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The Petrobras Crisis: Arbitrating Investors' Claims Against the Brazilian Federal Government

Roberto Castro de Figueiredo (Tribe Arbitration and St Mary's University) · Saturday, March 6th, 2021

The recent crisis between the Brazilian president Jair Messias Bolsonaro and the Brazilian national oil company Petrobras may result in a wave of investors' claims submitted to arbitration against the Brazilian Federal Government for abuse of controlling power and breach of fiduciary duties under the [Brazilian Companies Act 1976](#).

During a [live broadcast](#) on February 18th via Facebook, Bolsonaro expressed his unhappiness with the constant rises in fuel prices charged by Petrobras. The next day, Bolsonaro [insisted](#) that, while he would not interfere in Petrobras' fuel pricing policies, he nevertheless foreshadowed that changes would be made in Petrobras. This announcement led to a [sharp drop](#) of the shares negotiated in the Brazilian stock exchange, representing a market value loss of approximately USD 5.4 billion, amid investors' fears that the Brazilian Federal Government would control fuel prices. Later that evening, after the close of the Brazilian stock exchange, Bolsonaro [announced](#) that he had appointed a retired army general to replace Petrobras' current president. The immediate reaction in the market was a [drop by 9.45%](#) of Petrobras' shares' depositary receipts ('ADRs') negotiated in New York through after-hours trading. After trading on the Brazilian stock exchange resumed the next day, Petrobras [suffered](#) a further market value loss of approximately USD 14 billion.

Bolsonaro's row with Petrobras is not new. Back in April 2019 Bolsonaro [ordered](#) Petrobras to cancel a rise in fuel prices. Since then, the decline in international oil prices during the first months of the pandemic avoided new fuel prices hikes and kept Bolsonaro's disagreement with Petrobras out of sight. But after international oil prices regained pre-pandemic levels and the Brazilian national currency Real [fell around 40%](#) against the US dollar during the pandemic, Petrobras increased fuel prices once again. According to the [Brazilian press](#), Bolsonaro fears that fuel prices hikes would affect opinion polling on his administration and reduce his chances of re-election in 2022.

The Brazilian Federal Government [controls](#) Petrobras together with the Brazilian federal development bank BNDES, but their shareholding sums around 37% of Petrobras' total shares. The remaining 63% are negotiated in the market and at least 43% of Petrobras' shares are held by non-Brazilian investors. Since the company lost in 1997 the [monopoly over the exploitation of oil resources in Brazil](#), Petrobras, under [Brazilian law](#) and its corporate [bylaws](#), must follow market-oriented policies and compete on equal footing with other oil companies despite being partially owned by the Brazilian Federal Government. On top of that, the Brazilian Companies Act 1976

provides that controlling entities of companies partially owned by public entities have fiduciary duties to the company and to minority shareholders, and they can be held liable for abuse of controlling power.

Pursuant to the arbitration clause available at Article 58 of Petrobras' bylaws, disputes between shareholders concerning the application of the Brazilian Companies Act 1976 and the company's bylaws must be settled in accordance with the rules of arbitration of the [Chamber of Arbitration of the Market – CAM](#), a Brazilian arbitration institute created by the Brazilian stock exchange in 2001. The arbitration clause excludes from arbitration disputes arising out of Petrobras' business orientations by the Brazilian Federal Government, but such exception is limited to disputes concerning votes casted by the Brazilian Federal Government at the shareholders' general meetings that are aimed at orienting the Petrobras to meet the public interest that justified the creation of the company. It will not be a surprise, however, if the Brazilian Federal Government alleges that the matter is not arbitrable as a matter of law pursuant to the [Brazilian Arbitration Act 1996](#) and, therefore, that any such disputes must be decided by Brazilian federal courts.

In any case, it is not known how investors who acquired Petrobras' ADRs in New York would prefer to resolve such disputes. They may choose to submit their claims against the Brazilian Federal Government to arbitration pursuant to Article 58 of Petrobras' bylaws or to bring lawsuits, including class actions, before American courts. There is precedent for the latter approach. In 2015, the U.S. District Court of the Southern District of New York was presented with a class action brought against Petrobras and other defendants. The class members alleged a mixed set of claims, with some plaintiffs having claims arising under the [U.S. Securities Exchange Act of 1934](#), and others with claims arising under Brazilian law, collectively for liability owing to the sharp decline in Petrobras' value following the disclosure of fraud and corruption scandals. The Court held that the arbitration clause at Article 58 of Petrobras' bylaws did not cover claims under the [U.S. Securities Exchange Act of 1934](#), but class members with claims arising under Brazilian law would need to arbitrate their claims (*In re Petrobras Securities Litigation*, 116 F. Supp. 3d 368, 386–89 (S.D.N.Y. 2015)). In practical terms, the decision excluded from the class action all investors who acquired Petrobras' shares in Brazil, but allowed the class action to move forward in relation to investors who acquired Petrobras' ADRs in New York because their claims were based the violation of the U.S. Securities Exchange Act of 1934. Accordingly, under present circumstances, for ADR investors to avoid Petrobras' arbitration clause, they would have to claim the violation of U.S. Securities Exchange Act of 1934, but not the violation of the Brazilian Companies Act 1976 and of Petrobras' bylaws.

But litigation before American courts is not easy and free of hurdles. First, ADR investors must establish that the case falls within the “commercial activities” exception of the [U.S. Foreign Sovereign Immunities Act 1976](#), which otherwise provides the Brazilian Federal Government with jurisdictional immunity in U.S. courts. Second, ADR investors would also have to convince American courts not to apply the act of State doctrine, according to which a court should refrain from deciding on the lawfulness of an act of a State performed within its territory.

Arbitrating disputes involving [public entities in Brazil](#) is nothing new and Brazilian courts have long recognised that public entities may enter into and be bound by arbitration agreements. But most disputes involving public entities submitted to arbitration in Brazil arise out of contracts, including concession agreements. The possibility of investors of Petrobras arbitrating their claims against the Brazilian Federal Government is something certainly new and is a development that should be closely watched.

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