA, https://data.worldbank.org/indicator/ny.gdp.mktp.cd?most_recent_value_desc=true&view=map [https://perma.cc/QP5B-JKUP].

8. Focusing on commonalities can also be illuminating. For the examination of Brazilian corporate law from such a perspective, see Armour, Hansmann, Kraakman & Pargendler, *supra* note 1, at 53–57.

liability. Finally, investor ownership is not the only paradigm for corporate enterprise in Brazil, given the prevalence of corporate ownership by the state, which typically pursues public policy objectives beyond financial gain. Although these differences are merely relative[9] and nuanced, taken together they are noteworthy in reflecting a broader effacement of the canonical corporate elements.

My argument about the observed "decorporatization" in Brazil relates to, but differs from, the lines of work seeking to "put the corporation in its place" by emphasizing the historical prevalence of other types of business entities, especially in civil law jurisdictions,[10] or by hailing the broad rise of "uncorporate" forms of organization.[11] Brazil's experience generally supports these claims. As in other countries, by far the most popular form of business organization in Brazil is the limited liability company ("*sociedade limitada*" or "*Ltda.*") which is a special or partial corporate form tailored to closely-held firms.[12]

However, the fundamental point here is different and more profound: even the S.A., which is widely recognized as the functional equivalent of the business corporation, has a lower degree of corporateness than one would assume based on traditional doctrine and foreign experience. In other words, the "glue" of corporate law binding the legal entity is simply not as potent in Brazil.[13] This is especially significant since Brazilian law offers entrepreneurs no legal entity or organizational form other than the S.A. to obtain the key attributes of the business corporation.[14] The aim here is not to demarcate the ontology of the business corporation—identifying when

9. James Q. Whitman, *The Two Western Cultures of Privacy: Dignity Versus Liberty*, 113 YALE L.J. 1151, 1163 (2004) ("[T]he issue is not whether there is an absolute difference. Comparative law is the study of *relative* differences.").

10. *See, e.g.*, Timothy Guinnane et al., *Putting the Corporation in Its Place*, 8 ENTERPRISE & SOC'Y 708 (2007).

11. *See, e.g.*, Joseph A. McCahery et al., *A Primer on the Uncorporation*, 14 EUR. BUS. ORG. L. REV. 305 (2013); LARRY E. RIBSTEIN, THE RISE OF THE UNCORPORATION (2010).

12. With the exception of small enterprises (which cannot be organized as S.A.s to enjoy favorable tax treatment), tax laws are not usually a main consideration in the choice of organizational form in Brazil. The same tax rules generally apply to both S.A.s and *limitadas*, taxing the entity but not its members or shareholders (since dividend distributions are currently exempt from tax).

13. *See* Simon Deakin et al., *Legal Institutionalism: Capitalism and the Constitutive Role of Law*, 45 J. COMP. ECON. 188, 194–97 (2017).

14. Beyond the *limitada* and the S.A.s, the most popular legal entities in Brazil are individual enterprises with limited liability (EIRELI) and cooperatives, but they do not offer most of the corporate attributes.

one ceases to exist, giving rise to a different organizational form—but to show how differences in the strength of the corporate attributes can be far stronger and more consequential than usually appreciated.

After mapping this phenomenon, an immediate question arises: what explains such deviation? Existing theories about differences in commercial laws around the world offer interesting, but ultimately unsatisfactory explanations. For instance, one could attribute the fragility of the core corporate elements in Brazil to the incomplete or failed legal transplantation of the corporate form in the past, which did not take root in unreceptive soil.[15] Alternatively, one could assume that other complementary local conditions have led to deep-rooted forms of path dependence for "uncorporate" forms of organization. Relatedly, the explanation for such disparity could lie entirely in interest group politics.[16]

The "decorporatization" of the Brazilian S.A. defies these assumptions. It is hardly a remnant of the distant past. On the contrary, the weakening of the core elements of the corporate form has taken place in the last few decades and continues to accelerate. The influence of interest groups is not entirely apparent, either. While part of this process has its roots in federal legislation, a significant portion of it is the product of court-driven indigenous developments that largely favor disorganized constituencies. Moreover, contrary to prevailing practice in civil law jurisdictions and emerging markets, the influence of legal scholars and foreign trends on this transformation range from modest to non-existent.

While the political determinants of decorporatization in Brazil remain a puzzle, this Article takes a first step towards evaluating this phenomenon based on efficiency and distributional considerations. This analysis reveals that, quite surprisingly, there is at least a theoretical case that Brazil's watered-down corporate regime is in many respects the most efficient model—not only for Brazil, but everywhere. In this view, Brazil could be seen as a pioneer in implementing, albeit unknowingly, famous proposals by U.S. law and economics scholars. Brazil's experiment with decorporatization also raises new theoretical questions. One promising possibility is that the efficiency of the corporate form is contingent on the quality of the institutional environment. The business corporation famously gives rise to severe agency problems and permits the externalization of costs.

15. *See* Daniel Berkowitz et al., *The Transplant Effect*, 51 AM. J. COMP. L. 163, 167 (2003) (arguing that legal transplants are unlikely to be effective unless they map principles that are already familiar internally or are adapted to the new context).

16. *Id*. at 189.

Policing such agency problems and curbing externalities can be very difficult in practice. In the absence of a sophisticated institutional infrastructure able to restrain such costs, it may be more efficient to mitigate or eliminate the very element of the corporate form that gave rise to the problem in the first place.

For instance, high managerial agency costs, if unaddressed, may lead to less managerial delegation. The lack of protection against minority exploitation through voice or liability may encourage the use of alternative devices, such as strong withdrawal rights. The absence of constraints against opportunism vis-à-vis creditors, or weaknesses in the regulatory system in curbing externalities (such as systemic risk or environmental harm), could favor diluting the protection of limited liability or having the state intervene through other means like holding shares in major firms. In this view, decorporatization is a second-best response to a weak institutional environment.

A different and complementary efficiency account posits that, whatever its origins and causes, the phenomenon of decorporatization is self-reinforcing. The reason is that the different attributes of the corporate form are highly complementary to one another. Once one or some of the elements are gone, there is a stronger case for diluting the other elements. For instance, shareholders' newly found ability to withdraw capital from the firm harms creditors and therefore strengthens the case for unlimited liability for corporate debts. However, the reverse is also true: the application of unlimited liability to minority shareholders helps justify granting minority shareholders meaningful exit rights. The prospect of unlimited liability also creates strong incentives for shareholders to take an active role in firm management, reducing their willingness to delegate power to the board. In turn, the absence of capital lock-in, limited liability, and delegated management weakens private enterprise, thereby encouraging state ownership as an alternative with which to promote long-term investment.

Another view is that decorporatization in Brazil promotes distributional considerations. The weakening of the corporate attributes in Brazil might serve not to increase the size of the pie but to provide a greater slice of it to the parties that are more likely to be economically vulnerable, such as minority shareholders, workers, consumers, and environmental stakeholders.

Law and economics scholarship has traditionally loathed the pursuit of distributional goals through private law. This is because a tax-and-transfer system is, at least in theory, superior in accomplish-

ing distributional outcomes.[17] Yet the incorporation of distributional concerns into private law adjudication has recently encountered renewed favor even among economically oriented scholars in the United States, who increasingly recognize the costs of and political hurdles to an effective tax-and-transfer system.[18]

In Brazil, the incorporation of distributional objectives into corporate law seems particularly fitting. Brazil's activist judiciary has arguably taken up the task of directly implementing the constitutional mandate for a "free, fair, and solidary society"[19] since the country's system of taxation and spending has largely failed to redress exceedingly high levels of inequality. In most respects, decorporatization seems to favor the interests of the parties that are economically weaker, and the impact of this move in tackling inequality remains dubious.

Of course, it is also possible that the undoing of the corporate form in Brazil may end up being deleterious, rather than benign. Through a series of gradual legal developments to accommodate the specificities of the institutional environment, the key economic functions performed by the business corporation appear to be at risk. This form of "institutional band-aids" can have both predictable and unintended consequences for development. It also points to a new set of challenges facing legal evolution in emerging markets.

The remainder of this Article is organized as follows. Part I describes how the core attributes of the corporate form have lost traction in the Brazilian context. Part II explores the potential of alternative normative assessments of this development in Brazil, as well as on its practical implications. Part III speculates on the possible manifestations of this phenomenon beyond Brazil. Part IV concludes by reflecting on the lessons for comparative scholarship and organizational theory.

17. *See, e.g.*, Louis Kaplow & Steven Shavell, *Why the Legal System Is Less Efficient Than the Income Tax in Redistributing Income,* 23 J. LEGAL STUD. 667 (1994). *But see* Chris Sanchirico, *Taxes Versus Legal Rules as Instruments for Equity: A More Equitable View*, 29 J. LEGAL STUD. 797, 806 (2000) (arguing that legal rules should be used for purposes of redistribution even in the presence of an optimal tax system because marginal deviations from the efficient rule do not affect total utility).

18. *See* Lee Anne Fennell & Richard H. McAdams, *The Distributive Deficit in Law and Economics*, 100 MINN. L. REV. 1051 (2016); Zachary D. Liscow, *Reducing Inequality on the Cheap: When Legal Rule Design Should Incorporate Equity as Well as Efficiency*, 123 YALE L.J. 2478, 2481 (2014).

19. CONSTITUIÇÃO FEDERAL [C.F.] [CONSTITUTION] art. 3º, I (Braz.).

I. EVOLUTION (OR INVOLUTION) OF CORPORATE ELEMENTS IN BRAZIL

A. Legal Personality and Lock-In

Legal personality is the first and most basic attribute of the corporate form. At a fundamental level, it indicates the corporation's ability to hold assets, enter into contracts, and sue and be sued in its own name. There is no question that the Brazilian S.A., as well as most company and partnership forms (*sociedades*), have legal personality under Brazil's Civil Code,[20] which provides for the formal separation between the assets of the corporation and those of its shareholders.

In the last few decades, however, scholars have noted that the separation between the assets of the firm and its owners allow for different gradations. As first highlighted by Henry Hansmann and Reinier Kraakman, the degree of separation afforded by the corporation is strong: neither shareholders nor personal creditors of shareholders can withdraw corporate assets unless a majority of shareholders decides to liquidate the firm, in which case corporate creditors will be paid first.[21] This feature stands in contrast to the weak form of separation provided by the partnership, which has traditionally permitted partners and personal creditors of partners to force a dissolution of the firm unilaterally.[22]

Corporate shareholders and their creditors generally have no claim over the corporation's assets. Once a shareholder makes her investment, either by subscribing to newly issued shares or by purchasing existing shares in the secondary market, her economic claims vis-à-vis the firm are limited. Absent fundamental changes to the corporation's structure which permit the exercise of appraisal rights, a shareholder is only entitled to: (i) a proportionate share of dividend distributions, conditioned upon both the existence of profits *and* the corporation's decision to distribute dividends; and (ii) a proportionate share of the residual if the firm is liquidated, provided there is anything left after creditors are paid in full.

This limitation on capital withdrawals by shareholders has been a longstanding feature of the corporate form, dating back to at

20. CÓDIGO CIVIL [C.C.] [CIVIL CODE] arts. 44, 1.088–9 (Braz.).

21. Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 YALE L.J. 387, 394, 434–45 (2000); Henry Hansmann et al., *Law and the Rise of the Firm*, 119 HARV. L. REV. 1333, 1341 (2006).

22. Hansmann & Kraakman, *supra* note 21, at 394.

least the Dutch East India Company of the seventeenth century. Nevertheless, this trait has only recently attracted the dedicated attention of legal scholars and economists. For convenience, I will use the term "lock-in"[23] to refer to the notion that, save for fundamental changes warranting statutory appraisal rights, corporate shareholders and their creditors have no claim over the firm's assets unless a majority of shareholders decides to put an end to the corporation's existence through formal liquidation proceedings.

There are several reasons for the growing recognition that lock-in performs a central economic function for the success of the corporate form, which some scholars believe is equal to, or more fundamental than, limited liability.[24] First, lock-in ensures that the financial condition or preferences of individual shareholders will not affect the operation of the firm, whose assets will remain intact irrespective of shareholders' liquidity needs and obligations to creditors.[25] This eliminates the need for inter-shareholder monitoring, making lock-in highly complementary to other features of the corporate form, such as delegated management and transferable shares.[26]

Second, lock-in promotes the continuity and integrity of the corporate form over time, thereby encouraging firm-specific investments by different participants in the enterprise.[27] It protects going-concern value and strengthens the pool of assets available to corporate creditors, which enhances the corporation's creditworthiness and reduces its cost of capital. Third, lock-in avoids hold-up problems by minority shareholders when there is a predominance of match assets—that is, assets that are worth more to insiders jointly than to outsiders separately.[28]

Finally, while private contracting may suffice to produce other features of the corporate form—such as limited liability—lock-in necessarily requires law.[29] Obtaining lock-in vis-à-vis creditors

23. Margaret M. Blair, *Locking In Capital: What Corporate Law Achieved for Business Organizers in the Nineteenth Century*, 51 UCLA L. REV. 387, 394 (2003); Lynn Stout, *On the Nature of Corporations*, 2005 U. ILL. L. REV. 253, 254 (2005).

24. Hansmann & Kraakman, *supra* note 21, at 423–28; Stout, *supra* note 23, at 256.

25. Hansmann & Kraakman, *supra* note 21, at 402.

26. *Id.* at 424.

27. Blair, *supra* note 23, at 392.

28. Edward B. Rock & Michael Wachter, *Waiting for the Omelet to Set: Match-Specific Assets and Minority Oppression in Close Corporations*, 24 J. CORP. L. 913, 915 (1999).

29. Hansmann & Kraakman, *supra* note 21, at 407–12.

would require shareholders to negotiate individual subordination agreements with each of their personal creditors—a proposition fraught with moral hazard concerns and transaction costs.[30] The provision of lock-in among owners is less daunting, but still legally uncertain. In Brazil, as elsewhere, it is unclear that the owners' agreement not to partition property would be effective in view of the law's strong stance toward permitting tenants in common to partition joint property.[31]

The essential role of law in creating or recognizing lock-in is critical. Once Brazilian courts eliminate this legal attribute, it is doubtful that parties will be able to obtain the same result through private contracting. For instance, an attempt to write a shareholder agreement providing for lock-in faces two obstacles: (i) it does not bind creditors of shareholders, which are third parties vis-à-vis the contract; and (ii) it cannot last for an unlimited or even long period of time, given the public policy against perpetual contracts.[32] Moreover, courts have at times applied the same rationale used to grant withdrawal rights—breach of *affectio societatis*, as discussed below—to allow disgruntled shareholders to walk away from shareholder agreements.[33]

Nevertheless, lock-in entails costs as well as benefits. While the recognition of the economic benefits of lock-in is relatively recent, scholars and practitioners have long taken notice of its drawbacks.[34] By denying shareholders a claim on the corporation's assets, lock-in increases agency costs and facilitates the expropriation of minority investors. Economic historians have argued that the tradeoff between agency costs and untimely dissolution drove the choice between the partnership and the corporation in early U.S. corporate history, when legal minority protections were weak.[35] The

30. *Id.* at 408.

31. *Id.* at 411–12. While partnerships have long prevented partner withdrawals during a defined term, these agreements lack the legal force provided by the corporate form.

32. In civil law jurisdictions, courts may qualify an agreement for a very long term as amounting to an indefinite term, thus permitting unilateral termination at will.

33. *See, e.g.*, SUPERIOR TRIBUNAL DE JUSTIÇA [S.T.J.] [SUPERIOR COURT OF JUSTICE], Recurso Especial No. 388.423-RS, Relator: Min. Sálvio de Figueiredo Teixeira, 13.05.2003, DIÁRIO DA JUSTIÇA [D.J.] [JUSTICE GAZETTE], 04.08.2003 (Braz.).

34. *See, e.g.*, *infra* note 37 and accompanying text.

35. Naomi R. Lamoreaux & Jean-Laurent Rosenthal, *Corporate Governance and the Plight of Minority Shareholders in the United States before the Great Depression*, *in* CORRUPTION AND REFORM: LESSONS FROM AMERICA'S ECONOMIC HISTORY 125 (Edward L. Glaeser & Claudia Goldin eds., 2006).

persistent popularity of the partnership following the advent of general corporation laws in the nineteenth century suggests that investors and entrepreneurs were willing to tolerate unlimited liability, and the risk of untimely dissolution, to avoid the prospect of abuse by controlling shareholders that followed from lock-in.[36]

The agency costs between controlling and non-controlling shareholders are far greater in the close corporation context, where reduced regulation and the absence of a market for the corporation's shares leaves minority shareholders in a particularly fragile position. At least since the 1950s, various U.S. scholars have proposed the award of dissolution rights to minority shareholders in closely-held corporations *in analogy* to the rights enjoyed by members of a partnership.[37]

Since then, state legislatures and courts in the U.S. have been increasingly willing to force the corporation or controlling shareholders to buy back the minority as a remedy in cases of minority oppression.[38] Yet these decisions still require a showing of abuse and fall short of granting minority shareholders a put option against the corporation. Indeed, most U.S. scholars continue to believe that the risk of exploitation of minority shareholders in close corporations does not warrant the elimination of lock-in.[39] A prominent comparative study on the law of closed corporations in Europe has likewise concluded that "shareholders do not have the possibility of easily leaving the closed corporations and 'cashing in their shares.'"[40] The existing withdrawal rights in countries such as Germany and Switzerland still require a showing of cause, and attempts to introduce an unconditional statutory exit have failed.[41]

Curiously, just as lock-in was gaining popularity in international scholarship, Brazilian law made great strides to abolish it.[42]

---

36. *Id.* at 148.

37. Carlos L. Israels, *The Sacred Cow of Corporate Existence: Problems of Deadlock and Dissolution*, 19 U. CHI. L. REV. 778, 789–90 (1952); A.C. Hetherington & Michael P. Dooley, *Illiquidity and Exploitation: A Proposed Statutory Solution to the Remaining Close Corporation Problem*, 63 VA. L. REV. 1, 3 (1977).

38. For a description of statutory and case law on the subject, see Robert B. Thompson, *The Shareholder's Cause of Action for Oppression*, 48 BUS. LAW. 699 (1993).

39. *See, e.g.*, FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 238–43 (1991); Rock & Wachter, *supra* note 28, at 920.

40. BACHMANN ET AL., *supra* note 1, at 7.

41. *Id.* at 66.

42. The earliest precedent acceding to a partial dissolution of an S.A. dates back to 1982. TRIBUNAL DE JUSTIÇA DO ESTADO DE MINAS GERAIS [T.J.M.G.] [COURT OF JUSTICE OF

For the first time, minority shareholders came to enjoy the right to force a partial dissolution at will. In practice, this requires the company to buy back their shares without offering any countervailing mechanism to protect corporate creditors—who then effectively lose their priority over the corporation's assets to withdrawing shareholders. The recent elimination of lock-in represents a significant departure from Brazil's legal tradition, which had recognized lock-in as an essential element of the corporate form since the first business corporations of the nineteenth century.

Brazil's current corporations law of 1976 (*Lei das Sociedades por Ações* or LSA) permits voluntary dissolution by a majority shareholder vote or involuntary judicial dissolution when an action is brought by shareholders representing at least five percent of the company's capital and there is proof that the corporation cannot fulfill its purpose.[43] In fact, Brazil's corporate statute appears to be nominally *more* protective of lock-in than the law of other jurisdictions. It qualifies the "liquidation of a prosperous corporation" as an "abuse of control power" that gives rise to controlling shareholder liability—an unusual provision from a comparative standpoint.[44]

Short of the full liquidation of the firm, withdrawal rights only apply to shareholders dissenting from fundamental decisions involving the corporation. Such shareholder "appraisal rights" are available under the LSA in cases of mergers, spin-offs, changes to the mandatory dividend, creation of new types of preferred shares or modification of their rights, participation in a corporate group, change of corporate purpose, and, more recently, the adoption of an arbitration clause.[45] However, numerous exceptions apply to limit the availability of appraisal rights in these situations, such as the need to show lack of liquidity and dispersion in the event of a merger.[46]

THE STATE OF MINAS GERAIS], Ap. Civ. No. 58.092, Relator: Des. Danilo Furtado, 17.11.1982, 286, REVISTA FORENSE [R.F.] [FORENSIC MAGAZINE], 1984, 281 (Braz.). Throughout the 1990s, however, most courts continued to deny requests for partial dissolution, which only became generally accepted in the late 2000s.

43. Lei No. 6.404, de 15 de Dezembro de 1976, DIÁRIO OFICIAL DA UNIÃO [D.O.U.] [OFFICIAL GAZETTE OF THE UNION] de 17.12.1976, art. 206 (Braz.) [hereinafter LSA]. Other statutory bases for dissolution include the expiration of the company's term, cases provided in the charter, the existence of a single shareholder, the end of legal authorization to operate (if required), the annulment of the act of incorporation, and the decision of an administrative authority (as provided by special statutes).

44. *Id.* art. 117, § 1º(b). For a comparative perspective, see Edward Rock et al., *Fundamental Changes*, *in* ANATOMY OF CORPORATE LAW, *supra* note 1, at 171, 202.

45. LSA, *supra* note 43, arts. 136-A, 137.

46. *Id.* art. 137, II–III.

To understand the doctrinal routes that courts have used to allow partial dissolutions of close corporations, one must first examine the evolution of the law of limited liability companies (*sociedades limitadas* or Ltdas.) in Brazil. The *limitada* was first introduced in Brazilian law in 1919, in what was allegedly a transplant of Portuguese law and an indirect transplant of German law on the *Gesellschaft mit beschränkter Haftung* (GmbH) of 1892. The Brazilian *limitada* offered both legal personality and limited liability, but imposed fewer formalities than the business corporation. As in other civil law jurisdictions, the *limitada* soon became the most popular form of organization for commercial enterprise in Brazil.[47]

Brazil's first statute on *limitadas* was silent on lock-in but provided that, whenever the articles of association were silent, the corporations law would apply to *limitadas* as appropriate.[48] One could have naturally interpreted this rule as requiring the application of the corporate law regime—including lock-in—to *limitadas*. The foreign-law counterparts to the Brazilian *limitada*—such as the Italian S.r.l., the French Sarl, and the German GmbH—have always enjoyed lock-in by generally banning withdrawals without cause. Brazilian scholars and courts, however, predominantly embraced a different interpretation, holding that the general provisions of the Commercial Code applicable to partnerships also governed *limitadas* whenever the statute was silent.[49] These provisions included the traditional rule of partnership law permitting any partner to withdraw at will and prompt the dissolution of the firm.[50]

Evidently, the extension of the partnership regime to *limitadas* triggered the problem of untimely dissolution since any mem-

47. Guinnane et al., *supra* note 10 (describing the predominance of private limited liability companies similar to the Brazilian *limitada* over business corporations in France and Germany). For contemporary data on the ample use of *limitadas* in Brazil, see Mariana Pargendler, *Direito Societário em Ação: Análise Empírica e Proposições de Reforma*, 59 REVISTA DE DIREITO BANCÁRIO E DO MERCADO DE CAPITAIS 215 (2013).

48. Decreto No. 3.708, de 10 de Janeiro de 1919, D.O.U. de 15.1.1919, art. 18 (Braz.).

49. *See*, *e.g.*, ALFREDO RUSSEL, CURSO DE DIREITO COMMERCIAL BRASILEIRO 369 (1923) (arguing that *limitadas* are subject to the same dissolution provisions as partnerships); WALDEMAR FERREIRA, SOCIEDADES POR QUOTAS 908 (5th ed. 1958). *But see* MAURO RODRIGUES PENTEADO, DISSOLUÇÃO E LIQUIDAÇÃO DE SOCIEDADES 126–28 (2d ed. 2000) (arguing that the corporate regime should apply to limitadas); EGBERTO LACERDA TEIXEIRA, DAS SOCIEDADES POR QUOTAS DE RESPONSABILIDADE LIMITADA 126–28 (1956) (arguing that partnership or corporate provisions of the Commercial Code should apply depending on the "capitalist" or "personalist" character of the company).

50. CÓDIGO COMERCIAL [C.COM.] [COMMERCIAL CODE] art. 335 (repealed 2002) (Braz.).

ber's decision to withdraw, or involuntary events such as death or bankruptcy of the member, would put an end to the firm's existence. Despite the clear language of the Commercial Code calling for the company's dissolution, Brazilian courts bent this rule. Starting in the 1940s, courts began granting only partial dissolution in these cases, reasoning that the rule providing for full dissolution was a default rule that was waived by the parties.[51] Decades later, courts began to justify their decisions in favor of partial dissolution on the basis of preserving the enterprise and its social function, irrespective of any contractual terms and without any form of protection for creditors' rights.[52] Existing case law on *limitadas* has not only recognized the ability of members to withdraw at any time as a default rule but has also thwarted the parties' ability to obtain lock-in through private contracting.[53] Nevertheless, entrepreneurs seeking lock-in of capital could still obtain it by incorporating the firm as an S.A.

For close corporations, however, this avenue has been compromised within the last decade.[54] While the first precedents on this subject date back to the 1980s and 1990s,[55] it was in the middle and late 2000s that Brazilian law effectively abandoned lock-in as an attribute of close corporations. Two key *en banc* decisions by the private law chambers of the Brazilian Superior Court of Justice (*Superi-*

51. Courts reasoned that, whenever the articles of association provided for the continuity of the company in case of death or withdrawal (as they usually did), these clauses operated as a waiver of the right to claim full dissolution, and instead led to a partial dissolution of the firm. *See* SUPREMO TRIBUNAL FEDERAL [S.T.F.] [SUPREME FEDERAL COURT], Recurso Extraordinário No. 9.929, Relator: Min. Flamínio de Rezende, 04.01.1946, REVISTA DOS TRIBUNAIS [R.T.] [REVIEW OF THE COURTS] 166/843 (Braz.).

52. For a leading case on this matter, see S.T.F., Recurso Extraordinário No. 89464, Relator: Min. Cordeiro Guerra, 12.12.1978, SUPREMO TRIBUNAL FEDERAL JURISPRUDÊNCIA [S.T.F.J.] [SUPREME FEDERAL COURT JURISPRUDENCE], 04.05.1979 (Braz.).

53. For a discussion and critique of this approach, see ANDRÉ LUIZ CARDOSO SANTOS, APURAÇÃO DE HAVERES NA SOCIEDADE LIMITADA: UMA ANÁLISE CRÍTICA DA JURISPRUDÊNCIA (2015).

54. I am aware of only one lawsuit involving a request for partial dissolution of a publicly-traded company. The Court of Appeals of the State of Rio Grande do Sul granted the request for partial dissolution in the case, arguing that the firm's shares lacked liquidity, which made it akin to a closed corporation. TRIBUNAL DE JUSTIÇA DO ESTADO DE RIO GRANDE DO SUL [T.J.R.S.] [COURT OF JUSTICE OF THE STATE OF RIO GRANDE DO SUL], Ap. Civ. No. 70071296446, Relator: Des. Luís Augusto Coelho Braga, 29.06.2017, D.J., 12.07.2017 (Braz.). Some commentators have long advocated this possibility, by analogizing the listed company whose shares are not liquid to the *limitada*. *See, e.g.*, MAURO RODRIGUES PENTEADO, *supra* note 49, at 190.

55. *See supra* note 42 and accompanying text.

or Tribunal de Justiça or STJ)[56] settled this new legal controversy, including among its own chambers.

In 2006, the court's first *en banc* decision concerned a request for judicial dissolution of COCELPA, a pulp and paper corporation.[57] This lawsuit was filed in 1991 by the estates of two minority shareholders against the company and the remaining shareholders, including the equity arm of the Brazilian National Development Bank. Pointing to irregularities in the company's management, the lack of profits, and the longstanding absence of dividend distributions, the plaintiffs argued that the company could not fulfill its purpose under Art. 206, II, *b* of the LSA, and therefore ought to be fully dissolved. Alternatively, the plaintiffs requested the partial dissolution of the corporation.

The Court's decision focused not so much on the absence of dividend distributions but on another element of the claim—the breach of *affectio societatis*, a Roman law concept denoting the willingness to take part in a joint enterprise.[58] The opinion noted that, in Brazil, numerous close corporations have familial ties and are formed *intuitu personae*, which means that the identity of the shareholders is key to corporate success.[59] In these companies, the breach of *affectio,* which is understood as the "affinity and personal identification among shareholders, marked by mutual confidence," prevented the corporation from fulfilling its purpose under the LSA.[60]

The Court unknowingly embraced reasoning that mirrored the arguments made by U.S. scholars decades earlier, holding that such a business corporation was, in essence, a "*sociedade limitada* in disguise."[61] Nevertheless, the Court found that "the rule of full dissolution, in these cases, would not assist the social values involved, with

56. The constitutional mission of the STJ is to guarantee the uniform interpretation of federal legislation in Brazil. C.F. art. 104.

57. S.T.J., Embargos de Divergência em Recurso Especial No. 111.294–PR, Relator: Min. Castro Filho, 28.06.2006, D.J., 10.09.2007 (Braz.).

58. *Affectio societatis* is a concept that arguably dates back to Roman law, a legal system that lacked a corporate form. For a critique of the use of this concept by Brazilian courts, see Erasmo Valladão Azevedo e Novaes França & Marcelo Vieira von Adamek, *Affectio Societatis: Um Conceito Jurídico Superado No Moderno Direito Societário Pelo Conceito De Fim Social*, *in* DIREITO SOCIETÁRIO CONTEMPORÂNEO 131, 132, 140 (QUARTIER LATIN, 2009).

59. S.T.J., Embargos de Divergência em Recurso Especial No. 111.294–PR, *supra* note 57, at 14.

60. *Id.*

61. *Id.*

respect to the preservation of jobs, collection of taxes, and the country's economic development."[62] As a result, it granted the request for partial dissolution as "the solution that best reconciles the individual interest of the withdrawing shareholders with the principle of preservation of enterprise and its social utility."[63]

In 2008, the STJ issued its second *en banc* decision on the topic in the case of Luiz Kirchner S/A Indústria de Borrachas.[64] The Court effectively expanded its prior holding in the COCELPA case by clarifying the applicability of partial dissolutions for breach of *affectio societatis* without the need to allege economic abuse or the absence of dividend distributions. As in that prior precedent, the plaintiff in this lawsuit was also the estate of a former shareholder. The Court read the COCELPA decision as considering "the preponderance in small and medium corporations of the existence of *affectio societatis*, without which the presumed belligerent climate among the shareholders militates against the preservation of the enterprise, becoming an obstacle to its corporate purpose, which will not be fulfilled."[65]

Prior to reaching the STJ, the Court of Appeals of the State of São Paulo (TJSP) had decided this case in a split decision that highlighted the arguments for both sides. The majority, which granted the request for partial dissolution, relied heavily on the constitutional protection of freedom of association, which provided that no one may be compelled to associate or to remain associated.[66] The dissenting opinion, by contrast, emphasized that the company in question began as a *limitada* and later converted to a corporation, when it received non-family shareholders, to protect the firm from disputes among heirs. The dissent concluded by denying the request for partial dissolution because the company was lucrative and was fulfilling its purpose, "which is not to maintain harmony among the descendants of the founder."[67]

Since these landmark decisions, the absence of lock-in in close corporations is widely accepted by courts. Brazil's Code of

62. *Id.* at 15.

63. *Id.* at 16.

64. S.T.J., Embargos de Divergência em Recurso Especial No. 419.174–SP, 28.05.2008, Relator: Min. Aldir Passarinho, D.J., 04.08.2008 (Braz.).

65. *Id.* at 6.

66. C.F. art. 5º.

67. TRIBUNAL DE JUSTIÇA DE SÃO PAULO [T.J.S.P.] [COURT OF JUSTICE OF SÃO PAULO], Ap. Civ. No. 003.299-4/0, Relator: Des. Mohamed Amaro, 19.02.1998 (Braz.).

Civil Procedure of 2015 explicitly alludes to the partial dissolution of close corporations that cannot fulfill their purpose.[68] This provision, as well as the case law which inspired it, creates an awkward doctrinal construction in which a corporation that is deemed not to fulfill its purpose is still allowed to exist due to the partial nature of the dissolution.

Beyond the now common claims for partial dissolution by minority shareholders, Brazilian courts have weakened lock-in in another way: by granting requests for expulsion of shareholders that are harming the company's operations. Unlike dissolution, claims for expulsion are subject to more exacting standards in that the remaining shareholders must show wrongdoing by the shareholder they want to expel. As the STJ put it, "expulsion is an extreme measure in view of the efficiency of the enterprise's activities, for which it becomes necessary to expunge the shareholder that brings about harm or the possibility of grave harm to the firm, being indispensable the existence of proof of just cause."[69] However, at least one decision by the STJ has blurred the distinction between partial dissolution and expulsion by asserting that there is "no ontological difference" between both categories, thereby permitting the shareholder majority to request the withdrawal of minority shareholders due to breach of *affectio societatis*.[70]

Requests for expulsion and partial dissolution have the same consequence: the termination of shareholder status and the withdrawal of a proportionate share of the corporation's assets. The draconian remedy of expulsion is also available in other jurisdictions, but only in exceptional circumstances.[71]

In their embrace of partial dissolution and expulsion, Brazilian courts have increasingly come to rely on exit as a substitute for liability. Considerations of institutional competence and capacity likely play a role in this shift. Assessing the existence of wrongdoing and the amount of damages can be more burdensome for the courts than simply granting exit rights and leaving the question of valuation

68. Lei No. 13.105, de 16 de Março de 2015, D.O.U. de 17.03.2015, art. 599, § 2º (Braz.).

69. *See, e.g.*, S.T.J., Recurso Especial No. 917.531-RS, Relator: Min. Luis Felipe Salomão, 17.11.2011, D.J., 01.02.2012 (Braz.).

70. S.T.J., Recurso Especial No. 1.128.431-SP, Relator: Min. Nancy Andrighi, 11.10.2011, D.J., 25.10.2011 (Braz.). By permitting majority shareholders to freeze out the minority at any time, this case aggravates, rather than mitigates, the problem of minority expropriation.

71. *See* BACHMANN ET AL., *supra* note 1, at 73–74.

to a battle of the experts. The mitigation of lock-in is also instrumental to the implementation of other public policies seeking to ensure that heirs and spouses receive their fair share of assets in the event of death or divorce.

The elimination of lock-in has caused surprisingly little scholarly uproar despite its radical break with both Brazil's legal tradition and comparative experience. To be sure, various scholars continue to disavow the possibility of partial dissolution of business corporations.[72] The vast majority of commentators, however, has come to approve of partial dissolutions with considerable enthusiasm, either unconditionally or with relatively modest qualifications, such as the need to prove the breach of *affectio societatis*.[73]

B. Limited Liability

Limited liability is the second and certainly most celebrated attribute of the corporate form.[74] Limited liability, or what Hansmann, Kraakman and Squire call, "owner shielding," is the reverse of "entity shielding."[75] It ensures that the personal creditors of shareholders will have exclusive access to shareholders' assets, while the corporate creditors have exclusive access to the corporation's assets. Despite the traditional centrality of limited liability to the business corporation and its assumed importance to the modern capitalist economy, Brazilian law has greatly reduced its scope.

The benefits of limited liability are well-known and manifold. It greatly relieves shareholders from the burden of monitoring managers and other shareholders, which encourages transferability and diversification. Because of limited liability, the pricing of corporate shares does not depend on the creditworthiness of owners, which fa-

72. *See, e.g.*, NELSON EIZIRIK, A LEI DAS S/A COMENTADA 157–62 (2011).

73. *See, e.g.*, MODESTO CARVALHOSA, COMENTÁRIOS À LEI DE SOCIEDADES ANÔNIMAS 44–45 (5th ed. 2011).

74. For a recent vigorous defense of limited liability, see STEPHEN M. BAINBRIDGE & M. TODD HENDERSON, LIMITED LIABILITY: A LEGAL AND ECONOMIC ANALYSIS 2 (2016) (describing limited liability as "[t]he key feature of the corporation that makes it such an attractive form of human cooperation and collaboration"). *See also* EASTERBROOK & FISCHEL, *supra* note 39, at 40 ("Limited liability is a distinguishing feature of corporate law—perhaps *the* distinguishing feature"); David Leebron, *Limited Liability, Tort Victims, and Creditors*, 91 COLUM. L. REV. 1565, 1566 (1991) ("No principle seems more established in capitalist law or more essential to the functioning of the modern economy [than the principle of limited liability].").

75. Hansmann et al., *supra* note 21, at 1339.

cilitates transferability and the operation of the market for corporate control. Limited liability also generally decreases the costs of investing in business corporations and therefore promotes such investments.[76] The recognized importance of limited liability to the corporate form is such that the apparent expansion of the U.S. doctrine of "piercing the corporate veil" in the late twentieth century raised provocative warnings against the "killing of the corporation."[77]

Although widespread today, limited liability was not a constant feature of early business corporations.[78] For instance, California did not offer limited liability until 1931,[79] and U.S. banks imposed "double liability" on shareholders during the period between the Civil War and the Great Depression.[80] In contrast, Brazil was an early adopter of limited liability generally—including for financial institutions—since the very first business corporations of the nineteenth century. The royal charter establishing the first Bank of Brazil in 1808 specifically mentioned limited liability of shareholders and so did subsequent special charters for other banks.[81]

For most of its corporate history, Brazil lacked any doctrine of veil piercing whatsoever beyond the limited imposition of enterprise liability in the labor law context.[82] It was not until 1969 that Brazilian scholar Rubens Requião published the first work on the topic, which denounced how the "absolutism" of legal personality permitted its use for fraudulent purposes. Requião then advocated the application in Brazil of the so-called "disregard doctrine" of the

76. For broad overviews of the benefits of limited liability, see BAINBRIDGE & HENDERSON, *supra* note 74; Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89, 111 (1985); THE ANATOMY OF CORPORATE LAW, *supra* note 1.

77. Stephen B. Presser, *Thwarting the Killing of the Corporation: Limited Liability, Democracy, and Economics*, 87 NW. U. L. REV. 148 (1992).

78. MORTON J. HORWITZ, THE TRANSFORMATION OF AMERICAN LAW, 1870–1960, at 94 (1992) ("[T]ruly limited shareholder liability was far from the norm in America even as late as 1900.").

79. Mark I. Weinstein, *Share Price Changes and the Arrival of Limited Liability in California*, 32 J. LEGAL STUD 1, 1–2 (2013).

80. Jonathan R. Macey & Geoffrey P. Miller, *Double Liability of Bank Shareholders: History and Implications*, 27 WAKE FOREST L. REV. 31, 31 (1992). Double liability differs from unlimited liability in that shareholders are only liable up to the par value of their stock. *Id.*

81. *See, e.g.*, Decreto No. 888, de 22 de Dezembro de 1851, art. 10 (Banco da Província de Pernambuco); Decreto No. 4.390, de 15 de Julho de 1869, art. 30 (Banco Commercial do Maranhão).

82. *See infra* notes 91–93 and accompanying text.

common law to curb such abuses.[83] This article was highly influential in Brazilian courts, which began applying the doctrine despite the absence of legislative authorization. Nonetheless, the embrace of veil piercing was fairly circumscribed, leading to convergence, rather than divergence, vis-à-vis the international norm.

However, recent developments accelerating since the 1990s have significantly eroded the protection of limited liability in Brazil—so much so that, in 2014, Brazilian scholar Bruno Salama declared "the end of limited liability" in the country.[84] This is not to deny that the application of veil-piercing doctrine in other countries, and especially in the United States, can seem highly litigated,[85] messy,[86] controversial and even alarming.[87] Yet, as we shall see below, there is an important difference of degree with respect to the willingness of legislators and courts to do away with limited liability in Brazil. Scholars have claimed that veil piercing "occurs with more frequency in the United States than anywhere else in the world,"[88] but it is actually far more prevalent in Brazil. While U.S. scholars have found around 9,000 to 11,000 cases of veil piercing in U.S. electronic databases,[89] recent searches for the term in the websites of

83. Rubens Requião, *Abuso de Direito e Fraude através de Personalidade Jurídica (Disregard Doctrine)*, 410 REVISTA DOS TRIBUNAIS 13 (1969).

84. BRUNO MEYERHOF SALAMA, O FIM DA RESPONSABILIDADE LIMITADA (2014).

85. Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036, 1036 (1991) ("Piercing the corporate veil is the most litigated issue in corporate law."). *But see* Peter Oh, *Veil Piercing*, 89 TEX. L. REV. 81, 90 (2010) ("Veil-piercing is misdubbed the most litigated issue in corporate law."). While veil-piercing cases are numerous, claims regarding the liability of directors and officers and dissolutions appear to be more common. *Id.* at 90–91.

86. Christina L. Boyd & David A. Hoffman, *Disputing Limited Liability*, 104 NW. U. L. REV. 853, 904 (2010) (finding that extralegal influences play an important role in veil piercing cases); Jonathan Macey & Joshua Mitts, *Finding Order in the Morass: The Three Real Justifications for Piercing the Corporate Veil*, 100 CORNELL L. REV. 99, 103 (2014) (describing the apparently incoherent stance of U.S. courts in applying the traditional doctrinal grounds for veil piercing and proposing an alternative taxonomy).

87. Stephen M. Bainbridge, *Abolishing Veil Piercing*, 26 J. CORP. L. 479, 481 (2001); Presser, *supra* note 77.

88. Robert B. Thompson, *Piercing the Veil: Is the Common Law the Problem?*, 37 CONN. L. REV. 619, 619 (2005). Scholars have since shown that the rate of veil piercing is greater in China than in the United States. Hui Huang, *Piercing the Corporate Veil China: Where Is It Now and Where Is It Heading?*, 60 AM. J. COMP. L. 743, 774 (2012) (finding that Chinese courts pierced the veil in sixty-three percent of the ninety-nine cases adjudicate since the 2005 statute, "a rate significantly higher than in the United States, the United Kingdom and Australia").

89. Macey & Mitts, *supra* note 86, at 141; Oh, *supra* note 85, at 100.

the Court of Appeals in the State of São Paulo (TJSP) and in the Regional Labor Court for the Second Region (Tribunal Regional do Trabalho da Segunda Região) alone unearthed over 42,000 and 18,000 judicial opinions addressing this topic, respectively.[90]

The first restriction to limited liability dates back to Brazil's Labor Law of 1943 (*Consolidação das Leis do Trabalho* or CLT).[91] The statute, which is still in force in modified form,[92] provided a version of enterprise liability: whenever one or more firms are under the control of another, constituting an industrial or commercial group, the parent and the subsidiaries will be jointly and severally liable for labor obligations. This meant that, for labor purposes, asset boundaries were eliminated within the group but not outside of it.[93]

This labor law rule initially did not impinge on the protection of limited liability enjoyed by individual controlling or minority shareholders. However, despite the narrow and clear statutory language, labor courts in the 1970s and 1980s began holding individual shareholders (including, at times, minority shareholders) liable for the company's labor obligations. This position has become dominant in the last few decades.[94] While the imposition of shareholder liability for labor debts is not unheard of from a comparative perspective,[95] veil piercing in labor claims assumes special significance in Brazil due to its doctrinal breadth and the extraordinarily high volume of litigation in labor courts, in which employers bear the burden of proof and workers often prevail.[96]

Arguably the first statutory encroachment into limited liability of individual shareholders took place in 1987.[97] By law, financial

90. This is according to a search conducted in November 2017 using the single search expression "desconsideração da personalidade jurídica" (disregard of legal entity) to avoid duplicative findings. This is likely to underestimate the number of decisions, especially because not all decisions are published on the courts' website.

91. Decreto No. 5.452, de 1 de Maio de 1943, D.O.U. de 09.08.1943 (Braz.).

92. *See infra* notes 134–139 and accompanying text.

93. As discussed below, the conventional view is that the elimination of asset partitioning within a corporate group is far less controversial than outside of it. *See infra* note 192 and accompanying text.

94. SALAMA, *supra* note 84, at 156.

95. *See* N.Y. BUS. CORP. LAW § 630 (LexisNexis 2019) (imposing joint and several liability for labor debts on the ten largest shareholders of close corporations).

96. *See Employer, Beware*, ECONOMIST, Mar. 10, 2011 ("In 2009, 2.1m Brazilians opened cases against their employers in the labour courts. These courts rarely side with employers.").

97. Decreto-Lei No. 2.321, de 25 de Fevereiro de 1987, D.O.U. de 26.02.1987, art. 15

institutions in Brazil must necessarily adopt the corporate form.[98] The statute provides that when financial institutions are subject to Central Bank intervention due to insolvency or wrongdoing, controlling shareholders are jointly and severally liable with managers for any outstanding debts. The statute explicitly provides that such liability accrues irrespective of negligence or willful misconduct.[99] This rule extended to controlling shareholders and strengthened the already strict rule applicable to managers since 1974. According to the 1974 statute, the directors and officers of financial institutions are jointly and severally liable for the obligations assumed during their tenure, and their personal assets become inalienable when the institution is subject to intervention or insolvency proceedings.[100] A 1997 statute extended the liability of controlling shareholders to other cases of intervention and liquidation.[101]

A fair reading of the law is that neither managers nor controlling shareholders of financial institutions enjoy limited liability.[102] As a prominent Brazilian economist and former governor of the Central Bank described it, in Brazil, "there is no 'principle of limited liability' in the financial system."[103] The accounting fraud that led to the near failure of Banco PanAmericano, whose controlling shareholder was TV host and tycoon Silvio Santos, serves as a useful illustration. Even though Silvio Santos was not in any way involved in the management of the bank, he ended up providing shares in 34 firms as collateral for a loan from Brazil's Deposit Insurance Fund (*Fundo Garantidor de Crédito* or FGC) to save the institution. This prevented the bank from undergoing formal liquidation or intervention by the Central Bank, which would have resulted in his personal

(Braz.).

98. Lei No. 4.595, de 31 de Dezembro de 1964, D.O.U. de 31.12.1964, art. 25 (Braz.).

99. Decreto-Lei No. 2.321, de 25 de Fevereiro de 1987, D.O.U. de 26.02.1987, art. 15 (Braz.). Both the Central Bank and the judiciary have traditionally interpreted the statute as imposing strict liability for the bank's obligations. However, recent judicial decisions have held that the imposition of liability on managers is fault-based but subject to a rebuttable presumption of fault. *See* Luiz Carlos Sturzenegger, *Apontamentos Sobre Responsabilidade Civil de Controladores e Administradores de Instituições Financeiras*, 52 REVISTA DE DIREITO BANCÁRIO E MERCADO DE CAPITAIS 199 (2011).

100. Lei No. 6.024, de 13 de Março de 1974, D.O.U. de 14.03.1974, arts. 36, 40 (Braz.).

101. Lei No. 9.447, de 14 de Março de 1997, D.O.U. de 15.03.1997 (Braz.).

102. Gustavo H.B. Franco & Luiz Alberto C. Rosman, *A Responsabilidade Ilimitada em Instituições Financeiras no Brasil*, *in* A REFORMA DO SISTEMA FINANCEIRO AMERICANO (2009).

103. GUSTAVO H.B. FRANCO, AS LEIS SECRETAS DA ECONOMIA 88 (2012).

liability.[104] Despite the stricture of this regime, all Brazilian banks have controlling shareholders.

Another significant statutory exception to limited liability comes from the Consumer Protection Code of 1990. The relevant provision is the fifth and last paragraph of Art. 28 of the statute, which states that a judge may also disregard the legal entity "whenever its personality is, in any way, an obstacle to the compensation of harm caused to consumers."[105] This rule was not present in the bill drafted by prominent Brazilian scholars and consumer advocates. Instead, it was included in the legislative process as an amendment proposed by two House representatives of right-wing (PFL) and center-left (PTB) parties.[106] Curiously, the enactment of this provision may have been inadvertent. The scholars involved in drafting the bill have argued that this extreme provision was supposed to have received a presidential veto but did not due to a typographical error.

This rule generated significant doctrinal controversy, with most scholars defending a purposive interpretation according to which Paragraph 5 did not permit veil piercing in the absence of fraud or abuse.[107] Nevertheless, courts embraced a literal reading of the statute. The leading case on this issue involved a tragic explosion in a shopping mall, which killed or injured numerous bystanders.[108] In a split opinion, the STJ decided to disregard the entity of the shopping mall, a *limitada*, as well as its holding corporation, to hold their managers liable.[109] Since then, numerous decisions have pierced the corporate veil to reach the assets of shareholders and managers.[110]

This interpretation has spanned far beyond the consumer context. First, labor courts increasingly applied the consumer protection legislation by analogy to pierce the corporate veil liberally for the benefit of workers.[111] Second, subsequent statutes closely repro-

104. *Nothing to See Here: The Central Bank Claims Credit for a Banking Bail-Out in Brazil*, ECONOMIST, Nov. 20, 2010, at 88.

105. Lei No. 8.078, de 11 de Setembro de 1990, D.O.U. de 12.09.1990 (Braz.).

106. DIÁRIO DO CONGRESSO NACIONAL, 27.06.1990, at 7932 (Braz.).

107. *See* ADA PELLEGRINI GRINOVER ET AL., CÓDIGO DE DEFESA DO CONSUMIDOR: COMENTADO PELOS AUTORES DO ANTEPROJETO 237 (8th ed., 2005).

108. *Id.* at 239.

109. S.T.J., Recurso Especial No. 279.273-SP, Relator: Min. Ari Pargendler, Relator p/: Acórdão Min. Nancy Andrighi, 02.12.2003, D.J., 03.03.2004 (Braz.).

110. *See*, *e.g.*, S.T.J., Agravo Regimental no Recurso Especial No. 1.106.072-MS, Relator: Min. Marco Buzzi, 02.09.2014, D.J., 18.09.2014 (Braz.).

111. SALAMA, *supra* note 84.

duced the language of the consumer protection code. Brazil's 1998 law on criminal and administrative sanctions for environmental violations provided for the disregard of legal entity "whenever legal personality is an obstacle for the compensation of harm caused to the quality of the environment."[112]

When it comes to corporate groups, the LSA explicitly provides that each entity belonging to a group of companies retains separate legal personality and patrimony.[113] However, various recent statutes have also weakened the separation of assets among firms belonging to the same corporate group. For example, a 1991 statute imposes joint and several liability on firms belonging to the same "economic group" with respect to unpaid social security contributions.[114] Joint and several liability within the economic group also applies in the tax context if the relevant firms participated in the taxable activity and/or have an interest in it.[115] Brazil's competition law of 2011 does the same, imposing joint and several liability on companies belonging to the same economic group and providing for veil piercing in cases of insolvency or bankruptcy caused by "poor corporate administration."[116] Similarly, the recent Anticorruption Law of 2013 provides that "the companies controlling, controlled by or affiliated with, or tied by a consortium contract within the scope of the contract, are jointly and severally liable for the practice of the acts described in the statute, this liability being limited to the obligation of payment of the fine and the full compensation of the damages caused."[117] Although such liability does not reach individual controlling shareholders, it is expansive in explicitly encompassing "affiliated companies" (*sociedades coligadas*), defined as companies that are under "significant influence" of another which however falls short of control.[118]

Courts have also disregarded the legal personality of group

112. Lei No. 9.605, de 12 de Fevereiro de 1998, D.O.U. de 13.02.1998, art. 4º (Braz.).

113. LSA, *supra* note 43, art. 266. This is irrespective of the standards governing related-party transactions within formal or de facto groups.

114. Lei No. 8.212, de 24 de Julho de 1991, D.O.U. de 25.7.1991, art. 30, IX (Braz.).

115. Lei No. 5.172, de 25 de Outubro de 1966, D.O.U. de 27.10.1966, art. 124, I (Braz.); *see also*, *e.g.*, S.T.J., Recurso Especial No. 859.616-RS, Relator: Min. Luiz Fux, 18.09.2007, D.J., 15.10.2007 (Braz.).

116. Lei No. 12.529, de 30 de Novembro de 2011, D.O.U. de 01.12.2011, arts. 33, 34 (Braz.).

117. Lei. No. 12.846, de 1 de Agosto de 2013, D.O.U. de 02.08.2013, art. 4º, § 2º (Braz.).

118. LSA, *supra* note 43, art. 243, § 1º.

companies quite liberally, even in the absence of special statutory regimes. An empirical study found that, between 2005 and 2010, the court of appeals for the state of São Paulo decided 214 cases involving veil piercing in economic groups that did not involve any special statute.[119] Of these, the court disregarded corporate boundaries in 134 cases, or nearly two-thirds of the total.[120]

Bankruptcy law is another field that has increasingly overcome limited liability and, more broadly, the very notion of legal personality. It has disregarded the internal boundaries of corporate groups and combined the entities into a single pool of assets and group of creditors. Like veil piercing, this mechanism, which is known under U.S. law as "substantive consolidation," is not unique to Brazil. The difference again lies in the Brazilian courts' greater willingness to use it.[121]

In other areas, such as tax law, higher courts have adopted a relatively restrictive stance toward veil piercing, imposing liability only on managers and controlling shareholders that have committed unlawful acts beyond the non-payment of taxes.[122] Nevertheless, the "law in action" paints a different picture. Tax authorities often issue tax bills against shareholders and managers, who then face the major burden of depositing the amounts charged before they can challenge these bills in court. This practice, combined with government-friendly interpretations by lower courts and the fact that the payment of taxes extinguishes possible criminal penalties under Brazilian law, arguably leads to a system of "judicial blackmailing" against shareholders and managers.[123]

For the most part, the judiciary has not only endorsed, but expanded, the statutory grounds for shareholder liability. Labor courts, in particular, have routinely pierced the corporate veil to reach the assets of shareholders (including, on several occasions, minority shareholders) of close corporations based on a logic of "deep pockets"—or, in its doctrinal formulation, the unwritten "principle of non-

119. Anna Beatriz Alves Margoni, *A Desconsideração da Personalidade Jurídica nos Grupos de Sociedades* 10, 150 (Universidade de São Paulo Faculdade de Direito, 2011).

120. *Id.* at 153.

121. The judicial restructuring of Rede Energia is illustrative of this more liberal approach toward substantive consolidation in Brazil compared to that of U.S. courts. *See In re* Rede Energia S.A., 515 B.R. 69 (Bankr. S.D.N.Y. 2014).

122. *See*, *e.g.*, S.T.J., Recurso Especial No. 1.141.977-SC, Relator: Min. Benedito Gonçalves, 21.10.2010, D.J., 04.10.2010 (Braz.).

123. The expression comes from SALAMA, *supra* note 84, at 185.

imputation of the risks of the enterprise to the employee."[124] Strikingly, the liability imposed on managers and shareholders is joint and several, not *pro rata*.[125] Virtually all such cases involve close corporations so the applicability of veil piercing to public companies remains largely untested. There is one precedent from the Superior Court of Labor (*Tribunal Superior do Trabalho* or TST) which permitted veil piercing in a publicly-traded company to reach the assets of a shareholder who had been an officer prior to the employee's hiring.[126]

The proliferation of exceptions does not eradicate the protection of limited liability in its entirety. In private transactions outside of the labor and consumer settings, limited liability is generally upheld.[127] Veil piercing in this case is subject to the more rigorous prerequisites set forth in Article 50 of the *Civil Code*, which require "deviation of corporate purpose" or "commingling of assets." In contrast to their stance in other areas, courts have been reluctant to pierce the corporate veil in civil and commercial contexts, to the point of imposing conditions that go beyond those prescribed by the Code. For instance, an *en banc* decision by the STJ has held that veil piercing is inapplicable in the absence of fraud or willful misconduct even when no such requirement can be found in the statutory text.[128]

Moreover, an important precedent by Brazil's Supreme Court (*Supremo Tribunal Federal* or STF) took the bold view that statutory encroachment into limited liability may run afoul of the Constitution. The Court's decision concerned a 1993 federal statute that made members of *limitadas* jointly and severally liable for the firms' un-

124. TRIBUNAL SUPERIOR DO TRABALHO [T.S.T.] [SUPERIOR LABOR COURT], Agravo de Instrumento em Recurso de Revista No. 1365.56, Relator: Min. Lelio Bentes Corrêa, 21.08.2013, TRIBUNAL SUPERIOR DO TRABALHO JURISPRUDÊNCIA [T.S.T.J.] [SUPERIOR LABOR COURT JURISPRUDENCE], 21.08.2013 (Braz.). Some decisions, however, restrict the imposition of liability to controlling shareholders. *See*, *e.g.*, T.S.T., Agravo de Instrumento em Recurso de Revista No. 119600.07, Relator: Min. José Roberto Freire Pimenta, 22.04.2015, T.S.T.J., 23.04.2015 (Braz.).

125. On the benefits of pro rata over joint and several liability, see Henry Hansmann & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879, 1892–1924 (1991).

126. T.S.T., Agravo de Instrumento em Recurso de Revista No. 3262200-18, Relator: Des. José Maria Quadros de Alencar, 27.11.2013, T.S.T.J., 17.12.2013 (Braz.).

127. SALAMA, *supra* note 84, at 211 (noting that, unlike other areas, unlimited liability in civil and commercial matters is "quite restrained").

128. S.T.J., Embargos de Divergência em Recurso Especial No. 306.553-SC, Relator: Min. Maria Isabel Gallotti, 10.12.2014, D.J., 12.12.2014 (Braz.).

paid social security obligations.[129] The unanimous opinion held the provision unconstitutional since it was unreasonable and unduly restrictive of private enterprise and violated the constitutional right to freedom of trade, occupation and profession, and the free exercise of economic activity.[130]

Overall, however, the sweeping application of veil piercing in Brazil contradicts conventional wisdom that political obstacles to imposing unlimited liability on shareholders are insurmountable.[131] Interestingly, this dramatic erosion of limited liability has occurred in a context where existing elites have been quite effective in opposing reform efforts to increase investor protection.[132]

While the business community and legal scholars have repeatedly criticized the expansive and unprincipled application of unlimited liability by the Brazilian judiciary, the main attempts at reform have thus far been quite narrow in scope. Brazil's new Code of Civil Procedure of 2015 created procedural safeguards for the application of veil piercing due to concerns over due process and following lobbying efforts by business associations. The statute now explicitly conditions veil piercing on either: (i) the inclusion of such a request in a legal complaint and the naming of shareholders or managers as defendants; or (ii) on the petition by a party or the Public Prosecutor's Office (*Ministério Público*) to open an incidental procedure to that effect at any time during the judicial proceeding.[133] This unusual provision is a reaction to previous judicial practice: courts would simply redirect the execution of the amounts due against shareholders or managers, without their previous participation as defendants in the lawsuit, in an apparent violation of due process.

Brazil broadly overhauled its labor legislation in 2017, incorporating several provisions aimed at reining in the wild use of veil piercing by labor courts.[134] The reform is considered drastic and highly controversial since it took place under a president who came into office following the impeachment of his predecessor and who re-

129. Lei No. 8.620, de 5 de Janeiro de 1993, D.O.U. de 6.106.01.1993, art. 13 (Braz.).

130. S.T.F., Recurso Extraordinário No. 562.276-PR, Relator: Min. Ellen Gracie, 03.11.2010, D.J. , 10.02.2011 (Braz.).

131. Peter Conti-Brown, *Elective Shareholder Liability*, 64 STAN. L. REV. 409, 460 (2012).

132. Ronald J. Gilson, Henry Hansmann & Mariana Pargendler, *Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the United States, and the European Union*, 63 STAN. L. REV. 475, 482–86 (2013).

133. Lei No. 13.105, de 16 Março de 2015, D.O.U. de 17.03.2015, arts. 133–37 (Braz.).

134. Lei No. 13.467, de 13 de Julho de 2017, D.O.U. de 14.07.2017 (Braz.).

lied on the support of the business community rather than popular support.[135] Although important, the new restrictions to veil piercing in this otherwise ambitious reform effort are modest and surprisingly sanction the imposition of shareholder liability for labor debts. The amended law explicitly contemplates a clear priority for the satisfaction of labor debts, with the employing firm coming first, followed by current shareholders, and only then by former shareholders. The latter may now only be held liable for claims filed within two years of the transfer of shares in the absence of fraud.[136] Similarly, only the successor corporation in a corporate reorganization may be held liable for labor obligations in the absence of fraud.[137] The reform restricts the imposition of joint and several liability on member firms of an economic group to cases in which they have shared interests and act in a coordinated manner, making clear that the mere identity of common shareholders no longer suffices.[138] It also explicitly provides that the new procedural safeguards for veil piercing created by the new Code of Civil Procedure of 2015 also apply to labor claims.[139]

The new "Law on Economic Freedom" (*Lei da Liberdade Econômica*) of 2019—which seeks to promote the liberalization of private law and business regulation in Brazil—is similarly shy in its treatment of veil piercing.[140] The new sole paragraph of Article 49-A strikingly offers a normative justification for asset partitioning, stating "the patrimonial autonomy of legal persons is a lawful instrument for the allocation and segregation of risks, established by law with the aim of promoting enterprise, for the creation of jobs, taxes, income and innovation for the benefit of all."[141] In addition, the law specifies and limits the scope of Article 50 of the *Civil Code*, which provided the standards for veil piercing in civil and commercial transactions, and the interpretation of which was already quite restrictive.[142] The new Article 50 explicitly states that veil piercing may

135. For a description and evaluation of the reform, see *Bye-Bye, Benito*, ECONOMIST, July 20, 2017, at 59.

136. Lei No. 13.467, de 13 de Julho de 2017, D.O.U. de 14.07.2017, art. 10 (Braz.).

137. *Id.* art. 448-A.

138. *Id*. art. 2º, § 2º. Until the reform, labor courts used to impose joint and several liability on companies that had a common shareholder, even if not controlling—a regime that was especially troublesome for the private equity and venture capital industries.

139. *Id.* art. 855-A.

140. Lei No. 13.874, de 20 de Setembro de 2019, D.O.U. de 20.09.2019 (Braz.).

141. *Id.* art. 7º.

142. The new statute clarifies that (i) deviation of purpose requires fraud with the

only reach the assets and shareholders who benefited directly or indirectly from the abuse and that the mere existence of an economic group in the absence of abuse and commingling of assets does not authorize veil piercing.[143] The reform, however, leaves untouched the areas of law (such as labor, consumer, and environmental law) where veil piercing is truly rampant.

C. Delegated Management Under a Board Structure

The third core attribute of the corporate form is the existence of delegated management under a board structure. On a basic level, this element is also present under Brazilian corporate law. Shareholders are not agents of the firm and cannot bind it in contract. This is a prerogative of corporate officers (*diretores*)—duly elected by shareholders or by the board of directors—or agents of corporate officers acting within the scope of their power of attorney.[144]

Various aspects of Brazilian corporate law and practice, however, greatly mitigate the strength of delegated management. First, Brazilian publicly-traded corporations often have highly concentrated ownership in the hands of a single controlling shareholder or group of shareholders. Although the level of ownership concentration has decreased in Brazil in the last decade, dispersed ownership remains exceedingly rare. In general, the presence of controlling shareholders tends to reduce managerial delegation—since managers and shareholders are more likely to coincide—and Brazil is no exception. Concentrated ownership is the prevailing ownership structure around the world and is particularly pervasive in emerging markets.[145]

Further divergences appear by looking at the balance of power between shareholders and managers envisioned by Brazil's corporate law. There is well-established variation among different jurisdictions in this area, with European jurisdictions generally conferring far greater rights on shareholders than board-centric U.S. law.[146] The

purpose of harming creditors or undertaking unlawful acts of any kind and (ii) commingling of assets means the absence of actual separation of assets. *Id.*

143. *Id.* art. 7º, main body & § 5º.

144. LSA, *supra* note 43, art. 144. For a description of the board structures available under Brazilian law and their applicability, see *infra* note 162 and accompanying text.

145. *See*, *e.g.*, Mariana Pargendler, *Corporate Governance in Emerging Markets*, *in* OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2017) [hereinafter OXFORD HANDBOOK].

146. Sofie Cools, *The Real Difference in Corporate Law Between the United States and Continental Europe: Distribution of Powers*, 30 DEL. J. CORP. L. 697, 765–66 (2005).

difference here is one of degree, with Brazilian corporate law being even more shareholder-centric than these already shareholder-friendly jurisdictions.

As a starting point, the LSA permits shareholders to adjudicate the majority of corporate decisions beyond the very few matters that fall within the exclusive powers of the board.[147] Art. 121 provides that "[t]he shareholder assembly, called and installed in according to the law and the charter, has powers to decide *all matters relating to the purpose of the company and make the resolutions that it deems convenient for its defense and development*."[148] This shareholder power is broad, in particular because the statute grants five percent shareholders the right to call a meeting at any time whenever the board refuses to do so at their request.[149]

The LSA is unusual not only in determining what shareholders *may* decide, but also what they *must* decide. As in other legal systems, Brazilian law requires shareholders to approve certain key corporate decisions. While Brazil follows other jurisdictions in imposing a shareholder vote with respect to charter amendments, mergers, and dissolution, it goes beyond international practice by also demanding shareholder approval of bankruptcy filings, as well as bond issuances by close corporations.[150] In cases of urgency, managers must still obtain the informal consent of the controlling shareholder to file for bankruptcy, and a shareholder meeting must follow to ratify the decision.[151] While "say on pay" has only recently spread around the world (and, even so, it is non-binding in most instances), Brazilian law has since 1976 required shareholders to approve the total amount of executive compensation packages.[152]

Unlike the United States, but like other jurisdictions, Brazilian law requires shareholder approval of dividend distributions.[153] Moreover, like a few French civil-law jurisdictions (though not France), Brazilian law imposes mandatory dividends,[154] which it sets

147. *See infra* note 157 and accompanying text.

148. LSA, *supra* note 43, art. 121 (emphasis added).

149. *Id.* art. 123, c–d.

150. *Id.* art. 122. A 2011 amendment to the statute now permits the board of directors of publicly-traded companies to authorize bond issuances.

151. *Id*. art. 122 (sole paragraph).

152. *Id*. art. 152.

153. *Id*. art. 132, II.

154. La Porta et al., *supra* note 4, at 1132.

at the default rate of twenty-five percent of net profits.[155] This goes against the prevailing international understanding that "[d]irectors have legal discretion to decide whether or not a dividend should be declared" and that "[s]hareholders do not have the legal right to demand dividends."[156]

Compared to these broad shareholder powers, the board of directors has a correspondingly discreet role under Brazilian corporate law. According to the LSA, the necessary functions of the board of directors are to: (i) determine the general orientation of the company's business, (ii) elect officers and monitor their performance, (iii) call the shareholders' meeting (though, as noted, five percent of shareholders may also call meetings if the board refuses to do so), (iv) appoint and remove the independent auditors, if applicable, and (iv) authorize the sale of non-circulating assets and the provision of guarantees.[157] Although this list may seem long, key corporate decisions are conspicuously absent. The statute does not technically require the board's authorization or opinion with respect to fundamental changes such as mergers, acquisitions, dissolutions, or charter amendments. These changes instead can be initiated and must be approved by shareholders. Except for charter amendments—which typically require board initiative in the United States but not in other countries—these fundamental decisions usually necessitate board action in most jurisdictions.[158]

One of the most controversial mechanisms of the Brazilian system of corporate governance is the power afforded to shareholder agreements. Contrary to international norms, and to the dismay of corporate governance advocates, Brazilian law permits shareholder agreements to bind directors' votes. Since a 2001 amendment to the LSA, votes cast in violation of a duly filed agreement are not even counted in shareholder and board meetings.[159] Conversely, if shareholders or directors bound by the agreement are absent from a meeting, the other party may cast a vote on their behalf.[160] Admittedly, the LSA expressly provides that a shareholder agreement cannot

155. LSA, *supra* note 43, art. 202.

156. Lynn Stout et al., *The Modern Corporation Statement on Company Law* 2 (Oct. 2016), https://ssrn.com/abstract=2848833 [https://perma.cc/2TJL-MBU3].

157. LSA, *supra* note 43, art. 142.

158. Edward Rock et al., *Fundamental Changes*, *in* ANATOMY OF CORPORATE LAW, *supra* note 1.

159. LSA, *supra* note 43, art. 118, § 8º.

160. *Id.* art. 118, § 9º.

override the fiduciary duties of controlling shareholders.[161] Nevertheless, shareholder agreements remain largely self-enforcing, with the effect that aggrieved shareholders seeking to challenge decisions mandated by such agreements face an uphill battle.

All of this suggests that the management of Brazilian corporations, including publicly-traded corporations, is not that delegated. An additional distinction applies to the qualification of delegated management "*under a board structure*." The discussion so far has alluded to a board of directors (*conselho de administração*), which is mandatory for publicly-traded corporations, mixed enterprises controlled by the state, and companies subject to the regime of authorized capital under the LSA.[162] Prior to this statute, the concept of a board of directors did not exist under Brazilian law, with the previous statute of 1946 providing that all corporations would have one or more officers and a "board of supervisors" (*conselho fiscal*) elected by shareholders to monitor the company's accounts.[163]

Even today, however, closely-held corporations do not require a board of directors but only a "board of officers" (*diretoria*). Translating *diretoria* as a board, however, is somewhat of a misnomer. Even though the LSA provides that *diretoria* must have at least two officers and contemplates meetings of *diretoria* as determined by the charter, the law does not require officers to make collegial decisions, as they can bind the company by acting unilaterally according to the powers conferred on them by the charter. The statutory framework in Brazil thus assigns a modest role to the board of directors when it exists and dispenses with a board structure altogether in other contexts.

Brazil has not been immune to the international sway of corporate governance best practices, which focus heavily on strong and independent board decision-making. Brazil's securities regulators increasingly rely on independent committees to address conflicts of interest.[164] Nevertheless, the rise of board centrality is often illusory, either because shareholders are present or represented on the board, or because shareholder agreements have previously determined the board's votes. This is not to deny the existence of delegated management in Brazil. The difference is subtler and one of degree, but

161. *Id.* art. 118, § 2º.

162. *Id.* art. 138, § 2º, art. 239.

163. Decreto No. 2.627, de 16 de Setembro de 1940, D.O.U. de 01.10.1940, arts. 116, 124 (Braz.).

164. *See*, *e.g.*, Parecer de Orientação, Comissão de Valores Mobiliários [CVM] No. 35 (2008).

turns out to be critical in assessing the degree of "corporateness" enjoyed by the organization.

D. Transferable Shares

The fourth element of the corporate form is transferable shares. Compared to other core attributes of the business corporation, the mitigation of this element under Brazilian law is less evident and more nuanced. It is not so much that Brazilian law unusually restricts the transferability of shares, though certain limitations apply. Instead, the most important limitations to transferability are side effects from the legal rules governing control transfers and the depletion of limited liability.

Similarly to other jurisdictions, the general rule under Brazilian law is that close corporations may impose restrictions on the transferability of shares by charter provision, "provided that these limitations do not prevent their tradability nor subject the shareholder to the discretion of management bodies or the shareholder majority."[165] Restrictions on the transferability of shares imposed by subsequent charter amendment do not bind non-consenting shareholders.[166] These aspects of Brazilian law are not surprising since the imposition of restrictions on share transfers in close corporations is prevalent in other international contexts.[167]

If the legal restrictions on share transferability look relatively modest, the practical restrictions can be significant. In Brazil, as elsewhere, there is usually no liquid market, or no market at all, for minority shares in close corporations. Brazil also has a particularly large number of formally listed companies whose shares are seldom traded and lack liquidity, thereby reducing the practical benefits of free transferability.

Another obstacle to transferability in public companies comes from the mandatory bid rule imposed by law (known in Brazil as "tag-along rights") and from Brazilian-style "poison pills," which are more stringent mandatory bid rules adopted by charter provision.[168]

The mandatory bid rule requires the party acquiring control to

165. LSA, *supra* note 43, art. 36.

166. *Id.* (sole paragraph).

167. Armour, Hasnmann, Kraakman & Pargendler, *supra* note 1, at 10.

168. These "poison pills" are typically triggered at the acquisition of a lower threshold of shares (e.g., fifteen to thirty percent) and often require the payment of a significant premium over the market price of shares in a given period.

offer to buy out the remaining shares. According to the LSA, the mandatory bid rule applies only to common shares and requires the payment of at least eighty percent of the price paid to controlling shareholders.[169] The premium stock exchange listing standards, such as Novo Mercado and Level 2, exceed the statutory minimum to impose the payment of the same price received by controlling shareholders to all minority shareholders. However, the mandatory bid rule famously discourages both efficient and inefficient control transfers.[170]

This deterrent effect, however, is likely greater in Brazil. According to an influential study by Dyck and Zingales, Brazil had the highest level of private benefits of control among their sample of thirty-nine countries during the 1990s.[171] High private benefits of control mean that controlling shares are disproportionately more valuable than minority shares. By allowing minority shareholders to sell their shares at the same or similar price paid to controlling shareholders—which presumably far exceeds what their minority shares are worth—the mandatory bid rule makes it inordinately expensive to acquire control of Brazilian public companies.

Mixed enterprises, in which the government holds a majority stake (*sociedades de economia mista*), face even greater legal restrictions on transferability. These entities are created by law to promote public policy and profit-making objectives and play a major role in Brazilian capital markets. However, the government may not dispose of its controlling stake in these entities in the absence of statutory authorization. In fact, courts have held that even the partial transfer of certain decision or veto rights to private shareholders by means of a shareholder agreement run afoul of the government's authority.[172]

Perhaps the strongest limitation on transferability under Brazilian law stems from the disincentives to share transfers posed by other features of the legal regime. The mitigation of limited liability plays an important role here. There are numerous decisions by labor

169. LSA, *supra* note 43, art. 254-A.

170. *See, e.g.*, Lucian A. Bebchuk, *Efficient and Inefficient Sales of Corporate Control*, 1994 Q.J. ECON. 957.

171. Dyck & Zingales, *supra* note 3, at 538 (analyzing the control premium paid in sales of control transactions, and estimating private benefits of control that ranged from positive sixty-five percent in Brazil to negative four percent in Japan).

172. *See* T.J.M.G., Ap. Civ. No. 1.0000.00.199781-6/000(1), Relator: Des. Garcia Leão, 07.08.2001, DIÁRIO DE TRIBUNAL DE JUSTIÇA DO ESTADO DE MINAS GERAIS [D.J.M.G.] [COURT OF JUSTICE OF THE STATE OF OF MINAS GERAIS GAZETTE], 07.09.2001 (Braz.).

courts holding former shareholders liable for corporate obligations to workers.[173] Various precedents limit the extent of liability to controlling shareholders, and to former shareholders who have withdrawn from the firm within two years, as dictated by the Civil Code rule governing partnerships.[174] However, at least one decision confirmed by the Superior Court of Labor held that holding voting shares, even if non-controlling, disqualified a former shareholder as a "mere investor" and resulted in his continued liability for labor obligations irrespective of the two-year time limit.[175]

Outside of the labor sphere, other potential liabilities of former shareholders can also hamper mergers and acquisitions. For instance, business groups have paused before selling subsidiaries that have long-term contracts with consumers out of fear that they would remain exposed to future liabilities. Most courts have ruled that there is no statute of limitations for veil piercing to reach the assets of former shareholders.[176]

The continued liability of selling shareholders, even if limited to a two-year period and based solely on acts that occurred prior to the sale, can discourage share transfers. In the employment context, for instance, workers typically do not sue until they leave the firm due to layoffs or their own volition. Because the corporation's conduct post-sale can affect both resignations and dismissals leading to the liability of former shareholders, a sale of corporate control poses a moral hazard problem. Controlling shareholders may therefore prefer to keep control over firm operations to reduce their risk of future liability. While the parties can conceive contractual solutions to address these problems (for instance, including indemnities and post-closing covenants in the share purchase agreement), these mechanisms are unlikely to be bulletproof and may be difficult to en-

173. *See*, *e.g.*, T.S.T., Agravo de Instrumento em Recurso de Revista No. 17200-66.2000, Relator: Min. Márcio Eurico Vitral Amaro, 15.04.2015, T.S.T.J., 15.04.2015 (Braz.).

174. *Id.*; *see also* C.C. art. 1.003 (sole paragraph) ("For up to two years after the registration of the change to the agreement, the transferring partner is jointly and severally liable together with the transferee, to the partnership and third-parties, for the obligations it had as partner"). *See, e.g.*, T.S.T., Agravo de Instrumento em Recurso de Revista No. 7300-66, Relator: Min. João Oreste Dalazen, 13.08.2014, T.S.T.J., 14.08.2014 (Braz.).

175. T.S.T., Agravo de Instrumento em Recurso de Revista No. 1365-56, Relator: Min. Lelio Bentes Corrêa, 21.08.2013, T.S.T.J., 21.08.2013 (Braz.).

176. For an example of this more rigorous approach, see S.T.J., Recurso Especial No. 1.180.714–RJ, Quarta Turma. Relator: Min. Luís Felipe Salomão. 05.04.2011, DIÁRIO DO JUDICIÁRIO ELETRÔNICO [D.J.e.] [ELECTRONIC JUSTICE GAZETTE], 06.05.2011 (Braz.). In this case, however, there was evidence of fraud.

force.[177]

All of this suggests that the legal restrictions and practical hurdles to share transferability in Brazil are greater than one would expect based on international experience. The next section turns to the last element of the corporate form—investor ownership—which is also weaker in the Brazilian context.

E. Investor Ownership

Investor ownership means that the corporation's shareholders are primarily interested in a financial return on their investment and that corporate laws operate with the interests of investors in mind. Investor ownership, however, is far from the only paradigm for business corporations in Brazil. State ownership, both directly and through state-owned institutional investors, remains pervasive in the country. State-owned enterprises (SOEs) and state-controlled institutional investors (such as Brazil's National development bank and public pension funds) are major players in Brazilian capital markets.[178]

The state, of course, is not a typical investor. As a controlling shareholder in a mixed enterprise, the state does not—and, as some constitutional and administrative lawyers would argue, cannot—run the firm simply to maximize profit.[179] If state intervention is warranted in the first place, then profit maximization is likely to be inappropriate. Moreover, even in contexts where profit maximization may be appropriate, as in the case of state-controlled pension funds or, less forcefully, investments by the development bank, political interference in view of other objectives is often present.

The actual behavior of SOEs or shadow SOEs confirms the suspicion that the state does not act as a typical investor. In 2011, for instance, state-owned institutional investors catered to pressure from then President Lula to dismiss the CEO of Vale, which then had a stellar financial performance, due to concerns about excessive firings

177. On the challenges to contract enforcement in Brazil, see notes 209–210 and accompanying text.

178. Mariana Pargendler, *Governing State Capitalism: The Case of Brazil*, *in* REGULATING THE VISIBLE HAND 386 (Benjamin H. Liebman & Curtis J. Milhaupt eds., 2015).

179. *See, e.g.*, Mario Engler Pinto Jr., *A Atuação Empresarial do Estado e o Papel da Empresa Estatal*, *in* 151/152 REVISTA DE DIREITO MERCANTIL: INDUSTRIAL, ECONÔMICO E FINANCEIRO 256, 263 (2009).

of workers and underinvestment in the country.[180] More recently, Petrobras has endured serious losses due to oil price controls imposed by the government to curb inflation, which led the company to purchase oil at the higher international price and sell it at the lower controlled price—a far cry from what a rational investor would do.[181]

The presence of the state as an important controlling and minority shareholder has shaped Brazilian law in important ways. The state has used its political influence to increase its power as a shareholder and to decrease minority investor protections.[182] It has also pushed corporations law in directions that are less tailored to the interests of outside investors. For instance, the LSA provides that controlling shareholders breach their fiduciary duties when they direct the company to pursue a goal that is foreign to its purpose or harmful to the "national economy."[183] It is difficult to see how this provision has the interests of investors in mind. Moreover, the LSA also provides that managers shall discharge their duties in view of the company's purpose but with due regard to the "requirements of public good and of the social function of enterprise."[184]

II. Evaluating the Dwindling of Corporate Attributes in Brazil

What, then, to make of the dwindling of corporate attributes in Brazil? Is such a deviation from the international norm a damaging distortion, as is conventionally assumed with respect to developing countries, or could it be a fruitful adaptation to local peculiarities? Or could Brazil be leading in the adoption of a superior regime from an efficiency or distributional perspective? The analysis that follows takes but a first step in considering different arguments about the efficiency and distributional properties of the trend towards decorporatization in Brazil. However, it does not—indeed cannot—take a firm stance on the consequences and merits of this new model, which undoubtedly requires further research.

180. Pargendler, *supra* note 178.

181. *See* Curtis J. Milhaupt & Mariana Pargendler, *Governance Challenges of Listed State-Owned Enterprises Around the World: National Experiences and a Framework for Reform*, 50 CORNELL INT'L L.J. 473 (2017).

182. For an expanded version of this argument, see Mariana Pargendler, *State Ownership and Corporate Governance*, 80 FORDHAM L. REV. 2917 (2012).

183. LSA, *supra* note 43, art. 117, § 1º(a).

184. *Id*. art. 154.

A. Efficiency

At first blush, examining the efficiency case for the weakening of corporate attributes in Brazil seems like a strange endeavor. There is a large and robust literature highlighting the importance of the corporate form and the efficiency of its core elements.[185] The spread of the business corporation over time and around the globe offers further evidence of its functionality. One intuitive conclusion would be that the observed decorporatization in Brazil is not the product of efficiency considerations but of something else.

Instead of dismissing the efficiency account outright, however, I will explore it more fully. There are at least three variations of the efficiency claim. The first version posits that the best response to some of the agency problems and externalities produced by the corporate form is to mitigate the strength of its core elements. This is an argument of general applicability and does not depend on the characteristics of the Brazilian environment. By contrast, the other two variations of the efficiency account are, in essence, second-best arguments.

The second version of the efficiency argument is based on the notion of institutional complementarities.[186] It postulates that the core elements of the corporate form will only work satisfactorily in the presence of complementary mechanisms of shareholder protection, creditor protection, and regulation to protect external constituencies. The absence of a strong legal regime to that effect, in turn, may warrant the mitigation of the corporate attributes in developing countries. This argument would suggest similar developments in emerging economies with similar institutional deficiencies, well beyond Brazil.

The third efficiency interpretation, which reinforces the two previous arguments, relies on the interdependence between the elements of the corporate form. Given the strong complementarity among them, the elimination of one or more of the attributes weakens the case for the persistence of the others. Like in the general theory of second best in microeconomics,[187] the elimination of one of the pillars of the efficient regime may erode the justification for the oth-

185. *See, e.g.*, EASTERBROOK & FISCHEL, *supra* note 39; Armour, Hansmann, Kraakman & Pargendler, *supra* note 1.

186. The term comes from VARIETIES OF CAPITALISM: THE INSTITUTIONAL FOUNDATIONS OF COMPARATIVE ADVANTAGE (Peter A. Hall & David Soskice eds., 2001).

187. *See* R. G. Lipsey & Kelvin Lancaster, *The General Theory of Second Best*, 24 REV. ECON. STUD. 11 (1956).

ers.

1. Limited Liability

To explore whether efficiency considerations may explain the mitigation of corporate characteristics in Brazil, I begin with the attribute of limited liability. The application of limited liability to involuntary creditors has long been controversial.[188] Straightforward economic analysis suggests that limited liability encourages the imposition of externalities on third-parties since shareholders benefit from the upside of risky activities but are not responsible if certain costs (e.g., of a systemic or environmental nature) materialize. Accordingly, prominent scholars have advocated against the protection of limited liability for torts.[189]

Lucian Bebchuk and Jesse Fried have drawn a more general distinction between adjusting and non-adjusting creditors.[190] Even contractual creditors such as workers and consumers may be non-adjusting, and therefore comparable to tort victims, if their relatively small claims (combined with limited information and foresight) prevent them from adjusting their contract terms to account for the risk of default.[191] Extending the argument against limited liability from tort creditors to non-adjusting creditors is a relatively small step. By taking it, one will conclude that the mitigation of limited liability in Brazil for the benefit of workers, consumers, and the environment is *the* efficient outcome—not only in Brazil, but globally. This means that, while Brazilian law still falls short of eliminating limited liability against all non-adjusting creditors, it is ahead of other jurisdictions in overcoming the inertia and interest group pressure that blocks the adoption of this more efficient regime.

The case for enforcing limited liability and capital lock-in within the context of a corporate group is less compelling than the case for doing so outside of it.[192] The separation of assets within the

188. *See, e.g.*, Richard A. Posner, *The Rights of Creditors of Affiliated Corporations*, 43 U. CHI. L. REV. 499, 520 (1976) (noting that pursuing separate incorporations for purposes of evading tort liability permits the externalization of costs and is socially inefficient).

189. Hansmann & Kraakman, *supra* note 125.

190. Lucian A. Bebchuk & Jesse M. Fried, *The Uneasy Case for the Priority of Secured Claims in Bankruptcy*, 105 YALE L.J. 857 (1996). For a discussion of the distinction between adjusting and non-adjusting creditors in the context of limited liability, see John Armour et al., *Transactions with Creditors*, *in* ANATOMY OF CORPORATE LAW, *supra* note 1.

191. Bebchuck & Fried, *supra* note 190, at 883.

192. Easterbrook & Fischel, *supra* note 76, at 111; Henry Hansmann & Richard Squire,

corporate group—what Hansmann and Squire term "internal partitioning"—generates higher costs but provides only a fraction of the benefits compared to "external partitioning" vis-à-vis the individuals who own the firm.[193] Some of the benefits of lock-in and limited liability, such as liquidity and the reduced need to monitor other shareholders, are generally unavailable in non-pyramidal corporate groups. Other benefits, such as reduced creditor information costs, are also often unavailable due to the widespread use of cross-guarantees.[194] At the same time, the costs of these attributes are higher because they encourage debtor opportunism in shuffling assets among different companies in the group.[195] This line of reasoning suggests that the greater willingness of Brazilian courts to grant substantive consolidation in bankruptcy may well guarantee the most efficient outcome.

Similarly, the existence of limited liability for shareholders of financial institutions has long attracted scholarly criticism,[196] which only grew stronger after the global financial crisis in 2008. The challenge to limited liability in this context follows the same logic: risk-taking by financial institutions can benefit shareholders, but the failure of systemically important financial institutions imposes significant negative externalities on the economy. In other words, limited liability exacerbates the problem of moral hazard faced by financial institutions.[197]

The traditional approach to this problem has been the governmental imposition of prudential regulation and the provision of deposit insurance. Nevertheless, the perceived failure of government regulation in the United States to prevent the global financial crisis[198]—and, in fact, the competing notion that government policies may have promoted risky behavior by financial institutions[199]—has

External and Internal Asset Partitioning: Corporations and Their Subsidiaries, *in* OXFORD HANDBOOK, *supra* note 145.

193. Hansmann & Squire, *supra* note 192.

194. *Id.*

195. *Id.*

196. Macey & Miller, *supra* note 80.

197. Marie-Laure Djelic & Joel Bothello, *Limited Liability and Moral Hazard Implications: An Alternative Reading of the Financial Crisis* (2014), http://ssrn.com/abstract=2418901 [https://perma.cc/6SDC-P2TT].

198. *See, e.g.*, RICHARD POSNER, A FAILURE OF CAPITALISM (2011); Patricia A. McCoy, Andrey D. Pavlov & Susan M. Wachter, *Systemic Risk Through Securitization: The Result of Deregulation and Regulatory Failure*, 41 CONN. L. REV. 493 (2009); Lynn A. Stout, *Derivatives and the Legal Origin of the 2008 Credit Crisis*, 1 HARV. BUS. L. REV. 1 (2011).

199. *See, e.g.*, RAGHURAM G. RAJAN, FAULT LINES (2010) (interpreting the government's

cast doubt on the effectiveness of this solution. Consequently, new calls for the mitigation or elimination of limited liability for financial institutions have reemerged in various forms.[200] While these proposals have not yet been adopted in the wealthy West,[201] Brazilian law eliminated the protection of limited liability for financial institutions decades ago.[202] As Brazilian commentators have argued, the erosion of limited liability for financial institutions in Brazil intervenes in the *ex ante* incentives of controlling shareholders and managers of banks and presents a regulatory option that may be more effective than a system of command-and-control regulation.[203] Moreover, because Brazilian banks typically have concentrated ownership, the imposition of liability on controlling shareholders is more likely to be effective in deterring risk-taking there than the application of shareholder liability in the U.S. context of dispersed ownership.[204]

Whether Brazil's stance toward unlimited liability deserves wide emulation is debatable. A more moderate, but still controversial, view is that the efficiency of limited shareholder liability for corporate obligations critically depends on the ability of the legal regime to curb opportunism vis-à-vis contractual creditors and restricts the corporation's ability to impose externalities on third parties. If the legal regime fails in these respects, the case for limited liability also falters.

promotion of credit and consumption as an attempt to counterbalance growing inequality); Peter J. Wallison, *Cause and Effect: Government Policies and the Financial Crisis,* 21 Critical Review: A Journal of Politics and Society AEI Online 365 (2008), https://doi.org/10.1080/08913810902934158 [https://perma.cc/8H6R-AP9K].

200. *See*, *e.g.*, Conti-Brown, *supra* note 131; Djelic & Bohello, *supra* note 197; Kevin Dowd, *Moral Hazard and the Financial Crisis*, 29 CATO J. 141 (2009); Willem H. Buiter, *Lessons from the Global Financial Crisis for Regulators and Supervisors* (Discussion Paper Series, Discussion Paper No. 635, 2009), http://www.lse.ac.uk/fmg/assets/documents/papers/discussion-papers/DP635.pdf [https://perma.cc/Y47N-HYMQ].

201. However, the United States has arguably imposed shareholder liability on bank holding companies since the Dodd-Frank Act, if not earlier. *See* James Si Zeng, *Internal and External Shareholder Liability in the Financial Industry: A Comparative Approach*, 37 REV. BANKING & FIN. L. 285, 290 (2017).

202. *See supra* notes 94–101 and accompanying text.

203. Franco & Rosman, *supra* note 102; FRANCO, *supra* note 103.

204. Since the U.S. banks contributing to the financial crisis were widely held, some scholarly proposals have focused on the imposition of stronger liability standards on bank directors rather than shareholders, though they have not been adopted to date. *See*, *e.g.*, John Armour & Jeffrey N. Gordon*, Systemic Harms and Shareholder Value*, 6 J. LEGAL ANALYSIS 35–85 (2014).

Certain weaknesses in Brazil's institutional environment help explain the observed pattern of unlimited liability. As discussed above, Brazilian courts are likely to overcome limited liability in three contexts: (i) claims by involuntary or non-adjusting creditors, such as workers, consumers, and victims of environmental harm, (ii) corporate groups, and (iii) financial institutions. In the presence of limited liability, the protection of involuntary or non-adjusting creditors requires a dedicated and effective regulatory infrastructure. Such capabilities of regulatory design and administrative enforcement may be missing in Brazil.

The same difficulties appear with respect to the regulation of financial institutions. The financial industry is generally able to thwart regulatory efforts because it is politically powerful, dynamic, and complex. Yet weaknesses in the regulatory apparatus, and the high concentration of the Brazilian financial sector in a few "too-big-to-fail" groups, exacerbates systemic risk. The prevailing view is that the Brazilian financial system is both strong and conservative.[205] In praising the financial performance and resilience of the Brazilian financial system after the global financial crisis, the controlling shareholder of BTG Pactual, Brazil's largest investment bank, explicitly singled out the role of unlimited liability. As he told the Financial Times: "[I]f something goes wrong with Pactual, people can get my house," which "is a very different philosophy than the U.S. and Europe."[206]

The application of limited liability to corporate groups is more controversial due to its more limited benefits and greater potential for abuse.[207] Curbing corporate opportunism vis-à-vis creditors in the group context requires courts to satisfactorily police related-party transactions within the group and rigorously enforce contractual protections negotiated by corporate creditors. But policing related-party transactions is an exceedingly difficult task that Brazilian courts do not seem to perform well.[208] Judicial enforcement of contracts is also suboptimal in Brazil. According to the World Bank's Doing Business Report, Brazil ranks as the 48th country in terms of

205. FRANCO, *supra* note 103, at 90.

206. Joe Leahy, *Brazil Banks Outshine Global Rivals: Reforms over the Past 20 Years Appear to Be Paying Off for the Sector*, FINANCIAL TIMES (Nov. 6, 2011), https://www.ft.com/content/497aeb38-085f-11e1-bc4d-00144feabdc0 [https://perma.cc/QU2P-BHVP].

207. *See supra* notes 192–195 and accompanying text.

208. The extremely high levels of private benefits of control in Brazil suggest that this is indeed the case.

contract enforcement and fares quite poorly with respect to the long duration of its legal proceedings.[209] Moreover, prominent Brazilian economists have claimed the existence of an anti-creditor bias by Brazilian courts.[210]

Finally, the optimality of limited liability depends on complementary features of the corporate form itself. First, there is a close relationship between lock-in and limited liability: they constitute opposite dimensions of the separation of assets between the firm and its owners. Whereas limited liability removes shareholder assets from the reach of corporate creditors, lock-in guarantees that corporate creditors will have priority over the corporation's assets. The rise of the partial dissolution of S.A.s in Brazil reverses this logic, permitting disgruntled shareholders to withdraw corporate assets before creditors are paid in full. Partial dissolution does not offer any type of protection to corporate creditors (who effectively lose priority to some shareholders), thus reducing the creditworthiness of the company. This, in turn, strengthens the case for enhanced creditor protection through unlimited liability.

Second, there is also close interdependence between limited liability and delegated management. One of the main justifications for limited liability is to specifically acknowledge and encourage the delegation of control. It seems unfair to hold shareholders liable for decisions they did not control. But delegated management is far weaker in Brazil: capital markets are only relatively developed, most listed companies have controlling shareholders, and corporate law discourages delegation by granting unusually strong powers to shareholders.

Third, limited liability also relates to transferability both indirectly, by encouraging delegated management, and directly, by permitting the uniform pricing of corporate shares irrespective of the financial condition of owners. In fact, another traditional justification for limited liability is that it permits the uniform pricing of corporate shares and thus facilitates hostile takeovers, which can be a powerful remedy against managerial agency costs. However, the concentrated ownership structure of most Brazilian corporations makes hostile

209. *See Ease of Doing Business in Brazil*, WORLD BANK: DOING BUSINESS (last visited Oct., 9, 2019), http://www.doingbusiness.org/data/exploreeconomies/brazil/#enforcing-contracts [https://perma.cc/Q78G-EADT].

210. Persio Arida et al., *Credit, Interest, and Jurisdictional Uncertainty: Conjectures on the Case of Brazil*, *in* INFLATION TARGETING AND DEBT: THE CASE OF BRAZIL 271–73 (Francesco Giavazzi, Ilan Goldfajn & Santiago Herrera eds., 2005).

takeovers impossible,[211] eliminating this justification.

Last, the paradigm of investor ownership strongly supports limited liability because it aims to limit the risk exposure of financially-motivated shareholders and to encourage participation in risky, but potentially fruitful, ventures. Limited liability is far less consequential in the context of state ownership because it is unclear that, as a practical matter, SOEs have limited liability. International experience and investors' perceptions instead suggest that states are likely to bail out SOEs, and the adoption of the corporate form with limited liability is not a credible commitment to the contrary.[212] In fact, the formal exclusion of SOEs from bankruptcy laws in Brazil further supports this reasoning.[213]

2. Lock-In

There is also an efficiency case for granting minority shareholders withdrawal rights in close corporations. In abolishing lock-in for close corporations, Brazilian courts have unwittingly implemented the recommendations of certain U.S. scholars since the 1950s.[214] The usual justification for this view lies in the lack of protection and liquidity for minority shareholders, which permits exploitative behavior by the majority. Both historical and contemporary evidence suggests that investors have favored liberal withdrawal rights whenever agency costs are particularly severe.[215]

A modified version of the efficiency argument against lock-in takes into consideration the existence of complementary institutions. Even the strong defense of lock-in by Edward Rock and Michael

---

211. Érica Gorga, *Changing the Paradigm of Stock Ownership from Concentrated Towards Dispersed Ownership? Evidence from Brazil and Consequences for Emerging Countries*, 29 NW. J. INT'L L. & BUS. 439 (2009).

212. *See* Mauricio Jara-Bertin et al., *Implicit Bailouts and the Debt of Wholly State-Owned Enterprises* (July 26., 2018) (working paper), http://ssrn.com/abstract=2670899 [https://perma.cc/K7YA-RM35] (finding that SOEs have access to more favorable financing terms due to expectations of an implicit guarantee).

213. Lei No. 11.101, de 9 de Fevereiro de 2005, art. 2, D.O.U. de 09.02.2005, art. 2º (Braz.).

214. *See supra* note 37 and accompanying text.

215. For historical evidence, see Lamoreaux & Rosenthal, *supra* note 35. For contemporary evidence on the different transaction structures used by the venture capital industry, see Kate Litvak, *Firm Governance as a Determinant of Capital Lock-In*, (UNIV. OF TEX. LAW, Law & Econ. Research Paper No. 95, 2006), https://ssrn.com/abstract=915004 [https://perma.cc/4X49-5E56].

Wachter explicitly relies on "vigorous judicial enforcement" of the rule requiring *pro rata* distributions.[216] Yet such vigorous judicial enforcement is notoriously absent in Brazil. Recall that existing estimates describe the level of private benefits of control extracted from public corporations in Brazil as among the highest in the world.[217] Given the lack of regulatory oversight and exit options for minority investors, the opportunity for exploitation tends to be greater in close corporations. All of this suggests that there is a stronger case for protecting minority shareholders through exit rights in this context.

Beyond that, the decline of lock-in in Brazil relates in important ways to the other corporate attributes. While the disappearance of lock-in strengthens the case for unlimited liability, the reverse is also true. The rise of unlimited liability militates in favor of providing a fair exit option to minority shareholders, who lack control over corporate operations yet face potential future liability to workers, consumers, and environmental victims.

Not only does lock-in entail greater costs in Brazil, but some of its alleged benefits are less likely to be present. Specifically, the benefits of lock-in in protecting specific investments by non-shareholder constituencies presupposes limited shareholder power. However, most corporations in Brazil have powerful controlling shareholders. Lock-in is unavailable against controlling shareholders since corporate law generally permits a majority or supermajority of shareholders to liquidate the firm.[218] Delegated management and board independence are also particularly fragile in Brazil, which reinforces controlling shareholders' ability to hold up other constituencies.[219] Therefore, the promotion of specific investments as a justification for lock-in is comparatively less important in the Brazilian context.

Although less apparent, there is a plausible connection between the lack of lock-in and the decline of investor ownership. The absence of lock-in decreases the ability of private corporations to raise debt and commit to long-term projects, furthering the case for state ownership. Mixed enterprises, by contrast, enjoy a stronger

216. Rock & Wachter, *supra* note 28, at 915.

217. *See supra* note 171 and accompanying text.

218. *See* Lynn A. Stout, *The Corporation as Time Machine: Intergenerational Equity, Intergenerational Efficiency and the Corporate Form*, 38 SEATTLE U. L. REV. 685, 689 (2016) ("[I]t is much harder to lock assets into a company that has controlling shareholders.").

219. *Id.* ("Only as directors become independent of shareholders does asset lock-in become possible.").

version of lock-in since the state may not liquidate the firm or sell a substantial part of its assets in the absence of special legislative authorization. Finally, lock-in is the flip side of transferable shares: it is precisely because corporate shares are transferable that shareholders are denied the exit option in the form of withdrawals of capital. To the extent that Brazilian corporate law and market structure hinder transferability, there is also a relatively stronger case for abolishing lock-in and permitting withdrawals at will.

3. Delegated Management

The optimal degree of managerial delegation and shareholder empowerment is a central, and largely unresolved, question in contemporary corporate governance.[220] Some scholars have claimed that there is room for far greater shareholder power than U.S. law has traditionally allowed. Lucian Bebchuk, the most vocal supporter of shareholder empowerment, has argued that shareholders should, at the very least, decide the rules of the game by controlling the process of charter amendments.[221] But Brazilian law goes far beyond Bebchuk's dream since the mandatory nature of most corporate law rules makes it difficult for charter amendments to abridge the powers of the shareholder majority in public companies.[222]

In contrast to the Brazilian law approach to limited liability and lock-in, it does not follow that such a toned-down form of managerial delegation is more likely to be efficient. However, a weak version of delegated management may be a plausible response to a deficient institutional environment. A system that so poorly protects minority shareholders would likely also permit high managerial agency costs if ownership were dispersed. A strong level of controlling shareholder involvement in management could then be a response to these costs. Causation may, however, run in the opposite direction, with a lack of delegated management facilitating the extraction of extraordinary private benefits of control. In other words, controlling shareholders may be able to exploit minority investors with such ease precisely because they do not face any countervailing

220. For a discussion of the tradeoffs involved, see Zohar Goshen & Richard Squire, *Principal Costs: A New Theory for Corporate Law and Governance*, 117 COLUM. L. REV. 767 (2017).

221. Lucian Arye Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833 (2005).

222. *See*, *e.g.*, LSA, *supra* note 43, art. 36, which only permits close corporations to adopt supermajority approval requirements for shareholder decisions.

checks within the firm.

Another view is that weak managerial delegation is a second-best response to the dwindling of other corporate attributes. The erosion of shareholder limited liability encourages shareholders to eschew diversification and instead take an active part in company management. Conversely, given that controlling shareholders take an active part in management, the case for limited liability is correspondingly weaker.

There are complementarities with other elements as well. The protection afforded by lock-in to specific investments by various corporate constituencies presupposes the absence of shareholder control. Delegated management also goes hand-in-hand with transferability. However, the relationship between delegated management and state ownership is less clear. From a political economy perspective, the state's interests as a shareholder have arguably played a role in strengthening shareholder power and weakening the role of the board. However, the efficiency argument likely runs in the opposite direction, with influential guidelines on SOE governance advocating for strong and independent boards to improve corporate performance.[223]

4. Transferable Shares

Share transferability is the least controversial feature of the corporate form. Although transferability per se do not pose major costs, this attribute becomes contentious when it comes to control transfers. In the international context, the main debate in this area relates to the board's ability to thwart hostile takeover threats, as permitted under Delaware law through the use of poison pills, or prohibited under the non-frustration rule of EU law.[224] This debate, however, loses significance in the Brazilian context since hostile takeovers are virtually non-existent due to the prevalence of concentrated ownership.

Instead, the main normative debate in this area concerns the scope and desirability of a mandatory bid rule. While law and economics scholars have questioned the efficiency of the mandatory bid rule,[225] investors in Brazil generally favor this mechanism. This

223. *See* ORG. FOR ECON. CO-OPERATION & DEV., OECD GUIDELINES ON CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES 26 (2015).

224. For a discussion of these mechanisms, see Paul Davis et al., *Control Transactions*, *in* ANATOMY OF CORPORATE LAW, *supra* note 1.

225. Clas Bergström et al., *The Optimality of the Mandatory Bid Rule*, 13 J.L. ECON. &

mandatory bid rule has been adopted in their stock exchange's most rigorous listing standards,[226] suggesting that the desirability of this rule may depend on the underlying context.

Finally, recall that important obstacles to transferability in Brazil come from the disincentives to share transfers posed by unlimited liability. The choice of a timing rule for the apportionment of shareholder liability is particularly relevant here. The impingement on transferability is stronger when judicial decisions impose liability on shareholders for obligations accruing, or claims filed in periods, outside of their tenure as shareholder—that is, before they bought or after they sold their shares. It is particularly difficult to justify on efficiency grounds the imposition of liability on former shareholders for contracts or torts that take place after the transfer of the shares, as some Brazilian courts have done with respect to labor claims.[227]

5. Investor Ownership

The mainstream view today is that ownership by private investors is generally the most efficient form of enterprise organization.[228] At the same time, heterodox critiques and some empirical studies point to the efficiency of state ownership in certain contexts.[229] In this latter view, which is particularly popular in some Latin American countries, the prevalence of state ownership in Brazil constitutes a sign of economic and social progress.

A more broadly accepted claim is that certain deficiencies in the institutional environment may at times tip the balance in favor of state ownership in developing countries. Even strong defenders of private ownership recognize that its superiority often hinges on the existence of good contract institutions.[230] Likewise, there is a long

ORG. 433, 447–48 (1997); Frank H. Easterbrook & Daniel R. Fischel, *Corporate Control Transactions*, 91 YALE L.J. 698, 716, 737 (1982); Marcel Kahan, *Sales of Corporate Control*, 9 J.L. ECON. & ORG. 368, 378 (1993).

226. Gilson, Hansmann & Pargendler, *supra* note 132, at 491.

227. *See* Hansmann & Kraakman, *supra* note 125, at 1896–98 (proposing a system by which shares would be transferred to shareholders free of liability for prior acts).

228. *See*, *e.g.*, William L. Megginson & Jeffry M. Netter, *From State to Market: A Survey of Empirical Studies on Privatization*, 39 J. ECON. LIT. 321, 380 (2001) (concluding that "privately owned firms are more efficient and more profitable than otherwise-comparable state-owned firms").

229. *See, e.g.*, HA-JOON CHANG, GLOBALISATION, ECONOMIC DEVELOPMENT, AND THE ROLE OF THE STATE 225–26 (2003).

230. *See*, *e.g.*, Andrei Shleifer, *State Versus Private Ownership*, 12 J. ECON. PERSP. 133,

tradition of defending the role of state ownership in the catch-up process in environments where capital market failures prevent sizable investments in long-term projects.[231]

As implied earlier, the decline of the other elements of the corporate form may play a role in weakening the investment capacity of private enterprise and, consequently, strengthen the case for state ownership. The erosion of limited liability increases the risk and decreases the reward of private entrepreneurship. Even when limited liability is inefficient, as it is for involuntary or non-adjusting creditors, it constitutes a subsidy for, and therefore encourages, private risk-taking. The elimination of lock-in, in turn, hampers investments in long-term or risky projects and hinders the continuity of the enterprise over time.

B. Distribution

Another line of interpretation is that distributional considerations, not efficiency, best justify the phenomenon of decorporatization in Brazil. This interpretation finds support in the widespread narrative that (re)distribution—specifically, the promotion of "social justice"—is a central objective of the Brazilian Constitution and a key factor motivating judicial decisions. In the last few decades, Brazil seems to have favored distributive policies in lieu of growth.[232]

Multiple considerations complicate the assessment of this rationale. First, while redistribution can enhance social welfare, there is no consensus on the optimal degree of inequality and, therefore, on the optimal level of redistribution. Second, distribution-oriented policies resulting from interest group pressure can easily be regressive and, as a result, decrease social welfare. Third, and relatedly, there is the well-known risk that a private law policy aimed at reducing inequality or poverty may produce the opposite result. The brief discussion that follows will not attempt to resolve these very difficult questions. Instead, it will be limited to examining whether distributional intentions provide a *prima facie* plausible explanation for the decline of corporate attributes in Brazil and making initial reflections on the

144 (1998).

231. *See generally* ALEXANDER GERSCHENKRON, ECONOMIC BACKWARDNESS IN HISTORICAL PERSPECTIVE: A BOOK OF ESSAYS (1962).

232. *See* Fernando de Holanda Barbosa Filho & Samuel de Abreu Pessoa, *A Desaceleração Veio da Nova Matriz, Não do Contrato Social*, *in* ENSAIOS IBRE DE ECONOMIA BRASILEIRA–II 27 (Regis Bonelli & Fernando Veloso eds., 2014).

promise of these strategies to reduce inequality.

At first glance, the distribution account appears to have significant purchase, particularly for explaining features of Brazilian law that appear to entirely lack an efficiency explanation, such as imposition of joint and several liability among shareholders in cases of veil piercing. Expansive veil piercing under Brazilian law favors parties that are presumably weaker, like workers and consumers, while the elimination of lock-in favors minority shareholders.[233] Distributional considerations are also a plausible justification for continued state ownership.

While further investigation is necessary to determine the effects of such a distribution-oriented approach, there is reason to be skeptical about its efficacy in tackling the broader problem of inequality in Brazil. Veil piercing under labor laws only benefits formal workers, who constitute little more than half of Brazil's labor force. Informal workers, who are often the poorest, remain unprotected. The effects of state ownership on redistribution are also dubious.

In some respects, Brazilian law is a dream come true for progressive corporate law scholars, but its effects remain to be seen. Brazil's continuously high levels of inequality suggest that abating the private business corporation is no panacea and might be counterproductive insofar as it discourages investment and induces shareholders and managers to hide their assets offshore. The agency problems and externalities generated by the corporate form may well be worthwhile, such that it may be in society's interest to subsidize entrepreneurial activity through a strong commitment to limited liability because of its potential impact on innovation.[234] This profound question, however, remains unsettled.

C. The Significance of Decorporatization

Finally, one may wonder about the actual scope of decorporatization and its practical implications. As described above, the erosion of corporate attributes like lock-in and limited liability in Brazil seem to apply primarily to closely-held corporations rather than the more scarce publicly-held corporations. This raises the question: does the dwindling of corporate attributes in Brazil have practical and

233. While veil piercing per se could be explained in terms of efficiency, the imposition of joint and several liability by labor courts lacks an efficiency explanation and can therefore be best understood in terms of distribution.

234. For a similar argument, see Presser, *supra* note 77, at 172.

theoretical relevance?

To begin with, the trend toward decorporatization in Brazil is not limited to close corporations. The mitigation of delegated management, share transferability, and investor ownership are clearly present in the public corporation context. The use of partial dissolution and veil piercing in the public company context is mostly untested, rather than discarded. Indeed, the only judicial decisions concerning publicly-traded firms in this area have done away with lock-in and limited liability.[235]

But even if decorporatization in Brazil was limited to close corporations, would this make it trivial? Not necessarily. Close corporations matter because of their numbers and economic clout. The vast majority of corporations are closely held and account for key sectors of the economy. This is true not only in Brazil, whose capital markets are relatively underdeveloped,[236] but also around the world. Silicon Valley start-ups are often formed as close corporations to benefit from lock-in and avoid the problem of untimely or opportunistic dissolution requests.[237] The core attributes thus appear to perform a valuable economic function in at least certain types of closely-held firms.

Another possibility is that *formal* decorporatization may not necessarily entail *functional* decorporatization if there are extralegal substitutes for the core attributes of the corporate form. The leading case on partial dissolution involving COCELPA illustrates this point.[238] Even though shareholders filed suit in 1991 and obtained a final decision recognizing the right to a partial dissolution by the Superior Court of Justice in 2007, the proceedings are still ongoing, and they have yet to receive the amounts owed. This shows that, even if the parties no longer enjoy lock-in by law, a sluggish judiciary may effectively provide lock-in in practice and mitigate the problem of untimely decapitalization of the firm due to opportunistic hold-up by minority shareholders or to their idiosyncratic liquidity needs.

More generally, the use of various tactics to hide assets from creditors—from fraudulent transfers to friends and relatives to the

235. *See supra* notes 54 and 126 and accompanying text.

236. As of August 2018, Brazil had fewer than 500 public companies listed on its stock exchange, whose market capitalization was approximately forty percent of GDP, and nearly 19,000 firms registered as business corporations (S.A.) in the state of São Paulo alone.

237. Rock & Wachter, *supra* note 28, at 915.

238. S.T.J., Embargos de Divergência em Recurso Especial No. 111.294–PR, *supra* note 57.

growing use of offshore holding companies—may reestablish limited liability in some contexts. This, of course, does not mean that these substitutes are always effective or without cost—a theme that also deserves further investigation. But if the corporate attributes do not matter for close corporations, or there are effective extralegal substitutes for them, we should rethink the role of the business corporation in the modern economy and the law's contribution to it.

III. BEYOND BRAZIL

The foregoing discussion raises the question of whether Brazil's experience with decorporatization is exceptional or represents a broader trend among other jurisdictions and, in particular, developing countries. This is a difficult question to answer. While the prevalence of state ownership in continental Europe and emerging markets is well documented,[239] we still know little about possible variations in the strength of the corporate form's other core elements.

The existing literature in this area focuses primarily on limited liability and the exceptions created by the doctrine of veil piercing. As a general matter, developing countries appear to be latecomers in recognizing exceptions to the attribute of limited liability. Recall that this was also the case in Brazil, where the doctrine only gained ground in the last few decades. However, most emerging market jurisdictions appear to have been slower than Brazil in incorporating even the most restrained version of veil piercing premised on the existence of fraud or egregious abuse—the adoption of which would lead to convergence, rather than divergence, from the norm in mature economies.

Recent studies continue to describe the application of veil piercing in Spain and Hispanic America as relatively narrow in scope.[240] There is, however, some evidence of veil piercing and the application of enterprise liability in the context of corporate groups for the benefit of workers and tax authorities in certain Latin American jurisdictions.[241] Colombia's bankruptcy law explicitly makes parent companies presumptively liable for the debts of their subsidi-

239. *See* Pargendler, *supra* note 145.

240. *See*, *e.g.*, JOSÉ MARIA LEZCANO NAVARRO, PIERCING THE CORPORATE VEIL IN LATIN AMERICAN JURISPRUDENCE (2016); Dante Figueroa, *Comparative Aspects of Piercing the Corporate Veil in the United States and Latin America*, 50 DUQ. L. REV. 683 (2012).

241. Figueroa, *supra* note 240, at 738, 772–75.

aries.[242] Nevertheless, the general sense remains that courts are reluctant to pierce the corporate veil in civil law jurisdictions.[243] Business lobby groups have successfully opposed a recent bill in Ecuador that sought to eliminate shareholder limited liability with respect to tax claims.[244]

There is by now a sizeable literature on the adoption and growing use of veil piercing in China, whose evolution may indicate a broader trend towards decorporatization. Prior to 2006, Chinese law did not formally recognize a doctrine of veil piercing. Although there were a few isolated cases of the judicial application of the concept, scholars viewed the status quo as insufficient to curb abusive uses of legal personality to the detriment of corporate creditors.[245]

As part of its corporate law overhaul in 2006, China enacted specific statutory provisions on veil piercing for the first time. Article 20 of the Company Law provides for joint and several liability of shareholders in cases where the abuse of the independent status of the company "seriously damages the interests of any creditors."[246] Article 64 also contains a specific rule for one-shareholder companies that reverses the burden of proof, making the single shareholder liable whenever she is unable to prove that the company's property is independent from her property.[247] These provisions were allegedly the product of a political compromise that took into account the government's hostility to veil piercing in view of its interest as a major shareholder in SOEs.[248]

Since the 2006 reform, China appears to be far more prone to piercing the corporate veil than mature economies. In a study of the

242. L. 1116, diciembre 27, 2006, DIARIO OFICIAL (Colom.).

243. MARCO VENTORUZZO ET AL., COMPARATIVE CORPORATE LAW 130–31, 170–71 (2015).

244. Evelyn Tapia, *La Propuesta de Que Accionistas Respondan por Deudas Tributarias Genera Cuestionamientos*, EL COMERCIO (Nov. 9, 2017), https://www.elcomercio.com/actualidad/propuesta-accionistas-deudas-tributarias-economia.html [https://perma.cc/K7QT-W5Z2].

245. *See*, *e.g.*, David M. Albert, *Addressing Abuse of the Corporate Entity in the People's Republic of China: New Thoughts on China's Need for a Defined Veil Piercing Doctrine*, 23 U. PA. J. INT'L ECON. L. 873, 884, 896 (2002).

246. Chao Xi, *Piercing the Corporate Veil in China: How Did We Get There?*, 2011 J. BUS. L. 413, 413–14 (2011).

247. For a translation and discussion of the relevant provisions, see Mark Wu, *Piercing China's Corporate Veil: Open Questions from the New Company Law*, 117 YALE L.J. 329, 333–535 (2007).

248. Huang, *supra* note 88, at 772–73.

judicial application of veil piercing between 2006 and 2010, Hui Huang found 99 reported opinions in this area—a figure he describes as "remarkably high" from a comparative perspective—and a decision to pierce the veil in nearly two-thirds of these opinions.[249] A more recent study by Kimberly Bin Yu and Richard Krever showed that these cases grew exponentially in the five years following Huang's survey, and the success rate of creditors also increased significantly.[250] At least some of these decisions seem to take an expansive reading of the statute. While Article 20 appears to cover only "vertical piercing" between the parent and its subsidiaries, courts have also permitted "horizontal piercing" among companies under common control.[251] Moreover, Chinese regulators have conditioned the formation of private commercial banks, permitted since 2003, on an agreement by five percent of shareholders to compensate the losses caused to depositors up to a specified cap.[252]

Commentators have offered numerous explanations for the surprisingly high incidence of veil piercing in China. They range from the lack of sophistication and paternalistic attitudes of Chinese judges to the particular wording of the statute that shifts the burden of proof in the case of one-member companies.[253] These accounts, however, have generally failed to consider one of the central hypotheses advanced in this Article—namely, that the weakening of corporate attributes might be a second-best response to a deficient institutional environment.

Furthermore, there is evidence that the weakening of corporate attributes in China spans beyond limited liability. Curtis Milhaupt has showed that, at least with respect to the SOEs that dominate China's economy, each of the corporate elements takes a modified and blander form—a phenomenon that he attributes to the "adaptability" of the business corporation.[254] It also appears that some of the peculiar features of the Chinese system—such as the role of the Chinese Communist Party in sidelining the board of direc-

249. *Id.* at 748–49.

250. Kimberly Bin Yu & Richard Krever, *The High Frequency of Piercing the Corporate Veil in China*, 23 ASIA PAC. L. REV. 63, 80 (2015).

251. Xi, *supra* note 246, 413, 429.

252. Zeng, *supra* note 201, at 3, 29, 36–37 (attributing the Chinese regime of shareholder liability to a lack of regulatory capacity). The cap is either the capital invested or 500,000 RMB for each public depositor. *Id.* at 29.

253. Yu & Krever, *supra* note 250, at 81–82.

254. Milhaupt, *supra* note 1, at 296.

tors[255]—are not limited to the SOE context but are present in private enterprises as well. In Milhaupt's view, the corporate form has "a chameleon-like ability to take on the characteristics of the political economy in which it operates."[256] This view, however, may lead one to underestimate the degree of divergence in the relevance of the corporate attributes. It is possible that, at some point along this transformation to suit local features, the organization in question may no longer qualify as a business corporation but instead become a different animal altogether. Ascertaining the existence and extent of decorporatization around the world, as well as its potential causes, undoubtedly requires future research. The claim advanced in this Article about the significant erosion of the corporate elements in Brazil is a novel one and has not been documented to date. Instead, the available descriptions of Brazil's corporate law by both scholars and practitioners have failed to highlight its significant departure from international practice. Moreover, this is a recent phenomenon, and one that may only recently be beginning to take hold elsewhere. Any verification of the incidence and degree of decorporatization in other contexts will require scholars to scratch beyond the surface of textbook accounts and conduct dedicated country studies.

IV. CONCLUSION

The conventional understanding is that the history of the corporate form is one of acclaimed success as well as continued and inevitable expansion to different contexts. Once restricted by the government, the corporate attributes are deemed ever more widely available, irrespective of old constraints such as corporate taxation or accompanying mandatory terms. Contemporary Brazilian law, however, shows a certain degree of involution and therefore subverts these understandings.

Although scholars have mounted theoretical challenges against the expansive application of certain corporate elements—most conspicuously limited liability—these critiques are generally dismissed as impractical exercises of institutional imagination that stand no chance of actual implementation. However, the recent Brazilian experience gives pause to the inevitability of the business corporation's core traits. Through a series of judicial decisions and statutes, Brazilian law has significantly weakened the canonical

255. *Id.* at 291.

256. *Id.* at 296.

corporate elements. The strong version of the corporate form, which is generally assumed to be universal, is no longer available under Brazilian law. The roots of the observed decorporatization of Brazilian enterprise are unlikely to be monocausal, but there is an efficiency case for most, though by no means all, of these new doctrinal developments. As with most things, the efficiency of the corporate form may be contingent on the underlying institutional environment.

Brazil's experiment with decorporatization points to new directions in comparative law and economics. The enduring debate on the degree of convergence and persistence in corporate governance assumes either the approximation of legal systems or the conservation of deep-rooted differences. Most analyses of legal developments in emerging economies focus on foreign transplants from mature economies, greatly discounting the degree of local ingenuity and originality. The prospect of newly-minted divergence that originates in developing countries is generally disregarded. Finally, comparative corporate governance has focused on the content of corporate law, overlooking differences in the strength and operation of the corporate form itself, which may be far more substantial than usually acknowledged.

For better or worse, the persistence of a strong version of the corporate form does not seem to be inevitable. While Brazil's trajectory shows that its history has not ended, it also makes the case for reflection on the merits of the different corporate attributes all the more pressing. Fortunately, these changes provide an interesting, but thus far underutilized, laboratory for such purposes.