

# CONFLICTS OF INTEREST IN PORTUGAL

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## FINANCIAL INSTITUTIONS

### 1. GENERAL INTRODUCTION

Conflicts of interest of financial institutions have long been a concern in Portugal as these entities have progressively widened their range of activities from the traditional commercial banking to universal banking, including investment and insurance services. However, the issues raised following the financial scandals in the United States and in Europe originated a new level of reform, not only at European level but also at national level.

Financial Institutions, clients and regulators play a significant role in the shift in perception of matters such as conflicts of interests. Financial institutions, in particular, are not only encouraged by law but also with a view of ensuring a trustful commercial relationship with their clients, to adopt new measures and procedures so as to prevent and to deal more effectively with existing or potential conflicts of interests.

The Portuguese regulation of conflicts of interest affecting financial institutions is basically contained in the General Regime of Credit Institutions and Financial Companies (“GRCIFC”), approved by Decree-law no. 298/92, of December 31; Portuguese Securities Code, approved by Decree-law 486/99, of November 13 (“Securities Code”); CMVM Regulation 12/2000 on Financial Intermediation Activities. As regards case law, as far as we can tell, there is no relevant decision on conflicts of interests of financial institutions.

The regulation and supervision of financial institutions in Portugal is primarily carried out by the Bank of Portugal (*Banco de Portugal*)(the “BP”) and the Portuguese Securities Commission (*Comissão do Mercado de Valores Mobiliários*)(the “CMVM”). The BP is in charge of the supervision of credit institutions, financial companies and investment firms. The CMVM is responsible

for the supervision of financial institutions, which is meant to include credit institutions, financial companies and investment firms, which carry out financial intermediation activities (e.g., securities investment services, ancillary services of investment services or management of collective investment undertakings). Further enforcement of the obligations imposed on Portuguese financial institutions, besides that of the BP and the CMVM, is a specific power of the courts. The Financial Supervisors National Council (*Conselho Nacional de Supervisores Financeiros*), created in 2000 to coordinate the national strategies in the areas of banking, capital markets and insurance supervision has no direct powers over financial institutions.

The issue of conflicts of interest in financial institutions, further developed in Section 4 below, is currently discussed in Portugal from two perspectives: (i) internal conflicts of interests, i.e. with members of corporate bodies and other employees, advisers and representatives; and (ii) external conflicts, i.e. conflicts of interests with clients.

## **2. BACKGROUND AND ENVIRONMENT**

The GRCIFC, approved in 1992, sets out several business conduct rules applicable both to financial institutions and to members of their corporate bodies and employees, including rules on professional secrecy and conflicts of interest. In 2002, some of these provisions were amended in order to prevent conflicts of interest more effectively.

The GRCIFC only refers to internal conflicts of interest, i.e. conflicts between the interests of the institution itself and the interests of those in charge of its management, which may result in damages to the institution and its shareholders.

The Securities Code, on the other hand, deals with external conflicts of interest, on the basis of the following main rules: (i) financial intermediaries shall avoid conflicts of interests; (ii) whenever a conflict of interest with their clients occurs, financial intermediaries shall act in a fair and transparent way; and (iii) whenever a conflict of interest occurs with their own interests, the interests of members of their corporate bodies or of their employees, financial intermediaries shall ensure that clients' interests prevail.

Although all these rules were already part of Portuguese law prior to the approval of the Securities Code, they were subject to a very useful amplification and detailing in this code. The detailing efforts were particularly strong regarding transactions for the financial intermediary's own account, prevention of front running, rules aiming to prevent the financial intermediary emerging as its client's competitor, prevention of churning, as well as several organisational duties aimed at reducing conflicts of interests.

Portugal is represented in the International Organisation of Securities Commissions (IOSCO) and in the Committee of European Securities Regulators (CESR) by the CMVM. Therefore, the CMVM, within the scope of its regulatory

and supervisory duties, seeks to uphold the standards and international recommendations issued by the above mentioned international organisations.

### **3. APPLICABLE LAW, REGULATION, CODES AND CASE LAW**

The main sources of law regarding conflicts of interests of financial institutions are the following:

- (a) The General Regime of Credit Institutions and Financial Companies, approved by the Decree-law no. 298/92, of December 31, as amended;
- (b) The Portuguese Securities Code, approved by Decree-law no. 486/99, of November 13, as amended, which adopted into Portuguese law the Directives 2003/6/EC, of January 28, 2003/124/EC, of December 22, 2003/125/EC, of December 22, and 2004/72/EC, of April 29;
- (c) CMVM Regulation 12/2000, on Financial Intermediation Activities, as amended;
- (d) Collective Investment Undertakings and Management Companies Regime, approved by Decree-law no. 252/2003, of October 17 (“CIUMCR”);
- (e) CMVM Regulation 15/2003 on Collective Investment Undertakings, as amended; and
- (f) Real Estate Investment Funds Regime, approved by Decree-law no. 60/2002, of March 20, as amended.

Aside from the legal provisions mentioned above, certain private associations of financial institutions in Portugal (e.g., the Portuguese Banks Association or the Portuguese Investment Companies Association) have published codes of conduct for their members. Codes of conduct shall be either approved by the BP and/or registered with the CMVM.

### **4. THE REQUIREMENTS**

As for internal conflicts of interests regarding members of corporate bodies, Article 85 of the GRCIFC, applicable to all credit institutions, financial companies and investment firms (except when specific legislation ruling each specific activity provides otherwise) sets out several restrictions regarding (i) the grant of credit and guarantees to members of their management or supervisory boards, their spouses, relatives by blood, relatives by marriage in the first degree and companies/other legal entities controlled by any of the latter persons; and (ii) the purchase of shareholdings in companies controlled by any of the latter persons.

As for internal conflicts of interests with directors, management officers, and other employees, advisers and representatives of financial institutions, Article 86 of the GRCIFC also provides that they shall not intervene in the appraisal and taking of decisions on operations in which they, their spouses, relatives by blood or relatives by marriage in the first degree, as well as companies/other legal

persons controlled by any of the latter persons, are directly or indirectly the parties concerned.

Moving on to external conflicts of interests, i.e. with clients - the issue on which this study is focused - it should be highlighted, first of all, that credit institutions, financial companies and investment firms, whenever carrying out financial intermediation activities under the terms set out in the Securities Code, are considered as financial intermediaries.

Article 309 of the Securities Code provides that financial intermediaries shall organize themselves so as to reduce to the minimum extent risks of conflict of interest, ensuring transparent and equal treatment to clients and making their interests prevail. For the purposes of this article, the CIUMCR sets forth that a collective investment undertaking is deemed to be a client of its management company.

As a result of this principle, according to Article 328 of the Securities Code, when a financial intermediary cannot execute an order from its client, it must pass it on to another financial intermediary capable of executing it. Unless otherwise provided by the entity placing the order, the financial intermediary can arrange in a single order the orders of several entities to be executed in a registered market, provided that (i) such procedure is compatible with the nature of the orders, (ii) does not cause damage to the entities placing the order and (iii) the financial intermediary is able to allocate to each entity the operations so executed, in accordance with transparent procedures.

In case of joint orders issued in relation to several collective investment undertakings, the management company is bound to allocate the assets and costs proportionally, under Article 34 of the CIUMCR.

A very important source of conflicts of interests is “churning”, which is dealt with in the Securities Code by Article 310. In order to avoid it, financial intermediaries shall refrain from causing clients to engage in repeated operations on securities or from doing so on account of clients, when such operations are carried out with the purpose of obtaining high sales commissions or achieving goals contrary to the interests of clients.

Another important risk of conflicts of interests are the transactions made on the own account of the financial intermediary. In those cases where the financial intermediary acts as counterparty to the client, unless the client is an institutional investor or the transaction is made in the regulated market (where best execution is ensured), the financial intermediary must obtain its client’s written authorization or confirmation, pursuant to Article 346 of the Securities Code. Moreover, whenever executing operations on its own account to fulfil clients’ orders, the financial intermediary shall make securities available to such clients at the same price they were purchased. In addition, under Article 347, a financial intermediary shall refrain from: (i) executing operations on its own account together with operations on the account of its clients; (ii) purchasing for itself any securities, where there are clients that have requested such securities at the same

or at a higher price (this is meant to include call transactions executed by the financial intermediary prior to the execution of orders from its clients); (iii) selling of securities it holds instead of selling securities of the same category, which sale has been ordered by its clients at the same or lower price.

Nowadays, financial intermediaries are authorised to carry out several financial intermediation services and activities, such as transactions on their own account and on the account of third parties, investment advice and research. Information used by one department and that should be kept confidential may be easily accessed by another department of the same financial intermediary, giving rise to conflicts of interest. One of the most common examples is the research department that, instead of basing its analysis on information obtained independently, uses the information collected from clients by other departments within the same financial intermediary. “Chinese walls” or “firewalls” have their origin in this kind of experience and aim to segregate information inside the financial intermediary, in order to reduce the risk of conflicts of interest.

Therefore, in accordance with the CMVM Regulation 12/2000, financial intermediaries pursuing more than one intermediation activity, are legally bound to organise and manage the intermediation activities carried out so as to prevent the occurrence of conflicts of interest with their clients or between different clients, as well as the disclosure of privileged information. In addition, this Regulation also provides that each financial intermediation activity shall be independently organised and managed by personnel allocated to each activity, without interference in or from any other activity with which conflicts of interest may occur.

Also with a view to minimize the risk of conflicts of interest, financial intermediaries must adopt the necessary measures in their internal organisation to ensure that: (i) any information of which they became aware in the course of their business, particularly information not yet public and price sensitive, is of limited access to the departments and persons directly involved in the transaction and (ii) any such information is not used in transactions in which the financial intermediary itself, the persons responsible for its administration and auditing or its personnel are involved, or in which other clients or third parties are interested - e.g., the research department cannot base its analysis on the information collected by the corporate department.

In line with the above, the CIUMCR sets out in relation to investment funds’ management companies, that employees and those in charge of management, having investment decision and execution powers within a management company, are not allowed to have similar powers in another management company. Moreover, pursuant to the same regime, a management company that is authorised to perform the activity of portfolio management on behalf of a third party, on a discretionary and individualized basis, under a client’s mandate, may not invest the whole or part of a client’s portfolio in units marketed or of collective investment undertakings managed by itself, unless with previous consent of the relevant client.

## 5. OUTLOOK

Directive 2004/39/EC, of April 21, 2004, on financial instruments markets, also known as the New Investment Services Directive (which is designed to include some innovation in the area of conflicts of interests between financial intermediaries and their clients or between clients) has brought new challenges for the supervisory authorities regarding its implementation in the national regulation. Member States shall adopt the laws, regulations and administrative provisions necessary to comply with this Directive by April 2005 at the latest.

As already referred to in Section 4 above, the expanding range of activities that many financial intermediaries undertake at the same time has significantly increased the risk of conflicts of interest between each one of its activities and the interests of its clients. Therefore, it is necessary to provide for rules in order to ensure that these conflicts do not adversely affect the interests of clients.

Under this Directive, financial intermediaries shall maintain and operate effective organisational and administrative arrangements with a view of taking all reasonable steps to prevent conflicts of interest from affecting their clients' interests, which if not duly ensured, obliges financial intermediaries to clearly disclose the general nature and/or sources of conflicts of interest to clients before undertaking business on their behalf.

The European Commission is required to adopt the necessary measures to allow the effectiveness of these desiderata, according to the Lamfalussy Process.

In addition, the CMVM has recently approved and published for public discussion a draft of amendment to Regulation 12/2000, with the purpose of strengthening investors' protection schemes and adapting financial intermediation activities to the most recent changes in the capital markets. In relation to conflicts of interests, the following rules from the draft Regulation should be highlighted: (i) those responsible for compliance may only execute transactions if previously authorised by the board of directors, and (ii) financial analysts are not allowed to execute transactions over the securities analysed within a period from thirty days prior to the conclusion of the research report up to the market session subsequent to the distribution of the said report to its addressees.

## 6. USEFUL REFERENCES

The contacts of the entities in charge of the supervision and enforcement of the rules on the conflicts of interest of financial institutions are as follows:

Comissão do Mercado de Valores Mobiliários

Av. da Liberdade 252, 1056-801 Lisboa

Tel: +351 213 177 000

Fax: +351 213 537 077

Toll Free Number (if calling from Portugal): 800 205 339

E-mail: [cmvm@cmvm.pt](mailto:cmvm@cmvm.pt)

Website: [www.cmvm.pt](http://www.cmvm.pt)

Banco de Portugal  
Rua do Ouro 27, 1100-150 Lisboa  
Tel: +351 213 213 200  
Fax: +351 213 464 843  
Website: [www.bportugal.pt](http://www.bportugal.pt)

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## AUDITORS

### 1. GENERAL INTRODUCTION

Considering that there were no major scandals in Portugal, as there have been in recent years in the United States and in many European countries, the debate on such issues as auditors' independence and conflicts of interest in Portugal followed a different path than that of the directly affected countries. There was no broad public discussion on these issues, just specific debates promoted, on one side, by the Portuguese securities commission, the *Comissão do Mercado de Valores Mobiliários* ("CMVM"), and, on the other, by the auditors association, the *Ordem dos Revisores Oficiais de Contas* ("OROC"). The CMVM, through the promotion of debates and the implementation of new Regulations, sought to promote corporate transparency, investors' protection and market stability, following the European Commission recommendations on the improvement of audit quality and auditors independence. The OROC, through specific debates and by proposing the implementation of new legislation by the government, intended to clarify that international scandals were caused not so much by auditors' failure, but by management misconduct, that there was a real "expectations gap" between what investors expected and what auditors could deliver, and that the reforms under discussion at international level were too harsh for auditors.

There are three main sources of law and practice regarding audit quality and auditors independence in Portugal: (i) the Legal Regime of the Statutory Auditors, approved by the Decree-Law no. 487/99, of November 16 (the "LRSA"); (ii) the Portuguese Companies Code, approved by the Decree-Law no. 262/86, of September 2 (the "Companies Code"); and (iii) the Portuguese Securities Code, approved by the Decree-Law no. 486/99, of November 13 (the "Securities Code"). These sources, explained below, are complemented by the Regulations of the CMVM, amongst others.

The OROC is the primary body responsible for the surveillance of the auditor's activity, as well as the interpretation and enforcement of the LRSA, through its disciplinary powers over its members. Although the OROC is a public administrative entity, it is totally independent from the Government. It is "responsible for representing and grouping its members (...) as well as overseeing all aspects pertaining to the statutory auditing profession".

The CMVM is responsible for the public registration of auditors entitled to audit listed companies as well as ensuring the accuracy of the financial information disclosed by such companies. It has broad powers to rule on all aspects of the securities market (as it did in relation to the auditors of listed companies), as well as to enforce the Securities Code and its Regulations.

In Portugal, conflicts of interests are related to self-interest, self-review, advocacy, familiarity or trust, and intimidation. The provision of non-audit services by auditors combines several of the said threats to their independence and is probably



one of the most keenly debated risks of auditors' conflicts of interest in Portugal. In fact, auditors commonly provide non-audit services, such as tax consulting services. The same originally applied to management consulting services, although the tendency has been for some time now to separate such services, which are now rendered by different companies. As for legal services, it has been common for auditors to have agreements with law firms, involving different levels of business integration, but in general maintaining different legal entities to provide the said services.

## **2. BACKGROUND AND ENVIRONMENT**

In Portugal the regulation of audit services has long been divided between the direct regulation of the audit profession by the LRSA, and the indirect regulation by the companies and securities law. All three sources of law provide for audit quality and independence requirements.

Since the creation of the OROC in 1972, auditors have tried to improve and ensure the status and dignity of the audit profession, through self-regulation and disciplinary powers. The last step was the enactment of the new LRSA in 1999. The nature and powers of the OROC have deeply influenced the current environment as the audit profession continues to be generally subject to self-regulation and, considering the position of the OROC on the causes of the financial crisis, not many changes are expected in the near future regarding auditors independence. The exception to the self-regulation principle relates to the audit of listed companies, as the CMVM Regulations, which develop the Securities Code, impose specific duties on the auditors of such companies.

In 2000, the CMVM issued Regulation 6/2000, on Auditors, establishing the rules applicable to registration with the CMVM and the performance of specific duties. After the international financial scandals and the approval of the European Commission's Recommendation on the independence of statutory auditors, the CMVM issued Regulation 11/2003, amending Regulations 7/2001 and 11/2000, on Corporate Governance. This amendment raised the regulatory standards applicable to listed national companies. As a result, new disclosure duties for listed companies were created, including the disclosure of information on the services provided by their auditors. The underlying objective of this regulatory intervention was to perfect the Portuguese corporate governance structures by aligning them with good international practices and in this manner renew the investors' confidence in the Portuguese stock market and the models of corporate governance therein.

## **3. APPLICABLE LAW, REGULATION, CODES AND CASE LAW**

As referred to above there are three main sources of law regarding auditors' independence: the LRSA; the Companies Code; and the Securities Code. The first governs the organisation of the OROC, the scope of the audit profession and the rights and duties of its members; the second governs the relationship between the auditor and the audited companies in order to ensure an adequate legal certification of their annual accounts (Article 414 on the requirements that must

be fulfilled so that an auditor may be lawfully appointed should be highlighted); and the third establishes specific rules regarding the audit of listed companies and the report of the external auditor.

These sources of law are complemented by the Regulations issued by the CMVM regarding the audit of listed companies. Regulation 6/2000, on auditors, should be highlighted, as it establishes the requirements that auditors must fulfil in order to be registered with the CMVM and, moreover, to be able to issue an audit report on the annual accounts of listed companies. We should also highlight Regulation 7/2001, on Corporate Governance, as amended by regulation 11/2003, which requires that listed companies present an annual report on their corporate governance, including the description of non-audit services provided by their auditor, the price paid for such services, the relationship between the amounts paid for such services and the overall total amounts paid by the company to such auditor, and the description of the safeguard measures adopted to ensure the auditor's independence.

Furthermore, the Law no. 49/2004, of August 29, sets out the acts that can only be performed by lawyers.

Finally, although not binding, the Portuguese Auditors' Code of Ethics, approved by OROC (the "Code of Ethics") provides the audit profession with important guidelines to minimize conflicts of interest, focusing on auditors' independence and responsibility as the main principles.

As for case law, according to our knowledge and the information provided by the OROC, there is no relevant case law regarding auditors' independence or conflicts of interest.

#### **4. THE REQUIREMENTS**

We present below the requirements imposed on auditors by the different sources of law referred above.

##### **4.1. The LRSA**

According to the LRSA, auditors are not allowed to be members of corporate bodies of any company (except in the position of judicial liquidator). Furthermore, they are prohibited from rendering any audit services to a company where (a) the auditor, his spouse or a blood relative in a direct line holds any shares; (b) the auditor's spouse, any blood relative or relative in law in direct line or other close relatives, is a member of the Board of Directors; (c) the auditor carries out any other remunerated activity that may jeopardise its independence; and (d) the auditor has acted, in the previous three years, as a member of the Board of Directors. The LRSA also set out a "cooling-off" period of three years in which auditors may not be appointed as members of executive bodies of a former audited company.

According to the LRSA, auditors can only render the services included in the OROC's qualifying exam, which includes, amongst others, law (including tax law), accountancy, economics, auditing, finance. Notwithstanding the broad scope of this provision, including many non-audit services, the services that may be rendered by auditors are limited by other laws, such as the above referred Law no. 49/2004, of August 29, which establishes the acts that can only be performed by lawyers. Those acts include legal consultancy; drafting of contracts; all preparatory acts leading to the constitution, amendment or termination of contracts, namely those carried out before public notaries and registrars; all acts relating to judicial claims against the acts issued by the Tax Authorities. According to the said law, only firms exclusively composed by lawyers, or by lawyers and paralegals (*solicitadores*) are entitled to perform such acts.

However, the wording of this law sets out that it shall apply without prejudice to other acts that may be carried out by other professions which are subject to a specific regulation - such as auditors. Based on this, OROC has already issued a statement stressing that the enactment of the said law will not affect, in any manner, the scope of action of the auditors, who may continue to provide all the services included in its qualifying exam, including tax and legal advice relating to the auditing activity.

#### **4.2. The Companies Code**

According to the Companies Code, auditors shall be appointed by the General Shareholders Meeting, for a period set forth in the Articles of Association, and which shall not exceed four years. The General Shareholders Meeting is also entitled to dismiss the auditors provided that a justified reason occurs.

Pursuant to Article 414 of the Companies Code, those who (a) benefit from any advantages relating to the audited company; (b) hold, or have held, in the previous three years, any management position in the audited company; (c) are members of the Board of Directors of a company of the same group of the audited company; (d) perform permanent remunerated functions to the audited company or to a company of the same group; or (e) hold any position in a competitor company; may not be appointed as its auditor.

#### **4.3. Regulation 6/2000**

Pursuant to the Securities Code, the CMVM issued Regulation 6/2000 which requires that, in order to be registered with the CMVM and, therefore, to be able to issue an audit report on the annual accounts of listed companies, auditors must fulfil certain requirements, namely:

- (a) auditors/audit firms must be equipped with the human, material and financial resources deemed necessary to guarantee their suitability, independence and technical competence;
- (b) audit firms must have no less than three full-time chartered accountants/auditors working exclusively for them;

- (c) auditors operating as sole practitioners or, in the case of audit firms, one of the partners (chartered accountant) must have at least five years of effective professional experience and must have been practising exclusively for at least three years;
- (d) the net assets of the audit firm can not be worth less than €50,000;
- (e) audit firms must have a business volume above € 250,000, and sole practitioners overall total fees earned must be no less than €150,000;
- (f) no client may represent more than 15% of the total annual business volume of an audit firm or of the total annual fees of a sole practitioner; (g) they must hold a professional insurance policy worth no less than €2,500,000; and
- (g) they must have an adequate knowledge of financial instruments and of the operation of the securities market; (i) they must show evidence of having sufficient organisational, human and material resources to carry out their duties as set out by the Portuguese Securities Code and the Regulations of the CMVM.

In relation to conflicts of interests, Article 11 of Regulation 6/2000 further provides that auditors registered with the CMVM and, in the case of audit firms, also their partners, are expressly forbidden from benefiting from private advantages or hold, either directly or through an intermediary, any securities whatsoever issued by entities to whom they provide auditing services; or by any other organisations with which they are in a parent-subsidiary or group relationship. This rule also applies to the spouses and partners of statutory auditors.

#### **4.4. Code of Ethics**

In order to promote the independence of auditors, the Code of Ethics suggests certain rules, such as:

- (a) auditors must refuse to render any services whenever the free judgement and the capacity to independently consider the situations may be to some extent jeopardised; or where any doubts about his independence may be raised by third parties;
- (b) auditors shall refuse to receive from third parties any instructions on the work to be carried out or on the conclusions to be drawn within the scope of the work;
- (c) auditors shall neither organise nor assume legal responsibility for the accountancy of companies where the same auditor, his spouse, a relative or relative in law, provide auditing services; and
- (d) fees to be invoiced to the clients must not exceed 15% of the global annual fees of the auditor.

## 5. OUTLOOK

First of all, the outlook of this issue in Portugal over the next coming years will depend on the approval of the Directive proposed by the European Commission in March 2004, on statutory audit of annual accounts and consolidated accounts, by the European Parliament and the European Council. As referred to in the press release of the European Commission, the objectives of this proposed Directive are “to ensure that investors and other interested parties can rely fully on the accuracy of audited accounts and to enhance the EU's protection against the type of scandals that recently occurred in companies such as Parmalat and Ahold. The proposed Directive would clarify the duties of statutory auditors and set out certain ethical principles to ensure their objectivity and independence, for example where audit firms are also providing their clients with other services”.

Moreover, although there was no broad public debate in Portugal regarding auditors' independence, as referred to above, there have been specific debates and discussions promoted by the CMVM and the OROC. As a result, the OROC presented proposals for the amendment of the major sources of law, specifically to those applying to listed companies, in order to reinforce the auditors independency towards its clients and increase the accuracy and truthfulness of the financial information provided. The most relevant proposals for the amendment of LRSA consist of, amongst other things, establishing a rotation period of five years for single auditors (or for the auditor responsible for the team in charge of rendering audit services) and seven years for audit companies. Additionally, the proposal also specifies the non audit services which auditors are not entitled to perform simultaneously with their audit services.

## 6. USEFUL REFERENCES

We present below the contacts of the Portuguese entities in charge of the surveillance and enforcement of auditors' independence obligations:

Ordem dos Revisores Oficiais de Contas

Address: Rua do Salitre 51/53

1250 Lisboa

Tel.: (+351) 21 353 61 58

Fax: (+351) 21 353 61 49

Website (only in Portuguese): <http://www.cidadevirtual.pt/croc/>

Comissão de Mercado dos Valores Mobiliários

Address: Avenida da Liberdade 252

1056-801 Lisboa

Tel.: (+351) 21 317 70 00

Fax.: (+351) 21 353 70 77

Website: <http://www.cmvm.pt>

E-mail: [cmvm@cmvm.pt](mailto:cmvm@cmvm.pt)

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# LAWYERS

## 1. GENERAL INTRODUCTION

In Portugal, considering the duty of a lawyer to serve the interests of justice as well as those whose rights and liberties he is trusted to assert and defend, it has been generally considered that his independence is one basic supports of the administration of justice. That is why the regulation of conflict of interests of lawyers is increasingly stricter under Portuguese law. Such regulation seeks, on one hand, to protect and promote the dignity and independence of the lawyer, in his role as a true participant in the administration of justice, and, on the other hand, to ensure the relationship of trust that must be established between the lawyer and his client.

The main sources of law regarding conflict of interests of lawyers are (i) the legal regime of the Portuguese bar association (*Estatuto da Ordem dos Advogados*), approved by the Law no. 15/2005, of January 26, (the “*Estatuto*”); (ii) the legal regime of law firms (*Regime Jurídico das Sociedades de Advogados*), approved by the Decree-Law no. 229/2004, of December 10 (the “*RJSA*”); and (iii) the Criminal Code (*Código Penal*), approved by the Decree-Law no. 400/82, of September 3 (the “*Criminal Code*”). These sources are complemented by the opinions and decisions issued by the Portuguese bar association (*Ordem dos Advogados*)(the “*OA*”). Finally, it should be noted that the provision of legal services in Portugal by lawyers from the European Economic Area is also subject to the Code of Conduct for Lawyers in the European Union, as approved by the Council of the Bars and Law Societies of Europe (CCBE).

The OA is the primary responsible for the surveillance and enforcement of the said sources of law, as it has disciplinary power over its members. However, the decisions of the OA can be appealed before the administrative Courts, under Article 6 of the *Estatuto*. Furthermore, the Courts are responsible for the enforcement of the law in any other proceedings other than disciplinary proceedings.

## 2. BACKGROUND AND ENVIRONMENT

Conflict of interests have always been a matter of central importance to the Portuguese legislator. In fact, it was regulated in the old Judicial Statute (*Estatuto Judiciário*), approved by the Decree-Law no. 13,809, of June 22, 1927, which established, for the first time, the applicable regime to the profession, the rights and duties of lawyers and of the OA. This issue was also regulated in subsequent laws, such as the former and the current *Estatuto*, approved by Decree-Law no. 84/84, of March 16, and Law no. 15/2005, of January 26, respectively. The RJSA, approved in 2004, provided for further regulation of this issue. Conflict of interests were, therefore, progressively regulated in a stricter and exhaustive way. Nevertheless, even if certain practices and conduct of lawyers were not initially

considered as relevant to ascertain the existence of conflict of interests for legal purposes, the fact is that, in practice, lawyers were already subject to several severe and strict obligations on in this matter, based on established but not written ethical principles and practices.

The current legal regime still considers conflict of interests as a central issue, providing for the prevention and prohibition of any conduct which may create a situation of conflict of interests for the lawyer or its firm. In order to prevent these situations from arising (every day increasingly complex and difficult to identify), it is usual for the main Portuguese and foreign law firms to adopt a conflict-check procedure using specialist software.

### **3. APPLICABLE LAW, REGULATION, CODES AND CASE LAW**

As referred to above, the main sources of law in Portugal are:

- (i) the legal regime of the Portuguese bar association (*Estatuto da Ordem dos Advogados* - “Estatuto”), approved by the Law no. 15/2005, of January 26;
- (ii) the legal regime of law firms (*Regime Jurídico das Sociedades de Advogados* - “RJSA”), approved by the Decree-Law no. 229/2004, of December 10; and
- (iii) the Criminal Code (*Código Penal*), approved by the Decree-Law no. 400/82, of September 3.

Also as referred to above, please note that these sources are complemented by (i) the opinions and decisions issued by the OA and (ii) the Code of Conduct for Lawyers in the European Union. The first seeks to clarify the law and to provide guidance to lawyers in the exercise of their profession. In this way, there are an endless number of decisions that clarify the scope of the law, through real situations which have occurred in practice, enabling lawyers to better understand and prevent any conflict of interests. The second governs the provision of legal services in Portugal by lawyers from the European Economic Area, and deals with conflict of interests in Section 3.2. This code of conduct was originally adopted at the CCBE Plenary Session held on October 28, 1988, and subsequently amended at the CCBE Plenary Sessions of November 28, 1998, and December 6, 2002.

The Estatuto establishes the duties which lawyers are obliged to comply with in their relations with clients. Article 94 deals specifically with possible causes of conflict of interests, establishing several duties upon lawyers in order to prevent such situations. A breach of these duties may lead to disciplinary proceedings under Article 110 (which decision may be appealed before the administrative courts, as above referred, under Article 6) and to subsequent disciplinary penalties, that may range from a mere warning to expulsion from the OA, under Article 125.

The RJSA deals, in Article 60, with conflict of interests within law firms.

Finally and as we discuss below, the Criminal Code establishes that certain abuses of situations of conflicts of interest by lawyers are deemed to be criminal offences.

## **4. REQUIREMENTS**

### **4.1. Criminal Code**

Article 370.2 of the Criminal Code establishes that a lawyer or paralegal (*solicitador*) who acts in a situation where the interests of its clients are conflicting, with intention to benefit or damage one of them, shall be punishable with three years imprisonment or with a fine.

As far as we can tell, there is no relevant case law on this matter.

### **4.2. Estatuto**

Article 94 of the Estatuto deals with the possible conflict of interests, setting out several rules:

- (a) A lawyer must refuse sponsorship of a case - judicial or not - in which he has intervened in any other quality, or that is connected with another case in which he represents, or has represented, the counterparty;
- (b) A lawyer must refuse sponsorship against who, in any other pending cause, is sponsored by himself;
- (c) A lawyer cannot advise, represent or act for the count of two or more clients, in the same matter or in related matters, if any conflict exists between the interests of those clients;
- (d) If there is any conflict between the interests of two clients, or there is a risk of violation of its confidentiality duty or a decrease of its independence, a lawyer must cease to act for the count of both clients involved in that conflict;
- (e) The lawyer must refuse to sponsor a new client if that represents any risk of violation of its confidentiality duty to a former client, or if the knowledge of the issues of its former client represents an illegitimate or unjustified advantage for the new client;
- (f) Whenever a lawyer exercises his activity in association with other lawyers, whether or not in a law firm, the foregoing rules are applicable to the association and to each of its members.

The lawyer's wilful or negligent violation of the foregoing rules may give rise to disciplinary liability, which is independent of any eventual civil or criminal liability.



#### **4.3. RJSA**

The RJSA sets out, in Article 60, that the creation of independent internal work groups does not exclude the application of the rule referred to above in paragraph (f) of the previous section, which states that whenever a lawyer exercises his activity in association with other lawyers, whether or not in a law firm, the rules on conflicts of interest are applicable to the association and to each of its members.

In order to clarify these questions, it is usual for law firms to create internal rules that provide guidance to lawyers when dealing with these issues.

#### **5. OUTLOOK**

As referred above, the regime of conflict of interests in Portugal was developed towards a more strict and thorough regime. In fact, further to the recent approval of the new Estatuto and the RJSA, the legal concept of conflict of interests currently comprises an extensive range of situations that, as such, are prohibited and punished by law. It should be highlighted that according to this evolution, it seems that the Portuguese law is evolving towards the exclusion of the so-called “Chinese walls” or “firewalls” as valid mechanisms to overcome the limitations imposed upon law firms. However, considering that both the new Estatuto and the RJSA are very recent, there is no relevant case law or opinions or decisions of the OA, on the extent, practical application and impact of these rules in Portugal.

Considering all the above, we do not expect any new legislation on this issue, but we do expect the development of case law and opinions and decisions of the OA following the tendency of stricter restriction of lawyers’ conduct in order to avoid any possible situation of conflict of interests arising, especially within law firms, whose size and number are increasing every day. The high degree of complexity of transactions, dealing with several parties interests, is another important and relevant factor that contributes to the complexity of this issue.

Finally, it should be mentioned that no specific rules regarding securities lawyers are expected for the time being. In fact, although the Sarbanes Oxley Act was enacted in the United States in 2002, deeply influencing the reform of financial and company law at European level, it is yet to be discussed whether such rules as “reporting up the ladder” and “noisy withdrawal” should be applicable in Europe and, more specifically, in Portugal.

#### **6. USEFUL REFERENCES**

The contacts of the OA, which is the primary organisation responsible for the supervision and enforcement of the rules on the conflict of interests of lawyers are as follows:

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