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Strengthening Asset Recovery: The Continued Use of Reverse Veil Piercing

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In Brazil, it is not uncommon for debtors to use legal entities to conceal assets, thereby illegally frustrating creditors' attempts to recover debts. To address this issue, Brazilian law allows, in exceptional circumstances and under certain conditions, the disregard of the legal entity to access the assets of companies used to defraud third parties.

This mechanism, outlined in Article 50 of the Civil Code and Articles 133 to 137 of the Civil Procedure Code, enables courts to disregard the separate legal personality of a company and reach assets that have been shielded to evade creditors. By doing so, the company involved in the fraud becomes jointly liable for the specific obligations impacted by the debtor's wrongful acts.

Typically, in cases involving clear asset commingling or abuse of the company's legal personality to defraud creditors, the court may reach the personal assets of the company's partners if they were responsible for such an illegal situation. This process is known as direct disregard of the legal entity. However, there is also a reverse disregard, where the company's assets may be used to satisfy the debts of a partner or another beneficiary involved in fraudulent activity.

This reverse theory was recently applied by the Superior Court of Justice (SCJ) in Special Appeal No. 2,095,942-PR. Although the SCJ emphasized the exceptional nature of the reverse disregard of the legal entity, it applied the doctrine in this case due to the clear fraudulent intent behind the operations involving the debtors and their children's company.

According to the SCJ's ruling, the debtors had transferred a property to a third party at a price 18 times lower than its market value, using such property to capitalize a new company owned by their children. A year later, the third party withdrew from the company, receiving only the amount initially paid for the property, leaving the company entirely in the hands of the debtors' children.

Given these facts, the SCJ approved the reverse disregard of the legal entity, holding the company jointly liable for the debt. The sale of the property at an artificially low price, the formation of the company with the debtors' children, the third party's subsequent withdrawal, and the absence of proof of payment for the third party's shares all clearly indicated an attempt to shield assets and defraud creditors. This was deemed inadmissible by the court.

Although the application of reverse disregard of the legal entity remains limited, decisions like this one from the SCJ help solidify the doctrine and provide guidance for its application by lower courts. Ultimately, it serves as another tool for creditors seeking judicial recovery of debts when faced with fraudulent schemes designed to block such recovery.

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