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Brazilian Arbitration Law: First Impressions on the Recent Amendment Regarding Bylaw Arbitration Clauses

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The enforceability of arbitration clauses in the bylaws of companies set up under Brazilian law has long been a source of controversy. The topic is now in the spotlight with the notorious *In Re Petrobras Securities Litigation*, a class action filed before the US District Court for the Southern District of New York claiming that Petrobras issued misleading financial statements, which allegedly harmed shareholders and ADR holders who overpaid for stock priced on wrong information. The lead plaintiff, Universities Superannuation Scheme, Ltd argues that the arbitration clause in Petrobras' bylaws is not binding: *"Neither Petrobras shareholders nor ADS holders have ever expressly consented to an arbitration proceeding"*. The company, however, disagrees on the grounds that shareholders and ADR holders gave their consent *"By acquiring shares of Petrobras long after the bylaws were amended in 2002 of require arbitration of disputes"*.

The purpose of this post is not to analyze the *In Re Petrobras Securities Litigation,* but to make a commentary on a recent amendment to the Brazilian Corporations Law (BCL) aimed at preventing (or at least mitigating the risk of) future discussions similar to the one briefly reported above.

In addition to altering certain provisions of the Brazilian Arbitration Act (BAA), Law 13,129, of May 26, 2015 also amended the BCL to grant dissenting shareholders the right to withdraw from a company in case a shareholders general meeting (Under Brazilian law, the board of directors does not have authority to approve the inclusion of an arbitration clause in the bylaws) approves the inclusion of an arbitration clause in the bylaws (A higher quorum for such deliberation was also put in place. There are two cases where the right to withdraw is not applicable – such cases will not be discussed in this post). Such amendment to the BCL, according to some Brazilian scholars, was carried out with a view to overcome the commonly raised objection – based on constitutional grounds – that dissenting shareholders are not bound to arbitration clauses inserted in the bylaws by majority vote because they did not consent thereto.

In fact, article 5, XXXV of the Brazilian Federal Constitution provides that *"the law shall not exclude any injury or threat to a right from the consideration of the Judiciary"*. The Brazilian Supreme Court has decided that the BAA is compatible with this constitutional right because the existence of valid consent of all interested parties is imposed as a legal requisite to the enforceability of arbitration clauses (i.e., the BAA does not allow arbitration to be imposed unilaterally).

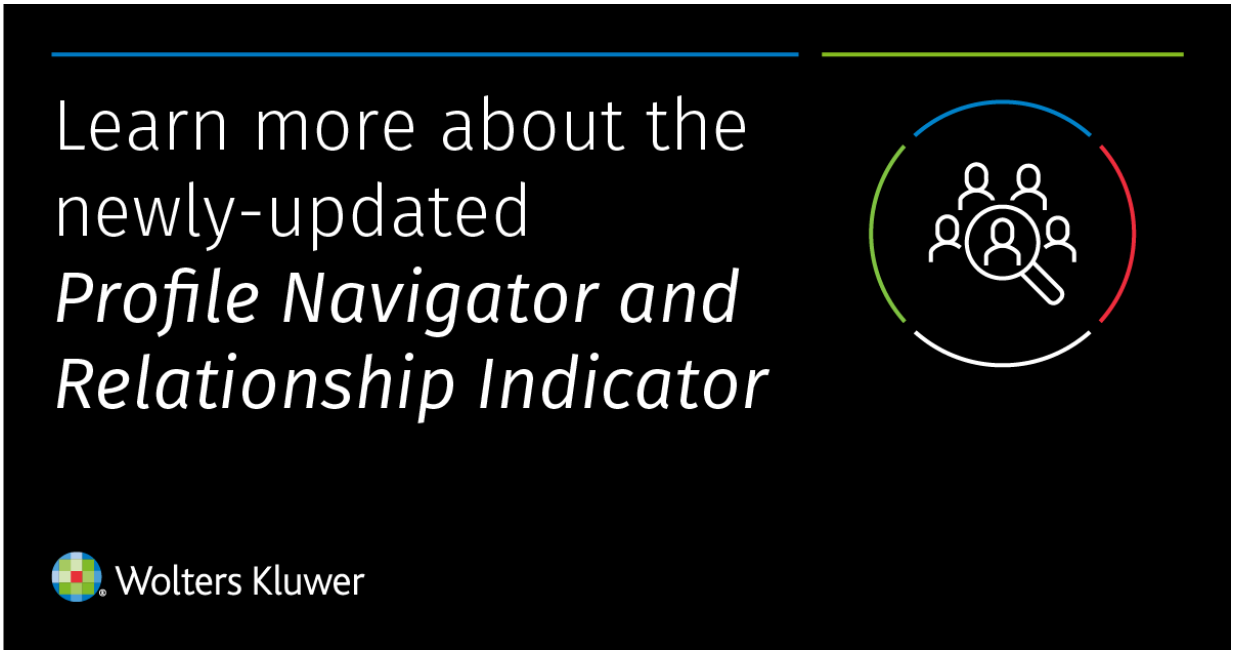
Drafters of the amendment to the BCL claim that the rationale thereof is the following: since the right to withdraw was made available, it may be taken for granted that shareholders who continued to hold their shares after the approval of an arbitration clause tacitly agreed to resort to arbitration (as also did those investors who bought shares after such approval

Not all Brazilian scholars agree that such tacit consent is sufficient to meet the constitutional "valid consent" requirement, though. There is a group of scholars that equate corporate bylaws to adhesion contracts. And based on a provision of the BAA holding that the adherent party to an adhesion contract with an arbitration clause is bound to this clause only if such party expressly agreed to resort to arbitration, said group reasons that only the shareholders who voted in favor of including an arbitration clause in the bylaws are bound by such clause.

On the other hand, there is another group of scholars who not only reject such equation, but also argues that the amendment to the BCL was not even necessary to face constitutional challenges to arbitration clauses approved by majority vote. Such group holds that in buying shares of a company, investors tacitly agree to be bound by the majority principle and therefore to the possibility of having the bylaws amended against their vote. Moreover, in this group's view, the right to withdraw has historically been limited to a very few cases, where key aspects to evaluating the expected return / risk of the investment in shares of a company are at stake. The inclusion of an arbitration clause in the bylaws – the argument goes – is not one of those key aspects and thus should be treated as all other numerous, relevant matters in the life of a company, which are routinely decided by majority vote, without right to withdraw, as all shareholders tacitly agreed.

There is not yet case law on whether tacit agreement is sufficient to comply with the constitutional requisite to the enforceability of arbitration clauses. Although one may assume that the chances of enforceability are substantially higher now that dissenting shareholders were given the right to withdraw, there is no certainty on how Brazilian courts, and especially the Supreme Court, would rule if confronted with such a controversial issue.

Since numerous Brazilian companies have inserted arbitration clauses in their bylaws, and many other are expected to follow suit, it is not unlikely that, despite the recent amendment to the BCL, we come to see in the near future discussions similar to the one held in *In Re Petrobras Securities Litigation* also being brought about in Brazil.



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